

Meeting: International Public Sector Accounting
Standards Board

Meeting Location: Abu Dhabi, UAE

Meeting Date: March 11–14, 2013

Agenda Item 4

For:

☒ Approval

☒ Discussion

☐ Information

Reporting on the Long-Term Sustainability of an Entity's Finances

Objective(s) of Agenda Item

1. The objectives of this session are:
 - (a) To **obtain directions** from the IPSASB on the issue of fiscal drag; and
 - (b) To **approve** the draft RPG 1, *Reporting on the Long-Term Sustainability of an Entity's Finances*.

Material(s) Presented

Agenda Item 4.1	Issues Paper
Agenda Item 4.2	Draft RPG 1, <i>Reporting on the Long-Term Sustainability of an Entity's Finances</i> Marked-Up Version
Agenda Item 4.3	Draft RPG 1, <i>Reporting on the Long-Term Sustainability of an Entity's Finances</i> Clean Version—Core text and Basis for Conclusions only

Action(s) Requested

2. The IPSASB is asked to consider the “Matters for Consideration” in Agenda Paper 4.1 and undertake a page-by-page review of the draft RPG with a view to approving it.

Issues Relating to

Draft RPG 1, *Reporting on the Long-Term Sustainability of an Entity's Finances*

Objectives of this Session

1. The objectives of this session are:
 - (a) To **obtain directions** from the IPSASB on the issue of fiscal drag; and
 - (b) To **approve** the draft RPG 1, *Reporting on the Long-Term Sustainability of an Entity's Finances*.
2. A marked-up version of the draft RPG is in Agenda Paper 4.2 and the clean version is in Agenda Paper 4.3.

Structure of this Issues Paper

3. The paper is divided into the following sections:
 - (a) Definition of “projection” and replacement of the term “supportable assumptions”;
 - (b) How the draft RPG will deal with fiscal drag;
 - (c) Names and definitions of the dimensions of long-term fiscal sustainability;
 - (d) Review of draft RPG; and
 - (e) Approval of draft RPG.

Definition of “Projection” and Replacement of the Term “Supportable Assumptions”

4. The definition of projection considered at the December 2012 meeting is as follows:

A **projection** is prospective financial information prepared on the basis of supportable assumptions about the entity's policies, future economic and other conditions.
5. The IPSASB directed staff to consider whether a clearer term could be used instead of “supportable assumptions.” Staff proposes that this term could be replaced with “current policy assumptions.” This has the advantage that the term “current” is used.
6. The proposed definition of a projection is as follows:

A **projection** is prospective financial information prepared on the basis of the entity's current policy ~~supportable assumptions about the entity's policies~~, and future economic and other conditions.
7. The meaning of “current policy assumptions” is then explained in the section on “Current and Future Policy Assumptions.” Proposed changes to the wording of that section are explained below.

Matter(s) for Consideration

1. The IPSASB is asked to confirm that the proposed definition of projection, set out in paragraph 6,

is appropriate?

Fiscal Drag

8. Paragraphs 40–42 of the draft RPG presented at the December 2012 meeting explain that an entity can depart from using current policy to calculate its projections (a) where there is a conflict between current policy and legal obligations and (b) where a policy has “sunset provisions.” At that meeting, staff proposed an additional departure from current policy where a policy has been changed in a consistent direction over time. The intention of this proposed departure from current policy was to address a concern raised by a respondent to ED 46 that the concept of current policy should be broader than that proposed in the ED to deal with issues such as fiscal drag.
9. Fiscal drag refers to the phenomenon that income tax inflows grow faster than the income it is levied on because, as an individual’s income grows, an increasing proportion of it is taxed at a higher rate. Fiscal drag occurs if the rates and thresholds for the taxation of individuals are not adjusted over time. Not addressing fiscal drag has the potential for an entity to overstate revenue inflows from taxation which would not reflect an entity’s long-term fiscal sustainability position.
10. The IPSASB appeared to express contradictory views over the proposal to include an additional departure from current policy where a policy has been changed in a consistent direction over time, as follows:
 - (a) The additional departure from current policy where a policy has been changed in a consistent direction over time should be **deleted** because it would considerably widen the instances where an entity could depart from current policy and this would lead to projections being calculated using assumptions that are not supportable thereby disguising the entity’s long-term fiscal position.
 - (b) The additional departure from current policy where a policy has been changed in a consistent direction over time should be **kept** because it is essential that the draft RPG explicitly addresses the issue of fiscal drag and other instances where a departure from current policy is necessary. It was also noted that addressing only the issue of fiscal gap would not address other situations where policy has been changed in a consistent direction over time.
 - (c) The additional departure from current policy where a policy has been changed in a consistent direction over time should be **moved** to become a discussion in the Basis for Conclusions together with the example of fiscal drag. Staff considers that it is not clear whether this suggestion would implicitly permit projections to be adjusted for fiscal drag or whether projections can only be adjusted for the situations listed in the core text and therefore adjustment for fiscal drag is not permitted.
11. Consequently, this section sets out options as to how the issue of fiscal drag could be addressed and the related proposed amendments to the sections on “Approach to Revenue Inflows” and “Current and Future Policy Assumptions” in the draft RPG.
12. The relevant sections of the draft RPG presented at the December 2012 meeting are set out in Table 1.

Table 1: "Current and Future Policy" and "Approach to Revenue Inflows" Sections of Draft RPG
(December 2012 Clean Version)

Current and Future Policy

40. Where flows for particular programs and activities are individually modeled, the policy assumption should be based on current policy. That policy should be held constant through the entire projection period. However, there may be instances where a departure from current policy may be appropriate, as follows:
- (a) Where there is a conflict between current policy and legal obligations;
 - (b) Where a policy has "sunset provisions"; or
 - (c) Where a policy has been changed in a consistent direction over time.
- 40A. An example of a conflict between a policy and legal obligations is a social security program which has legal provisions that make it unlawful to make payments once an earmarked fund is exhausted, although entitlements of beneficiaries will continue after the exhaustion of that fund. Assuming that the fund will not meet obligations once it is exhausted might reflect a strict legal position, but an entity may need to assess whether the presentation of projections on such a basis underestimates projected outflows and therefore the extent of the fiscal challenge facing the social security program. In this situation an entity may calculate its projections based on current policy despite legal restrictions.
41. A policy may have sunset provisions whereby it terminates after a specific period. In many cases there may be a strong probability that such programs will be replaced by similar programs. Adopting a strict legal termination principle could underestimate projected outflows, and therefore impair the usefulness of the information.
- 41A. An example of a policy that has been changed in a consistent direction over time may be the income threshold for the taxation of individuals (this is sometimes called "fiscal drag"). Assuming that the threshold remains at the same monetary amount might reflect the strict legal position, but if there is a strong probability that the threshold will be raised, an entity may need to assess whether the presentation of projections on a fixed threshold basis would overestimate projected inflows, thereby impairing the usefulness of information.
42. For flows that are not individually projected, the distinction between current and future policy is unlikely to be critical to the projections and it may be sufficient to disclose general assumptions.
- 42A. Policy assumptions may also be affected by legal changes that have been enacted before the reporting date which have a specific implementation date within the time horizon of the projections. In these circumstances, assuming a current policy remains in force for the entire projection period will not be appropriate.

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Approach to Revenue Inflows

43. Significant sources of taxation and other revenue flows, such as inter-governmental transfers, may be projected to grow in line with gross domestic product (GDP) or an inflation index or may be individually modeled based on current policy.

Approach to Revenue Inflows

13. Staff considers that the "Approach to Revenue Inflows" section of the draft RPG appears to indirectly address fiscal drag because it explains that significant sources of revenue from taxation and other sources may be projected to grow in line with GDP or an inflation index or may be individually modeled based on current policy. Therefore, staff assumes that if an entity does not individually model taxation, the issue of fiscal drag can be addressed. However, if an entity individually models particular tax sources then it would not be able to address the issue of fiscal drag because that departure from current policy is scoped out of the draft RPG. Paragraph 43 (in the December 2012 version of the draft RPG, now paragraph 46 in March 2013 version of draft RPG) is not clear as to whether an entity can individually model a revenue inflow based on current policy for the early years of the time horizon and use an index for the later years of the time horizon.
14. Staff considers that this paragraph could be clarified as follows:

Significant revenue inflows from ~~sources of~~ taxation and other ~~sources revenue flows~~, such as inter-governmental transfers, may be individually modeled based on current policy assumptions. Significant revenue inflows from taxation and other sources that are not modeled individually are projected to grow (or diminish) in line with gross domestic product (GDP) or another index such as the inflation index ~~or may be individually modeled based on current policy~~.

Matter(s) for Consideration

2. The IPSASB is asked to confirm that the proposed amendments to paragraph 43 of the draft RPG, set out in paragraph 14, are appropriate?

Current and Future Policy

15. Staff considers that the section on "Current and Future Policy" is not clear as to what current policy means. For example, does current policy mean only current legislation or regulation, with no departures except for specific circumstances outlined in the draft RPG? This could be addressed by clarifying what is meant by "current policy" by using the term "current policy assumptions" (from the revised definition of projection).
16. The contradictory views expressed at the December 2012 meeting are also reflected in the views of the Task Force. Therefore, staff has outlined a number of options as to the meaning of "current policy assumptions" below and has also included options for retaining the proposal from the December 2012 meeting or retaining the view in ED 46.

Option A: Current Legislation or Regulation with Specific Exceptions

17. The term "current policy assumptions" means current legislation or regulation with departures from current legislation or regulation being limited to the specific exceptions listed in the draft RPG: (a) where changes to current legislation or regulation have been enacted before the reporting date which have a specific implementation date within the time horizon of the projections, (b) where the provisions in current legislation or regulation are internally inconsistent (formerly "a conflict in legal obligations") and (c) where current legislation or regulation has "sunset provisions."
18. The Basis for Conclusions would explain that the view of the IPSASB is that current policy is assumed to continue (except for the three departures listed in the draft RPG) for inflows or outflows

that are individually projected. An entity can address the issue of fiscal drag by not individually modeling income tax inflows. The Basis for Conclusions would also explain that the IPSASB considered permitting a departure from current policy where a policy has been changed in a consistent direction over time to address the issue of fiscal drag. However, the IPSASB concluded that this exception to current policy would enable entities to have wide discretion over the number of departures from current policy. Thereby, potentially enabling the calculation of projections to be subject to political interference. This could result in the projections presenting a misleading view of the entity's long-term fiscal sustainability.

19. A member of the Task Force commented that an entity can address fiscal drag under Option A by presenting a baseline projection using current legislation or regulation and also presenting alternative projections which show what policy proposals, such as those addressing fiscal drag, would do to the projections if they were enacted.

Option B: Current Legislation or Regulation with Departures where Appropriate

20. The term "current policy assumptions" means current legislation or regulation with departures where appropriate.
21. Option B differs from Option A in that departures from current policy are not limited to the specific exceptions listed in the draft RPG and instead they are examples of where a departure from current policy may be appropriate. The examples would be the same as those departures from current policy listed in Option A. Therefore, this option gives preparers more discretion over when to depart from current policy.
22. The Basis for Conclusions would explain that the issue of fiscal drag is not explicitly addressed in the core text of the draft RPG because it is included in "with departures where appropriate." This approach would mean that where an entity considers that current policy will be changed in a specific direction, such as the increase in the thresholds for the application of progressive taxation, it can adjust its projections accordingly.
23. This option has the drawback that preparers have discretion over when to depart from current policy and consequently, this could allow the assumptions to be subject to political interference and result in an entity presenting projections that disguise the true nature of the entity's long-term fiscal sustainability.

Option C: Current Policy includes Situations where Policy has changed in a Consistent Direction

24. Option C keeps the proposal from the December 2012 meeting which extended the proposals in ED 46 to include an exception to current policy where policy has been changed in a consistent direction over time and illustrate this using the example of fiscal gap.
25. A member of the Task Force supports this option. He considers that this issue is fundamental and needs to be addressed in the core text of the draft RPG. This member considers that the draft RPG should explicitly allow a departure from current policy where there has been a history of changing current policy in a consistent direction.
26. This option has the drawback that it would considerably widen the instances where an entity could depart from current policy and this would lead to projections being calculated using assumptions that are not supportable, thereby disguising the entity's long-term fiscal position.

Option D: ED 46 Proposals—Current Policy Held Constant through-out Projection Period

27. Option D keeps the proposals in ED 46—for programs and activities that are individually modeled, current policy is held constant through-out the entire projection period. Two examples are given where judgment is required to determine whether or not a strict legal position is used. They are: (a) there is a conflict in legal obligations and (b) if current programs have “sunset provisions.”
28. Retaining the approach in ED 46 would not address the concerns expressed by a respondent to ED 46 who suggested that the concept of current policy should be broader than that proposed in the ED to deal with issues such as fiscal drag.
29. Staff considers that if the proposals in ED 46 are reflected in the draft RPG, some amendment would be necessary to clarify whether the examples given are the only circumstances in which an entity could depart from current policy. The Basis for Conclusions would explain that an entity can address the issue of fiscal drag by not individually modeling income tax inflows.
30. Staff asks the IPSASB for direction on this issue.

Matter(s) for Consideration

3. The IPSASB is asked to indicate which option they support:
 - (a) Option A: Current Legislation or Regulation with Specific Exceptions.
 - (b) Option B: Current Legislation or Regulation with Departures where Appropriate.
 - (c) Option C: Current Policy includes Situations where Policy has changed in a Consistent Direction.
 - (d) Option D: ED 46 Proposals—Current Policy Held Constant through-out Projection Period.

Names and Definitions of the Dimensions of Long-Term Fiscal Sustainability

31. At its December 2012 meeting, the IPSASB directed staff to:
 - (a) Change the name of the vulnerability dimension to “revenue vulnerability” and consider developing a new term for fiscal capacity.
 - (b) Restructure the definition of vulnerability so that an entity’s dependency on funding sources outside its control is first.
 - (c) Amend the definition of fiscal capacity to include reference to the raising of debt.
 - (d) Include an explanation of any changes in terminology and potential implications in the Basis for Conclusions.

