



**INTERNATIONAL FEDERATION  
OF ACCOUNTANTS**

545 Fifth Avenue, 14th Floor  
New York, New York 10017  
Internet: <http://www.ifac.org>

Tel: (212) 286-9344  
Fax: (212) 286-9570

**Agenda Item  
3**

---

**DATE:** May 12, 2009  
**MEMO TO:** Members, Technical Advisors and Observers of the IPSASB  
**FROM:** Ian Carruthers-Task Force Chairman-& John Stanford  
**SUBJECT:** Long-Term Fiscal Sustainability

---

**ACTION REQUIRED**

Members, Technical Advisors and Observers are asked to:

- **Consider** the preliminary draft Consultation Paper, “Long-Term Fiscal Sustainability Reporting in the Context of General-Purpose Financial Reporting”;
- **Comment** on its structure, coverage, and content; and
- **Provide guidance** on the specific issues highlighted in this memorandum, as well as the preliminary views expressed in the draft Consultation Paper. .

**MATERIAL ATTACHED**

- 3.1 Preliminary draft Consultation Paper, “Long-Term Fiscal Sustainability in the Context of General-Purpose Financial Reporting”
- 3.2 Extract from Minutes of Zurich Meeting, October 2008
- 3.3 Project Brief

**OBJECTIVE OF THIS SESSION**

The objective of this session is to obtain the Board’s views on the structure and coverage of the preliminary draft Consultation Paper, the content (particularly the level of detail) and the preliminary views expressed. This will enable a further draft to be brought to the September meeting with a view to approval for issuance.

**BACKGROUND**

At its meeting in Beijing in November 2007, Members agreed to initiate a project on long-term fiscal sustainability. Members acknowledged that the issue of prospective information in the context of general purpose financial reporting (financial reporting) was under consideration in the Conceptual Framework project and that subsequently constituents would be asked for their views on the scope of financial reporting. Nevertheless, because of its importance, Members decided that this project should not be deferred until after responses to the Consultation Paper had been analyzed. Therefore, a Project Brief was issued in February 2008. The response was generally supportive of the IPSASB’s decision to initiate the project. The IPSASB also agreed that a Task Force should be established. Ian Carruthers, the UK Technical Advisor, was appointed as Chair. The Task Force had its first meeting in London in September 2008.

At the Zurich meeting a preliminary discussion was held on a proposed outline of the structure and content envisaged by the Task Force. This discussion was informed by a questionnaire completed by members of the Task Force providing details of approaches

to long-term fiscal sustainability reporting in their jurisdictions. The minutes from that meeting are attached at Appendix A. In particular Members directed that:

- The project's scope should not be restricted to the national government level as the Task Force had proposed;
- The project should be more clearly linked to the proposed conceptual framework, in particular to the objective of accountability and the qualitative characteristics of financial reporting; and
- Although there is no global consensus on the definition of the term, a working definition of the term "long-term fiscal sustainability" was necessary.

The Task Force, including additional representatives from the Organization for Economic Co-operation and Development (OECD), subsequently met in Paris in March 2009 and considered an early outline draft report. The OECD has recently initiated a project on Fiscal Futures and the IPSASB project has benefitted greatly from some of the material compiled for this project by Barry Anderson and James Sheppard. The current structure of the Consultation Paper reflects the outcome of the Task Force's deliberations at that meeting.

## **KEY ISSUES**

The following key issues on which the views of the Board are solicited:

- Definition of "Long-Term Fiscal Sustainability"
- Alignment of fiscal sustainability reports and GPFSSs
- What is a general-purpose financial report?
- High level principles-based approach
- Assurance

### **Key Issue 1: Definition of "Long-Term Fiscal Sustainability"**

The Task Force responded to the Board's view that a working definition of the term "long-term fiscal sustainability is necessary by adopting the following working definition: *"the ability of government to manage its finances so it can meet financial commitments both new and in the future."* This is a modification of the definition used in the Australian budget papers. The definition seeks to recognize that sustainability is dependent upon an ability to fund spending levels to provide goods and services, but also that it extends to debt servicing obligations. The definition attempts to acknowledge some flexibility in governments' ability to modify taxation levels, and also reflects that governments have an ability to modify current policies for the delivery of goods and services.

### **IPSASB View Required**

Is the working definition of long-term fiscal sustainability in Section 1 of the Paper appropriate? If not, how should the definition be modified?

**Key Issue 2: Alignment of fiscal sustainability reports and general purpose financial statements (GPFSS)**

The Consultation Paper puts forward preliminary views that:

- The presentation of information on long-term fiscal sustainability is necessary in GPFs in order for the objectives of financial reporting accountability and decision making as proposed in the IPSASB's Consultation Paper, "Conceptual Framework for General-Purpose Financial Reporting by Public Sector Entities" to be achieved. (Preliminary View 1); and
- Requirements and guidance for long-term fiscal sustainability should be linked to the concept of the reporting entity. Requirements should not be limited to a particular level of government. Controlled entities should not have to report on long-term fiscal sustainability unless users for such information can be identified. (Preliminary View 3)

The Task Force member from the Australian Department of Finance and Deregulation is firmly of the view that, although long-term fiscal sustainability reports are important documents for the attainment of accountability, such reports should remain outside the general-purpose financial statements (GPFSS) and that there should not be an attempt to align long-term fiscal sustainability reports with the reporting entity for the GPFSS.

The Consultation Paper reflects a more widely held view that such an approach would not meet the objectives of general-purpose financial reporting, because a characteristic of GPFs is that they present highly aggregated information that is understandable to users. Highly detailed technical descriptions and complex presentational formats can impair understandability. Consequently it is questionable whether a reliance on voluminous and complex long-term fiscal sustainability reports would achieve the objectives of GPFs (see also below Key Issue 3). This issue is fundamental to the project and it is important that Members provide the Task Force with a view in order to allow the Consultation Paper to be finalized.

**IPSASB View Required**

Do you agree that long-term fiscal sustainability information should be presented in general-purpose financial reports, and that boundary for such information should be linked to the reporting entity?

**Key Issue 3: What is a general purpose financial report?**

Key Issue 3 is closely related to Key Issue 2. Section 3 of the Consultation Paper has identified a number of reports on long-term fiscal sustainability at the national level. The Task Force is of the view that, with the exception of the Statement of Social Insurance published in the Annual Report of the US Federal Government, these are reports in the "special purpose (and other reporting category)" and therefore are not GPFs. This issue is crucial, because, if these reports are characterized as GPFs, then, arguably, the IPSASB should be developing requirements and guidance for long-term sustainability reports, rather than exploring how the information in these reports can be used in GPFs or GPFSS.

Such a development would have major resource implications for this project and would also necessitate significant modifications to the timescales and the way in which the project is communicated to other professional groups, as the development of fiscal sustainability projections has not been an area in which financial accountants have been heavily involved in most jurisdictions.

A related and fundamental issue is whether information has to be published with the GPFSs in order to meet the definition of GPFR. The memorandum on the response to the first Conceptual Framework Consultation Paper (Agenda Item 2A.0) indicates that there was considerable ambiguity on this issue on the part of respondents. A number of respondents hold an expectation that the IPSASB views a GPFR as a single report that will encompass all matters identified as within the scope of financial reporting. The memorandum states a Staff view that Staff does not believe this was intended by the IPSASB and that GPFRs may encompass separate reports dealing with particular aspects of the broad scope proposed in that first Conceptual Framework Consultation Paper, as appropriate.

Given this broader ambiguity about the nature of a GPFR, it is important for IPSASB to provide a view on whether information has to be published with the GPFSs in order to meet the definition of GPFR or, if not, provide greater clarity on what does constitute a GPFR.

**IPSASB Views Required**

Do you agree that the reports on long-term fiscal sustainability identified in section 3 of the Paper are in the “special purpose and other reports” category and are not GPFRs?

Does a report have to be published with a GPFS in order to meet the definition of a GPFS?

**Key Issue 4: Principles-based approach**

The Consultation Paper adopts a high level principles-based approach that emphasizes the importance of disclosure. The Paper therefore does not go into detail on issues of specific methodology, such as discounting and sensitivity analysis, covered in Section 7. The Task Force Chair and Staff believes that this is in accordance with the approach outlined in the project brief (see Agenda Item 3.3) and reflects the view in the first Consultation Paper on the Conceptual Framework that special purpose (and other such) reports are outside the IPSASB’s purview. Issues such as discounting and sensitivity analysis are highly complex and detailed consideration of them would drastically change both the shape of the project and the resource requirements and skill sets necessary to progress the project. They would also require considerable interaction with the key professional groups involved in the development of fiscal sustainability projections.

**IPSASB View Required**

Does the IPSASB accept the approach to methodology should be high level and principles-based?

**Key Issue 5: Assurance**

The Consultation Paper puts forward a tentative preliminary view (in Section 8 of the paper) that formal assurance should be provided on the reasonableness of the assumptions underpinning long-term fiscal sustainability projections in GPFRs. Such assurance might be on a “negative” basis. Some Task Force members, principally the Australian member, while relatively content with the discussion in the paper, have reservations about prescription on the form of audit assurance prior to further discussion with auditing bodies/standard-setters. Other Task Force members emphasize the importance of peer review and a more general requirement for disclosure of steps taken to ensure the reliability of the projections rather than formal audit assurance. Subject to the views of Members, it is intended to ask staff of the International Auditing and Assurance Standards Board to provide views on this section of the Paper.

**IPSASB View Required**

Are members content with the direction of the discussion on Assurance in section 8 of the Paper and that this should be forwarded to IAASB staff as the IPSASB’s tentative view?

**Ian Carruthers, Chair of Task Force**  
**John Stanford: Deputy Technical Director**

**Consultation Paper  
October XX 2009**

**REVISED DRAFT (VERSION 5)**

# **Long-Term Fiscal Sustainability in the Context of General Purpose Financial Reporting**

**International Federation of Accountants**

**International Public Sector Accounting Standards Board**

## **REQUEST FOR COMMENTS**

The IPSASB welcomes comments on the proposals in this Consultation Paper. Please submit your comments, preferably by email, so that they will be received February 28, 2010. All comments will be considered as a matter of public record. Comments should be addressed to:

Technical Director  
International Public Sector Accounting Standards Board  
International Federation of Accountants  
277 Wellington Street West  
Toronto Ontario Canada M5V 3H2

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

Copies of this Consultation Paper may be downloaded free-of-charge from the IFAC website at <http://www.ifac.org>.

Copyright *October* 2009 by the International Federation of Accountants. All rights reserved. Permission is granted to make copies of this work to achieve maximum exposure and feedback provided that each copy bears the following credit line:  
“Copyright © *October* 2009 by the International Federation of Accountants. All rights reserved. Used with permission.”

**Executive Summary**

**TO BE INSERTED IN VERSION FOR SEPTEMBER 2009 VERSION**



## **REQUEST FOR COMMENTS**

The IPSASB welcomes comments on whether you agree or disagree with the Preliminary Views in this Consultation Paper. Comments are most useful when they include the reasons for agreeing or disagreeing.

1. The presentation of information on long-term fiscal sustainability is necessary in GPFs in order for the objectives of financial reporting (accountability and decision making) as proposed in the IPSASB's Consultation Paper, "Conceptual Framework for General-Purpose Financial Reporting by Public Sector Entities" to be achieved.
2. For the objectives of financial reporting as proposed in the IPSASB's Consultation Paper, "Conceptual Framework for General-Purpose Financial Reporting by Public Sector Entities" to be achieved, specific financial statements providing details of forward fiscal sustainability information must be included in the GPFs, or forward projections initially prepared for other reports must be included in the management commentary.
3. Requirements and guidance for long-term fiscal sustainability should be linked to the concept of the reporting entity. Requirements should not be limited to a particular level of government. Individual controlled entities should not have to report on long-term fiscal sustainability unless users for such information can be identified.
4. The choice of long-term fiscal sustainability indicators to be reported should be made by each entity undertaking such reporting, based on the relevance of indicators to its situation and on the extent to which they meet the qualitative characteristics of financial reporting.
5. The basis on which inflows from taxation and other material revenue sources is made should be disclosed.
6. All key assumptions underpinning long-term fiscal sustainability projections should be disclosed in the GPFs.
7. All material programs and transactions must be reflected in long-term fiscal sustainability projections.
8. Disclosures should be on the basis of current policy regardless of future events and deviation from this principle should be disclosed.
9. Projections on long-term fiscal sustainability should be on a bottom-up basis in which material individual expenditure or revenue items are projected and aggregated.

10. Details of key aspects of governing legislation and regulation, and the underlying macro-economic policy and fiscal framework should be disclosed.
11. Time horizons for fiscal sustainability projections should be disclosed in the GPFRs as well as the reason for modifying time horizons and any published plans to modify those horizons.
12. Long-term fiscal sustainability information disclosed in GPFRs must have been prepared or updated within five years of the reporting date.
13. Where discount rates are used, those rates should be disclosed, together with the rationale for their selection.
14. The results of sensitivity analyses should be disclosed.
15. Formal assurance should be provided on the reasonableness of the assumptions underpinning long-term fiscal sustainability projections in GPFRs. Such assurance might be on a “negative” basis.

## **TABLE OF CONTENTS**

		Page
1	Introduction: What is Fiscal Sustainability? .....	8
1.1	Global Challenges Facing Governments .....	8
1.2	Definitions of long-term fiscal sustainability .....	9
1.3	Existing types of fiscal sustainability reporting.....	10
2.	Relevance of Long-Term Fiscal Sustainability Information for General Purpose Financial Reporting .....	11
2.1	The Objectives of General Purpose Financial Reporting .....	11
2.2	Information currently provided in General Purpose Financial Statements..	13
2.3	The “Going Concern” Assumption underlying GPFSs .....	14
2.4	The Gaps in Information Currently Provided in General Purpose Financial Statements .....	14
2.5	Long-Term Fiscal Sustainability Reporting: How it could fill the gaps in GPFS.....	17
3.	How Could Long-Term Fiscal Sustainability Information be Reported in GPFRS?.....	19
3.1	Fixed sustainability reporting at national government levels .....	19
3.2	Fiscal Sustainability Reporting at Sub-National levels .....	20
3.3	Potential models for reporting information on long-term fiscal sustainability in GPFRs .....	21
3.4	Preliminary IPSASB views.....	25
4.	The Reporting Entity and Long-Term Fiscal Sustainability Reporting.....	27
4.1	Introduction.....	27
4.2	Boundary issues .....	27
4.3	Consolidated financial statements or financial statements of individual entities? .....	29
5	Which Fiscal Sustainability Indicators Should be Reported?.....	30
5.1	Introduction.....	30
5.2	Indicators currently used.....	30
5.3	Qualitative Characteristics of Financial Reporting.....	30
5.4	Relevance of different types of indicators .....	31
6	Basis of Preparation: Key Principles .....	34
6.1	Introduction.....	34
6.2	Revenue Inflows .....	34

6.3	Demographic and economic assumptions.....	35
6.4	Age-related and non age-related programs .....	36
6.5	Current versus future policy.....	37
6.6	Bottom-up versus top-down approaches.....	38
6.7	Impact of Legal Requirements and Policy Frameworks.....	38
7	Specific Methodology Issues .....	41
7.1	Introduction.....	41
7.2	Time horizons for projections and their rationale.....	41
7.3	Frequency of reporting.....	43
7.4	Discount rates.....	44
7.5	Sensitivity analysis.....	45
8	Assurance .....	46
8.1	Introduction.....	46
8.2	ISAE 3000 assurance engagements other than audits or review of historical financial information.....	46
8.3	ISA 620, “using the work of an expert.”.....	47

## **1 INTRODUCTION: WHAT IS FISCAL SUSTAINABILITY?**

### **1.1 Global Challenges Facing Governments**

- 1.1.1 Regardless of the stage of economic development of their jurisdictions, governments are increasingly faced with the challenges of maintaining, or if possible increasing, both the quantity and quality of goods and services provided to citizens, meeting entitlements for state pensions and other cash transfer entitlement programs and servicing debt obligations within acceptable taxation levels.
- 1.1.2 Recently the ability of governments to manage the public finances so that an unfair burden is not placed on future generations of taxpayers has become an increasing concern, as a result of factors such as demographic change, technological advances creating new demands by citizens, and by costs in certain sectors, particularly health, accelerating more quickly than the general rate of inflation. In many developed countries the focus has been primarily on ageing populations which are leading to increases in health care expenditure and pensions. However, in developing countries fiscal pressures are more likely to arise from a younger demographic profile, which brings a demand for greater educational spending as well as different types of health spending such as neo-natal care.
- 1.1.3 As well as many of the above factors, the OECD's recently initiated project on Fiscal Futures identifies further challenges in the form of:
- The risks imposed by climate change and natural disasters and their impact on future economic growth; and
  - The need to replace ageing infrastructure
- 1.1.4 The current global financial crisis has given rise to further fiscal pressures in many jurisdictions as citizens question the long-run financial consequences of the various corporate support mechanisms, such as loan guarantees and insurance for bank deposits and toxic assets, that have been adopted to deal with the crisis in the banking and manufacturing sectors and the broader fiscal stimuli deployed by governments. .
- 1.1.5 All these factors have led to an increasing awareness of the importance of long-term fiscal sustainability reporting in enabling stakeholders to hold governments to account and make key decisions. Users of financial statements are likely to be interested in the extent of the fiscal challenge facing governments in reconciling their spending and taxation policies over the medium to long term. The urgency with which this challenge needs to be tackled as the conditions above emerge and crystallize, and how this challenge is changing over time, is also likely to be of interest, so that decisions are well informed and governments can be held to account for the long term impact of their decisions. In addition, capital markets are looking for assurance that plans are in place to meet obligations to repay levels of national debt that are unprecedented in recent times

## 1.2 Definitions of long-term fiscal sustainability

- 1.2.1 At a very high level, fiscal sustainability involves an assessment of the extent to which governmental policies under existing legal frameworks can be met in the future, assuming certain fiscal constraints, principally on taxation levels. There is however no single, widely accepted global definition of the term “long-term fiscal sustainability”.
- 1.2.2 Fiscal sustainability has been linked to the concept of inter-generational equity or fairness, which evaluates the extent to which future generations of taxpayers will have to deal with the fiscal consequences of current policies. The concepts of intergenerational efficiency and intergenerational effectiveness are also used in some jurisdictions. Intergenerational efficiency highlights the risk that failure to address long-term issues in a timely manner may force future governments to adopt policies, the cost of which to the future population will significantly exceed costs borne by taxpayers today. Intergenerational effectiveness highlights a further risk that the failure to address long term fiscal pressures may weaken the ability of governments to respond to other, less predictable future problems.
- 1.2.3 A number of governments have developed formal or implied definitions of fiscal sustainability. In many cases these definitions are located in the context of medium-term fiscal planning, fiscal frameworks or budgetary frameworks; for example, long-term fiscal sustainability is typically linked to specific targets such as a pre-determined Net Debt/Gross Domestic Product (GDP) ratio or a Gross/Net Debt/GDP per capita ratio and the maintenance of taxation at a specified level of GDP. Where fiscal sustainability is defined by reference to specific targets overall governmental spending is said to be fiscally sustainable if it is contained within these pre-determined and publicly communicated targets over a specified period. In many European countries the frameworks adopted are largely those developed by the European Commission in the context of the Stability and Growth Pact.
- 1.2.4 The Australian Budget papers for 2008-2009 define fiscal sustainability as “the ability of government to manage its finances so it can meet its spending commitments, both now and in the future.” In its Exposure Draft, “Reporting Comprehensive Long-Term Fiscal Projections for the U.S. Government”, the US Federal Accounting Standards Advisory Board used a more rigorous working definition of “fiscal sustainability” as the federal government’s “ability to continue, both now and in the future, current policy without change regarding public services and taxation, without causing debt to rise continuously as a share of GDP.” This definition is close to the approach linking long-term fiscal sustainability with debt not being on an “explosive” path.
- 1.2.5 In the absence of a more formal definition a slightly adapted version of the Australian definition is used as a working definition in this Consultation Paper:

*“the ability of government to manage its finances so it can meet financial commitments both now and in the future.”*

The definition seeks to recognize that sustainability is dependent upon an ability to fund spending levels to provide goods and services, but also that it extends to debt servicing obligations. The definition also does not constrain governments' ability to modify taxation levels, (notwithstanding the fact that the extent of this ability may be quite heavily constrained in the current global environment) and also that they have an ability to modify current policies for the delivery of goods and services.

- 1.2.6 The above definition applies only to fiscal sustainability. It does not directly address environmental sustainability. Nevertheless, there is an increasing recognition that assumptions about future levels of economic growth are likely to be affected by factors such as climate change.

### **1.3 Existing types of fiscal sustainability reporting**

- 1.3.1 Information about the anticipated long term consequences of governmental programs has become a regular aspect of public reporting in a number of jurisdictions. In most cases this is a relatively recent development (initiated over the last 10-15 years).
- 1.3.2 Fiscal sustainability can be assessed by looking at the expected path of capital and operating expenditure in the future, what that implies for taxes, and the risks that assumptions used in determining that path will fluctuate materially. Such information typically includes the future cost of goods and services, the cost of entitlement programs, the tax revenues and other resources that will need to be generated in the future to fund them and the cost of servicing debt obligations. Information about the likely future resource needs for continued operation of those programs at existing levels will also provide input to decisions, such as whether to support continued operation of the program and at what level, or to advocate changes to a government's service delivery priorities.
- 1.3.3 Broadly there are 4 types of reporting considered in this paper:
- Country Specific Fiscal Sustainability Reports
  - Reports by National Governments to Supra-National Bodies
  - Reports by Entities at Sub-National Levels
  - Financial Statements presenting prospective cash flows
- 1.3.4 The discussion of existing types of fiscal sustainability reporting in this paper is based on an informal survey completed by Task Force members and on information collected and summarized by the Organisation for Economic co-operation and Development (OECD).
- 1.3.5 The next section of this paper considers how information on long-term fiscal sustainability relates to the reporting objectives proposed by the Board in its first Consultation Paper, "Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities.

## 2. RELEVANCE OF LONG-TERM FISCAL SUSTAINABILITY INFORMATION FOR GENERAL PURPOSE FINANCIAL REPORTING

This section considers the need for information on long-term fiscal sustainability information in GPFRs in the context of:

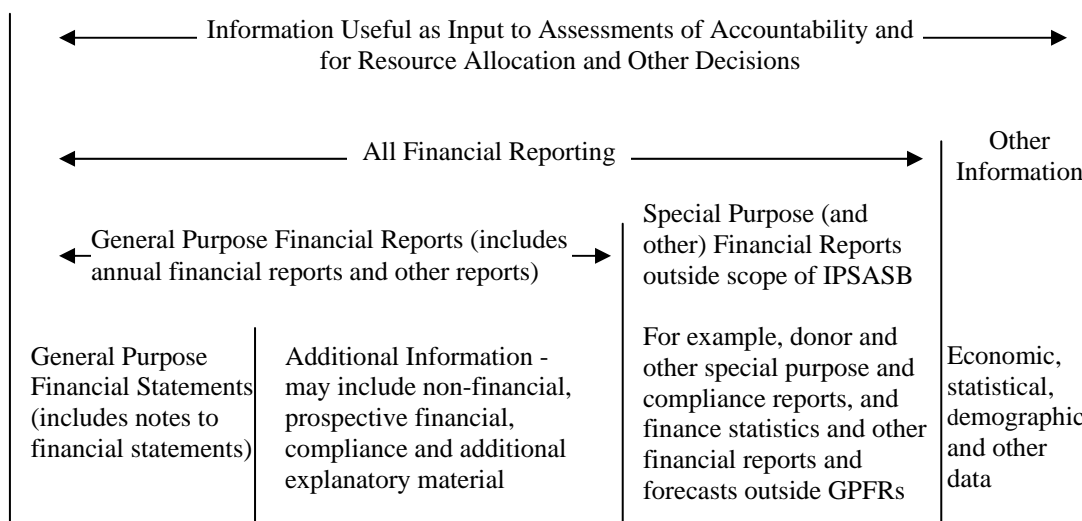
- The objectives of General Purpose Financial Reporting;
- Information currently provided in GPFSS
- The ‘going concern’ assumption underlying GPFSS.
- The gaps in information currently provided in GPFSS; and
- Long-term fiscal sustainability reporting: How it could fill the gaps in GPFSS

### 2.1 The Objectives of General Purpose Financial Reporting

- 2.1.1 In its first Conceptual Framework Consultation Paper the IPSASB distinguished general purpose financial statements (GPFSS) and general purpose financial reports (GPFRs). GPFRs are financial reports intended to meet the common information needs of a potentially wide range of users who are unable to demand the preparation of financial reports tailored to their specific information needs. This is consistent with the approach taken by other global and national standard-setters. Although the Consultation Paper relates to the accrual-based financial reporting, reporting on long-term fiscal sustainability is equally applicable to governments that report on the cash basis. Exhibit One (reproduced from that Consultation Paper) below illustrates the relationship between GPFSSs and GPFRs.

#### Exhibit One

##### Information needs of users



- 2.1.2 GPFSSs may comprise historical information, prospective information or both historical and prospective information. They include statements dealing with an entity's financial position at a specified reporting date, and financial performance,



cash flows and changes in net assets/equity over a specified reporting period. Although such terms have not been used or defined by the IPSASB these statements are sometimes described as the primary, traditional or basic financial statements. GPFSs also include notes on the basis of preparation of, and accounting policies governing, the financial statements, information required in specific accounting standards and additional information relevant to an understanding of the statements.

- 2.1.3 GPFRs are broader than the GPFSs and provide information about the past and future. However, there is considerable debate on the type and format of information that should be referred to as GPFRs and GPFSs. Both include prospective information and contextual information, but, information about the past and present is more common than information about the future. Exhibit One also recognizes other information useful for decision-making and the assessment of accountability that are outside the GPFRs. Such information includes financial reports that are not GPFRs and a range of economic, statistical, demographic and other data.
- 2.1.4 Both GPFSs and GPFRs are intended to meet the common information needs of a potentially wide range of users, who are unable to demand the preparation of financial reports tailored for their specific information needs. They are therefore often distinguished from Special Purpose Financial Reports, where users are in a position to specify their information needs and the format of reporting.
- 2.1.5 In its first Conceptual Framework Consultation Paper the IPSASB put forward a preliminary view that the scope of GPFRs includes “prospective financial and other information about the reporting entity’s future service delivery activities and objectives, and the resources necessary to support those activities.” The Consultation Paper also noted that the scope of financial reporting and information that may be provided by GPFRs is developing and evolving in response to a number of factors including:
- The changing operating environment faced by entities which prepare GPFRs; and
  - Users’ needs for reliable and relevant information about new and innovative transactions that have an impact on matters such as the assessment of the financial position and performance of the entity, and the discharge of its accountability.
- 2.1.6 In practice the distinction between a GPFR and reports in the special purpose financial report and other category can be ambiguous. It is not immediately clear whether the budget documents and long-term fiscal sustainability reports that are made publicly available in some jurisdictions should be classified as GPFRs. In other words, is it appropriate to set standards for information on long-term fiscal sustainability? Is a different view reached if such information is provided in a stand-alone report, or if the information is attached to GPFSs. The rest of this section of the paper addresses these issues.

## **2.2 Information currently provided in General Purpose Financial Statements**

2.2.1 IPSAS 1, Presentation of Financial Statements” states that a complete set of GPFSs comprises:

- A statement of financial position
- A statement of financial performance
- A statement of changes in net assets/equity
- A cash flow statement
- Notes, including a statement of significant accounting policies

2.2.2 Where the entity makes its approved budget publicly available, IPSAS 1 also requires a comparison of budget and actual amounts as either a separate additional financial statement or by way of additional columns in the financial statements.

2.2.3 A key attribute of the current suite of GPFSs is that they are historical in nature. This historical focus is useful for both accountability and decision-making purpose, but it constrains the way in which commitments to provide public services and entitlements and fund those commitments through taxation and other significant revenues are reported in the financial statements..

2.2.4 Although financial statements use estimation techniques to determine the future recoverable amount of assets and the value of liabilities that will not be settled until future reporting periods, they are limited to present rights and obligations that arise from past events, In making these measurements, however, GPFSs generally assume that the entity’s activities are sustainable-the going concern assumption (see below section 2.3).

2.2.5 As noted above, the first Conceptual Framework Consultation Paper proposed that GPFSs may include both historical and prospective information. Historical information is needed to address accountability questions including the costs of services provided during the period and whether resources have been used economically, efficiently and effectively. However, prospective information is needed to assess the sustainability of government operations and to consider the anticipated cost of future service delivery activities. Thus, a major question in considering the question of fiscal sustainability is whether GPFSs can be considered complete if there is no statement providing comprehensive prospective information. Such prospective information may be considered essential to meeting the common information needs of users of GPFRs, but the information may take many forms—tables, charts, and narrative—that are not consistent with typical GPFSs forms. Thus, if prospective information is a necessary component of a GPFR, is it a component of GPFS, or additional information as envisioned in Exhibit One?

## **2.3 The “Going Concern” Assumption underlying GPFSS**

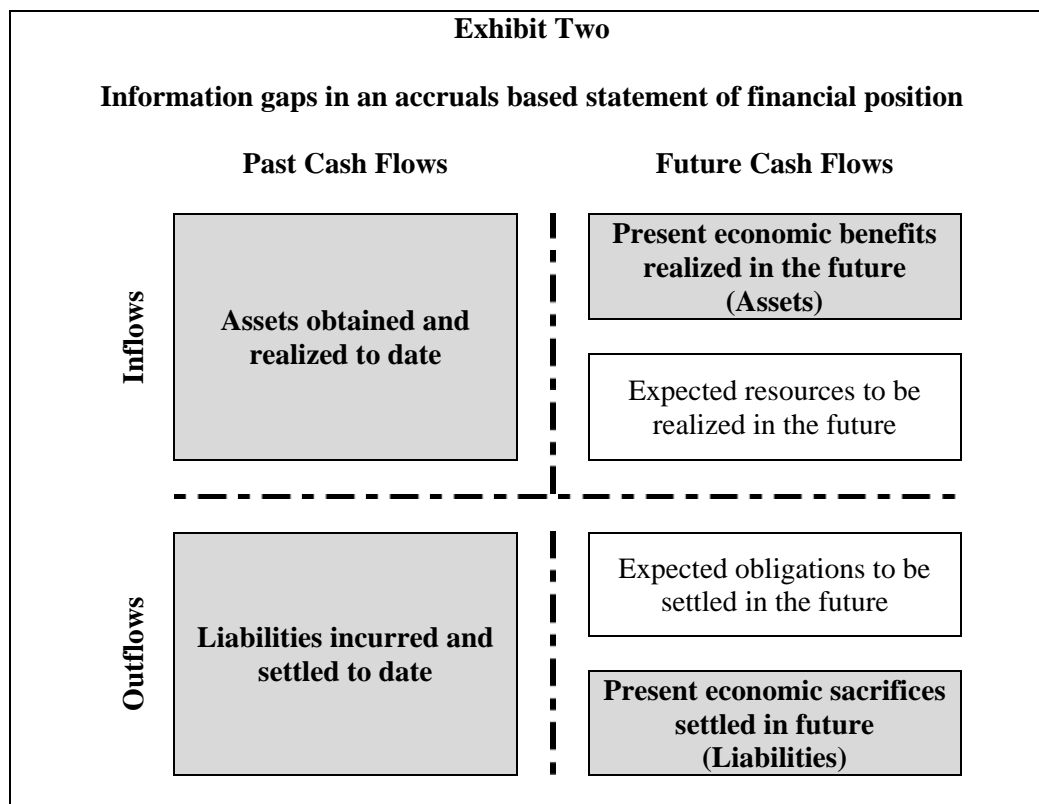
- 2.3.1 The “going concern” assumption is fundamental to the preparation of financial statements in both the private and public sectors. Its future perspective is a relevant consideration of the extent to which the GPFSSs provide adequate information on the viability of entities into the future. Under both IPSAS 1, “Presentation of Financial Statements” and its private sector equivalent IAS 1, “Presentation of Financial Statements” management is required to assess an entity’s ability to continue as a going concern when compiling GPFSSs. GPFSSs are required to be prepared on a going concern basis, unless there is an intention to liquidate the entity, to cease operating or there is no realistic alternative to do so. Where there are material uncertainties that cast significant doubt upon the entity’s ability to continue as a going concern, those uncertainties must be disclosed. The assessment of the adequacy of the “going concern” assumption is a key aspect of an auditor’s work in forming a view on the GPFSSs and the recent global financial crisis has stimulated considerable discussion of the topic.
- 2.3.2 The standards are not prescriptive about the time horizon over which the going concern assumption is to be assessed; the minimum requirement is for a period of twelve months from the date of authorization of the GPFSSs. Although this is a minimum period, the use of a twelve month horizon suggests that “going concern” in the context of the financial statements is a short-medium term notion.