Revenue Vulnerability Dimension

32. The definition of revenue vulnerability from the December 2012 meeting, amended so that the characteristic of an entity’s dependency on funding sources outside its control is first, is as follows:

Revenue vulnerability is (a) the entity’s dependency upon funding sources outside its control and (b) the ability of the entity to vary existing taxation levels or other revenue sources and to introduce new sources of taxation or other revenue, over the period of the projections, which finance the entity’s policies for service delivery to recipients and entitlements for beneficiaries, and remain within debt constraints.

33. The IPSASB derived this definition from the definition of vulnerability in Statement of Recommended Practice 4 (SORP-4), *Indicators of Financial Condition* issued by the Canadian Public Sector Accounting Board. The definition in SORP-4 is as follows:

Vulnerability is the degree to which a government is dependent on sources of funding outside its control or influence or is exposed to risks that could impair its ability to meet its existing financial obligations both in respect of its service commitments to the public and financial commitments to creditors, employees and others.

34. The tentative decision at the December 2012 meeting to change the name of the definition from “vulnerability” to “revenue vulnerability” has the effect of more closely reflecting the substance of the definition while retaining the original intent of the IPSASB to include a dimension that highlights the degree to which an entity is dependent on, and therefore vulnerable to, sources of funding outside its control or influence.
35. Staff proposes an amendment to the definition to reflect the proposal to use the term “current policy assumptions” instead of “supportable assumptions” in the definition of projection which is explained in the previous section of this Agenda Paper. The proposed definition marked-up for these changes is as follows:

Revenue vulnerability is (a) the entity's dependency upon funding sources outside its control and (b) the ability of the entity to vary existing taxation levels or other revenue sources ~~or and to introduce new sources of taxation or other revenue sources~~, over the period of the projections, ~~to which finance current policy assumptions the entity's policies~~ for service delivery to recipients and entitlements for beneficiaries, while remaining and remain within debt constraints.

36. Staff considers that the proposed amendments to the revenue vulnerability dimension are consistent with the intentions of the IPSASB when developing this definition for ED 46.
37. Staff has received offline comments that the phrase “service delivery to recipients and entitlements for beneficiaries” in the revenue vulnerability definition (and also in the fiscal capacity definition) is a very long phrase and they questioned whether it is necessary in these definitions. They suggested that it could be just used in the service capacity definition alone or in supporting commentary. Staff would like feedback on this suggestion.

Fiscal Capacity Dimension

38. The inclusion of the term “revenue” in the revenue vulnerability dimension has implications for the name of the fiscal capacity dimension because the dictionary definition of “fiscal” includes revenue.¹
39. The definition of fiscal capacity considered at the December 2012 meeting is as follows:

Fiscal capacity is the ability of the entity to meet financial commitments, such as the servicing and repayment of debt, over the period of the projections, using the entity's policies for service delivery to recipients and entitlements for beneficiaries, and for raising taxes and other revenue.

40. The IPSASB derived this definition from the definition of fiscal capacity in the US Governmental Accounting Standards Board's (GASB's) document *Preliminary Views of the Governmental*

¹ The definition of fiscal is “of or relating to taxation, public revenues, or public debt” (Webster's Ninth New Collegiate Dictionary, 1984).

*Accounting Standards Board on Major Issues related to Economic Condition Reporting: Financial Projections.*² This document defines fiscal capacity as:

Fiscal capacity is the government's ability and willingness to meet its financial obligations as they come due on an ongoing basis.

41. The definition of fiscal capacity relates to the ability of the entity to meet financial commitments, in other words, its ability to maintain and service its debt. Therefore staff proposes that the name of the definition could be changed to debt capacity. Staff considers that this proposed change would more closely reflect the substance of the definition and is consistent with the IPSASB's intention to include a dimension that highlights the sustainability of debt.
42. At the December 2012 meeting, the IPSASB also directed staff to amend the definition to include reference to the raising of debt. Similarly to the revenue vulnerability dimension, staff proposes a further amendment to reflect the use of the term "current policy assumptions" instead of "supportable assumptions" in the definition of projection. Staff has also received offline comments to improve the readability of the definition. The proposed definition marked-up for these changes is as follows:

Debt Fiscal capacity is the ability of the entity over the period of the projections to meet its financial commitments as they come due ~~such as the servicing and repayment of debt, or to raise debt as necessary, over the period of the projections, using the entity's policies based on current policy assumptions~~ for service delivery to recipients and entitlements for beneficiaries, and for raising revenue from taxation ~~taxes and other revenue sources~~.

43. Staff considers that the proposed amendments to the fiscal capacity dimension are consistent with the intentions of the IPSASB when developing this definition for ED 46.

Service Capacity Dimension

44. Consequential amendments are necessary to the service capacity dimension to reflect the use of the term "current policy assumptions" instead of "supportable assumptions" in the definition of projection and offline comments. The proposed definition marked-up for these changes is as follows:

Service capacity is the ability of the entity over the period of the projections to maintain the volume and quality of services provided to recipients and meet obligations related to entitlement programs for beneficiaries, ~~over the period of the projections, using based on current policy assumptions the entity's policies~~ for raising revenue from taxation ~~taxes and other revenue sources, while remaining and remain~~ within debt constraints.

45. The IPSASB derived this definition from the definition of service capacity in the US GASB's document Preliminary Views on Economic Condition Reporting: Financial Projections. This document defines service capacity as:

Service capacity is the government's ability and willingness to meet its commitments to provide services on an ongoing basis.

46. Staff considers that the proposed amendments to the service capacity dimension are consistent with the intentions of the IPSASB when developing this definition for ED 46.

² Issued in November 2011.

Matter(s) for Consideration

4. The IPSASB is asked to confirm:
- (a) That the proposed name and definition of the “revenue vulnerability” dimension, set out in paragraph 35, is appropriate;
 - (b) That the proposed name and definition of the “debt capacity” dimension, set out in paragraph 42, is appropriate; and
 - (c) That the proposed definition of the “service capacity” dimension, set out in paragraph 44, is appropriate.

Review of Draft RPG

47. At its meeting in December 2012, the IPSASB agreed to consider a revised draft RPG at its March 2013 meeting. Agenda Paper 4.2 presents the marked-up version of the draft RPG. The Appendix to this Agenda Paper lists the paragraphs in the draft RPG and indicates the proposed changes from the December 2012 version of the draft RPG.

Matter(s) for Consideration

5. The IPSASB is asked to conduct a page-by-page review of the draft RPG in Agenda Paper 4.2 and provide feedback on the proposed amendments.

Approval of Draft RPG

48. Staff wishes to ask the IPSASB if they will approve the publication of the draft RPG.

Matter(s) for Consideration

6. The IPSASB is asked to approve the publication of the draft RPG.

Appendix: Proposed Changes from Draft RPG Presented at December 2012 Meeting

The table below lists the paragraphs in the draft RPG presented at this meeting and cross-references them to the draft RPG presented at the December 2012 meeting. It also explains the proposed changes.

Paragraph Number	Paragraph Number at December 2012 Meeting	Comment
Objective		
1	1	Editorial change.
2	1A	No change.
3	1B	Editorial change.
Status and Scope		
4	2 and 2A	No change.
5	3	Editorial change.
6	4	No change.
7	5	Editorial change.
8	6	No change.
9	6A	No change.
10	6B	No change.
Definitions		
11	7	See paragraphs 4–7 and 31–46 of this Agenda Paper for details of changes to definitions. The definitions of inflows and outflows have editorial changes.
–	8	Now paragraph 2.
–	9	Now paragraph 3.
Determining Whether to Report Long-Term Fiscal Sustainability Information		
12	10	Editorial change.
13	11	No change.
14	12	Editorial changes. Sub-paragraph (b) moved to disclosure paragraph 53(d).

Paragraph Number	Paragraph Number at December 2012 Meeting	Comment
		Sub-paragraph (c) deleted because it is not relevant.
Reporting Boundary		
15	13	No change.
–	14	Disclosure – moved to paragraph 53(c).
16	15	Third sentence deleted as covered by disclosure paragraph 53(c).
–	16	Deleted at December 2012 meeting.
Key Principles of Reporting Long-Term Fiscal Sustainability Information		
17	16A	Editorial change.
18	16B	Inserted reference to the pervasive constraints of financial reporting in place of the reference to materiality in paragraph 19. Editorial changes.
19	16C	Replaced paragraph on materiality with explanation that economic and other phenomena reported in LTFS information is uncertain and entities should use the best available information. Based on paragraph 3.15 in the <i>Conceptual Framework</i> .
20	16D	No change.
–	16E	Moved back to original position in ED 46 (as paragraph 18). Now paragraph 22.
Presenting Projections of Prospective Inflows and Outflows		
21	17	Amended as a consequence of amending the definition of projection (see paragraphs 4–7 of this Agenda Paper). Editorial changes.
22	18	Moved back to original position in ED 46. Was paragraph 16E. Second sentence is a disclosure – moved to paragraph 53(g).
23	19	Penultimate sentence deleted as covered by paragraph 18.
24	20	Last sentence is a disclosure – moved to paragraph 54(g). Editorial change.
–	21	Disclosure – moved to paragraph 54(e).
–	22	Deleted at December 2012 meeting.

Paragraph Number	Paragraph Number at December 2012 Meeting	Comment
–	23	Deleted at December 2012 meeting.
Time Horizon		
25	24	No change.
26	25	Amended to clarify meaning by deleting the term “fiscal dependency” and replacing it with “dependence on other entities for funding.”
27	26	Amended for same reason as paragraph 26.
–	26A	Disclosure – moved to paragraph 54(h) and (i).
–	26B	Moved to paragraph 30.
–	26C	Moved to paragraph 30.
–	26D	Deleted specific reference to indicators being calculated using GFS reporting guidelines or other requirements and moved disclosure to paragraph 55(c).
–	26E	Disclosure – moved to paragraph 55(a) and (b).
Addressing the Dimensions of Long-Term Fiscal Sustainability		
28	27	Amended to reflect proposed changes to the names of the dimensions.
29	27A	Inserted explanation of the linkage between the dimensions.
30	26B	Deleted sub-paragraphs (b) and (c) because they make the paragraph tautological.
Debt-Fiscal Capacity		
31	28	Amended as a consequence of amending the definitions of fiscal capacity and projection (see paragraphs 4–7 and 31–46 of this Agenda Paper).
32	29	Amended as a consequence of amending the definitions of fiscal capacity and projection (see paragraphs 4–7 and 31–46 of this Agenda Paper).
33	30	No change.
Service Capacity		
34	31	Amended as a consequence of amending the definitions of service capacity and projection (see paragraphs 4–7 and 31–46 of this

Paragraph Number	Paragraph Number at December 2012 Meeting	Comment
		Agenda Paper).
35	32	Amended as a consequence of amending the definitions of service capacity and projection (see paragraphs 4–7 and 31–46 of this Agenda Paper).
36	33	No change.
Revenue Vulnerability Capacity		
37	34	Amended as a consequence of amending the definitions of revenue vulnerability and projection (see paragraphs 4–7 and 31–46 of this Agenda Paper).
38	35	Editorial changes.
39	36	Editorial changes.
–	36A	Disclosure – moved to paragraph 55(d) and (e).
–	37	Deleted at December 2012 meeting.
–	37A	Deleted as covered by paragraph 55(a).
Principles and Methodologies		
–	38	Disclosure – moved to paragraph 56.
–	38A	Disclosure – moved to paragraph 56(f).
Updating Projections and Frequency of Reporting		
40	39	Editorial change.
–	39A	Disclosure – moved to paragraph 53(b), (e) and (f).
Impact of Legal Requirements and Policy Frameworks (moved section up from below “Approach to Age-Related and Non-Aged-Related Programs”)		
41	46	Added a sentence to say that legal requirements and policy frameworks are likely to specify or otherwise affect the principles, assumptions and approaches an entity should use in calculating its projections.
–	46A	Disclosure – moved to paragraph 56(a).and (b).
–	47	Disclosure – moved to paragraph 56(b).

Paragraph Number	Paragraph Number at December 2012 Meeting	Comment
Current and Future Policy Assumptions		
42	40	Two options shown to clarify what is meant by current policy (see paragraphs 8–30 of this Agenda Paper). Also amended as a consequence of amending the definition of projection (see paragraphs 4–7 of this Agenda Paper).
43	42A	Editorial changes.
44	40A	Editorial changes.
–	41A	Deleted at December 2012 meeting.
–	42	Deleted because all policy assumptions should be based on current policy and therefore it is not necessary to explain that flows not individually projected can be calculated using either current or future policy.
45	41	Editorial change.
–	42B	Disclosure – sub-paragraph (a) moved to paragraph 56(e). Sub-paragraphs (b) and (c) are deleted because they are too detailed and are covered by paragraph 56(e).
<i>Approach to Revenue Inflows</i> (changed to lower-level heading so that it is a part of the “Current and Future Policy Assumptions” section)		
46	43	Amended – See paragraphs 13–14 of this Agenda Paper.
47	43A	Editorial change.
–	43B	Disclosure – moved to paragraph 54(a) and (b). Deleted (c) as covered by paragraph 56(c).
<i>Approach to Age-Related and Non-Age-Related Programs</i> (moved sub-section up and changed to lower-level heading so that it is a part of the “Current and Future Policy Assumptions” section)		
48	45	No change.
–	45A	Disclosure – deleted because they are too detailed and are covered by sub-paragraph 56(c) and (e).
Demographic and Economic Assumptions		
49	44	No change.

Paragraph Number	Paragraph Number at December 2012 Meeting	Comment
–	44A	Disclosure – moved to paragraph 56(c) and (d).
Inflation and Discount Rates		
50	48	Editorial change.
–	48A	Disclosure – moved to paragraph 56(h) and (i).
Sensitivity Analysis		
51	49	Added sentence to explain that sensitivity analysis will help users to understand the impact of significant changes in assumptions on projections. Penultimate sentence deleted as unnecessary. Last sentence is deleted because it is covered by paragraph 56(g).
–	49A	Disclosure – moved to paragraph 56(g).
Reliability of Projections (deleted sub-section)		
–	50	Explanation that projections are uncertain is covered by paragraph 19. Disclosure – moved to paragraph 54(f).
<u>Disclosures</u> (inserted section so that disclosures are all located in one place)		
52	–	Added an overall disclosure objective that the disclosures should enable users to assess the LTFS of the entity. Second sentence based on third sentence of paragraph 38.
53	–	This paragraph groups together general disclosure recommendations that were previously in separate sections of the draft RPG.
54	–	This paragraph groups together disclosures that are recommended relating to the projections.
55	–	This paragraph groups together disclosures that are recommended relating to the dimensions of LTFS.
56	–	This paragraph groups together disclosures that are recommended relating to the principles, assumptions and approaches to methodology underpinning the projections.