## **2.4 The Gaps in Information Currently Provided in General Purpose Financial Statements**

- 2.4.1 Going concern deals with the potential demise of entities, which is likely to be less relevant in the public sector than in the private sector as it is unlikely that national governments will fail completely. While sub-national entities may get into financial difficulties it is likely that their service delivery functions will be transferred to successor entities. The limited time horizon of the “going concern” assumption and its focus on entities rather than programs therefore imposes an important constraint on the adequacy of the GPFSSs to provide information on the longer-term viability of programs to deliver goods and services. In addition, the historical nature of the GPFSSs inevitably means that there are gaps in information that users need for decision making and the evaluation of accountability.
- 2.4.2 Such gaps have also been acknowledged in the corporate sector, where considerable attention has been directed in recent years to narrative reporting, which has also been termed management commentary (by the IASB) and management discussion and analysis (by the Financial Accounting Standards Board in the United States). In its Discussion Paper, “Management Commentary” issued in 2005, the IASB noted that “management commentary is information that accompanies financial statements as part of an entity’s financial reporting.” One purpose of such commentary is a historically based explanation of the main trends and factors underlying the development, performance and position of the entity’s business during the period covered by the financial statements. However, the IASB also suggested that management commentary should address “the main

- trends and factors that are likely to affect the entity's *future* development, performance and position.” (IPSASB staff italicization)
- 2.4.3 In the public sector, the gaps are exacerbated because of the long-term nature of entitlement programs and increasing constraints on governments' abilities to fund these entitlements because of the impact of demographic changes and limitations on their ability to raise taxes.
- 2.4.4 Accrual-based or historical GPFSs are essential if GPFs are to meet accountability and decision-making needs of users. However, they are not sufficient to meet all such needs. They focus on such matters as:
- Resources currently available for providing services and claims on those resources;
  - The amount, sources, and uses of resources raised during the reporting period; and
  - The cost of services provided during the period.
- 2.4.5 Accrual-based statements are not intended to provide comprehensive forward looking information. They are intended to focus on the present circumstances—the balances of resources and obligations existing in the present—and the performance of the entity during the period of time covered by the statements.
- 2.4.6 The focus of accrual-based statements gives rise to a significant information gap with respect to expectations about the future. For example, the approach to the recognition of taxation revenue in the accrual-based statements excludes critical information about a major resource—the government's right to tax. In its project on intangible assets, the IPSASB, like most public sector standard setters that have considered the issue, has taken the view that a government's right to tax does not give rise to an intangible asset; a slightly different view is that the right to tax is an asset, but that it is immeasurable. For these reasons the IPSASs do not recognize, as an asset, prospective inflows of future tax revenue and other revenues anticipated to be generated to support the entity's activities in the future. Only revenue where a taxable event has been identified is recognized.
- 2.4.7 The approach to the recognition of liabilities in GPFSs is another major example of where such “gaps” exist. Liabilities are only recognized in the statement of financial position where present obligations have arisen. There has been considerable debate about when present obligations related to governmental programs arise and therefore the extent of resultant liabilities that should be recognized in the statement of financial position. The IPSASB has considered this explicitly in its project on social benefits. Generally, governments reporting on the accrual basis of accounting have adopted an approach known as “due and payable” under which liabilities recognized at the reporting date are limited to cash transfers to individuals or households for which eligibility criteria have been satisfied, but which have not been settled at the end of a reporting period.

- 2.4.8 The “due and payable” approach has the advantage of being straightforward to apply and is generally understandable. However, some have challenged it. They believe that obligating events for some social benefits, particularly contributory and entitlement programs, arise at a point before all eligibility criteria have been satisfied and that the extent of the obligation and therefore the resultant liability extends beyond amounts owing at the reporting date. They also have reservations why a “due and payable” approach should only be applied to cash transfers rather than individual goods and services. However, even a broader interpretation of present obligations and the recognition of larger liabilities will not fill all the information gaps in historical financial statements. In fact, based on the work that the IASB has undertaken in developing a modified definition of a liability as part of its Conceptual Framework project, it appears that the global trend is towards a narrower, more restrictive and more understandable definition of a liability, involving a notion of present enforceability.
- 2.4.9 Exhibit Two provides a simplified schematic of the statement of financial position. It illustrates that while the statement captures transactions in the shaded areas for which there have been identified past events, including liabilities which will be settled in future reporting periods, it does not embrace cash flows related to future revenues and future obligations for which there has been no identifiable past event.

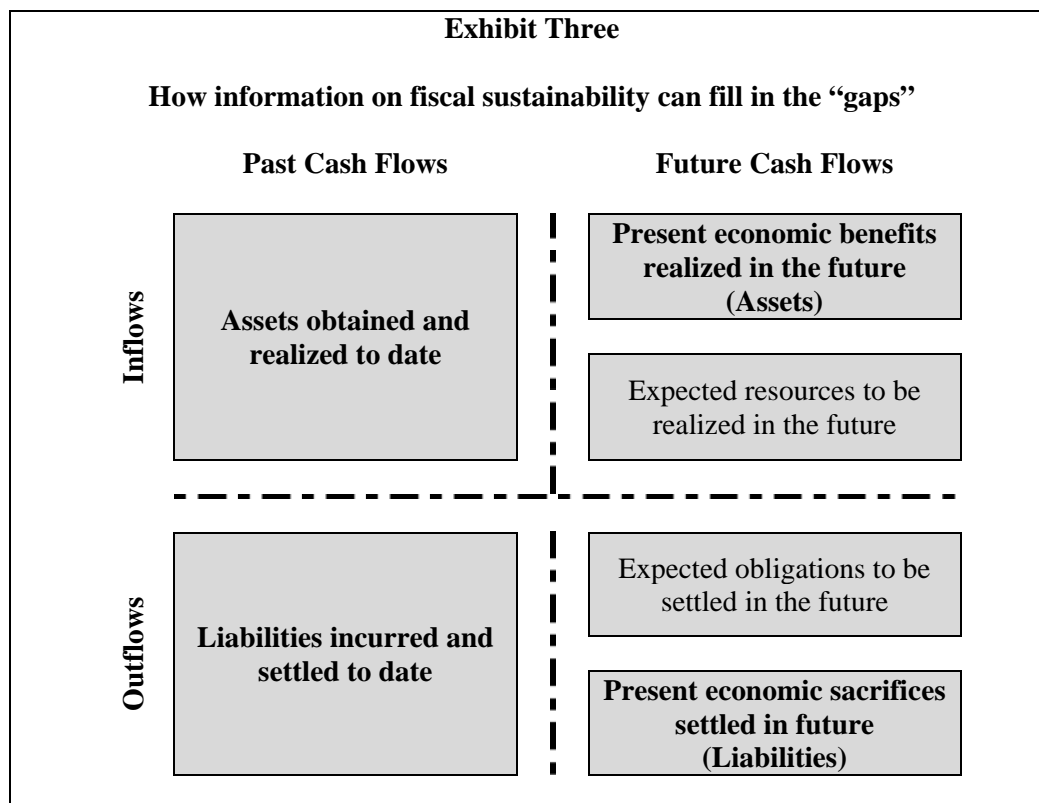


- 2.4.10 Consistent with the above analysis, during the development of its project on social benefits the IPSASB formed a preliminary view that the main historically-based financial statements of an entity-( the statement of financial position, statement of

financial performance, cash flow statement and notes thereto) cannot satisfy all the needs of users in assessing the future viability of that entity and its major programs. The IPSASB holds this view regardless of the approach that is taken to the point(s) at which a present obligation(s) occur(s) (which may vary for different types of social benefits and other government programs), the extent of those present obligations and the amount of the resultant liabilities. Therefore, in order to satisfy user-needs and meet the objectives of financial reporting, information presented in the financial statements needs to be complemented by the presentation of other information about the long-term fiscal sustainability of those programs, including their financing.

## 2.5 Long-Term Fiscal Sustainability Reporting: How it could fill the gaps in GPFS

- 2.5.1 Long-term fiscal sustainability reporting is not constrained by the focus on past events and the definitions of elements that govern the compilation of current GPFSs. Such reporting can provide greater flexibility and therefore has the potential to fill many of the gaps in the statement of financial position identified above, in particular by providing information on prospective revenue inflows and outflows related to future obligations. This is shown in Exhibit Three below that shows how such information can complement the information in the statement of financial position. Exhibit Three therefore demonstrates the importance of incorporating information on long-term fiscal sustainability in the GPFs.



- 2.5.2 The IPSASB considers the historically-based financial statements can certainly present the financial position at the reporting date. The statements may provide the baseline data for determining future viability, but they cannot show the complete picture. The long-term financial effect of government policies need to be made transparent for both decision-making and accountability purposes. To obtain a more complete picture of the sustainability of Government operations, information on long-term fiscal sustainability is required. The introduction of a section of the Management's Discussion and Analysis (MD &A) on financial condition in the 2007 Financial Report of the United States Federal Government summarizes the position in stating that "a complete assessment of the Government's financial or fiscal condition requires analysis of historical results, projections of future revenues and expenditures, and an assessment of the long-term fiscal sustainability of programs and services."

**Preliminary View One**

The presentation of information on long-term fiscal sustainability is necessary in GPFRs in order for the objectives of financial reporting (accountability and decision-making) as proposed in the IPSASB's Conceptual Framework project -accountability and decision making- to be achieved.

### **3. HOW COULD LONG-TERM FISCAL SUSTAINABILITY INFORMATION BE REPORTED IN GPFRS?**

#### **3.1 Fixed sustainability reporting at national government levels**

- 3.1.1 Exhibit Four provides an overview of what is currently produced at the national level.. It provides details of the title of sustainability reports, the originating government department or body, and the date at which such reports were first published. It is not an exhaustive listing.

#### **Exhibit Four Overview of Fiscal Future Reports at National and Supra-national Levels**

<b>Country</b>	<b>Legal Requirement</b>	<b>Title</b>	<b>Source</b>	<b>Start</b>
Australia	Charter of Budget Honesty	Intergenerational Report	Treasury	2002
Denmark		A Sustainable Future	Min of Finance	1997
Germany		Rpt on Sustainability of Public Finance	Min of Finance	2005
Korea		Vision 2030	Ministry of Planning and Budget	2006
Netherlands	EC Stability Program	Aging and the Sustainability of Dutch public finances	Central Planning Bureau	2000
New Zealand	Public Finance Act	LT Fiscal Position	Treasury	1993
Norway		2006 White Paper	Min of Finance	2004
Sweden		Sweden's Economy (annex to budget)	Min of Finance	1999
Switzerland		Long-term sustainability of public finance in Switzerland	Federal Dept of Finance	2008
United Kingdom	Code of Fiscal Stability	LT Public Finance Report	Treasury	1999
USA: CBO		LT Budget Outlook	Congressional Budget Office	1991-2000
USA: GAO		LT Fiscal Outlook	General Accountability Office	1992-97
USA: OMB		LT Budget Outlook in Analytical Perspectives	Office of Management and Budget	1979-97
USA: Financial Report of US Government		Statement of Social Insurance	Department of Treasury	2004
European Union Countries	Stability & Convergence Programming Surveillance	Public Finances – EMU	Economic Policy Comm.	2005
International Monetary Fund		Financial Transparency Reviews	Fiscal Affairs Department	2001

Source: OECD Fiscal Futures Project



- 3.1.2 Reporting on long-term fiscal sustainability has therefore become a feature of financial management in an increasing number of jurisdictions. It should be noted that the compilation of fiscal sustainability projections has generally been carried out by economists, statisticians and budget and policy specialists. Financial accountants have been peripheral to the process.

### **3.2 Fiscal Sustainability Reporting at Sub-National levels**

- 3.2.1 Although long-term fiscal sustainability reporting has become more widespread as shown in Exhibit 4, it is less common at the sub-national levels. Portland (Oregon) and Maricopa County (Phoenix, Arizona) are large municipal entities in the United States that have produced fiscal condition reports. The latter is the most rapidly growing statistical metropolitan area in North America. Both these reports are primarily historical in nature providing historic ten year trend information on a range of financial and demographic variables, highlighting favorable and unfavorable trends and in the case of Maricopa, presenting a significant amount of comparative data with other large US municipalities.
- 3.2.2 In Canada the Provincial Government of Ontario published a report, “Towards 2025: Assessing Ontario’s Long-Term Outlook”, in 2005. This report presented a long-range assessment of Ontario’s economic and fiscal future. It included a description of anticipated changes in the Ontario economy and in the province’s demographic profile over a 20 year horizon, a description of the potential impact of these changes on the public sector and on Ontario’s fiscal situation during that future period. It also presented an analysis of key fiscal issues likely to affect the long-term sustainability of the economy and the province’s public sector.
- 3.2.3 The US Governmental Accounting Standards Board (GASB), which promulgates accounting standards for the sub-federal levels in the USA, has a project on “Economic Condition Reporting: Fiscal Sustainability.” The project’s aim is to identify the information that users require to assess a sub-federal government entity’s economic condition, to compare these needs with the information users receive under current standards, and to consider whether guidance should be considered for the remaining information.
- 3.2.4 The definition of economic condition used by GASB comprises three components: financial position, fiscal capacity and service capacity. Financial position is the status of its assets, liabilities, and net assets, derived from the statement of financial position. Fiscal capacity is the ability to meet financial obligations as they come due on an ongoing basis and is therefore linked to debt maturity and liquidity, while service capacity is an entity’s ability and willingness to meet its commitments to provide services on an ongoing basis. Consistent with the IPSASB’s working definition the GASB definition recognizes both future service provision and the servicing of debt obligations. The ultimate objective of the project is to consider whether any additional information useful for assessing a government’s economic condition should be required or encouraged for inclusion in a government’s financial report.

**3.3 Potential models for reporting information on long-term fiscal sustainability in GPFRs**

3.3.1 This section considers how information on long-term fiscal sustainability might be reported in the GPFRs. It examines a spectrum of potential reporting approaches:

- Specific financial statements providing details of forward projections
- Including summaries of the results of forward projections in the Management Commentary
- Cross-reference in GPFR to reports outside the GPFR

These reporting approaches are not mutually exclusive. For example, it is possible to combine narrative reporting with a specific financial statement showing projected cash flows, as is currently done in the Annual Report of the US Federal Government.

*Specific Financial Statements Providing Details of Forward Projections*

3.3.3 As identified in Exhibit Four the Annual Financial Report of the US Federal Government includes a Statement of Social Insurance providing projected inflows and outflows of the most significant social insurance programs, principally Social Security, and Medicare. The format of this statement is shown in Exhibit Five. The estimates are actuarial present values of the projections and are based on the economic and demographic assumptions set forth in the Social Security and Medicare Trustees' reports and in the relevant agency performance and accountability reports for additional more minor programs. The Annual Report also includes a citizen guide that provides a broader narrative summary of financial condition (a prospective notion) and financial position (a current notion); this is also available as a stand-alone document: this summary is not limited to the entitlement programs reflected in the SOSI (see below paragraph 3.3.5).