Paragraph Number	Paragraph Number at December 2012 Meeting	Comment
Appendix A: Glossary of Indicators		
		Amended to update document references.
Appendix B: Existing Definitions in IPSASs		
		Amended to update paragraph references.

Final Pronouncement
March 2013

RPG 1

Recommended Practice Guideline

Reporting on the Long-Term Sustainability of an Entity's Finances



International Public
Sector Accounting
Standards Board

This document was developed and approved by the International Public Sector Accounting Standards Board (IPSASB).

The IPSASB sets International Public Sector Accounting Standards (IPSASs) and Recommended Practice Guidelines for use by public sector entities, including national, regional, and local governments, and related governmental agencies.

The objective of the IPSASB is to serve the public interest by setting high-quality public sector accounting standards and by facilitating the adoption and implementation of these, thereby enhancing the quality and consistency of practice throughout the world and strengthening transparency and accountability of public sector finances.

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REPORTING ON THE LONG-TERM SUSTAINABILITY OF AN ENTITY'S FINANCES

CONTENTS

	Paragraph
Objective	1–3
Status and Scope	4–10
Definitions.....	11
Determining Whether to Report Long-Term Fiscal Sustainability Information.....	12–14
Reporting Boundary	15–16
Key Principles of Reporting Long-Term Fiscal Sustainability Information	17–20
Presenting Projections of Prospective Inflows and Outflows.....	21–27
Time Horizon	25–27
Addressing the Dimensions of Long-Term Fiscal Sustainability.....	28–39
Debt Capacity	31–33
Service Capacity.....	34–36
Revenue Vulnerability.....	37–39
Principles and Methodologies	40–51
Updating Projections and Frequency of Reporting.....	40
Impact of Legal Requirements and Policy Frameworks.....	41
Current and Future Policy Assumptions	42–48
Demographic and Economic Assumptions.....	49
Inflation and Discount Rates.....	50
Sensitivity Analysis	51
Disclosures.....	52–56
Appendix A: Glossary of Indicators	
Appendix B: Existing Definitions in IPSASs	
Basis for Conclusions	

Objective

1. Reporting on the long-term sustainability of an entity's finances ("reporting long-term fiscal sustainability information") provides information on the impact of current policies and decisions made at the reporting date and supplements information in the general purpose financial statements ("financial statements"). This Recommended Practice Guideline (RPG) provides guidance on the approach to reporting long-term fiscal sustainability information. The aim of such reporting is to provide an indication of the projected long-term sustainability of ~~the~~ an entity's finances over a specified time horizon in accordance with transparent assumptions.
2. Long-term fiscal sustainability information is broader than information derived from the financial statements. It includes projected inflows and outflows related to the provision of goods and services and programs providing social benefits under current policy over a specified time horizon. It therefore takes into account decisions made by the entity on or before the reporting date that do not meet the definition and/or recognition criteria for liabilities. Similarly it takes into account future taxation receipts, contributions and inter-governmental transfers that do not meet the definition of, and/or recognition criteria for, assets.
3. Assessments of long-term fiscal sustainability involve ~~using~~ the use of a broad range of data. These data include financial and non-financial information about current economic and demographic conditions, assumptions about country and global trends such as productivity, the relative competitiveness of the national, state or local economy and expected changes in demographic variables such as age, longevity, gender, income, educational attainment and morbidity.

Status and Scope

4. This RPG provides guidance on reporting long-term fiscal sustainability information. The reporting of information in accordance with this RPG represents good practice. An entity reporting long-term fiscal sustainability information is encouraged to follow this RPG. Compliance with this RPG is not required in order for an entity to assert that its financial statements comply with International Public Sector Accounting Standards (IPSASs) applicable to the financial statements.
5. The scope of this RPG includes ~~all~~ an entity's projected flows. It is not limited to those flows related to programs providing social benefits. Nevertheless, this RPG acknowledges that the flows relating to programs providing social benefits, including entitlement programs that require contributions from participants, can be a highly significant component of reporting long-term fiscal sustainability information for many entities.
6. This RPG does not directly address issues associated with the reporting of environmental sustainability. However, an entity should assess any financial impacts of environmental factors and take them into account when developing its projections.
7. This RPG ~~applies~~ can apply to all public sector entities, except Government Business Enterprises (GBEs).
8. Although this RPG does not apply directly to GBEs, the prospective inflows and outflows to/from the entity from/to a GBE over the specified time horizon of the projections are within the scope of this RPG.
9. An entity whose long-term fiscal sustainability information complies with this RPG should make an explicit and unreserved statement of such compliance. Long-term fiscal sustainability information

should not be described as complying with this RPG unless it complies with all the requirements of this RPG.

10. This RPG does not provide guidance on the level of assurance (if any) to which long-term fiscal sustainability information should be subjected.

Definitions

11. The following terms are used in this RPG with the meaning specified:

Fiscal Debt capacity is the ability of the entity over the period of the projections to meet its financial commitments as they come due, such as the servicing and repayment of debt, or to raise debt as necessary, over the period of the projections, using based on current policy assumptions the entity's policies for service delivery to recipients and entitlements for beneficiaries, and for raising taxes revenue from taxation and other revenuesources.

Inflows are cash and cash equivalents projected to be received or accrued by the entity over the time horizon of the projections.

Long-term fiscal sustainability is the ability of an entity to meet service delivery and financial commitments both now and in the future.

Outflows are cash and cash equivalents projected to be paid or incurred by the entity over the time horizon of the projections.

A projection is prospective financial information prepared on the basis of supportable the entity's current policy assumptions about the entity's policies, and future economic and other conditions.

Service capacity is the ability of the entity over the period of the projections to maintain the volume and quality of services provided to recipients and meet obligations related to entitlement programs for beneficiaries, over the period of the projections, using based on current policy assumptions the entity's policies for raising revenue from taxation and other revenuesources, and remain while remaining within debt constraints.

Revenue vulnerability is (a) the entity's dependency upon funding sources outside its control and (b) the ability of the entity to vary existing taxation levels or other revenue sources and or to introduce new sources of taxation or other revenue sources, over the period of the projections, which to finance current policy assumptions the entity's policies for service delivery to recipients and entitlements for beneficiaries, and remain while remaining within debt constraints.

Determining Whether to Report Long-Term Fiscal Sustainability Information

12. In determining whether to report long-term fiscal sustainability information, an entity needs to assess whether which potential users exist for prospective financial information.
13. The relevance of reporting long-term fiscal sustainability information should be considered in the context of that entity's funding and capacity to determine service delivery levels. There are likely to be users for long-term fiscal sustainability information for entities with one or more of the following characteristics:
 - (a) Significant tax and/or other revenue raising powers;
 - (b) Powers to incur significant debt; or

- (c) The power and ability to determine the nature, level and method of service delivery including the introduction of new services.
14. ~~A If a controlled entity determines that there are users for long-term fiscal sustainability information, it should ensure that (a) the information reported is consistent with information reported by the its controlling entity, (b) the controlling entity is identified, and (c) users are made aware whether or not the controlling entity reports long-term fiscal sustainability information.~~

Reporting Boundary

15. An entity should use the same reporting boundary for reporting long-term fiscal sustainability information as that used for the financial statements. This enhances the understandability of projections and increases their usefulness to the users of general purpose financial reports (GPFRs).
16. An entity may report long-term fiscal sustainability information in respect of those entities that comprise the General Government Sector (GGS). This may be to enhance consistency and comparability with other jurisdictions or because there are other indicators that are used to assess long-term fiscal sustainability based on the GGS. ~~In this situation an entity should explain how the boundary of the GGS differs from that of the boundary for the financial statements.~~ Entities providing information on the GGS are encouraged to also present information in accordance with IPSAS 22, *Disclosure of Financial Information about the General Government Sector*.

Key Principles of Reporting Long-Term Fiscal Sustainability Information

17. Long-term fiscal sustainability information should enable users to form an overall assessment of the long-term fiscal sustainability of the entity, ~~and~~ including the nature and extent of risks that the entity faces.
18. The form and content of an entity's long-term fiscal sustainability information will vary depending on the nature of the entity and the regulatory environment in which it operates. A single presentation approach is unlikely to satisfy the objectives of financial reporting. To meet the objectives¹ and qualitative characteristics² of financial reporting while taking into account the pervasive constraints³, long-term fiscal sustainability information will usually include the following components:
- (a) Projections of prospective inflows and outflows displayed in tabular statements or graphical formats including a narrative discussion explaining the projections (see paragraphs 21–27 and 54);
 - (b) A narrative discussion of the dimensions of long-term fiscal sustainability including the indicators used to portray the dimensions (see paragraphs 28–39 and 55); and

¹ The objectives of financial reporting by public sector entities are to provide information about the entity that is useful to users of general purpose financial reports for accountability purposes and for decision-making purposes. See Chapter 2 of the *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities* (the *Conceptual Framework*) for further details.

² The qualitative characteristics of financial reporting are relevance, faithful representation, understandability, timeliness, comparability, and verifiability. See Chapter 3 of the *Conceptual Framework* for further details.

³ Pervasive constraints on information included in GPFRs are materiality, cost-benefit, and achieving an appropriate balance between the qualitative characteristics. See Chapter 3 of the *Conceptual Framework* for further details.

- (c) A narrative discussion of the principles, assumptions and approaches to methodology basis of preparation of underlying the projections (see paragraphs 40–51 and 56).
19. Long-term fiscal sustainability information should include only information that is material to the entity. The economic and other phenomena reported in long-term fiscal sustainability information generally occur under conditions of uncertainty. The projections are derived from models that rely on assumptions around which there is some uncertainty. To faithfully represent an entity's long-term fiscal sustainability information each input should reflect the best available information.
20. Long-term fiscal sustainability information may be published as a separate report or as part of another report. It may be published at the same time as the entity's GPFs or at a different time.

Presenting Projections of Prospective Inflows and Outflows

21. An entity should present projections of all prospective inflows and outflows, including those related to capital expenditure, commencing in the current reporting period for a specified time horizon. The projections should be prepared on the basis of supportable current policy assumptions about the entity's policies, and assumptions about future economic and other conditions.
22. An entity should assess the extent to which it can draw on the projections and indicators prepared by other entities, such as Ministries of Finance, rather than preparing the information itself, as this can reduce the cost of such reporting. When an entity uses projections and indicators prepared by other entities, it should disclose this fact. Where an entity has a budget or forecast that meets the definition of a projection, this information can be used for the relevant time period or periods.
23. Projections can be displayed in tabular statements or graphical formats providing details of the programs and activities giving rise to outflows and identifying the sources of inflows. In determining the format of tabular statements entities need to balance considerations of understandability and relevance. Multi-columnar presentation of a large number of time periods between the reporting date and the end of the time horizon provides a more complete information set, but such a presentation increases the risk of information overload and the impairment of understandability. Statements will need to be complemented by additional presentational methods involving a combination of narrative reporting, graphical presentation and the use of indicators. Projections of net debt are likely to be central for many reporting entities.
24. An entity should ensure that its presentation of projections is not skewed to present a misleadingly favorable or unfavorable picture. The formats and terms used should also be consistent between reporting periods. An entity should explain any modifications of formats between reporting periods and the reasons for such changes.

Time Horizon

25. In selecting an appropriate time horizon an entity needs to balance the qualitative characteristics of verifiability and faithful representation. The further the end of the time horizon is from the reporting date the more future events are captured. However, the assumptions underpinning the projections become less robust and potentially less verifiable. Conversely, excessively short time horizons may increase the risk that the consequences of events outside the time horizon may be ignored, thereby reducing the relevance of projections.
26. There is a strong relationship between dependence on other entities for funding fiscal dependency and time horizons. Generally, high levels of dependence fiscal dependency may lead to the

selection of shorter time horizons, because a high proportion of the entity's prospective inflows are dependent upon decisions by other entities over which the entity has no control and limited influence.

27. Apart from dependence on other entities for funding~~fiscal dependency~~, the length of the time horizon will reflect the characteristics of the entity. It is likely to be influenced by aspects such as the longevity of key programs, the estimated lives of major items of property, plant, and equipment, such as road networks, and the time horizons adopted by other comparable entities providing prospective information.

Addressing the Dimensions of Long-Term Fiscal Sustainability

28. An entity reporting long-term fiscal sustainability information should include a narrative discussion on the dimensions of long-term fiscal sustainability. This RPG discusses three inter-related dimensions of long-term fiscal sustainability:

- Fiscal Debt capacity;
- Service capacity; and
- Revenue ~~capacity~~vulnerability.

29. The dimensions are inter-related and changes in one dimension affect the other dimensions. For example, future services and entitlements to beneficiaries (service capacity) are funded either by maintaining or raising debt (debt capacity) or by maintaining or raising revenue from taxation and other sources (revenue vulnerability). The dimensions also highlight the entity's vulnerability to market expectations and economic conditions, changes in public demand for services, and dependency on revenue streams.

30. An entity can use indicators to portray various dimensions of long-term fiscal sustainability. An entity should choose its indicators based on ~~(a) their relevance to the entity; (b) The extent to which they meet the qualitative characteristics of financial reporting; and (c) Their ability to address the dimensions of long-term fiscal sustainability.~~ Examples of indicators are provided in the Glossary of Indicators at in Appendix A.

Fiscal Debt Capacity

31. Fiscal Debt capacity is the ability of the entity over the period of the projections to meet its financial commitments as they come due, such as the servicing and repayment of debt, over the period of the projections or to raise debt as necessary, using the entity's policies based on current policy assumptions for service delivery to recipients and entitlements for beneficiaries, and for raising taxes revenue from taxation and other revenuesources.
32. The level of net debt is important for an assessment of fiscal debt capacity, as, at any reporting date, it represents the amount expended on the past provision of goods and services that has to be financed in the future. By projecting current policy assumptions policies for the provision of goods and services, and current policies for raising taxes revenue from taxation and other revenuesources, projected levels of net debt can be presented. Users can then assess the entity's ability to raise and maintain such levels of debt and thereby evaluate fiscal debt capacity.
33. At national levels a factor to consider in presenting such projections is whether to distinguish: (a) the primary balance, which is total projected government spending, excluding interest payable on debt, minus tax revenues, and (b) the overall balance, which is the primary balance including

outflows related to interest payable on debt. At sub-national levels the focus may be on net debt as a percentage of total revenues. Increases in this indicator show that an increasing proportion of revenues will be required for debt servicing, thereby diverting resources from service delivery, and that the long-term fiscal position may become unsustainable.

Service Capacity

34. *Service capacity* is the ability of the entity over the period of the projections to maintain the volume and quality of services provided to recipients and meet obligations related to entitlement programs for beneficiaries, over the period of the projections, using based on current policy assumptions the entity's policies for raising revenue from taxation taxes and other revenuesources, and remain while remaining within debt constraints.
35. By projecting the impact of current policy assumptions policies for raising taxes-revenue from taxation and other revenuesources, and policies for raising and maintaining debt, long-term fiscal sustainability information can present the amounts available for the provision of goods and services under these policies. Users can contrast this information with the entity's service delivery commitments, and thereby evaluate service capacity.
36. A factor to consider in making such comparisons is the extent to which expenditure on certain programs is likely to increase more steeply than the overall levels of expenditure of the entity. This may be because the number of beneficiaries is projected to increase for a particular program or because costs associated with certain programs, such as healthcare, are projected to increase more quickly than the general inflation rate. For capital intensive activities the dimension of service capacity also involves an assessment of the useful lives and replacement cycles of items of property, plant, and equipment to assess whether service capacity is increasing or decreasing.

Revenue Vulnerability

37. *Revenue vulnerability* is (a) the entity's dependency upon funding sources outside its control and (b) the ability of the entity to vary existing taxation levels or other revenue sources and-or to introduce new sources-of taxation-or-other revenue sources, over the period of the projections, which-to finance current policy assumptions the entity's policies for service delivery to recipients and entitlements for beneficiaries, and remain while remaining within debt constraints.
38. An example of an indicator for revenue vulnerability is the proportion of total revenues that are received from entities at other levels of government or from international organizations. For example, a local government entity may be able to raise property taxes, but be partially dependent upon a mixture of general grants and specific grants from national and/or state governments. As policies for the provision of goods and services, and policies for managing debt are projected into the future, the level of revenue required to fund such policies can be presented. Users can then assess the entity's ability to raise and maintain its levels of revenue and thereby evaluate revenue capacityvulnerability.
39. Generally, an entity which has a limited ability to vary levels of revenue from taxation and other revenue sources is likely to have low-high revenue vulnerability. If inter-governmental transfers have constitutional or other legal underpinning, this may make the entity less susceptible to sudden adverse funding decisions by other entities and therefore increase the probability of continuing to receive funds. Trends indicating that revenue vulnerability is decreasing-increasing may suggest

that an entity's future sustainability is dependent upon funding decisions by entities at other levels of government.

Discussion of the Dimensions

~~37A. In providing narrative discussion on the dimensions of long-term fiscal sustainability, an entity should include an analysis of significant changes in the measures of the dimensions compared with those of the previous reporting period as this can help users to understand the reasons for any changes.~~

Principles and Methodologies

Updating Projections and Frequency of Reporting

40. While regular updates are desirable, this RPG acknowledges that annual updating may not be realistic for all entities. However, there is generally an inverse relationship between the robustness of assumptions on which projections are made and the amount of time since they were made. During periods of global financial volatility the risk that projections made some time before the reporting date are outdated increases, with a consequent reduction of the ability of such information to meet the objectives of accountability and decision-making. In this situation, an entity should consider updating its projections on a more frequent basis. An entity should also consider updating its projections after significant or major unexpected events such as natural disasters or other emergencies.

Impact of Legal Requirements and Policy Frameworks

41. In some jurisdictions reporting long-term fiscal sustainability information is governed by a legal or regulatory framework that applies at the national or state level. There may also be legal requirements for local government. These might include balanced budget requirements. These requirements are likely to specify or otherwise affect the principles, assumptions and approaches an entity should use in calculating its projections.

Current and Future Policy Assumptions

Option A: Current Legislation or Regulation with Specific Exceptions (see AP 4.1)

42. Where flows for particular programs and activities are individually modeled, the policy assumptions should be based on the continuation of current legislation or regulation except for the specific exceptions listed below and those assumptions-policy. That policy should be held constant through-out the entire projection period ("current policy assumptions"). ~~However, there may be instances where a departure from current legislation or regulation is permitted in the following circumstances may be appropriate:~~

- (a) Where changes to current legislation or regulation have been enacted before the reporting date which have a specific implementation date within the time horizon of the projections ~~a policy has been changed in a consistent direction over time;~~
- (b) Where the provisions in current legislation or regulation are internally inconsistent ~~there is a conflict between current policy and legal obligations;~~ or
- (c) Where current legislation or regulation ~~a policy~~ has "sunset provisions".

Option B: Current Legislation or Regulation with Departures where Appropriate (see AP 4.1)

42. Where flows for particular programs and activities are individually modeled, the policy assumptions should be based on the continuation of current legislation or regulation with departures where appropriate and those assumptions-policy. That policy should be held constant through-out the entire projection period ("current policy assumptions"). The starting point for current policy assumptions should be current legislation or regulation. However, there may be instances where a departure from current legislation or regulation ~~policy~~ may be appropriate, as follows for example:

- (a) Where changes to current legislation or regulation have been enacted before the reporting date which have a specific implementation date within the time horizon of the projections ~~a policy has been changed in a consistent direction over time;~~
- (b) Where the provisions in current legislation or regulation are internally inconsistent ~~there is a conflict between current policy and legal obligations;~~ or
- (c) Where current legislation or regulation ~~a policy~~ has "sunset provisions".

43. Current Ppolicy assumptions may ~~also~~ be affected by legal changes that have been enacted before the reporting date which have a specific implementation date within the time horizon of the projections. In these circumstances, assuming ~~a~~ current legislation or regulation ~~policy~~ remains in force for the entire projection period will not be appropriate.

44. An example of current legislation or regulation that is internally inconsistent ~~a conflict between a policy and legal obligations~~ is a social security program which has legal provisions that make it unlawful to make payments once an earmarked fund is exhausted, although entitlements of beneficiaries will continue after the exhaustion of that fund. Assuming that the fund will not meet obligations once it is exhausted might reflect a strict legal position, but an entity may need to assess whether the presentation of projections on such a basis underestimates projected outflows and therefore the extent of the fiscal challenge facing the social security program. In this situation

an entity may calculate its projections based on current policy assumptions despite legal restrictions.

45. Current legislation or regulation ~~A policy~~ may have sunset provisions whereby it terminates after a specific period. In many cases there may be a strong probability that such programs will be replaced by similar programs. Adopting a strict legal termination principle could underestimate projected outflows, and therefore impair the usefulness of the information.

~~41A. An example of a policy that has been changed in a consistent direction over time may be the income threshold for the taxation of individuals (this is sometimes called "fiscal drag"). Assuming that the threshold remains at the same monetary amount might reflect the strict legal position, but if there is a strong probability that the threshold will be raised, an entity may need to assess whether the presentation of projections on a fixed threshold basis would overestimate projected inflows, thereby impairing the usefulness of information.~~

~~42. For flows that are not individually projected, the distinction between current and future policy is unlikely to be critical to the projections and it may be sufficient to disclose general assumptions.~~

Approach to Revenue Inflows

46. Significant ~~sources of revenue inflows from~~ taxation and other ~~revenue flows~~sources, such as inter-governmental transfers, may be individually modeled based on current policy assumptions. Significant sources of taxation and other revenue inflows that are not modeled individually are projected to grow (or diminish) in line with gross domestic product (GDP) or another index such as the inflation index ~~or may be individually modeled based on current policy~~.
47. Other revenue inflows, such as royalties from natural resources, may also be projected to grow in line with GDP or an inflation index. They may also be individually modeled to address specific circumstances, such as when the natural resource is expected to be depleted.

Approach to Age-Related and Non-Age-Related Programs

48. Age-related programs are often subject to eligibility criteria including age and other demographic factors. In making projections, programs and activities that are age-related may be distinguished from non-age related programs. Age-related programs may be individually modeled while non-age-related programs may be projected to increase in line with other variables, such as GDP, or to be constant in real terms. Such an approach to non-age-related programs provides some flexibility, as it allows above GDP/real terms increases in some programs and activities to be offset by lower increases or spending declines in other areas.

Demographic and Economic Assumptions

49. Demographic assumptions are likely to include fertility, mortality and migration rates, and workforce participation rates. Economic assumptions are likely to include economic growth rates and inflation. Other economic assumptions may include environmental factors, such as the impact of the depletion and degradation of ecosystems and the depletion of water and finite natural resources on economic growth.

Inflation and Discount Rates

50. There are two main approaches to incorporating the effect of price inflation in projections. It may be taken into account in making projections or projections may be made at current prices (i.e., prices

prevailing at the reporting date). If the projections include inflation, then the discount rate should also include inflation. If the projections are at current prices, the discount rate should exclude inflation.

Sensitivity Analysis

51. Many assumptions on which projections are based are inherently uncertain. In some cases small changes in variables can have significant impacts on the projections. The use of sensitivity analysis will help users to understand the impact of significant changes in demographic and economic assumptions on the projections. It is unlikely to be appropriate for an entity to provide sufficient data to enable users to remodel projections by modifying assumptions. However, it may be appropriate for an entity to disclose the sensitivity of demographic and economic assumptions that could have a significant impact on the projections.

Reliability of Projections

Disclosures

52. The entity should disclose information that enables users of its long-term fiscal sustainability information to assess the projected long-term fiscal sustainability of the entity. Although this section discusses disclosures, if these disclosures do not meet the objectives of financial reporting, the An entity should make any disclose whatever additional disclosures information is necessary to meet those the objectives of financial reporting. [Was third sentence of paragraph 38]
53. An entity should disclose the following information:
- (a) The name of the entity;
 - (b) [Was paragraph 39A December version of RPG] The financial statements to which the long-term fiscal sustainability information relates;
 - (c) [Was paragraph 14 December version of RPG] Where different, the names of the entities within the reporting boundary for long-term fiscal sustainability information that are different to those for the financial statements; ~~those entities should be identified~~
 - (d) [Was paragraph 14(b)] Where the entity is a controlled entity, the identity of the controlling entity; ~~is identified~~
 - (e) [Was paragraph 39A December version of RPG] The date at which a full set of projections was made;
 - (f) [Was paragraph 39A December version of RPG] The basis and timing of subsequent updating; and
 - (g) [Was second sentence of paragraph 22] When an entity uses projections and indicators prepared by other entities, the identity names of those entities.
54. The narrative discussion of the projections should include disclosure of the following information:
- (a) [Was paragraph 43B(a) December version of RPG] The Significant sources of significant revenue inflows from taxation and other revenue flows sources;

- (b) [Was paragraph 43B(b) December version of RPG] An overview of the current policy assumptions policies for the significant sources of significant revenue inflows from taxation and other revenue flows sources, such as taxation threshold levels and allowances;
 - (c) The sources of significant outflows including capital expenditure;
 - (d) An overview of the current policy assumptions for the significant outflows including capital expenditure;
 - (e) [Was paragraph 21 December version of RPG] An ~~entity should explain~~ explanation of the changes in projections between reporting dates and the reasons for those changes;
 - (f) [Was paragraph 50 December version of RPG] An explanation that it is unlikely that projections over the specified time horizon will match the actual outcome and the extent of the difference will depend upon a range of factors, including the future actions of the entity in meeting any identified fiscal challenge;
 - (g) [Was third sentence of paragraph 24] An entity should explain any modifications of formats between reporting periods and the reasons for such changes;
 - (h) [Was paragraph 26A December version of RPG] The time horizon used for the projections and the reasons for selecting that time horizon; and
 - (i) [Was paragraph 26A December version of RPG] Where an entity changes the time horizon from that used in the previous reporting period, the reason for such a change.
55. [Was paragraph 26E] The narrative discussion of the dimensions of long-term fiscal sustainability should include disclosure of the following information:
- (a) [Was paragraph 26E December version of RPG] An analysis of significant changes in the indicators ~~Significant changes in the measures of indicators~~ compared ~~to with those of~~ the previous reporting period;
 - (b) [Was paragraph 26E December version of RPG] Changes ~~of in~~ the indicators ~~chosen used~~ to report long-term fiscal sustainability information from the previous reporting period, and the reasons for such changes;
 - (c) [Was paragraph 26D December version of RPG] Where an entity uses indicators that are based on amounts derived from non-IPSAS based sources, ~~it should disclose this fact the~~ indicators affected and, where possible, the estimated impact on the indicators;
 - (d) [Was paragraph 36A(a) December version of RPG] The main entities on which the entity is ~~fiscally~~ dependent on funding; and
 - (e) [Was paragraph 36A(b) December version of RPG] Details of constitutional or other legal underpinning for taxation and other revenue or grant arrangements.
56. [Was paragraph 38 December version of RPG] ~~The basis of preparation of projections should be made clear.~~ An entity should disclose the principles, assumptions and approaches to methodology that underpin the projections including the following information: ~~This section discusses:~~
- ~~Updating projections and frequency of reporting;~~
 - ~~Current and future policy;~~
 - ~~Approach to revenue inflows;~~

- ~~Demographic and economic assumptions;~~
 - ~~Approach to age-related and non-age-related programs;~~
 - ~~Impact of legal requirements and policy frameworks;~~
 - ~~Inflation and discount rates;~~
 - ~~Sensitivity analysis; and~~
 - ~~Reliability of projections.~~
- (a) [Was paragraph 46A(a) December version of RPG] Key aspects of governing legislation and regulation;
- (b) [Was paragraphs 46A(b) and 47 December version of RPG] Underlying macro-economic policy and fiscal frameworks including details of where other publicly available reports on these policies underlying macro-economic policy and fiscal frameworks can be accessed, including documents outside the GPFRs;
- (c) [Was paragraph 44A December version of RPG] The key current policy assumptions and the key demographic and economic assumptions that underpin the projections;
- (d) [Was paragraph 44A December version of RPG] ~~together with~~ Its policy for reviewing and updating current policy assumptions and, demographic and economic assumptions;
- (e) [Was paragraph 42B(a) December version of RPG] An explanation of the significant current policy ~~The assumptions that depart from current legislation or regulation; underlying the continuation of current policy through the projection period, including situations where a policy has been changed in a consistent direction over time~~
- (f) [Was paragraph 38A December version of RPG] An explanation of significant changes in the principles, assumptions and approaches to methodologies from the previous reporting period, the nature and extent of these changes, and the reasons for such changes;
- (g) [Was paragraph 49A December version of RPG] The results of any sensitivity analyses that could have a significant impact on the projections;
- (h) [Was paragraph 48A December version of RPG] The discount rates applied and the basis on which the discount rate has been determined; and
- (i) [Was paragraph 48A December version of RPG] The approach to inflation and the reason for this approach.