Exhibit Five

United States Government  
Statements of Social Insurance  
Present Value of Long-Range (75 Years, except Black Lung) Actuarial Projections

*****UNAUDITED*****					
(In billions of dollars)	2007	2006	2005	2004	2003
<b>Federal Old-Age, Survivors and Disability Insurance (Social Security): (Note 22)</b>					
<i>Revenue (Contributions and Earmarked Taxes) from:</i>					
Participants who have attained age 62.....	477	533	464	411	359
Participants ages 15-61.....	17,515	16,568	15,290	14,388	13,576
Future participants (under age 15 and births during period).....	16,121	15,006	13,696	12,900	12,213
All current and future participants.....	34,113	32,107	29,450	27,699	26,147
<i>Expenditures for Scheduled Future Benefits for:</i>					
Participants who have attained age 62.....	(6,329)	(5,866)	(5,395)	(4,933)	(4,662)
Participants ages 15-61.....	(27,928)	(26,211)	(23,942)	(22,418)	(21,015)
Future participants (under age 15 and births during period).....	(6,619)	(6,480)	(5,816)	(5,578)	(5,398)
All current and future participants.....	(40,876)	(38,557)	(35,154)	(32,928)	(31,075)
<i>Present value of future expenditures in excess of future revenue.....</i>	<i>(6,763)<sup>1</sup></i>	<i>(6,449)<sup>2</sup></i>	<i>(5,704)<sup>3</sup></i>	<i>(5,229)<sup>4</sup></i>	<i>(4,927)<sup>5</sup></i>
<b>Federal Hospital Insurance (Medicare Part A): (Note 22)</b>					
<i>Revenue (Contributions and Earmarked Taxes) from:</i>					
Participants who have attained eligibility age 65.....	178	192	162	148	128
Participants who have not attained eligibility age 15-64.....	5,975	5,685	5,064	4,820	4,510
Future participants (under age 15 and births during period).....	4,870	4,767	4,209	4,009	3,773
All current and future participants.....	11,023	10,644	9,435	8,976	8,411
<i>Expenditures for Scheduled Future Benefits for:</i>					
Participants who have attained eligibility age 65.....	(2,558)	(2,397)	(2,179)	(2,168)	(1,897)
Participants who have not attained eligibility age 15-64.....	(15,839)	(15,833)	(12,868)	(12,054)	(10,028)
Future participants (under age 15 and births during period).....	(5,118)	(3,904)	(3,417)	(3,246)	(2,653)
All current and future participants.....	(23,315)	(21,934)	(18,264)	(17,468)	(14,577)
<i>Present value of future expenditures in excess of future revenue.....</i>	<i>(12,292)<sup>1</sup></i>	<i>(11,290)<sup>2</sup></i>	<i>(8,829)<sup>3</sup></i>	<i>(8,492)<sup>4</sup></i>	<i>(6,166)<sup>5</sup></i>
<b>Federal Supplementary Medical Insurance (Medicare Part B): (Note 22)</b>					
<i>Revenue (Premiums) from:</i>					
Participants who have attained eligibility age 65.....	433	409	363	332	283
Participants who have not attained eligibility age 15-64.....	3,184	3,167	2,900	2,665	2,148
Future participants (under age 15 and births during period).....	1,172	908	924	891	888
All current and future participants.....	4,789	4,481	4,187	3,889	3,119
<i>Expenditures for Scheduled Future Benefits for:</i>					
Participants who have attained eligibility age 65.....	(1,834)	(1,773)	(1,622)	(1,475)	(1,306)
Participants who have not attained eligibility age 15-64.....	(12,130)	(12,433)	(11,541)	(10,577)	(8,845)
Future participants (under age 15 and births during period).....	(4,257)	(3,407)	(3,408)	(3,277)	(2,622)
All current and future participants.....	(18,221)	(17,613)	(16,571)	(15,329)	(12,773)
<i>Present value of future expenditures in excess of future revenue.....</i>	<i>(13,432)<sup>1</sup></i>	<i>(13,131)<sup>2</sup></i>	<i>(12,384)<sup>3</sup></i>	<i>(11,440)<sup>4</sup></i>	<i>(9,653)<sup>5</sup></i>
<b>Federal Supplementary Medical Insurance (Medicare Part D): (Note 22)</b>					
<i>Revenue (Premiums and State Transfers) from:</i>					
Participants who have attained eligibility age 65.....	167	173	185	176	
Participants who have not attained eligibility age 15-64.....	1,627	1,700	1,790	1,857	
Future participants (under age 15 and births during period).....	611	492	572	618	
All current and future participants.....	2,405	2,366	2,547	2,651	
<i>Expenditures for Scheduled Future Benefits for:</i>					
Participants who have attained eligibility age 65.....	(794)	(792)	(880)	(773)	
Participants who have not attained eligibility age 15-64.....	(7,273)	(7,338)	(7,913)	(7,566)	
Future participants (under age 15 and births during period).....	(2,699)	(2,121)	(2,440)	(2,431)	
All current and future participants.....	(10,766)	(10,250)	(11,233)	(10,770)	
<i>Present value of future expenditures in excess of future revenue<sup>6</sup>.....</i>	<i>(8,361)<sup>1</sup></i>	<i>(7,884)<sup>2</sup></i>	<i>(8,686)<sup>3</sup></i>	<i>(8,119)<sup>4</sup></i>	

Totals do not necessarily equal the sum of components due to rounding.

The accompanying notes are an integral part of these financial statements.

- 3.3.4 The US Federal level approach is important in the context of this report as it is the only jurisdiction in which a financial statement is currently required providing projections of inflows and outflows for specific programs. The Comptroller

General of the United States gave an unqualified audit opinion on the 2007 and 2008 SOSIs, although the form of the report differed from that given on the other financial statements. *(Staff Note: wording to be provide in subsequent version.*

- 3.3.5 The Federal Accounting Standards Advisory Board (FASAB), which promulgates accounting standards for the federal level in the USA, has recently completed a consultation period on an Exposure Draft that proposes extending prospective information beyond the SOSI. A new GPFS would provide information about federal spending and receipts, including spending on all programs including areas such as defense, education , as well as entitlement programs, and all revenue sources. The outline of how this Financial Statement might be presented is shown in Exhibit Six below. It includes current year and prior year projections and presents the inter-period change in both absolute terms and as a percentage of GDP.

**Exhibit Six**

<b>Basic Financial Statement</b> <b>Long-Term Fiscal Projections for the U.S. Government</b>						
<b>Long-Term Fiscal Projections for the U.S. Government</b> Amounts projected to 75 years						
	As of January 1, 20XX (Current Year)		As of January 1, 20XX (Prior Year)		Change from Prior Year	
	PV Dollars in trillions	% GDP*	PV Dollars in trillions	% GDP*	PV Dollars in trillions	% GDP *
<b>Receipts</b>						
Medicare	\$ 10.7	1.5%	\$ XX.X	X.X%	\$ XX	X.X%
Social Security	36.3	5.1%	XX.X	X.X%	XX	X.X%
All Other Receipts	<u>91.0</u>	<u>12.8%</u>	<u>XX.X</u>	<u>X.X%</u>	<u>XX</u>	<u>X.X%</u>
<b>Total Receipts</b>	\$ 137.9	19.4%	\$ XX.X	X.X%	\$ XX	X.X%
<b>Spending</b>						
Medicare	\$ 44.8	6.3%	\$ XX.X	X.X%	\$ XX	X.X%
Medicaid	15.6	2.2%	XX.X	X.X%	XX	X.X%
Social Security	40.5	5.7%	XX.X	X.X%	XX	X.X%
Rest of Federal Government**	<u>73.9</u>	<u>10.4%</u>	<u>XX.X</u>	<u>X.X%</u>	<u>XX</u>	<u>X.X%</u>
<b>Total Spending</b>	\$ 174.9	24.6%	\$ XX.X	X.X%	\$ XX	X.X%
Spending in excess of receipts	<u>\$ 37.0</u>	<u>5.2%</u>	<u>\$ XX.X</u>	<u>X.X%</u>	<u>\$ XX</u>	<u>X.X%</u>

- 3.3.6 Locating the current and proposed statements within the context of the spectrum of information discussed in Section 2 of this Paper is not straightforward. It is the intention of FASAB that the broader proposed statement discussed above will initially be considered supplementary information, but will become a basic financial statement after an initial period. Some argue that any statements presenting prospective information can and should be part of GPFSs; others that such information is non-historically based and therefore too remote for inclusion in the core GPFSs and should be in the GPFs:

*Including forward projections in the management commentary*

- 3.3.7 A second approach to reporting fiscal sustainability information in GPFRs is to mandate or permit management commentary to include information on long-term fiscal sustainability derived from other reports. Again recent US experience provides an example of how such reporting might be presented. The Management's Discussion and Analysis section of the 2008 Financial Report of the US Government contains a section entitled Government's Financial Condition, which uses graphs, charts and tabular projections to present both historical information and forward projections over a 75 year period.
- 3.3.8 Historical information includes that on the budget deficit, net operating cost, key national economic indicators, such as real GDP growth and real construction growth, the consumer price index and unemployment levels and historical trends of debt held by the public as a percentage of nominal GDP. A summary of measures to promote financial stability is also included.
- 3.3.9 Forward projections include expenditure on social insurance programs and other government programs, interest on debt, revenues and debt held by public as a percentage of GDP. The discussion in the MD & A has also been used as the basis of a separate stand-alone publication "A Citizen's Guide to the 2008 Financial Report of the US Government", which is available both on-line and in hard copy. The inclusion of fiscal sustainability information in narrative reports can involve boundary issues, where the fiscal projections are developed on a boundary basis that is not the same as that for the GPFs; for example the Citizen's Guide notes that the annual deficit on a budget basis, at just under \$455 billion, was about \$554 billion less than the net operating cost in the GPFs. This difference was largely related to unsettled employee benefits and veteran benefits not recognized in the budget-based deficit.

*Cross-reference in GPFRs to Other Reports*

- 3.3.10 A less ambitious approach to the reporting of long-term fiscal sustainability at the consolidated whole-of-government level in the GPFRs is to require references in narrative reports within the GPFRs to fiscal sustainability reports that are outside the GPFRs. This approach recognizes the importance of information on long-term fiscal sustainability in meeting the objectives of GPFRs, but acknowledges the difficulties in summarizing complex information in voluminous reports and the risks to faithful representation if such information is presented selectively. Therefore proponents of this approach do not advocate providing summarized information on fiscal sustainability in the GPFRs, but consider that user needs can be best satisfied through cross-references to other publicly available reports.

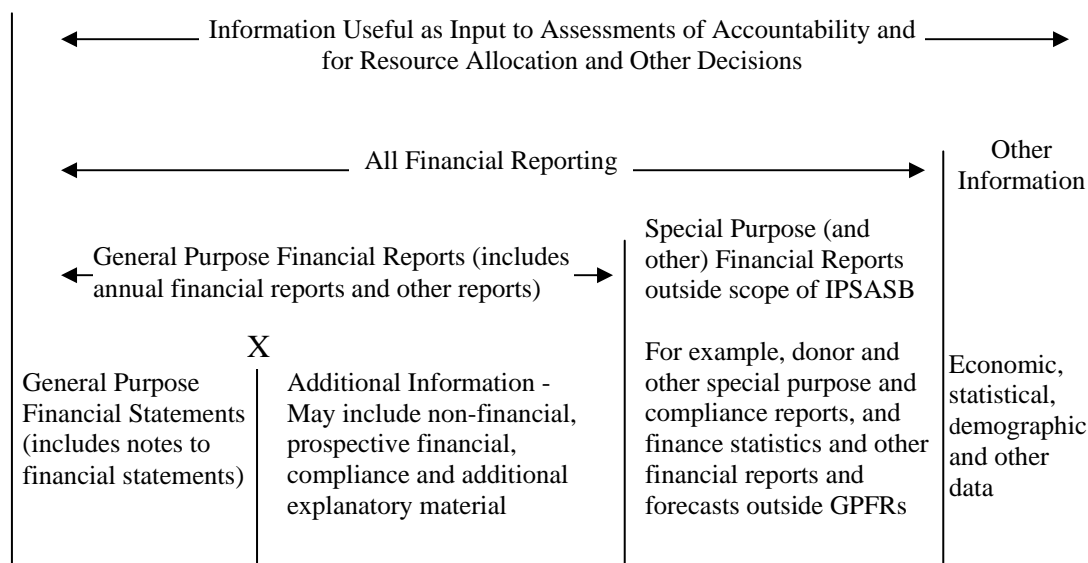
The converse view is that GPFRs present highly aggregated information that is understandable to users. Highly detailed technical descriptions and complex presentational formats can impair understandability. Consequently it is questionable whether references in narrative reports to separate complex and voluminous reports would achieve the objectives of GPFRs

### 3.4 Preliminary IPSASB views

- 3.4.1 In assessing how long term fiscal sustainability information could be reported in GPFRs, the Board made reference to the qualitative characteristics of information (i.e. relevance, faithful representation, timeliness, understandability, comparability and verifiability.) The tentative view, largely based on uncertainties with respect to faithful representation and verifiability, and the audit reporting position, is that the first option of Specific Financial Statements Providing Details of Forward Projections, as exemplified by the current, and proposed broader, financial statement in the US are on the boundary between GPFS and GPFRs (see X in Exhibit Seven below), but that such statements may move into the GPFS category in the future.

#### Exhibit Seven

##### Locating statements of financial projections in reporting spectrum



- 3.4.2 In considering the second and third options the Board highlighted an issue that the reporting boundary for specialist long-term fiscal sustainability reporting is unlikely to be the same as that for the GPFSs either presenting information from those reports or referring to them. In order to meet accountability and comparability requirements, explanations would have to be provided of entities and transactions that are within the boundary of the consolidated GPFSs, but not within the boundary for sustainability reporting and vice-versa.
- 3.4.3 Such a requirement for detailed explanations and reconciliations is likely to impair understandability. On the other hand, so long as the sustainability reporting addressed the major areas subject to demographic change, simplifying assumptions could allow an understandable and useful report to be derived in a cost-effective manner for inclusion in the GPFRSs. As noted in Preliminary View One, the Board does not consider that GPFRS are complete without adequate

consideration of the long-term impact of government policies. For this reason the Board's preliminary view is that references alone to specialist long-term fiscal sustainability reports is not an optimal method for providing users with the information that they need for decision-making and accountability purposes.

- 3.4.4 The Board believes that both the other two methods-specific financial statements providing details of forward projections and including forward projections derived from other reports in management commentary/narrative reporting would satisfy GFPR reporting objectives. This is an evolving area where many countries have yet to start reporting long-term fiscal sustainability information, and those that do undertake such reporting adopt a variety of approaches. Therefore the Board does not believe it should prescribe either approach at this stage. Instead it should encourage the production of specific financial statements providing details of fiscal sustainability information as an eventual objective, while allowing practice to evolve with the inclusion of such information in the management commentary as an acceptable interim stage.

#### **Preliminary View Two**

For the objectives of financial reporting as proposed in the IPSASB's Conceptual Framework project to be achieved specific financial statements providing details of forward fiscal sustainability information must be included in the GPFRs, or forward projections initially prepared for other reports must be included in the management commentary.

## **4. THE REPORTING ENTITY AND LONG-TERM FISCAL SUSTAINABILITY REPORTING**

### **4.1 Introduction**

#### **4.1.1 Previous sections of this Consultation Paper have:**

- Established that long-term fiscal sustainability reporting is an aspect of financial management of acknowledged, and growing, global importance,
- Identified ways in which long-term fiscal sustainability reporting might fill the “gaps” in GPFSs, and provided a preliminary view that information on long-term fiscal sustainability is necessary in GPFRs for the objectives of financial reporting to be achieved.
- Provided a brief summary of long-term fiscal sustainability reporting and have provided a preliminary view on how long-term fiscal sustainability reporting should be reported in the GPFRs.