Appendix A

Glossary of Indicators

Government Finance Statistics Reporting Guidelines

This Appendix lists examples of indicators. It is not intended to be an exhaustive list. Where an indicator includes a defined term, that term is shown in *italics* and its definition is shown after the indicators.

- **Gross debt, total:** Total gross debt—often referred to as “total debt” or “total debt liabilities”—consists of all *liabilities* that are *debt instruments*. A debt instrument is defined as a financial claim that requires payment(s) of interest and/or principal by the debtor to the creditor at a date, or dates, in the future. (Source: International Monetary Fund: *Public Sector Debt Statistics—Guide for Compilers and Users* 2011)
- **Net debt:** Net debt is calculated as gross debt minus *financial assets* corresponding to *debt instruments*. (Source: International Monetary Fund: *Public Sector Debt Statistics—Guide for Compilers and Users*: 2011)
- **Net financial worth:** Net financial worth of an *institutional unit* (or grouping of units) is the total value of its *financial assets* minus the total value of its outstanding *liabilities*. (Source: International Monetary Fund: *Public Sector Debt Statistics—Guide for Compilers and Users*: 2011)
- **Net worth:** Net worth of an *institutional unit* (or grouping of units) is the total value of its *assets* minus the total value of its outstanding *liabilities*. (Source: International Monetary Fund: *Public Sector Debt Statistics—Guide for Compilers and Users*: 2011)
- **Overall balance:** This term corresponds to the GFS 1986 terminology of “Overall Deficit/Surplus,” which is defined as revenue plus grants received less expenditure less “lending minus repayments.” The balance so defined is equal (with an opposite sign) to the sum of net borrowing by the government, plus the net decrease in government cash, deposits, and securities held for liquidity purposes. The basis of this balance concept is that government policies are held to be deficit- or surplus-creating, and thus the revenue or expenditures associated with these policies are “above the line.” Borrowing or a rundown of liquid assets, however, is deficit financing or “below the line.” It should be noted that the term **lending minus repayments** included above the line covers government transactions in debt and equity claims on others undertaken for purposes of public policy rather than for management of government liquidity or earning a return. (Source: International Monetary Fund: *Manual on Fiscal Transparency* (2007))
- **Primary balance:** The overall balance, excluding interest payments. Since interest payments represent the cost of past debt, and the determinants of future debt that are under policy control of government are other spending and revenue measures exclusive of interest payment, the primary balance is of particular importance as an indicator of the fiscal position in countries with high levels of debt. (Source: International Monetary Fund: *Manual on Fiscal Transparency* (2007))

Underlying Definitions

- **Debt instrument:** A debt instrument is defined as a financial claim that requires payment(s) of interest and/or principal by the debtor to the creditor at a date, or dates, in the future. (Source: International Monetary Fund: *Public Sector Debt Statistics—Guide for Compilers and Users* 2011)
- **Economic assets:** Economic assets are entities (i) over which economic ownership rights are enforced by institutional units, individually or collectively, and (ii) from which economic benefits may

be derived by their owners by holding them or using them over a period of time. (Source: International Monetary Fund: *Public Sector Debt Statistics—Guide for Compilers and Users* 2011)

- **Financial assets:** Financial assets consist of financial claims plus gold bullion held by monetary authorities as a reserve asset. A financial claim is an asset that typically entitles the owner of the asset (the creditor) to receive funds or other resources from another unit, under the terms of a liability. (Source: International Monetary Fund: *Public Sector Debt Statistics—Guide for Compilers and Users* 2011)
- **Institutional unit:** An institutional unit is an economic entity that is capable, in its own right, of owning assets, incurring liabilities, and engaging in economic activities and in transactions with other entities. (Source: International Monetary Fund: *Public Sector Debt Statistics—Guide for Compilers and Users* 2011)
- **Liability:** A liability is established when one unit (the debtor) is obliged, under specific circumstances, to provide funds or other resources to another unit (the creditor). (Source: International Monetary Fund: *Public Sector Debt Statistics—Guide for Compilers and Users* 2011)

Other Sources

- **Fiscal gap:** The **fiscal gap** is the change in non-interest spending and/or receipts that would be necessary to maintain public debt at or below a target percentage of gross domestic product (GDP).⁴ More specifically, the fiscal gap is the net present value of projected spending⁵ minus projected receipts, adjusted by the decrease (or increase) in public debt required to maintain public debt at or below the target percentage of GDP for the stated projection period. (Source: US Federal Accounting Standards Advisory Board: Statement of Federal Financial Accounting Standards 36: *Comprehensive Long-Term Projections for the U.S. Government* 2009)
- **Inter-temporal budget constraint:** The inter-temporal budget constraint is satisfied if the projected outflows of the government (current public debt and the discounted value of all future expenditure, including the projected increase in age-related expenditure) are covered by the discounted value of all future government revenue. (Source European Commission: *Sustainability Report* 2009))
- **Net Debt/Total Revenues:** Net debt as a proportion of total revenues. (Source Canadian Public Sector Accounting Board (PSAB): Statement of Recommended Practice 4 (SORP 4), *Indicators of Financial Condition*: 2009)

⁴ GDP is the total market value of all final goods and services produced domestically during a given period of time. The components of GDP are: private sector consumption and investment, government consumption and investment, and net exports (exports-imports).

⁵ Since interest is factored into the present value calculation, the fiscal gap as a share of spending is expressed as a share of spending excluding interest ("non-interest spending").

Appendix B

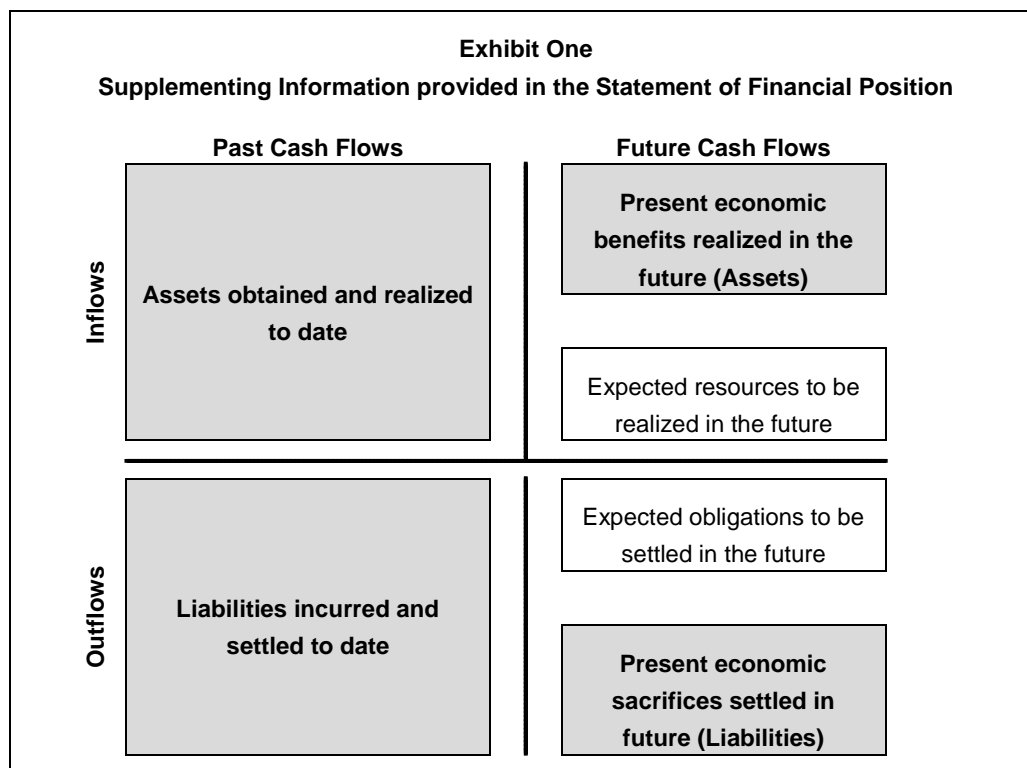
Existing Definitions in IPSASs

Term	Definition	Paragraph reference in this RPG
Assets	Resources controlled by an entity as a result of past events and from which future economic benefits or service potential are expected to flow to the entity.	2
Cash	Comprises cash on hand and demand deposits.	11
Cash equivalents	Short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.	11
Controlled entity	An entity, including an unincorporated entity such as a partnership, which is under the control of another entity (known as the controlling entity).	14
Controlling entity	An entity that has one or more controlled entities.	14
Government Business Enterprise	An entity that has all the following characteristics: (a) Is an entity with the power to contract in its own name; (b) Has been assigned the financial and operational authority to carry on a business; (c) Sells goods and services, in the normal course of its business, to other entities at a profit or full cost recovery; (d) Is not reliant on continuing government funding to be a going concern (other than purchases of outputs at arm's length); and (e) Is controlled by a public sector entity.	7
General government sector	Comprises all organizational entities of the general government as defined in statistical bases of financial reporting.	16
Liabilities	Present obligations of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits or service potential.	2
Reporting date	The date of the last day of the reporting period to which the financial statements relate.	1
Revenue	The gross inflow of economic benefits or service potential during the reporting period when those inflows result in an increase in net assets/equity, other than increases relating to contributions from owners.	11

Basis for Conclusions

Background

- BC1. The IPSASB initially launched a project on accounting for social policy obligations (subsequently re-termed social benefits) in 2002. This led to the publication of an Invitation to Comment (ITC), *Accounting for Social Policies of Governments*, in January 2004. Following an analysis of responses to that ITC, the IPSASB began to develop proposals for accounting for obligations related to different sub-categories of social benefits. In late 2006, due to failure to agree on recognition points and measurement requirements for liabilities, the IPSASB decided not to develop further proposals on recognition and measurement at that time.
- BC2. As an interim step the IPSASB developed proposals for the disclosure of amounts to be transferred to those eligible at the reporting date for cash transfers (benefits settled in cash). It expressly did not propose the disclosure of obligations and liabilities. ED 34, *Social Benefits: Disclosure of Cash Transfers to Individuals or Households* was issued in March 2008.
- BC3. The deliberations on identifying the point at which liabilities for social benefits arise had led the IPSASB to the view that the financial statements cannot provide all the information that users need on social benefits. This is illustrated in Exhibit One below where the shaded boxes indicate information provided in the financial statements. The IPSASB considered that before launching any further project it should consult constituents. Therefore the IPSASB raised this issue in a further Consultation Paper, *Social Benefits: Issues in Recognition and Measurement* and issued a Project Brief, *Long-Term Fiscal Sustainability Reporting*. Both these documents were issued at the same time as ED 34.



- BC4. In October 2008 the IPSASB reviewed responses to all of the above documents. In the light of these responses, it was decided not to develop ED 34 into an IPSAS. The IPSASB also noted that a large majority of respondents agreed that the financial statements cannot convey sufficient information to users about the long-term financial implications of governmental programs providing social benefits.⁶ In light of this view the IPSASB decided to initiate a project on long-term fiscal sustainability (subsequently re-termed "Reporting on the Long-Term Sustainability of Public Finances"). This led to the issue of a Consultation Paper, *Reporting on the Long-Term Sustainability of Public Finances*, in November 2009. Drawing on existing practice the Consultation Paper put forward the case for reporting ~~on on~~ long-term fiscal sustainability information, made suggestions on how such information might be presented and sought the views of constituents. The majority of respondents to the Consultation Paper favored the continuation of the project, although many said that they preferred the IPSASB to develop guidelines rather than requirements.
- BC5. Further work on proposals for the recognition and measurement of liabilities arising from obligations to deliver social benefits is progressing indirectly in Phase 2 of the *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities* project. This phase deals with elements, and includes the development of the definition of a liability and other relevant issues such as whether the power to tax is an asset. This work is likely to influence the approach to recognizing and measuring liabilities related to social benefits.
- BC6. In light of the responses to the Consultation Paper, the IPSASB developed Exposure Draft (ED) 46 Recommended Practice Guideline (RPG), *Reporting on the Long-Term Sustainability of a Public Sector Entity's Finances* which was issued in October 2011. This ED proposed non-authoritative guidance for public sector entities reporting long-term fiscal sustainability information.
- BC7. The IPSASB has further developed its thinking on reporting long-term fiscal sustainability information in the course of its project on *The Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities*. Chapter 2: Objectives and Users of General Purpose Financial Reporting reflects the Phase 1 of the IPSASB's project has considered the scope of financial reporting and adopted a view that, although the financial statements are at the core of financial reporting, a more comprehensive scope is necessary to meet the needs of users. Conceptual Framework ED 1, *Role, Authority and Scope; Objectives and Users; Qualitative Characteristics; and Reporting Entity* proposed a That scope ~~that~~ includes prospective financial information. The IPSASB has also noted that projected outflows relating to obligations as a result of past decisions and projected inflows related to sovereign powers and taxation powers may not be recognized or may only be partially recognized in the statement of financial position and the statement of financial performance. Therefore, in order to meet the objectives of accountability and decision-making, users need information on prospective inflows and outflows in order to supplement information on the entity's financial position in the financial statements.