#### **4.1.2 This section considers boundary issues related to the differences between boundaries based on the control concept that governs compilation of consolidated financial statements and reports based on the statistical basis of accounting and on budget accounting. These issues have already been noted in Section 3. It then further discusses whether long-term fiscal sustainability reports should be presented in the consolidated reports of government or in the reports of separate entities within the economic entity**

### **4.2 Boundary issues**

#### **4.2.1 Globally only a minority of governments use a boundary for sustainability reporting that is based on the control concept that governs the GPFS. The main issue is whether this is an obstacle to the reporting of information on long-term fiscal sustainability in the GPFRs and, if so, how significant an obstacle, and what steps can be taken to deal with it.**

#### *Reporting boundary based on the control concept*

#### **4.2.2 Both IPSAS 6, “Consolidated and Separate Financial Statements” and the separate IPSAS on the cash basis of accounting, “Financial Reporting Under the Cash Basis of Accounting” provide requirements and guidance for the determination of the reporting boundary for consolidation purposes. Under both IPSASs application of the concept of control determines whether an entity is within the reporting boundary. Control of an entity is defined as “the power to govern the financial and operating policies of another entity so as to benefit from its activities.” The term “economic entity”, rather than the private sector term “group reporting entity”, is used in both IPSASs. An economic entity is a group of entities and comprises a controlling entity and one or more controlled entities.**

#### **4.2.3 The definition of control includes both a “power element” (the power to govern the financial and operating policies of another entity, at least at the strategic level)**



and a “benefit element” (the ability of the controlling entity to benefit from the activities of the other entity. If either or both of these elements are absent an entity would not be controlled and would therefore not be within the reporting boundary.

*Reporting boundaries based on statistical accounting and budgeting approaches*

- 4.2.4 Although there are exceptions, such as New Zealand, many governments that report publicly information on long-term fiscal sustainability do not use the same boundary as for consolidated GPFs. They are more likely to adopt a boundary that is determined by statistical bases of accounting or based on the budget sector.
- 4.2.5 Statistical bases reflect requirements consistent with, and derived from, the System of National Accounts 1993 (SNA 93) prepared by the United Nations and other international organizations: SNA 93 is currently being updated and a revision is anticipated in 2009. These statistical bases of financial reporting focus on the provision of financial information about the General Government Sector (GGS). The GGS comprises those non-profit entities that undertake non-market activities and rely primarily on appropriations or allocations from the government budget to fund their service delivery activities. The full public sector comprises both the GGS and the public financial corporation sector (PFC), such as government financial institutions and public non-financial corporation sector (PNFC), such as government owned utilities
- 4.2.6 GPFs consolidate only controlled entities. Statistical bases of financial reporting may be more flexible. In some jurisdictions a national government controls state/provincial and local government entities, and therefore those entities are consolidated in the GPFs; in other jurisdictions there is no control relationship. For example, whereas the local government tier will be consolidated within whole of government accounts in the United Kingdom, that sector is not consolidated in whole of government accounts in Australia and New Zealand. Under the statistical basis of financial reporting, the GGS of all levels of government are combined. This means that in many jurisdictions the GGS will include units that are not consolidated in the GPFs. One obvious advantage of boundaries based on the GGS is that they enhance global comparability. Statistically-based information may therefore be useful to the users of GPFs, even where reporting is on a control basis.
- 4.2.7 Long-term fiscal sustainability projections on statistical accounting boundaries may provide information about the corporations sector of government which primarily engages in market activities (the public financial corporations (PFC) sector and the public non-financial corporations (PNFC) sectors). The PFC and PNFC sector are similar to Government Business Enterprises (GBEs) as defined in the IPSASB literature, but the mapping may not be identical as non-resident GBEs are not classified as PFCs and PNFCs. The statistical basis presents interests in public sector entities in those sectors as investments of the GGS; they are not consolidated as in IPSAS 6 and transactions between the GGS and the PFC and PNFC sectors are not eliminated. In its approach to assessing the

sustainability of particular jurisdictions the IMF considers that the inclusion of public corporations within the scope of reporting should depend on whether this sector exposes government to material fiscal risks.

- 4.2.8 IPSAS 22, “Disclosure of Financial Information about the General Government Sector” prescribes reconciliation requirements for entities which elect to disclose financial information about the statistically based GGS and provides illustrative examples of how reconciliations might be presented. In order to meet accountability requirements the Board believes that long-term fiscal sustainability information should be prepared for the same reporting entity as for financial reporting. Where the underlying fiscal sustainability information is prepared using another boundary, it should be adjusted to provide consistency with the GPFR/GPFS reporting boundary.

#### **4.3 Consolidated financial statements or financial statements of individual entities?**

- 4.3.1 Regardless of the levels of government at which entities are required to report information on fiscal sustainability, there is an issue whether requirements should be linked and restricted to the consolidated financial statements, comprising the controlling entity and controlled entity/entities, or whether they should apply to the separate financial statements of controlled entities.
- 4.3.2 Determining whether the benefits of information for the users of the financial statements of controlled entities justify the costs of providing that information, may depend on factors such as whether a controlled entity has significant tax generating powers, and therefore whether users exist for fiscal sustainability information. In general, it seems questionable whether the cost of producing reports on fiscal sustainability by individual entities, within the economic entity, justify the benefits to users of the information and there may be risks to understandability if individual entities within an economic entity producing a number of separate sustainability reports and disclosures.

#### **Preliminary View Three**

Requirements and guidance for long-term fiscal sustainability should be linked to the concept of the reporting entity. Requirements should not be limited to a particular level of government. Individual controlled entities should not have to report on long-term fiscal sustainability unless users for such information can be identified.

## **5 WHICH FISCAL SUSTAINABILITY INDICATORS SHOULD BE REPORTED?**

### **5.1 Introduction**

- 5.1.1 This section considers how information should be reported by different entities in the context of the qualitative characteristics of financial reporting.

### **5.2 Indicators currently used**

- 5.2.1 Publicly available reports on fiscal sustainability contain a range of indicators.

Examples of reported indicators include:

- Net debt
- Gross debt
- Comprehensive Net Worth
- Net Financial Worth
- Fiscal gap
- Financing/Tax gap
- Inter-temporal budget gap

*(NOTE: DEFINITIONS OF THESE TERMS HAVE NOT BEEN PROVIDED AT THIS STAGD)*

- 5.2.2 Some of the above indicators are presented as a proportion of Gross Domestic Product or in per capita terms. An obvious question is whether the IPSASB should prescribe or recommend a minimum set of indicators, which should be disclosed in the GPFRs regardless of the prominence that they play in a particular jurisdiction's fiscal framework. The advantage of such an approach is that it promotes global consistency. The disadvantage is that there appears to be no consensus on the relevance of these indicators and they may be of limited local or regional significance. For example, gross debt may be misleading as it fails to recognize trends such as the accumulation of assets in public sector pension funds. Misgivings have been expressed in New Zealand about the use of fiscal gap information, and in Australia the primary indicator of fiscal sustainability has been changed from net debt to net financial worth. The profile of indicators across time is also likely to be significant as the indicators may be volatile; reporting an indicator at just one point in time may therefore be misleading.

### **5.3 Qualitative Characteristics of Financial Reporting**

- 5.3.1 IPSASB's project on the public sector conceptual framework has considered the qualitative characteristics of financial reporting. The qualitative characteristics of information included in GPFRs are the attributes that make that information conducive to the achievement of the objectives of financial reporting – that is, for accountability purposes and for making resource allocation, political and social decisions.

- 5.3.2 The qualitative characteristics of information included in GPFRs are relevance, faithful representation, timeliness, understandability, comparability and verifiability. Materiality, cost and achieving an appropriate balance between the qualitative characteristics are pervasive constraints on that information. In evaluating information on long-term fiscal sustainability provided in the GPFRs all these characteristics must be considered.
- 5.3.3 In order for prospective information to be decision-useful and valuable in demonstrating accountability it needs to be transparent, thereby reflecting the qualitative characteristics of relevance and faithful representation. It is therefore important that assumptions are based on published fiscal frameworks and targets. The use of prospective information also gives rise to reservations about the verifiability of information. These reservations are discussed in the final section of the paper.

#### 5.4 Relevance of different types of indicators

- 5.4.1 In considering approaches to the disclosure of information in management commentaries the conceptual framework developed by Allen Schick is useful. Schick puts forward four dimensions of fiscal sustainability
- **Solvency:** the capacity of governments to finance existing and probable future liabilities/obligations
  - **Growth:** the capacity of government to sustain economic growth over an extended period.
  - **Fairness:** the capacity of government to provide net financial benefits to future to future generations that are not less than the net benefits provided to current generations.
  - **Stable taxes:** the capacity of governments to finance future obligations without increasing the tax burden.

The dimensions of solvency and fairness map the notions of fiscal capacity and service capacity developed in the GASB project discussed in Section Three.

- 5.4.2 Solvency is relevant at all levels of the public sector. Therefore forward debt projections will be relevant to all bodies. However, the relevance and salience of the other dimensions above may vary between governmental levels and will depend on factors such as size and tax-generating powers. For example, the growth dimension is important for national governments and for larger sub-national entities, particularly those with powers over corporate taxation and economic regeneration powers. However it may be of more limited significance in predominantly suburban and residential municipalities with a limited ability to affect economic activity in the larger regional area
- 5.4.3 The stable taxation dimension will be at the core of analysis for national governments, but may be of more limited relevance for entities with limited tax-

generating powers, which are dependent on inter-government transfers for a high proportion of their revenues.

- 5.4.4 Gross Domestic Product is a relevant indicator for large and economically significant sub-national entities in federalized structures such as American states, Australian states, certain Canadian provinces and certain European regions with high levels of economic activity. It is unlikely to be relevant or available for small municipalities. Similarly concepts of fiscal gap and inter-temporal budget constraints are national level constructs that apply to the entire public sector and cannot easily be applied for discrete sub-national entities.
- 5.4.5 One factor which may be relevant to the issue of how entities should report on fiscal sustainability is the existence and extent of tax-raising powers. GASB has used the term “intergovernmental financial dependency” to indicate the extent to which entities rely on transfers from other tiers of government in order to meet financial obligations. It seems questionable whether entities that do not have significant tax generating powers and are heavily dependent on inter-governmental transfers for their fiscal capacity should be making projections for external general purpose users covering lengthy time horizons. It may suggest to users that entities have tax-generating powers that they do not control. This might be considered analogous to an entity that does not control an asset reporting that asset in the GPFs. The extent to which an entity is fiscally dependent upon the taxation policies of a higher level of government is likely to be an important indicator in illustrating the extent to which the maintenance of current service provision and the ability to meet financial obligations are dependent on the decision of other entities- a 1995 Canadian Institute of Chartered Accountants (CICA) report on Indicators of Financial Condition defined the term “vulnerability” to denote the degree to which a government becomes dependent on, and therefore vulnerable to, sources of funding outside its control or influence, both domestic and international.
- 5.4.6 Where they do provide prospective information, time horizons for sub-national reporting tend to be much shorter than those adopted at the national level. For example, the report by the province of Ontario, “Towards 2025”, published in 2005 adopted a 20 year horizon. Reports highlighted in the GASB project are primarily historical in nature. The Financial Condition Report on the State of New York by the State Comptroller primarily focuses on historical trends, but does include a section on “Implications for the Future” which illustrates forward trends over a 5 year horizon, including the proportion of state funds projected to be consumed on Medicaid, school funding and meeting debt service obligations. Financial condition reports at the municipal level include those produced in Portland, Oregon and Maricopa County, Arizona. These are again primarily historical.

#### **Preliminary View Four**

The choice of long-term fiscal sustainability indicators to be reported should be made by each entity undertaking such reporting, based on the relevance of indicators to its situation and on the extent to which the indicators meet the qualitative characteristics of financial reporting.

## **6 BASIS OF PREPARATION: KEY PRINCIPLES**

### **6.1 Introduction**

- 6.1.1 This section of the Consultation Paper looks at the programs and transactions that are covered by long-term fiscal sustainability reporting and the principles that should be adopted for their inclusion in GPFRs. There is some overlap with Section 5 because the basis of accounting—whether statistical, accrual or budget—can dictate the programs and transactions that are captured.

### **6.2 Revenue Inflows**

- 6.2.1 As already noted one of the main advantages of fiscal sustainability reporting is that, unlike the GPFSs, such reporting can take into account projected inflows from taxation and other sources for which the taxable event giving rise to an inflow is in the future. (See above Section 2.)
- 6.2.2 All the jurisdictions informally surveyed for this Paper included projections of taxation and other government financing in their projections. In most jurisdictions the approach is to assume an unchanged tax policy over the projection period. The European Commission suggests that this reflects two main assumptions:
- The main tax bases remain constant as a share of GDP and there is no change in the structural wage share of the economy, or the savings rate of households.
  - The average tax rate is constant on the different tax bases, which is consistent with assuming an indexation of all thresholds, bands, minima and exemption of the tax system on average wage.
- 6.2.3 Adopting such an approach involves a modification of the principle governing the GPFSs that only legally enacted measures should be taken into account. Assuming that personal taxation is a constant proportion of GDP is also a straightforward way of dealing with fiscal drag, where increases in nominal incomes result in individuals moving into higher tax bands. However, in its 2006 report on “Long-Term Fiscal Position” New Zealand expressed reservations about this approach by suggesting that “assuming a constant tax to GDP ratio is a strong assumption.” For personal taxation New Zealand is considering adoption of a modified and more sophisticated approach, where proposed staggered tax cuts will be captured in front end forecasts with fiscal drag allowed to take place for the following half a dozen years, before tax is held as a constant proportion of nominal GDP.
- 6.2.4 In the context of long-term fiscal sustainability projections in the GPFRs the most important requirements are that users are informed of the main sources of tax revenue and the way in which the tax base is projected to grow (or diminish) over the reported time horizon i.e., where revenues are individually modeled and the principal assumptions or where revenues are not individually modeled, but instead are projected to grow in line with GDP.

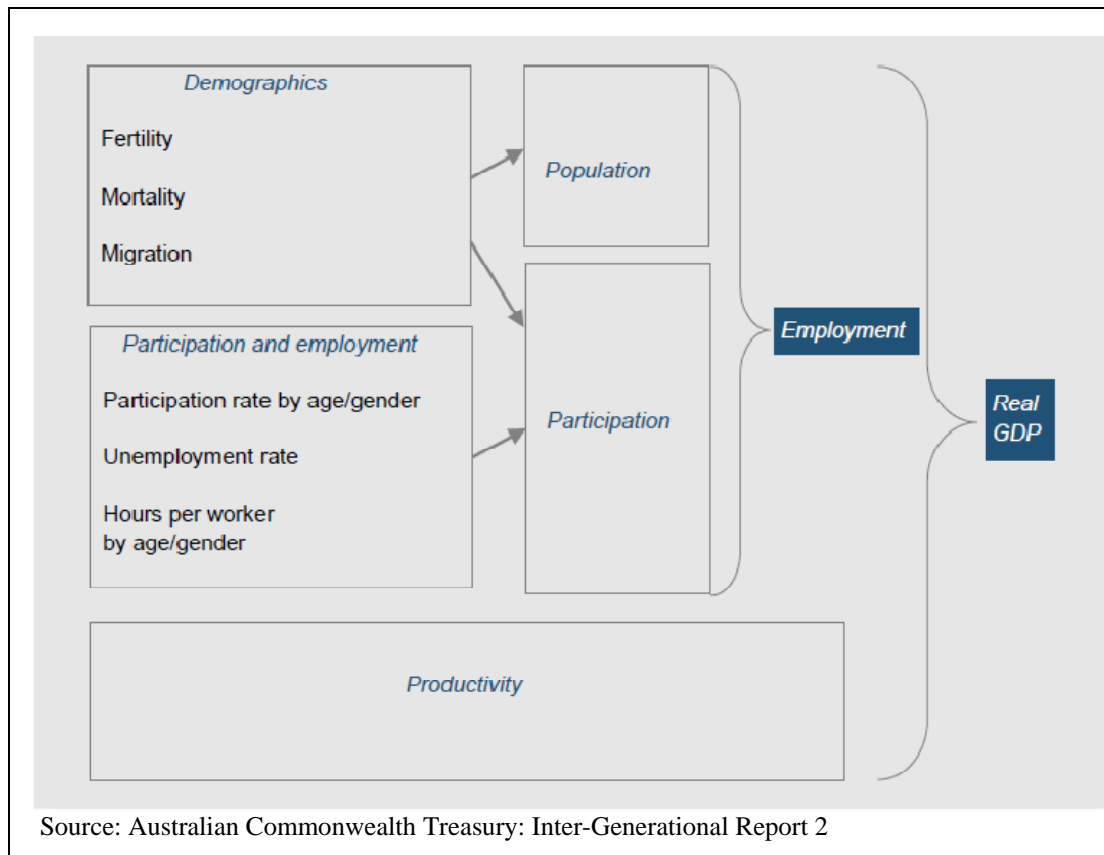
### Preliminary View Five

The basis on which inflows from taxation and other material revenue sources is made should be disclosed

## 6.3 Demographic and economic assumptions

- 6.3.1 While there is considerable congruence in the assumptions used by governments in making projections there are differing ways of classifying them. For example, Australia disaggregates real GDP into three components: population, participation and productivity. Population is the number of people of working age, participation is the average number of hours worked in the labor force by each working-age person and productivity is the average output produced per hour worked. Population is determined by assumptions about fertility, mortality and migration. Population also has an impact on participation because employment levels and hours worked are related to both age and gender. This disaggregation is shown schematically in Exhibit Eight.

**Exhibit Eight**  
**Disaggregating GDP: The Australian Commonwealth Approach**



- 6.3.2 Accounting standards that rely on prospective information to measure the impact of past events on items reported in the financial statements require disclosure of



the main assumptions. For example, IPSAS 25, “Employee Benefits” requires disclosure of principal actuarial assumptions for determining liabilities and asserts related to post-employment obligations. These include the expected return on plan assets, the expected rates of salary increases and medical cost trends.

- 6.3.3 The Board believes that all key assumptions underpinning long-term fiscal sustainability projections should be disclosed in the GPFRs. The challenge for preparers is how to distill a very complex process into an explanation that is succinct and understandable to users of the GPFRs, but does not over-simplify and therefore diminish the reliability of the information reported.

#### **Preliminary View Six**

All key assumptions underpinning long-term fiscal sustainability projections should be disclosed in the GPFRs.

### **6.4 Age-related and non age-related programs**

- 6.4.1 A common approach is to distinguish programs that are age-related and subject to demographic risk and programs that are non-age related or where ageing and demography are not key drivers of spending pressures. For example, in developing its Intergenerational Reports, the Australian Commonwealth Government has modeled individually health, aged care, social security payments and education - which accounted for around 70 per cent of government spending in 2007-08. Other areas of Government spending, such as defense and national security, the environment, transport and communications infrastructure, public order and safety have not been modeled individually, but have been assumed to grow broadly in line with GDP. The rationale is that these other areas do not have a clear link with demographic factors. Furthermore, given their diverse nature, it is difficult to project spending in these areas with certainty. This aggregated approach and the assumption that spending will grow in line with GDP provides some flexibility, because it allows spending to increase as a proportion of GDP in some areas while being offset by declines in other areas. France and Switzerland have adopted broadly similar approaches, distinguishing age-related and non-age related expenditure: non-age related expenditure is projected to be constant in real terms or to be a fixed proportion of GDP.
- 6.4.2 In order for information on long-term fiscal sustainability to be relevant to users of GPFRs all material programs and transactions must be reflected. If this is not the case it is important that the material programs and transactions that are not included are clearly identified. This particularly applies to entitlement programs such as social security, aged pensions and medical insurance and also obligations related to public sector occupational pension plans. Omission of such programs and plans will understate expenditure projections and may have an impact on the relevance and reliability of information.

**Preliminary View Seven**

All material programs and transactions must be reflected in long-term fiscal sustainability projections.

**6.5 Current versus future policy**

- 6.5.1 IPSASs have adopted the general principle that transactions and elements are evaluated and determined within current legal frameworks. This is based on the view that the preparers of the financial statements should not predict governmental actions and that there should be no assumption that programs will discontinue, unless legislation to that effect has been enacted at the reporting date. Although this principle is sound for the GPFs, it is less clear that it is always appropriate for fiscal sustainability projections elsewhere in the GPFs and its application may even lead to imprudent and unreliable projections.
- 6.5.2 In the context of long-term fiscal sustainability there can be tensions where legal obligations conflict or where current programs have sunset provisions. This is more likely to be a problem in certain countries- in both Australia and New Zealand it seems that cases of legal conflict are unlikely or highly limited and where they exist are reflected in policy assumptions. An example of such tension is where a requirement that benefits are only paid out of a segregated fund that is projected to be exhausted may not be compatible with the projected volume of entitlements. Programs subject to sunset provisions may be replaced by similar programs, so adopting a strict “legal termination” principle may lead to the understatement of projected outflows. A principle that has been largely adopted for reasons of prudence in the financial statements might lead to imprudent projections for long-term fiscal sustainability!
- 6.5.3 The projections of participation in the labor market in the UK’s December 2006 Long-Term Public Finance Report actually reflected Government intentions to raise the age of entitlement for the state pension even though legislation to effect such a change had not been enacted at the date of publication. The Report acknowledged the difficulty of predicting with complete accuracy the impact of changed state pension dates on labor markets and therefore modeled three different variants of that effect. Notwithstanding such estimation complexity the approach of the UK shows that there may be cases where making projections on the basis of firmly announced Government proposals can provide more robust information than using a current legal position which is highly likely to be superseded.
- 6.5.4 The preliminary view of the IPSASB is that disclosures should be on the basis of current policy regardless of future events and deviation from this principle should be disclosed. Such disclosures would include any anticipation of a change in legal position or entitlement criteria that have not been enacted at the reporting date.

### **Preliminary View Eight**

Disclosures should be on the basis of current policy regardless of future events and deviation from this principle should be disclosed.

## **6.6 Bottom-up versus top-down approaches**

- 6.6.1 One approach to dealing with legal obligations is to distinguish between top-down and bottom-up approaches. Under top-down approaches assumptions are made that tax policies and fiscal rules do not change. Conversely, under bottom-up approaches, each material individual expenditure or revenue item representing existing government policy is projected and agreed. The United Kingdom has used both approaches in its public reporting on fiscal sustainability: top-down modeling approaches in its “Economic and Fiscal Strategy Report” and bottom-up approaches in its “Long-Term Fiscal Sustainability Report.” New Zealand has also adopted a top-down approach to complement its analysis. Usually high-level constraints (on debt or deficit) almost always lead to a “non-explosive” debt path when they are respected.
- 6.6.2 Under bottom-up approaches each material individual expenditure or revenue item is projected and aggregated. Bottom up approaches can involve both a full set of modeled assumptions and projections and a more simplified approach whereby only certain programs are modeled and spending on other programs is assumed to remain constant as a proportion of GDP over the time horizon (see above section 6.4). Arguably, bottom-up approaches are more penetrative tools for identifying points of fiscal pressure and are therefore more relevant to the users of GPFRs.
- 6.6.3 It is the view of the Board that projections should be based on bottom-up approaches, but that top down approaches may complement bottom-up approaches by illustrating the scale of the change that is necessary to achieve a sustainable path. It is important that GPFRs disclose whether projections are made using top-down or bottom-up approaches or a combination of the two.

### **Preliminary View Nine**

Projections on long-term fiscal sustainability should be on a bottom-up basis in which material individual expenditure or revenue items are projected and aggregated.

## **6.7 Impact of Legal Requirements and Policy Frameworks**

- 6.7.1 In some jurisdictions long-term fiscal sustainability reporting is governed by a legal or regulatory framework (see Section 3.1 which notes legal requirements for sustainability reporting). Such frameworks typically cover responsibilities for preparation and presentation as well as many of the areas noted above. They may reflect the requirements of supra-national bodies such as the European

Commission. An example of such a national-level framework from New Zealand is shown below in Exhibit Nine.

<b>Exhibit Nine</b>	
<b>Governing Legal Framework for Development and Reporting of Long-Term Fiscal Sustainability in New Zealand</b>	
Section 26N of the Public Finance Act 1989 (as amended in 2004) states: Statement on long-term fiscal position	
1)	Before the end of the second financial year after the commencement of this section and then at intervals not exceeding 4 years:- <ol style="list-style-type: none"><li>The Treasury must prepare a statement on the long-term fiscal position; and</li><li>The Minister must present each statement to the House of Representatives.</li></ol>
2)	The statement must:- <ol style="list-style-type: none"><li>Relate to a period of at least 40 consecutive financial years commencing with the financial year in which the statement is prepared; and</li><li>Be accompanied by:-<ol style="list-style-type: none"><li>a statement of responsibility signed by the Secretary stating that the Treasury has, in preparing the statement under subsection (1), used its best professional judgments about the risks and the outlook; and</li><li>a statement of all significant assumptions underlying any projections included in the statement under subsection (1)</li></ol></li></ol>

6.7.2 It is important for the users of GPFRs to be provided with details of the key aspects of governing legislation and regulation. However, there is a risk that such information will be over-detailed and undermine understandability. It may therefore be appropriate for references to the made in the GPFRs to other publicly available reports

6.7.3 It is also important that the users are provided with sufficient information on the underlying macro-economic policy and fiscal framework to allow them to interpret projected information. The challenge is to provide such information in a form that is understandable and relatively concise, but also verifiable. In broader reports on long-term fiscal sustainability the Australian, New Zealand and United Kingdom Governments have attempted to do this. Exhibit Ten gives examples of the approaches taken at the Commonwealth level in Australia and by the European Commission.

**Exhibit Ten**

**Disclosing information on fiscal frameworks: Australia and the European Commission**

*Australia*

In its most recent Intergenerational Report, published in 2007, the Australian Commonwealth Government highlighted the key aspects of its macro-economic policy framework for fiscal policy and the “Charter of Budget Honesty” and medium-term fiscal strategy that both flow from that framework. The Charter requires the Government to frame its fiscal strategy having regard to fiscal risks, including the maintenance of general government debt at prudent levels, the state of the economic cycle, the adequacy of national saving, the stability and integrity of the tax system and the financial effect of policy decisions on future generations. Key aspects of the medium-term fiscal strategy include the maintenance of a balanced budget over the course of the economic cycle, with supplementary objectives of not increasing the overall tax burden from its 1996-1997 level and improving the Australian government net worth position over the medium to long-term. The macro-economic framework also includes an inflation target for inflation, based on the Consumer Price Index (CPI), to be 2-3 per cent per year on average over the course of the economic cycle.

*European Commission*

European Commission’s assessment of debt sustainability is derived from the inter-temporal budget constraint. This constraint requires that the current total liabilities of the government, i.e. the current public debt and the discounted value of future expenditure, should be covered by the discounted value of future government revenue. If current policies ensure that the intertemporal budget constraint is respected, current policies are considered sustainable. Two sustainability gap indicators measure the size of required permanent budgetary adjustments that enables one of the following conditions to be met : (i) reaching a target of 60 % of GDP for the Maastricht debt in 2050 (the S1 indicator); and (ii) fulfilling the inter-temporal budget constraint over an infinite horizon (the S2 indicator). The European Commission’s (DGEFIN)’s publication, “Long-Term Sustainability of Public Finances” published in 2006 provided projections for the assessment of the budgetary implications of demographic change and the sustainability of public finances across the 25 EU Member States. Based on the projected expenditure trends, deficit and debt levels were projected over a 50 year horizon.

**Preliminary View Ten**

Details of key aspects of governing legislation and regulation, and the underlying macro-economic policy and fiscal framework should be disclosed.

## **7 SPECIFIC METHODOLOGY ISSUES**

### **7.1 Introduction**

This section looks at time horizons for long-term fiscal sustainability projections, the frequency of such projections, discount rates and the role of sensitivity analysis.

### **7.2 Time horizons for projections and their rationale**

- 7.2.1 Globally there is significant variation in the time horizons- the period to which projections relate-used by governments to develop projections and report on long-term fiscal sustainability. Exhibit Eleven highlights the position for the national level reports identified in section 3. Both Australia and New Zealand currently uses a 40 year reporting horizon, in Europe 2050 is commonly used as the horizon, while in the US most of the federal agencies involved in projections use a 75 year horizon. This is also the time horizon used for the information reported in the Financial Report of the US Government.
- 7.2.2 In some jurisdictions projections may be made over much longer time horizons than those publicly reported- both the UK and Sweden make projections to the end of this century, but only publicly report up to 2050. There is an obvious relationship between the robustness of assumptions and the time horizon — the further the time horizon is from the reporting date the more future events are captured, but the less robust and potentially less verifiable the assumptions become. Conversely, excessively short time horizons may increase the risk that events and modified trends just outside the reporting horizon, or beyond the economic cycle, might have a significant impact on reported information. In the US, in the Annual Trustee Reports for Social Security and Medicare, the latter risk has been partially addressed by adopting an infinite time horizon for certain projections.
- 7.2.3 It is important that, at a minimum, time horizons should be disclosed in the GPFRs as well as the reason for modifying time horizons and any published plans to modify those horizons. There may also be a case for specifying that there should be a minimum time horizon of say 20 years.

**Exhibit Eleven**  
**Overview of Time Horizons in Selected Long-Term Fiscal Sustainability Reports**

<b>Country</b>	<b>Title</b>	<b>Time Horizon</b>
Australia	Intergenerational Report	40
Denmark	A Sustainable Future	9
Germany	Rpt on Sustainability of Public Finance	45
Korea	Vision 2030	25
Netherlands	Aging and Sustainability of Dutch Public Finances	Until 2100 (with separate discussion to 2040)
New Zealand	LT Fiscal Position	40
Norway	2006 White Paper	55
Sweden	Sweden's Economy (annex to budget)	45
United Kingdom	LT Public Finance Report	30
USA: CBO	LT Budget Outlook	75
USA: GAO	LT Fiscal Outlook	75
US: OMB	LT Budget Outlook in Analytical Perspectives	75
USA: Financial Report of US Government	Statement of Social Insurance	75
European Union Countries	Public Finances – EMU	55
Switzerland	Long-term sustainability of public finance in Switzerland	40

Source: OECD

### Preliminary View Eleven

Time horizons for fiscal sustainability projections should be disclosed in the GPFRs as well as the reason for modifying time horizons and any published plans to modify those horizons.

## 7.3 Frequency of reporting

- 7.3.1 Publication of the GPFs is, at a minimum, on an annual cycle. As for time horizons the frequency of public reporting of long-term fiscal sustainability reporting varies. Australia is required by legislation to publish Intergenerational Reports at least every five years. The legislative requirement in New Zealand is for a statement on New Zealand's long-term fiscal position to be published every four years. Switzerland also reports publicly every four years. Other governments report annually and may make projections more frequently e.g., Sweden. Exhibit Twelve gives the position for the jurisdictions identified in Section 3 of the paper.