⁶ Further work on proposals for the recognition and measurement of liabilities arising from obligations to deliver social benefits is progressing indirectly in Phase 2 of the Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities project. This phase deals with elements, and includes the development of the definition of a liability and other relevant issues such as whether the power to tax is an asset. This work is likely to influence the approach to recognizing and measuring liabilities related to social benefits.

- BC8. The IPSASB acknowledges that the rationale for [reporting](#) long-term fiscal sustainability ~~information reporting~~ in paragraph BC6 might indicate that for some entities such reporting should be required. However, the IPSASB concluded that it would be premature to issue an authoritative pronouncement, because reporting ~~on~~ long-term fiscal sustainability [information](#) in ~~the general purpose financial reports (GPFRs)~~ is an area where practice is developing and the IPSASB wishes to encourage innovative and flexible approaches. [Consistent with the views of the majority of respondents to the Consultation Paper, the majority of respondents to ED 46 supported the voluntary application of this guidance.](#)

Scope

- BC9. The IPSASB considered whether the scope of the RPG should be limited to the consolidated national and whole-of-government levels. The IPSASB acknowledged that reporting ~~on the~~ long-term [fiscal sustainability of the public finances information](#) is particularly relevant at these levels, but concluded that there might be significant user demand for such information at sub-national levels. The IPSASB therefore concluded that a narrow scope limited to the national and whole-of-government levels is not justified.

Definitions

[Long-Term Fiscal Sustainability](#)

- BC10. The Consultation Paper noted that there is no universally accepted definition of long-term fiscal sustainability and included a working definition that long-term fiscal sustainability is “the ability of government to meet its service delivery and financial commitments both now and in the future.” The IPSASB acknowledged the view that this definition is insufficiently rigorous and that a definition should be adopted that provides users with a clearer indication whether an entity's current economic position is sustainable. Such an approach might involve (a) linking current service delivery levels and the settling of obligations relating to entitlement programs to the maintenance of current taxation levels and (b) focusing on projected debt paths, ~~so that a~~ An entity that can only maintain current service delivery levels and meet entitlement obligations and financial obligations by increasing taxation or current debt levels is identified as being in an unsustainable position. Macro-economists tend to adopt this more rigorous approach and focus on “explosive” debt paths, which is a term that connotes that existing service levels and existing benefits from entitlement programs cannot be sustained without major increases in levels of indebtedness.
- BC11. The IPSASB decided to retain the definition [of long-term fiscal sustainability used](#) in the Consultation Paper [for ED 46 except for widening the scope to reflect that it can apply to all public sector entities \(except Government Business Enterprises\) rather than limiting it to governments.](#) In coming to this conclusion the IPSASB noted the need for governments and public sector entities to both (a) provide services and meet obligations relating to entitlement programs and (b) meet financial obligations, principally debt servicing. The IPSASB also noted the sovereign power of government to legislate for new taxation sources and to vary the levels of existing taxation, while acknowledging that in a global environment the ability to increase taxation might be practically constrained by a number of considerations. The IPSASB took the view that, provided an entity gives appropriate attention to the dimensions of ~~fiscal debt~~ capacity and service capacity, as highlighted in paragraphs [31–36–28 and 34](#), users will be given adequate information that an entity cannot maintain existing service levels, meet obligations to the current and future beneficiaries of entitlement programs and

meet financial obligations without increasing revenue from taxation and other sources or increasing borrowing.

Projection

BC12. Several respondents to ED 46 suggested that the relationship between projections, budgets and forecasts should be clarified. Given that there are no universally accepted definitions of these terms, the IPSASB decided to develop a definition of projection to clarify the characteristics of information that should be used in calculating the projections. The IPSASB considers that the key characteristics of a projection is that it:

- (a) Is prospective financial information;
- (b) Should be based on current policy assumptions (as that term is explained in paragraphs 42–48 of the RPG); and
- (c) Should be based on assumptions about economic and other conditions such as demographic conditions.

Determining Whether ~~an Entity Should to~~ Report ~~on Long-Term~~ Fiscal Sustainability Information

BC13. As discussed in paragraph BC87 the IPSASB concluded that the scope of the RPG should not be limited to particular levels of government. However, the IPSASB acknowledged that reporting ~~on the~~ long-term fiscal sustainability of their finances information might not be appropriate for all entities. The IPSASB considered this issue at length.

BC14. The Consultation Paper questioned whether reporting ~~on the~~ long-term fiscal sustainability information of its finances is appropriate for individual controlled entities. This reservation was based on a tentative view that (a) the cost of producing the information for such entities is likely to be greater than the benefits to users, (b) the production of separate reports and disclosures by individual entities within an economic entity might be confusing to users and (c) it could be misleading if entities with limited tax-raising powers and a dependency ~~on for~~ resources on entities at other tiers of government provide projections that are contingent on taxation decisions over which they have little or no control. Some respondents to the Consultation Paper challenged this view and suggested that there are cases where users for long-term fiscal sustainability information on the economic condition of controlled entities can be identified. The example of a local government entity controlled by a state or provincial government was cited. These respondents proposed that the test for whether an entity ~~provided information on the reports~~ long-term fiscal sustainability information of its finances should be to assess which potential whether it had identified users exist for this type of information. The IPSASB was persuaded by these arguments and the ED-RPG reflects these views in paragraphs 12–14.

BC15. The IPSASB acknowledged that direct evidence of the existence of users of ~~information on~~ long-term fiscal sustainability information might not be readily available. The IPSASB considered what proxies might indicate the existence of users. The IPSASB concluded that there are likely to be users for long-term fiscal sustainability information for entities with one of more of the following characteristics:

- (a) Significant tax and/or other revenue raising powers;
- (b) Significant powers to incur significant debt; or

- (c) ~~Wide decision-making The powers over to determine the nature, level and method of service delivery levels including the introduction of new services.~~

BC16. The IPSASB believes that reporting long-term fiscal sustainability information reporting is likely to be relevant at the whole of government level, consolidated national level, and for major sub-national entities such as regions, provinces, states and large local government entities (for examples, cities), which have tax raising powers enabling them to generate a significant proportion of their total revenues. The IPSASB remains of the view that reporting on the long-term sustainability of their finances information is unlikely to be appropriate for individual government departments. This is because often they do not have tax raising powers, their expenditure is controlled through appropriations, and they do not have powers to incur debt. ~~In addition, in many jurisdictions, government departments are subject to frequent changes after elections or when ministerial portfolios are amended.~~

Presenting Projections of Prospective Inflows and Outflows

BC17. The Consultation Paper considered three models for reporting information on long-term fiscal sustainability information and suggested that (a) the provision of additional statements providing details of projections and (b) summarized projections in narrative reporting were appropriate. Some respondents suggested that, although the Consultation Paper acknowledged that these reporting approaches were not mutually exclusive, the IPSASB should highlight that reporting on long-term fiscal sustainability information just by displaying projections in statements is insufficient to meet user needs and that other presentation methods need to be deployed. The IPSASB was persuaded by this view and it is reflected in paragraph 1820.

BC18. The IPSASB considered whether it should recommend time horizons for projections for entities at particular levels of government. It acknowledged the view that standard time horizons for particular classes types of public sector entity might enhance comparability. The IPSASB decided that such benchmarks would be over-prescriptive and impractical. The scope of the RPG is such that standard time horizons would have to be determined for a wide range of entities, including single-purpose entities.⁷ In addition the fiscal autonomy of entities at the same level of government can differ markedly between jurisdictions. The IPSASB concluded, however, that it is good practice for reporting entities to explain the reason for the time horizons that they select. The IPSASB considers that the extent of an entity's fiscal dependency on other entities for funding will have an impact on time horizons; the higher the level of fiscal dependency, the higher the likelihood of shorter time horizons.

BC19. The Consultation Paper included illustrative examples of tabular statements showing 75 year projections for key programs and activities. The IPSASB noted the view of some respondents that a focus on the position at the end of the time horizon may obscure events between the reporting date and the end of the time horizon. The IPSASB accepted this view and included guidance on the need to balance the qualitative characteristics of faithful representation and understandability and relevance in displaying projections in paragraph 2349.

⁷ For example, such entities might include school boards or bodies responsible for water and drainage.

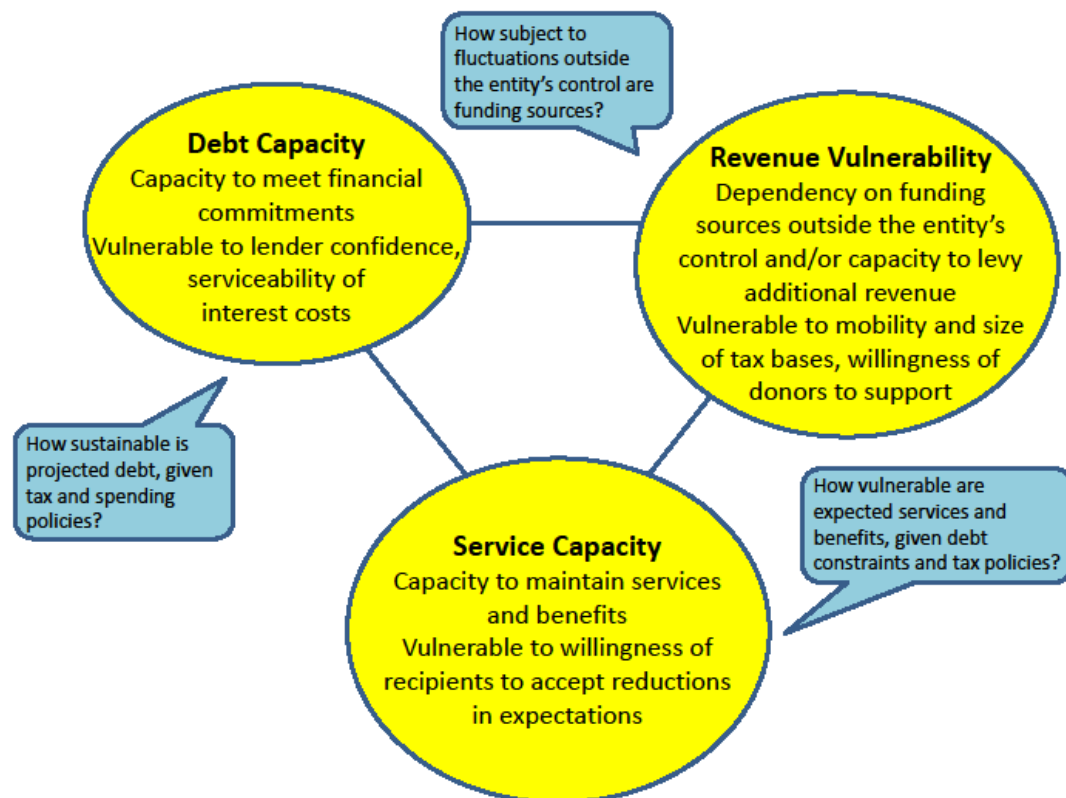
Addressing the Dimensions of Long-Term Fiscal Sustainability

- BC20. The IPSASB considered that providing a flexible framework for the disclosure of information might help entities to organize the way in which they communicate information and ensure that information is a faithfully representative of an entity's long-term fiscal sustainability information.
- BC21. ED 46 included three dimensions of long-term fiscal sustainability. The vulnerability definition was derived from the definition of vulnerability in Statement of Recommended Practice 4 (SORP-4), Indicators of Financial Condition issued by the Canadian Public Sector Accounting Board. The definition in SORP-4 is ~~The IPSASB also noted the PSAB's notion of "vulnerability" as~~ "the degree to which a government is dependent on sources of funding outside its control or influence or is exposed to risks that could impair its ability to meet its existing financial obligations both in respect of its service commitments to the public and financial commitments to creditors, employees and others." The IPSASB considered that a variant of this notion is particularly important for entities at sub-national levels which have limited taxation powers and are therefore exposed to decisions, over which they have no or very limited control, taken by other entities at other levels of government.
- BC22. When developing ED 46 into the RPG the IPSASB changed the name of the vulnerability dimension to "revenue vulnerability" to emphasize that this definition relates to changes in revenues while retaining its original aim of including a dimension that highlights the degree to which an entity is dependent on, and therefore vulnerable to, sources of funding outside its control or influence.
- BC23. The other two dimensions in ED 46 were derived from ~~The IPSASB noted the work done by the US Governmental Accounting Standards Board's (GASB)⁸ definitions of and the Canadian Public Sector Accounting Board (PSAB) in defining "components" and "elements" for reporting the long-term sustainability of an entity's finances. In particular the IPSASB considered that the GASB's notions of "fiscal capacity" and "service capacity," adopted in a slightly modified form.~~ The GASB define fiscal capacity as "the government's ability and willingness to meet its financial obligations as they come due on an ongoing basis" and service capacity as "the government's ability and willingness to meet its commitments to provide services on an ongoing basis."
- BC24. When developing ED 46 into the RPG, the IPSASB noted that the inclusion of the term "revenue" in the revenue vulnerability dimension has implications for the name of the fiscal capacity dimension because the dictionary definition of "fiscal" includes revenue.⁹ The definition of fiscal capacity relates to the ability of the entity to meet financial commitments, in other words, its ability to maintain and service its debt. Therefore the IPSASB decided that the name of the dimension should be changed to debt capacity to more closely reflect the definition.
- BC25. The relationship between these three dimensions can be illustrated in Diagram 1 below.

⁸ Preliminary Views of the Governmental Accounting Standards Board on Major Issues related to Economic Condition Reporting: Financial Projections, ~~Project on Economic Condition~~ (Governmental Accounting Standards Board: Norwalk, CT, USA, November 2011)

⁹ The definition of fiscal is "of or relating to taxation, public revenues, or public debt" (Webster's Ninth New Collegiate Dictionary, 1984).

Diagram 1: Relationship between the Dimensions of Long-Term Fiscal Sustainability



BC26. The IPSASB noted that the approach taken by these standard setters had similarities to the "dimensions" developed by Allen Schick¹⁰ and discussed in the Consultation Paper.