### Exhibit Twelve : Overview of Reporting Frequency in Certain Jurisdictions

Country	Title	Freq.
Australia	Intergenerational Report	Every 5 yrs
Denmark	A Sustainable Future	Every 5 yrs
Germany	Rpt on Sustainability of Public Finance	Every 3 yrs
Korea	Vision 2030	Ad Hoc
Netherlands	Aging and Sustainability of Dutch Public Finances	Ad Hoc
New Zealand	LT Fiscal Position	Every 4 yrs
Norway	2006 White Paper	Annually
Sweden	Sweden's Economy (annex to budget)	Annually
United Kingdom	LT Public Finance Report	Annually (not since 2006)
USA: CBO	LT Budget Outlook	Every 2 yrs
USA: GAO	LT Fiscal Outlook	3 times/yr
USA: OMB	LT Budget Outlook in Analytical Perspectives	Annually
USA: Financial Report of US Government	Statement of Social Insurance	Annually
European Union Countries	Public Finances – EMU	Annually
Switzerland	Long-term sustainability of public finance in Switzerland	Every 4 yrs

Source: OECD



- 7.3.2 Reporting frequencies for public reports outside the GPFRs are not within the scope of this Consultation Paper. However, where projections are made considerably earlier than the reporting date for the GPFRs, there is an issue whether they meet the qualitative characteristic of timeliness. One approach would be to require that the date at which key assumptions were made should be disclosed. A more rigorous approach would specify that long-term fiscal sustainability projections in the GPFRs should have been made within a pre-determined period before the reporting date for the GPFRs. For items subject to revaluation in GPFRs, intervals exceeding five years are not permitted. The Board's view is that this approach should be adopted for long-term fiscal sustainability information disclosed in GPFRs.

#### **Preliminary View Twelve**

Long-term fiscal sustainability information disclosed in GPFRs must have been prepared or updated within five years of the reporting date.

### **7.4 Discount rates**

- 7.4.1 Assumptions and projections may include discounting. The responses to the informal questionnaire indicated a variety of approaches to determining discount rates. These included growth – interest difference (number of EC member states), implicit interest rate paid on the public debt (Switzerland), and the average of 10 year and 90 day treasury interest rates at the US federal level.
- 7.4.2 Accounting standards generally require that when liabilities are to be settled more than one year after the reporting date they are discounted to present value using a specified discount rate. For example IPSAS 25, "Employee Benefits" requires that the discount rate should be a rate that reflects the time value of money and permits entities to make a judgment as to whether the time value of money is best approximated by market yields. A similar principle applies to cash-generating assets in determining the value-in-use of a cash-generating asset for impairment testing purposes the estimate of future cash flows that the entity expects to derive from the asset are to reflect the time value of money, represented by the current market risk-free rate of interest.
- 7.4.3 The issue is whether in order to enhance comparability consideration should be given to specifying that a discount rate should be used for discounting projections on long-term fiscal sustainability to present value in the GPFRs. The alternative would simply be to require disclosure of discount rates applied and their rationale. The Board believes that the latter approach would be acceptable at this stage given the developmental nature of this area and the range of professional groups involved.

### **Preliminary View Twelve**

Where discount rates used those rates should be disclosed, together with the rationale for their selection.

## **7.5 Sensitivity analysis**

- 7.5.1 Demographic and economic projections are inherently uncertain. Public reports on fiscal sustainability in many jurisdictions have therefore devoted considerable attention to the impact of variations to base case projections and assumptions about the drivers of economic growth. The most recent Australian IGR commented that “the projections in this report were built using assumptions to form a plausible central case. Significant uncertainties surround those assumptions and as a result, the projections in the report should not be treated as forecasts.”
- 7.5.2 In the context of the financial statements certain current Standards require the disclosure of specified sensitivity information. For example, IPSAS 25 mirrors IAS 19 by including a requirement for disclosure of the effects of a 1% increase and 1% decrease in the assumed medical cost trend rates on components of revenue and the accumulated post-employment benefit obligation for medical costs. IFRS 7, “Financial Instruments: Disclosure” requires a sensitivity analysis for each type of market risk to which an entity is exposed at the end of the reporting period and the methods and assumptions used in preparing the sensitivity analysis.
- 7.5.3 As for demographic and economic assumptions the issue is how the results of sensitivity analyses are best presented in the GPRSs. At this stage it is perhaps too early for the Board to be over-prescriptive in this area. However, a preliminary view is that the results of any sensitivity analysis should be disclosed.

### **Preliminary View Thirteen**

The results of sensitivity analyses should be disclosed.

## **8 ASSURANCE**

### **8.1 Introduction**

- 8.1.1 Currently there are few requirements that publicly reported long-term fiscal sustainability projections are subject to formal audit assurance. While there is a level of informal scrutiny by policy experts, academics and peer review in a number of jurisdictions, only in the United States are publicly reported projections subject to formal audit assurance.
- 8.1.2 In its “Code of Practice on Fiscal Sustainability” the IMF does not go as far as prescribing that fiscal sustainability projections should be subject to scrutiny by the national audit office (or equivalent). The Codes states that “Independent experts should be invited to assess fiscal forecasts, the macroeconomic forecasts on which they are based, and their underlying assumptions and that a national statistical body should be provided with the institutional independence to verify the quality of fiscal data.” A number of the responses to the informal questionnaire suggested that such processes are well established e.g., Eurostat and the Canadian Province of Ontario.
- 8.1.3 At the US federal level the Statement of Social Insurance (SOSI) has been a principal financial statement in the Financial Report of the US Government since 2006. The SOSI provides estimates of the financial condition of the most significant social insurance (contributory entitlement) programs of the federal government, principally most parts of Medicare and Social Security. The SOSI uses assumptions from Annual Trustee Reports and adopts a 75 year time horizon. The GAO disclaimed an opinion on the SOSI in 2006, but in 2007 the GAO gave an opinion that the SOSI “presents fairly, in all material respects, the financial condition of the US government’s social insurance programs.” Further information on the sensitivity of assumptions is contained in supplemental information and the MD & A, both of which are not subject to audit or assurance currently.
- 8.1.4 The absence of any form of assurance on long-term fiscal sustainability information reported in the GPFRs may give rise to reservations about the reliability of the information and the reasonableness of the assumptions underpinning the information. The initial key issue therefore is whether the lack of any form of audit assurance on long-term fiscal sustainability might reduce the confidence that a user can take in the reliability of the information reported to such an extent that it precludes the reporting of such information about long-term fiscal sustainability in either the notes to the financial statements or in other narrative commentary in the GPFRs.

### **8.2 ISAE 3000 assurance engagements other than audits or review of historical financial information**

- 8.2.1 If it is necessary for such information to be subject to audit the next issue is the level of assurance that should be provided. The International Auditing and

Assurance Standards Board (IAASB) is primarily associated with the development and maintenance of International Standards on Auditing that govern auditing requirements for the historical financial statements. However, the IAASB has developed a Standard to establish basic principles and essential procedures for, and to provide guidance on, the performance of assurance engagements other than audits or reviews of historical financial information: “International Standard on Assurance Engagements (ISAE) 3000: Assurance Engagements Other than Audits or Review of Historical Financial Information.”

- 8.2.2 The IAASB terms “reasonable assurance engagement” and “limited assurance engagement” are used to distinguish two types of assurance engagement. The objective of a reasonable assurance engagement is a reduction in assurance engagement risk to an acceptably low level in the circumstances of the engagement, as the basis for a positive form of expression of the auditor’s conclusion. In a limited assurance engagement the nature, timing and extent of evidence-gathering procedures is only sufficient for the auditor to obtain a meaningful level of assurance as the basis for a negative form of expression. ISAE 3000 also includes requirements and guidance on the use of an expert, which is likely to be relevant for projections informed by other professional groups (see also below Section 8.3).
- 8.2.3 The main difference between the two forms of assurance engagement is that a reasonable assurance engagement optimally results in a positive view that, in the auditor’s opinion, a particular position (or assertion) is fairly stated, whereas a limited assurance engagement can only express a view that nothing has come to the auditor’s attention that causes a belief that a position (or assertion) is not fairly stated. The form of opinion that an auditor is able to give on long-term fiscal sustainability information in specific financial statements will be a key determinant of whether it can be included in the GPFS or must instead be presented as part of broader GPFR information.

### **8.3 ISA 620, “using the work of an expert.”**

- 8.3.1 Long-term fiscal sustainability assessments are generally developed by economists, statisticians and policy specialists. The role of financial accountants is generally peripheral. IPSAS 17, “Property, Plant and Equipment” requires disclosure of whether an independent valuer was involved in revaluations. A similar disclosure requirement might be useful to the reader of GPFRs. An alternative view is that such information is superfluous, and that, in any case, defining specialisms may be too problematic.
- 8.3.2 The IAASB’s core suite of ISAs also includes ISA 620, “Using the Work of an Expert.” While this relates to the historical financial statements the guidance in it is likely to be relevant to auditors carrying out assurance engagements on long-term fiscal sustainability disclosures in GPFRs because of the involvement of experts in making those projections.

**Preliminary View Fourteen**

Formal assurance should be provided on the reasonableness of the assumptions underpinning long-term fiscal sustainability projections in GPFRS. Such assurance might be on a “negative” basis.

**EXTRACT FROM MINUTES OF ZURICH MEETING: OCTOBER 2008**

**LONG-TERM FISCAL SUSTAINABILITY**

**Discuss Issues**

The Chair of the Task Force and staff presented the results of the public consultation on the project brief, as well as the progress and preliminary conclusions of the Task Force, in particular data collection and an outline of the proposed Consultation Paper. The IPSASB noted the overall support for the project and its timing, and agreed that the project should proceed. The aim should be to produce a high level framework rather than detailed prescription. The form of the eventual output (in particular, whether guidance or a standard.) should emerge as work progresses. The Board was generally supportive of the Consultation Paper outline and the issues to be considered and the tentative conclusions drawn by the Task Force, except that it directed that:

1. Because all entities are subject to the objectives of financial reporting the project's scope should not be restricted to the national government level as the Task Force had proposed; and
2. The project should acknowledge the situation where a document meeting the definition of a general purpose financial report was published separately from the general purpose financial statement.

Members also directed that:

3. The Consultation Paper should position long-term fiscal sustainability information as accounting information drawing on the work of other professional groups;
4. The Consultation Paper should locate the provision of information on long-term fiscal sustainability as enhancing accountability;
5. A working definition of the term "long-term fiscal sustainability" is necessary;
6. Information on long-term fiscal sustainability in the general purpose financial reports should meet the qualitative characteristics of financial reporting; and
7. The Consultation Paper should propose that long-term fiscal sustainability projections include within their scope all material inflows and outflows and all material programs.

The Task Force had highlighted that, in many jurisdictions, projections of long-term fiscal sustainability are on a statistical accounting basis and the reporting boundary that of the general government sector. The IPSASB considered that the reporting of long-term fiscal projections should be firmly linked to the reporting entity as developed in the Conceptual Framework. There was a general distrust of reconciliations between information compiled under the statistical and accrual bases of accounting, although these had been a feature of IPSAS 22, "Disclosure of Information about the General Government Sector."

It was agreed that the Task Force should be broadened and that invitations should be extended to the Member from China and the OECD. It was also noted that the International Actuarial Association had requested representation on the Task Force. The Task Force Chair explained that the intention was not to examine different methodologies in depth. Dependent upon how the project progresses this request might be reconsidered.

It was agreed that a first draft of the consultation paper would be discussed at the May 2009 Board meeting with a view to approval of a final draft later in 2009.

# Long-Term Fiscal Sustainability Reporting



**International Federation  
of Accountants**



International Public Sector Accounting Standards Board  
International Federation of Accountants  
545 Fifth Avenue, 14th Floor  
New York, New York 10017 USA

This Project Brief was prepared by the International Public Sector Accounting Standards Board (IPSASB), an independent standard-setting body within the International Federation of Accountants (IFAC). The objective of the IPSASB is to serve the public interest by developing high quality accounting standards for use by public sector entities around the world in the preparation of general purpose financial statements. This will enhance the quality and transparency of public sector financial reporting and strengthen public confidence in public sector financial management.

This publication may be downloaded free-of-charge from the IFAC website: <http://www.ifac.org>. The approved text is published in the English language.

The mission of IFAC is to serve the public interest, strengthen the worldwide accountancy profession and contribute to the development of strong international economies by establishing and promoting adherence to high-quality professional standards, furthering the international convergence of such standards and speaking out on public interest issues where the profession's expertise is most relevant.

For further information, please email: [edcomments@ifac.org](mailto:edcomments@ifac.org)

Copyright © March 2008 by the International Federation of Accountants (IFAC). All rights reserved. Permission is granted to make copies of this work provided that such copies are for use in academic classrooms or for personal use and are not sold or disseminated and provided that each copy bears the following credit line: *"Copyright © March 2008 by the International Federation of Accountants (IFAC). All rights reserved. Used with permission of IFAC. Contact [permissions@ifac.org](mailto:permissions@ifac.org) for permission to reproduce, store or transmit this document."* Otherwise, written permission from IFAC is required to reproduce, store or transmit, or to make other similar uses of, this document, except as permitted by law. Contact [permissions@ifac.org](mailto:permissions@ifac.org).

ISBN: 978-1-934779-32-3

## **INTERNATIONAL PUBLIC SECTOR ACCOUNTING STANDARDS BOARD**

### **LONG-TERM FISCAL SUSTAINABILITY REPORTING**

#### **PROJECT BRIEF AND OUTLINE**

**1. Subject**

Reporting on the long-term fiscal sustainability of governmental programs and finances.

**2. Project Rationale and Objectives**

During the development of its project on social benefits the IPSASB has formed a view that the financial statements of an entity cannot satisfy all the needs of users in assessing the future viability of programs providing social benefits. The IPSASB holds this view regardless of the approach that is taken to the point(s) at which a present obligation(s) occur(s) (which may vary for different types of social benefits), the extent of those present obligations and the amount of the resultant liabilities. Information presented in the financial statements may need to be complemented by the presentation of other information about the long-term fiscal sustainability of those programs, including their financing.

**a) Objectives to be achieved**

The ultimate objective of the project is to produce a framework for the reporting of information related to the long-term fiscal sustainability of governmental programs and finances.

The intermediate objective is to produce a Consultation Paper. The Consultation Paper will highlight and analyze existing approaches in jurisdictions, where long-term fiscal sustainability reporting is a feature of governmental financial management, as well as the approaches of supra-national bodies (such as the European Commission and the International Monetary Fund) in making comparative fiscal projections.

The project is not directly related to the accrual basis of financial reporting and the traditional financial statements and is not linked to an existing International Financial Reporting Standard. It is therefore not feasible or appropriate to provide definitive final outputs at the initiation stage. Dependent upon decisions to be made following analysis of submissions on the Consultation Paper, a Standard (providing requirements) and/or Guidance will be developed.

**b) Link to IFAC/IPSASB Strategic Plans**

*Link to IFAC Strategic Plan*

Issuing requirements and guidance on public sector financial reporting issues is a primary role of the IPSASB. The development of such requirements and guidance supports IFAC's mission of serving the public interest by contributing to its aim of becoming the international standard setter for governmental financial reporting.

LONG-TERM FISCAL SUSTAINABILITY REPORTING  
PROJECT BRIEF AND OUTLINE

*Link to IPSASB Strategy*

This is an area which has become increasingly topical and relevant to the enhancement of public sector accountability. The absence of public sector specific guidance on fiscal sustainability reporting is a “gap” in the IPSASB literature that has become apparent during the IPSASB’s project on social benefits (see above). It is consistent with IPSASB’s strategic theme of developing requirements and guidance on public sector specific issues.

**3. Outline of the Project**

**a) Project Scope**

The scope of the project is reporting on the long-term fiscal sustainability of governmental programs, including their financing. The range of entities and levels of government to be within the scope of finalized outputs will be determined following analysis of submissions on a Consultation Paper.

Certain other issues relating to scope will be considered in the course of the project. These include whether:

- All governmental programs should be within the scope; or
- Whether the scope should be restricted to certain programs, for example, contributory programs or social insurance programs.

This project only addresses long-term fiscal sustainability reporting and not environmental sustainability. However, there may be linkages between environmental sustainability and long-term fiscal sustainability, because assumptions about environmental sustainability may impact upon financial assumptions such as changes in Gross Domestic Product (GDP) and demographic assumptions such as population growth, emigration and immigration. The project will acknowledge such potential linkages.

**b) Major Problems and Key Issues that Should be Addressed**

*(i) Definitions*

There is no globally accepted definition of fiscal sustainability or long term-fiscal sustainability, although a number of governments have developed formal or implied definitions of these terms or related terms. In some cases these definitions are located in the context of medium-term fiscal planning or budgetary frameworks, such as when long-term fiscal sustainability is linked to specific targets such as a pre-determined net debt/Gross Domestic Product (GDP) ratio or net debt/GDP per capita ratio. In these cases overall governmental spending is said to be fiscally sustainable if it is contained within these pre-determined and publicly communicated targets over a certain period.

At a very high level, long-term fiscal sustainability reporting involves an assessment of the extent to which service delivery can be maintained at existing levels, and the extent to which governmental obligations to citizens under

LONG-TERM FISCAL SUSTAINABILITY REPORTING  
PROJECT BRIEF AND OUTLINE

existing legal frameworks, can be met from predicted inflows over a pre-determined future period. The analysis of long-term fiscal sustainability therefore takes account of both current and future beneficiaries, regardless of whether governments have present obligations to them, determined in accordance with accrual accounting principles at the reporting date.

Long-term fiscal sustainability is sometimes coupled with the broad concept of inter-generational equity, which evaluates the extent to which future generations of taxpayers will be affected by the fiscal consequences of current policies for the delivery of goods and services.

As noted above, the reporting of long-term fiscal sustainability is also commonly linked to frameworks involving targets and benchmarks involving such indicators as:

- Net Debt;
- Net Debt/GDP;
- Fiscal Gap;and
- Fiscal Imbalance.

The project will therefore consider relevant terminology, the adequacy of existing definitions, and the extent to which those definitions need to be supplemented. It will also consider whether a Standard and/or guidance should specify or recommend that a minimum set of indicators should be reported.

(ii) *Status and Nature of Outputs*

The project will consider whether the IPSASB should be developing requirements and if so, whether such requirements should specify the information to be reported if an entity elects to report information about long-term fiscal sustainability or should require all entities within the scope of those requirements to provide specified information about long-term fiscal sustainability. This will involve determining whether all entities should be required to report on long-term fiscal sustainability as a regular feature of their general purpose reporting or whether the scope of the requirements should be restricted by, for example:

- Only applying to entities which elect to make their fiscal sustainability reports publicly available; or
- Only applying to entities that mention or discuss the fiscal sustainability report in the general purpose financial statements?

The project will also examine whether any requirements should apply to all entities that apply IPSASs or only to entities that apply accrual basis IPSASs. The rationale for not applying requirements to jurisdictions and entities on the cash-basis may be that to do so would be onerous.

LONG-TERM FISCAL SUSTAINABILITY REPORTING  
PROJECT BRIEF AND OUTLINE

(iii) *Reporting Entity for Long-Term Fiscal Sustainability Reporting*

The main issue is whether the requirements and guidance are to apply to all public sector entities; only entities at the national level, to the national whole-of-government level, to all levels of government combined, or to another level.

In this context, the project will consider the view that requiring individual entities to prepare and report information on the fiscal sustainability of operations is onerous and not proportionate to the benefit that users will derive from the information. It will also consider the view that only by developing requirements for all levels of government combined will user needs for information about the overall long-term fiscal sustainability of the public sector be satisfied – this particularly applies to nations with federalized structures, where the service delivery of significant public sector programs is the responsibility of entities at sub-national levels of government and where sub-national level entities have wide tax-raising powers.

National statistical accounting is used as the basis for long-term fiscal sustainability reporting in a number of jurisdictions. The project will therefore consider statistical accounting approaches and in particular whether the general government sector (GGS) may provide the appropriate reporting boundary for fiscal sustainability reporting. At a national level, the GGS encompasses all levels of government, as well as social security funds and non-market non-profit entities controlled by government units. At a jurisdictional level within a nation (for example, for a state government), the GGS is identified for that jurisdiction, and, in that instance, would have regard to whether control relationships exist. Under statistical accounting the public sector also comprises public financial corporations and public non-financial corporations. In contrast to the basis generally applied under accrual IPSAS, the GGS does not consolidate controlled entities outside the GGS sector and does not therefore eliminate balances and transactions between entities in the GGS and other sectors. It treats controlling interests in entities outside GGS as investments.

(iv) *Time Horizons*

In jurisdictions that make long-term fiscal sustainability reports publicly available there is variation in the time horizons adopted—the period over which projections are made. There is a relationship between the robustness of assumptions and the time horizon — the further the time horizon is from the reporting date the less robust and potentially less verifiable the assumptions become. Conversely, excessively short time horizons may increase the risk that events and modified trends just outside the reporting horizon might have a significant impact on reported information. The project will explore various time horizons and consider how prescriptive any reporting requirements should be.

LONG-TERM FISCAL SUSTAINABILITY REPORTING  
PROJECT BRIEF AND OUTLINE

(v) *Regularity of Reporting*

Publication of the general purpose financial statements is, at a minimum, on an annual cycle. The project will examine whether the same frequency of reporting should be required or recommended for long-term fiscal sustainability reporting. Factors to be considered include the costs of reporting and the view that material policy assumptions, demographic assumptions and economic assumptions are often unlikely to change sufficiently rapidly within a year to justify the additional costs of annual reporting. Conversely, there is a view that material changes in policy assumptions can be quite common, especially for pensions and social security programs. This militates towards more regular reporting or at least more regular updating.

The project will consider whether there should be minimum intervals between reporting or whether any requirements should be more flexible, for example, requiring reporting intervals to be disclosed with any changes to those intervals since previous reports were produced.

(vi) *Assumptions and Sensitivity of Assumptions*

Fiscal sustainability reporting entails a range of assumptions. These assumptions include:

- Policy assumptions;
- Demographic assumptions; and
- Economic assumptions.

The term *policy assumptions* refers to the basis on which future levels of service delivery will be determined and the approach to taxation levels, including fiscal drag (see also the section on tensions with Current Legal Frameworks below).

*Demographic assumptions* include mortality and fertility projections, estimates of immigration and emigration and participation levels in the workforce and education.

*Economic assumptions* include productivity changes, unemployment rates and participation rates in education and the workforce, and real and nominal economic growth rates.

The project will consider whether the IPSASB should develop for the reporting of these assumptions used for long-term fiscal sustainability analysis.. Assumptions also include discount rates for projection models.

(vii) *Tensions with Current Legal Frameworks*

As a general principle IPSASs have adopted the tenet that transactions and elements are evaluated and determined within current legal frameworks. This is largely based on the view that the preparers of the financial statements should not predict governmental actions and that there should be no assumption that programs will discontinue unless legislation to that effect has been enacted at

LONG-TERM FISCAL SUSTAINABILITY REPORTING  
PROJECT BRIEF AND OUTLINE

the reporting date. The project will consider whether such a principle is relevant for long-term fiscal sustainability reporting and whether a complementary approach for taxation inflows should be adopted, so that inflows should be determined using current legal requirements (including taxation rates) unless changes have been effected at the reporting date.

The project will consider approaches for reporting information on projections under current frameworks where different legal obligations conflict or where projections are clearly unreasonable. Examples might be where:

- There is a legal requirement for a balanced budget and that requirement cannot be met under existing expenditure projections unless expenditure is reduced, benefits changed, contributions and taxation raised or through extensive disposals of assets: should balanced budget requirements take precedence over entitlements determined under existing legal frameworks or predicted growth trends?; and/or
- Where a program is operated on a segregated fund basis and benefits cannot be paid once the fund's earmarked assets have been exhausted. If exhaustion of the fund is projected within the time horizon of the reporting framework; should that exhaustion be reflected in projections of outflows of benefits?

In many instances legal obligations cannot be discharged unless annual appropriations are in place; limiting projections to appropriations would result in very short time horizons. The relationship between ongoing spending commitments and appropriation mechanisms will therefore be examined.

*(viii) Approach to Discretionary Programs*

The project will explore possible approaches to reporting information on discretionary programs. Discretionary programs are programs that the government is not required to maintain under current legal requirements beyond a clearly specified date. Discretionary programs may be contrasted with mandatory programs that involve entitlements to individuals or households. Authorizations for discretionary programs may be renewed on an annual basis.

The main issue is whether expenditure projections should extend beyond the limit of current authorizations and, if so, how expenditure projections are to be projected for such programs. A related issue is that discretionary programs are likely to expire before the time horizons used for reporting. The project will therefore consider whether an assumption should be made that such programs will be renewed on expiry.

*(ix) Financing*

The project will consider the approaches to be taken to reporting information on estimates of financial resources (taxes and other revenue) available to fund the programs in question.



LONG-TERM FISCAL SUSTAINABILITY REPORTING  
PROJECT BRIEF AND OUTLINE

(x) *Assurance and Verifiability*

The project will explore whether information reported on long-term fiscal sustainability can and should be assured and, if so, the possible levels of that assurance. It will explore the balance of responsibilities between preparers of fiscal sustainability reports in ensuring the verifiability of assumptions and auditors in providing any appropriate level of assurance.

4. **Implications for Specific Groups**

a) International Accounting Standards Board (IASB)

There is an indirect relationship with the IASB's Conceptual Framework project, although this is primarily addressed through the IPSASB's own Conceptual Framework project. The IASB also has a project on Management Commentary and issued a Discussion Paper in late 2005. In December 2007, the IASB decided to add a project on Management Commentary to its active agenda. While this project will primarily have an influence on the planned IPSASB project on Management's Discussion and Analysis (see below) it will be relevant indirectly to this project. In its Discussion Paper the authors of the IASB Discussion Paper proposed that, in addition to consideration of the key aspects of performance in the period covered by the financial statements, the Management Commentary should take a prospective view in considering the main trends and factors likely to affect an entity's future development, performance and position.

b) Relationship to other IPSASB projects in process or planned

There are relationships with a number of current or planned IPSASB projects:

(i) *Social Benefits*

The IPSASB has an ongoing project on social benefits. Key outputs from that project have been issued with this project brief. The IPSASB's deliberations on social benefits have been catalysts in the decision to initiate this project. The approach in ED 34, "Social Benefits: Disclosure of Cash Transfers to Individuals or Households" is intended as a bridge between accrual approaches and the development of approaches to long-term fiscal sustainability reporting.

(ii) *Conceptual Framework*

A project to develop a public sector conceptual framework is underway. This is led by the IPSASB and carried out in collaboration with certain national standard setters. The components of that project dealing with the objectives of financial reporting, the qualitative characteristics of financial information, the scope of financial reporting, the reporting entity, and the elements of financial statements are especially relevant to this proposed project.



LONG-TERM FISCAL SUSTAINABILITY REPORTING  
PROJECT BRIEF AND OUTLINE

(iii) *Management's Discussion and Analysis (Management Commentary/Narrative Reporting)*

The IPSASB plans to initiate a project on Management's Discussion and Analysis (MD&A), also known as Management Commentary, narrative reporting or operating and financial review) in the first quarter of 2008. In some jurisdictions the MD&A or equivalent is the main means by which expected future trends and changing conditions to the operating environment and their potential impact on the reporting entity are highlighted. Both this project and the separate MD&A project will consider the extent to which the MD&A should include details, and indicators, of long-term fiscal sustainability.

c) Other projects

Reports on the long-term fiscal sustainability of governmental programs are made publicly available in a number of jurisdictions and supra-national bodies also make comparative analyses of the financial condition of nation states available: For example, the European Commission assesses comprehensively the sustainability of the public finances of each Member State of the European Union ever 4 years. This assessment is based on a common methodological framework to account for the budgetary risks of population ageing. It is partially updated every year when countries submit their medium-term budgetary plans ("stability and convergence programs").

Globally a number of public sector standard setters are considering or developing requirements for the reporting of aspects of long-term fiscal sustainability in the public sector:

- At the federal level, the Financial Report of the United States Government includes a Statement of Social Insurance (SOSI), which adopts a 75-year time horizon for specified programs;
- Also at the federal level the US Financial Accounting Standards Advisory Board (FASAB) has a Standard, SFFAS 17, "Accounting for Social Insurance (Revised 2006)", which provides requirements for the SOSI. FASAB is also developing a Standard, providing requirements for broader fiscal sustainability reporting;
- At the state, local and municipal level, the US Governmental Accounting Standards Board has a project on economic condition;
- The Canadian Public Sector Accounting Board has a project on indicators of financial condition, which is developing guidance in the form of a statement of recommended practice; and
- Other standard setters have projects considering prospective information and narrative reporting.

LONG-TERM FISCAL SUSTAINABILITY REPORTING  
PROJECT BRIEF AND OUTLINE

## 5. Development Process, Project Timetable and Project Output

### a) Development process

The development of outputs will be subject to the IPSASB's formal due process. The issuance of documents for public comment will be subject to the usual IPSASB voting rules. As the project progresses, regular assessments will be made to confirm the nature of the outputs and the proposed path in the project timetable. .

The initial output will be a Consultation Paper. Following analysis of submissions on the Consultation Paper a decision will be made on whether to develop an Exposure Draft of a Standard and/or Guidance. Any Exposure Draft will also be subject to formal due process, including a consultation period of at least four months.

### Project timetable

<b>2007</b>	
November	Project approved
<b>2008</b>	
February-March	Task Force selected and confirmed
February-March	Project brief finalized
March	Update to Meeting of IPSASB
March-September	Task Force develops Consultation Paper under oversight of Task Force
June	Update to Meeting of IPSASB
October	IPSASB reviews first draft of Consultation Paper
<b>2009</b>	
February	IPSASB reviews second draft of Consultation Paper and approves for publication
March	Publication of Consultation Paper
March-July	Exposure period for Consultation Paper
August-September	Staff analysis of submissions on Consultation Paper
September	Briefing for staff of International Auditing and Assurance Standards Board (IAASB) on assurance implications.
October	IPSASB considers analysis of submissions on Consultation Paper and adopts approach for final stage of project
<b>2010</b>	
February	IPSASB reviews first draft of Exposure Draft (ED) of an IPSAS and/or guidance
June	IPSASB approves ED and/or guidance
July	ED and/or guidance issued
July-November	Exposure period for ED and/or guidance
<b>2011</b>	
February	IPSASB considers analysis of submissions to ED/Guidance and provides directions for finalization of final stage outputs
June	IPSASB approves IPSAS and/or Guidance

LONG-TERM FISCAL SUSTAINABILITY REPORTING  
PROJECT BRIEF AND OUTLINE

(b) Project output

The initial output will be a Consultation Paper. As indicated above definitive final outputs will be determined following analysis of submissions on the Consultation Paper. Further final outputs may be a Standard and/or detailed Guidance.

**6. Resources Required**

a) Task Force

A task force of 8-10 (including Chair) is to be established – a task force of this size is necessary to reflect a broad cross section of IPSASB constituents and to enable a range of points of view, technical expertise and discussion for the development of this project.

Selection of task force members will be made by the Technical Director and IPSASB Chair.

Communication will be primarily carried out electronically. The majority of meetings are expected to be by conference call. It is expected that there will be at least two face-to-face meetings.

It is the current intention that all project materials will be developed by IPSASB staff.

b) Staff

It is envisaged that 0.75 Full Time Equivalent (FTE) resource (not dedicated) will be required to resource the project.

**7. Important Sources of Information that Address the Matter being Proposed**

- A number of governments and supra-national bodies publish reports on the long-term fiscal sustainability of programs;
- A number of standard setters have developed, are developing or refining existing requirements and guidance for long-term fiscal sustainability reporting or financial condition;
- A number of standard setters are developing approaches to public sector narrative reporting;
- Some standard setters have developed, or are in the process of initiating development, of requirements for prospective reporting; and
- Some auditors are reporting on financial condition.

**8. Factors that might add to complexity or length**

The project addresses a large subject in an area which is outside the general-purpose financial statements. This is a new topic for the IPSASB and there are few current pronouncements and therefore limited relevant experience to draw on. Decisions made following analysis of the initial consultation paper will also affect the length of the project, in particular whether it is decided to develop both requirements and guidance.