BC27. One of the dimensions that Schick discussed was "economic growth." The IPSASB considered that explicitly introducing a dimension of economic growth was inappropriate because the determinants of economic growth are complex and not under the control of the reporting entity. However, assumptions about economic growth will be critical to the development of projections and are likely to feature heavily in sensitivity analyses.

Disclosure of Principles and Methodologies

BC28. The Consultation Paper discussed the principles that should be adopted for the inclusion of programs and ~~transactions-activities~~ in reporting long-term fiscal sustainability ~~reporting information~~ and methodological approaches central to the outcome of projections. The areas addressed included whether projections should be based on current or future policy, the approach to revenue inflows, the approach to age-related and non-age-related programs and the approach to sensitivity analysis. The IPSASB considered whether, in order to meet the qualitative characteristic of comparability, the IPSASB should make firm recommendations on best-good practice ~~approaches~~.

BC29. The IPSASB did not consider it appropriate to make firm recommendations on best-good practice because (a) the scope of the RPG includes all public sector entities and practice that

¹⁰ Allen Schick, *Sustainable Budget Policy Concepts and Approaches* (OECD: Paris, 2008)

is appropriate at one level of government may not be suitable elsewhere in the public sector, (b) while reporting ~~on~~ long-term fiscal sustainability [information](#) has become a feature of financial management in an increasing number of jurisdictions it is at an early stage of development and (c) it is not the intention of the IPSASB to usurp the role of other professional groups with expertise in this area. In some cases the IPSASB has considered it appropriate to express a view on a preferred high level approach such as those projections are likely to be most useful when based on current policy [assumptions](#) and when they encompass both inflows as well as outflows. The IPSASB also noted that, at the national level, the Organisation for Economic Cooperation and Development has recommended that projections should be updated on an annual basis.

Option A: Current Legislation or Regulation with Specific Exceptions (see AP 4.1)

[Current and Future Policy Assumptions](#)

[BC29A.](#) Paragraphs 40–42 of ED 46 explain that an entity can depart from using current policy to calculate its projections (a) where there is a conflict between current policy and legal obligations and (b) where a policy has “sunset provisions.” A respondent to ED 46 raised a concern that the concept of current policy should be broader than that proposed in the ED to deal with issues such as fiscal drag.

[BC29B.](#) Fiscal drag refers to the phenomenon that income tax inflows grow faster than the income it is levied on because, as an individual's income grows, an increasing proportion of it is taxed at a higher rate. Fiscal drag occurs if the rates and thresholds for the taxation of individuals are not adjusted over time. Not addressing fiscal drag has the potential for an entity to overstate revenue inflows from taxation which would not reflect an entity's long-term fiscal sustainability position in a representationally faithful manner.

[BC29C.](#) The IPSASB considered permitting an additional departure from current policy where a policy has been changed in a consistent direction over time, to address the issue of fiscal drag. However, the IPSASB concluded that this exception to current policy would enable entities to have wide discretion over the number of departures from current policy thereby potentially enabling the calculation of projections to be subject to political interference. This could result in the projections presenting a misleading view of the entity's long-term fiscal sustainability.

[BC29D.](#) The IPSASB introduced the term “current policy assumptions” to clarify that current policy is assumed to continue (except for the three departures listed in the RPG) for inflows or outflows that are individually projected. Current policy assumptions means current legislation or regulation with departures from this being limited to: (a) where changes to current legislation or regulation have been enacted before the reporting date which have a specific implementation date within the time horizon of the projections, (b) where the provisions in current legislation or regulation are internally inconsistent (in ED 46 “a conflict in legal obligations”) and (c) where current legislation or regulation has “sunset provisions.”

[BC29E.](#) The IPSASB noted that an entity could present a baseline projection using current legislation or regulation and also present adjusted projections which show what policy proposals, such as those addressing fiscal drag, would do to the projections if they were enacted.

Option B: Current Legislation or Regulation with Departures where Appropriate (see AP 4.1)

Current and Future Policy Assumptions

BC29F. Paragraphs 40–42 of ED 46 explain that an entity can depart from using current policy to calculate its projections (a) where there is a conflict between current policy and legal obligations and (b) where a policy has “sunset provisions.” A respondent to ED 46 raised a concern that the concept of current policy should be broader than that proposed in the ED to deal with issues such as fiscal drag.

BC29G. Fiscal drag refers to the phenomenon that income tax inflows grow faster than the income it is levied on because, as an individual's income grows, an increasing proportion of it is taxed at a higher rate. Fiscal drag occurs if the rates and thresholds for the taxation of individuals are not adjusted over time. Not addressing fiscal drag has the potential for an entity to overstate revenue inflows from taxation which would not reflect an entity's long-term fiscal sustainability position in a representationally faithful manner.

BC29H. The IPSASB introduced the term “current policy assumptions” to clarify that current policy means current legislation or regulation with departures where appropriate for inflows or outflows that are individually projected. The RPG gives examples of where a departure may be appropriate.

BC29I. The IPSASB noted that the issue of fiscal drag does not need to be explicitly addressed in the core text of the draft RPG because an entity can depart from current legislation or regulation where appropriate. This approach means that where an entity considers that current policy will be changed in a specific direction, such as the increase in the thresholds for the application of progressive taxation, it can adjust its projections accordingly. The IPSASB also notes that paragraph 56(e) recommends that any departures from current legislation or regulation are disclosed together with the reasons for such departures.

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REPORTING ON THE LONG-TERM SUSTAINABILITY OF AN ENTITY'S FINANCES

CONTENTS

	Paragraph
Objective	1–3
Status and Scope	4–10
Definitions.....	11
Determining Whether to Report Long-Term Fiscal Sustainability Information.....	12–14
Reporting Boundary	15–16
Key Principles of Reporting Long-Term Fiscal Sustainability Information	17–20
Presenting Projections of Prospective Inflows and Outflows.....	21–27
Time Horizon	25–27
Addressing the Dimensions of Long-Term Fiscal Sustainability.....	28–39
Debt Capacity	31–33
Service Capacity.....	34–36
Revenue Vulnerability.....	37–39
Principles and Methodologies	40–51
Updating Projections and Frequency of Reporting.....	40
Impact of Legal Requirements and Policy Frameworks.....	41
Current and Future Policy Assumptions	42–48
Demographic and Economic Assumptions.....	49
Inflation and Discount Rates.....	50
Sensitivity Analysis	51
Disclosures.....	52–56
Appendix A: Glossary of Indicators	
Appendix B: Existing Definitions in IPSASs	
Basis for Conclusions	

Objective

1. Reporting on the long-term sustainability of an entity's finances ("reporting long-term fiscal sustainability information") provides information on the impact of current policies and decisions made at the reporting date and supplements information in the general purpose financial statements ("financial statements"). This Recommended Practice Guideline (RPG) provides guidance on the approach to reporting long-term fiscal sustainability information. The aim of such reporting is to provide an indication of the projected long-term sustainability of an entity's finances over a specified time horizon in accordance with transparent assumptions.
2. Long-term fiscal sustainability information is broader than information derived from the financial statements. It includes projected inflows and outflows related to the provision of goods and services and programs providing social benefits under current policy over a specified time horizon. It therefore takes into account decisions made by the entity on or before the reporting date that do not meet the definition and/or recognition criteria for liabilities. Similarly it takes into account future taxation receipts, contributions and inter-governmental transfers that do not meet the definition of, and/or recognition criteria for, assets.
3. Assessments of long-term fiscal sustainability involve using a broad range of data. These data include financial and non-financial information about current economic and demographic conditions, assumptions about country and global trends such as productivity, the relative competitiveness of the national, state or local economy and expected changes in demographic variables such as age, longevity, gender, income, educational attainment and morbidity.

Status and Scope

4. This RPG provides guidance on reporting long-term fiscal sustainability information. The reporting of information in accordance with this RPG represents good practice. An entity reporting long-term fiscal sustainability information is encouraged to follow this RPG. Compliance with this RPG is not required in order for an entity to assert that its financial statements comply with International Public Sector Accounting Standards (IPSASs) applicable to the financial statements.
5. The scope of this RPG includes an entity's projected flows. It is not limited to those flows related to programs providing social benefits. Nevertheless, this RPG acknowledges that the flows relating to programs providing social benefits, including entitlement programs that require contributions from participants, can be a highly significant component of reporting long-term fiscal sustainability information for many entities.
6. This RPG does not directly address issues associated with the reporting of environmental sustainability. However, an entity should assess any financial impacts of environmental factors and take them into account when developing its projections.
7. This RPG can apply to all public sector entities, except Government Business Enterprises (GBEs).
8. Although this RPG does not apply directly to GBEs, the prospective inflows and outflows to/from the entity from/to a GBE over the specified time horizon of the projections are within the scope of this RPG.
9. An entity whose long-term fiscal sustainability information complies with this RPG should make an explicit and unreserved statement of such compliance. Long-term fiscal sustainability information should not be described as complying with this RPG unless it complies with all the requirements of this RPG.

10. This RPG does not provide guidance on the level of assurance (if any) to which long-term fiscal sustainability information should be subjected.

Definitions

11. The following terms are used in this RPG with the meaning specified:

Debt capacity is the ability of the entity over the period of the projections to meet its financial commitments as they come due or to raise debt as necessary, based on current policy assumptions for service delivery to recipients and entitlements for beneficiaries, and for raising revenue from taxation and other sources.

Inflows are cash and cash equivalents projected to be received or accrued by the entity over the time horizon of the projections.

Long-term fiscal sustainability is the ability of an entity to meet service delivery and financial commitments both now and in the future.

Outflows are cash and cash equivalents projected to be paid or incurred by the entity over the time horizon of the projections.

A projection is prospective financial information prepared on the basis of the entity's current policy assumptions, and future economic and other conditions.

Service capacity is the ability of the entity over the period of the projections to maintain the volume and quality of services provided to recipients and meet obligations related to entitlement programs for beneficiaries, based on current policy assumptions for raising revenue from taxation and other sources, while remaining within debt constraints.

Revenue vulnerability is (a) the entity's dependency upon funding sources outside its control and (b) the ability of the entity to vary existing taxation levels or other revenue sources or to introduce new revenue sources, over the period of the projections, to finance current policy assumptions for service delivery to recipients and entitlements for beneficiaries, while remaining within debt constraints.

Determining Whether to Report Long-Term Fiscal Sustainability Information

12. In determining whether to report long-term fiscal sustainability information, an entity needs to assess which potential users exist for prospective financial information.
13. The relevance of reporting long-term fiscal sustainability information should be considered in the context of that entity's funding and capacity to determine service delivery levels. There are likely to be users for long-term fiscal sustainability information for entities with one or more of the following characteristics:
 - (a) Significant tax and/or other revenue raising powers;
 - (b) Powers to incur significant debt; or
 - (c) The power and ability to determine the nature, level and method of service delivery including the introduction of new services.
14. A controlled entity should ensure that the information reported is consistent with information reported by its controlling entity.

Reporting Boundary

15. An entity should use the same reporting boundary for reporting long-term fiscal sustainability information as that used for the financial statements. This enhances the understandability of projections and increases their usefulness to the users of general purpose financial reports (GPFRs).
16. An entity may report long-term fiscal sustainability information in respect of those entities that comprise the General Government Sector (GGS). This may be to enhance consistency and comparability with other jurisdictions or because there are other indicators that are used to assess long-term fiscal sustainability based on the GGS. Entities providing information on the GGS are encouraged to also present information in accordance with IPSAS 22, *Disclosure of Financial Information about the General Government Sector*.

Key Principles of Reporting Long-Term Fiscal Sustainability Information

17. Long-term fiscal sustainability information should enable users to form an overall assessment of the long-term fiscal sustainability of the entity, including the nature and extent of risks that the entity faces.
18. The form and content of an entity's long-term fiscal sustainability information will vary depending on the nature of the entity and the regulatory environment in which it operates. A single presentation approach is unlikely to satisfy the objectives of financial reporting. To meet the objectives¹ and qualitative characteristics² of financial reporting while taking into account the pervasive constraints³, long-term fiscal sustainability information will usually include the following components:
 - (a) Projections of prospective inflows and outflows displayed in tabular statements or graphical formats including a narrative discussion explaining the projections (see paragraphs 21–27 and 54);
 - (b) A narrative discussion of the dimensions of long-term fiscal sustainability including the indicators used to portray the dimensions (see paragraphs 28–39 and 55); and
 - (c) A narrative discussion of the principles, assumptions and approaches to methodology underlying the projections (see paragraphs 40–51 and 56).
19. The economic and other phenomena reported in long-term fiscal sustainability information generally occur under conditions of uncertainty. The projections are derived from models that rely on assumptions around which there is some uncertainty. To faithfully represent an entity's long-term fiscal sustainability information each input should reflect the best available information.

¹ The objectives of financial reporting by public sector entities are to provide information about the entity that is useful to users of general purpose financial reports for accountability purposes and for decision-making purposes. See Chapter 2 of the *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities* (the *Conceptual Framework*) for further details.

² The qualitative characteristics of financial reporting are relevance, faithful representation, understandability, timeliness, comparability, and verifiability. See Chapter 3 of the *Conceptual Framework* for further details.

³ Pervasive constraints on information included in GPFRs are materiality, cost-benefit, and achieving an appropriate balance between the qualitative characteristics. See Chapter 3 of the *Conceptual Framework* for further details.

20. Long-term fiscal sustainability information may be published as a separate report or as part of another report. It may be published at the same time as the entity's GPFs or at a different time.

Presenting Projections of Prospective Inflows and Outflows

21. An entity should present projections of prospective inflows and outflows, including capital expenditure, commencing in the current reporting period for a specified time horizon. The projections should be prepared on the basis of current policy assumptions and assumptions about future economic and other conditions.
22. An entity should assess the extent to which it can draw on the projections and indicators prepared by other entities, such as Ministries of Finance, rather than preparing the information itself, as this can reduce the cost of such reporting. Where an entity has a budget or forecast that meets the definition of a projection, this information can be used for the relevant time period or periods.
23. Projections can be displayed in tabular statements or graphical formats providing details of the programs and activities giving rise to outflows and identifying the sources of inflows. In determining the format of tabular statements entities need to balance considerations of understandability and relevance. Multi-columnar presentation of a large number of time periods between the reporting date and the end of the time horizon provides a more complete information set, but such a presentation increases the risk of information overload and the impairment of understandability. Projections of net debt are likely to be central for many entities.
24. An entity should ensure that its presentation of projections is not skewed to present a misleadingly favorable or unfavorable picture. The formats and terms used should also be consistent between reporting periods.

Time Horizon

25. In selecting an appropriate time horizon an entity needs to balance the qualitative characteristics of verifiability and faithful representation. The further the end of the time horizon is from the reporting date the more future events are captured. However, the assumptions underpinning the projections become less robust and potentially less verifiable. Conversely, excessively short time horizons may increase the risk that the consequences of events outside the time horizon may be ignored, thereby reducing the relevance of projections.
26. There is a strong relationship between dependence on other entities for funding and time horizons. Generally, high levels of dependence may lead to the selection of shorter time horizons, because a high proportion of the entity's prospective inflows are dependent upon decisions by other entities over which the entity has no control and limited influence.
27. Apart from dependence on other entities for funding, the length of the time horizon will reflect the characteristics of the entity. It is likely to be influenced by aspects such as the longevity of key programs, the estimated lives of major items of property, plant, and equipment, such as road networks, and the time horizons adopted by other comparable entities providing prospective information.

Addressing the Dimensions of Long-Term Fiscal Sustainability

28. An entity reporting long-term fiscal sustainability information should include a narrative discussion on the dimensions of long-term fiscal sustainability. This RPG discusses three inter-related dimensions of long-term fiscal sustainability:
- Debt capacity;
 - Service capacity; and
 - Revenue vulnerability.
29. The dimensions are inter-related and changes in one dimension affect the other dimensions. For example, future services and entitlements to beneficiaries (service capacity) are funded either by maintaining or raising debt (debt capacity) or by maintaining or raising revenue from taxation and other sources (revenue vulnerability). The dimensions also highlight the entity's vulnerability to market expectations and economic conditions, changes in public demand for services, and dependency on revenue streams.
30. An entity can use indicators to portray various dimensions of long-term fiscal sustainability. An entity should choose its indicators based on their relevance to the entity. Examples of indicators are provided in the Glossary of Indicators in Appendix A.

Debt Capacity

31. *Debt capacity* is the ability of the entity over the period of the projections to meet its financial commitments as they come due or to raise debt as necessary, based on current policy assumptions for service delivery to recipients and entitlements for beneficiaries, and for raising revenue from taxation and other sources.
32. The level of net debt is important for an assessment of debt capacity, as, at any reporting date, it represents the amount expended on the past provision of goods and services that has to be financed in the future. By projecting current policy assumptions for the provision of goods and services, and for raising revenue from taxation and other sources, projected levels of net debt can be presented. Users can then assess the entity's ability to raise and maintain such levels of debt and thereby evaluate debt capacity.
33. At national levels a factor to consider in presenting such projections is whether to distinguish: (a) the primary balance, which is total projected government spending, excluding interest payable on debt, minus tax revenues, and (b) the overall balance, which is the primary balance including outflows related to interest payable on debt. At sub-national levels the focus may be on net debt as a percentage of total revenues. Increases in this indicator show that an increasing proportion of revenues will be required for debt servicing, thereby diverting resources from service delivery, and that the long-term fiscal position may become unsustainable.

Service Capacity

34. *Service capacity* is the ability of the entity over the period of the projections to maintain the volume and quality of services provided to recipients and meet obligations related to entitlement programs for beneficiaries, based on current policy assumptions for raising revenue from taxation and other sources, while remaining within debt constraints.

35. By projecting the impact of current policy assumptions for raising revenue from taxation and other sources, and for raising and maintaining debt, long-term fiscal sustainability information can present the amounts available for the provision of goods and services under these policies. Users can contrast this information with the entity's service delivery commitments, and thereby evaluate service capacity.
36. A factor to consider in making such comparisons is the extent to which expenditure on certain programs is likely to increase more steeply than the overall levels of expenditure of the entity. This may be because the number of beneficiaries is projected to increase for a particular program or because costs associated with certain programs, such as healthcare, are projected to increase more quickly than the general inflation rate. For capital intensive activities the dimension of service capacity also involves an assessment of the useful lives and replacement cycles of items of property, plant, and equipment to assess whether service capacity is increasing or decreasing.

Revenue Vulnerability

37. *Revenue vulnerability* is (a) the entity's dependency upon funding sources outside its control and (b) the ability of the entity to vary existing taxation levels or other revenue sources or to introduce new revenue sources, over the period of the projections, to finance current policy assumptions for service delivery to recipients and entitlements for beneficiaries, while remaining within debt constraints.
38. An example of an indicator for revenue vulnerability is the proportion of total revenues that are received from entities at other levels of government or from international organizations. For example, a local government entity may be able to raise property taxes, but be partially dependent upon a mixture of general grants and specific grants from national and/or state governments. As policies for the provision of goods and services and for managing debt are projected into the future, the level of revenue required to fund such policies can be presented. Users can then assess the entity's ability to raise and maintain its levels of revenue and thereby evaluate revenue vulnerability.
39. Generally, an entity which has a limited ability to vary levels of revenue from taxation and other sources is likely to have high revenue vulnerability. If inter-governmental transfers have constitutional or other legal underpinning, this may make the entity less susceptible to sudden adverse funding decisions by other entities and therefore increase the probability of continuing to receive funds. Trends indicating that revenue vulnerability is increasing may suggest that an entity's future sustainability is dependent upon funding decisions by entities at other levels of government.

Principles and Methodologies

Updating Projections and Frequency of Reporting

40. While regular updates are desirable, this RPG acknowledges that annual updating may not be realistic for all entities. However, there is generally an inverse relationship between the robustness of assumptions on which projections are made and the amount of time since they were made. During periods of global financial volatility the risk that projections made some time before the reporting date are outdated increases, with a consequent reduction of the ability of such information to meet the objectives of accountability and decision-making. In this situation, an entity should consider updating its projections on a more frequent basis. An entity should also consider updating its projections after significant or major unexpected events such as natural disasters or other emergencies.

Impact of Legal Requirements and Policy Frameworks

41. In some jurisdictions reporting long-term fiscal sustainability information is governed by a legal or regulatory framework that applies at the national or state level. There may also be legal requirements for local government. These might include balanced budget requirements. These requirements are likely to specify or otherwise affect the principles, assumptions and approaches an entity should use in calculating its projections.

Current and Future Policy Assumptions

Option A: Current Legislation or Regulation with Specific Exceptions (see AP 4.1)

42. Where flows for particular programs and activities are individually modeled, the policy assumptions should be based on the continuation of current legislation or regulation except for the specific exceptions listed below and those assumptions~~policy. That policy~~ should be held constant through-out the entire projection period ("current policy assumptions"). ~~However, there may be instances where a departure from current legislation or regulation is permitted in the following circumstances may be appropriate:~~
- (a) Where changes to current legislation or regulation have been enacted before the reporting date which have a specific implementation date within the time horizon of the projections~~a policy has been changed in a consistent direction over time;~~
 - (b) Where the provisions in current legislation or regulation are internally inconsistent~~there is a conflict between current policy and legal obligations;~~ or
 - (c) Where current legislation or regulation~~a policy~~ has "sunset provisions".

Option B: Current Legislation or Regulation with Departures where Appropriate (see AP 4.1)

42. Where flows for particular programs and activities are individually modeled, the policy assumptions should be based on the continuation of current legislation or regulation with departures where appropriate and those assumptions~~policy. That policy~~ should be held constant through-out the entire projection period ("current policy assumptions"). The starting point for current policy assumptions should be current legislation or regulation. However, there may be instances where a departure from current legislation or regulation~~policy~~ may be appropriate, as follows for example:
- (a) Where changes to current legislation or regulation have been enacted before the reporting date which have a specific implementation date within the time horizon of the projections~~a policy has been changed in a consistent direction over time;~~
 - (b) Where the provisions in current legislation or regulation are internally inconsistent~~there is a conflict between current policy and legal obligations;~~ or
 - (c) Where current legislation or regulation~~a policy~~ has "sunset provisions".

43. Current policy assumptions may be affected by legal changes that have been enacted before the reporting date which have a specific implementation date within the time horizon of the projections. In these circumstances, assuming current legislation or regulation remains in force for the entire projection period will not be appropriate.

44. An example of current legislation or regulation that is internally inconsistent is a social security program which has legal provisions that make it unlawful to make payments once an earmarked fund is exhausted, although entitlements of beneficiaries will continue after the exhaustion of that fund. Assuming that the fund will not meet obligations once it is exhausted might reflect a strict legal position, but an entity may need to assess whether the presentation of projections on such a basis underestimates projected outflows and therefore the extent of the fiscal challenge facing the social security program. In this situation an entity may calculate its projections based on current policy assumptions despite legal restrictions.
45. Current legislation or regulation may have sunset provisions whereby it terminates after a specific period. In many cases there may be a strong probability that such programs will be replaced by similar programs. Adopting a strict legal termination principle could underestimate projected outflows, and therefore impair the usefulness of the information.

Approach to Revenue Inflows

46. Significant revenue inflows from taxation and other sources, such as inter-governmental transfers, may be individually modeled based on current policy assumptions. Significant sources of taxation and other revenue inflows that are not modeled individually are projected to grow (or diminish) in line with gross domestic product (GDP) or another index such as the inflation index.
47. Other revenue inflows, such as royalties from natural resources, may also be projected to grow in line with GDP or an inflation index. They may also be individually modeled to address specific circumstances, such as when the natural resource is expected to be depleted.

Approach to Age-Related and Non-Age-Related Programs

48. Age-related programs are often subject to eligibility criteria including age and other demographic factors. In making projections, programs and activities that are age-related may be distinguished from non-age related programs. Age-related programs may be individually modeled while non-age-related programs may be projected to increase in line with other variables, such as GDP, or to be constant in real terms. Such an approach to non-age-related programs provides some flexibility, as it allows above GDP/real terms increases in some programs and activities to be offset by lower increases or spending declines in other areas.

Demographic and Economic Assumptions

49. Demographic assumptions are likely to include fertility, mortality and migration rates, and workforce participation rates. Economic assumptions are likely to include economic growth rates and inflation. Other economic assumptions may include environmental factors, such as the impact of the depletion and degradation of ecosystems and the depletion of water and finite natural resources on economic growth.

Inflation and Discount Rates

50. There are two main approaches to incorporating the effect of price inflation in projections. It may be taken into account in making projections or projections may be made at current prices (i.e., prices prevailing at the reporting date). If the projections include inflation, then the discount rate should also include inflation. If the projections are at current prices, the discount rate should exclude inflation.

Sensitivity Analysis

51. Many assumptions on which projections are based are inherently uncertain. In some cases small changes in variables can have significant impacts on the projections. The use of sensitivity analysis will help users to understand the impact of significant changes in demographic and economic assumptions on the projections.

Disclosures

52. The entity should disclose information that enables users of its long-term fiscal sustainability information to assess the projected long-term fiscal sustainability of the entity. An entity should make any additional disclosures necessary to meet the objectives of financial reporting.
53. An entity should disclose the following information:
- (a) The name of the entity;
 - (b) The financial statements to which the long-term fiscal sustainability information relates;
 - (c) Where different, the names of the entities within the reporting boundary for long-term fiscal sustainability information that are different to those for the financial statements;
 - (d) Where the entity is a controlled entity, the identity of the controlling entity;
 - (e) The date at which a full set of projections was made;
 - (f) The basis and timing of subsequent updating; and
 - (g) When an entity uses projections and indicators prepared by other entities, the names of those entities.
54. The narrative discussion of the projections should include disclosure of the following information:
- (a) The sources of significant revenue inflows from taxation and other sources;
 - (b) An overview of the current policy assumptions for the sources of significant revenue inflows from taxation and other sources, such as taxation threshold levels and allowances;
 - (c) The sources of significant outflows including capital expenditure;
 - (d) An overview of the current policy assumptions for the significant outflows including capital expenditure;
 - (e) An explanation of the changes in projections between reporting dates and the reasons for those changes;
 - (f) An explanation that it is unlikely that projections over the specified time horizon will match the actual outcome and the extent of the difference will depend upon a range of factors, including the future actions of the entity in meeting any identified fiscal challenge;
 - (g) An entity should explain any modifications of formats between reporting periods and the reasons for such changes;
 - (h) The time horizon used for the projections and the reasons for selecting that time horizon; and
 - (i) Where an entity changes the time horizon from that used in the previous reporting period, the reason for such a change.

55. The narrative discussion of the dimensions of long-term fiscal sustainability should include disclosure of the following information:
- (a) An analysis of significant changes in the indicators compared with those of the previous reporting period;
 - (b) Changes in the indicators used to report long-term fiscal sustainability information from the previous reporting period, and the reasons for such changes;
 - (c) Where an entity uses indicators that are based on amounts derived from non-IPSAS based sources, the indicators affected and, where possible, the estimated impact on the indicators;
 - (d) The main entities on which the entity is dependent on funding; and
 - (e) Details of constitutional or other legal underpinning for taxation and other revenue or grant arrangements.
56. An entity should disclose the principles, assumptions and approaches to methodology that underpin the projections including the following information:
- (a) Key aspects of governing legislation and regulation;
 - (b) Underlying macro-economic policy and fiscal frameworks including details of where other publicly available reports on these policies and frameworks can be accessed, including documents outside the GPFRs;
 - (c) The key current policy assumptions and the key demographic and economic assumptions that underpin the projections;
 - (d) Its policy for reviewing and updating current policy assumptions and, demographic and economic assumptions;
 - (e) An explanation of the significant current policy assumptions that depart from current legislation or regulation;
 - (f) An explanation of significant changes in the principles, assumptions and approaches to methodologies from the previous reporting period, the nature and extent of these changes, and the reasons for such changes;
 - (g) The results of any sensitivity analyses that could have a significant impact on the projections;
 - (h) The discount rates applied and the basis on which the discount rate has been determined; and
 - (i) The approach to inflation and the reason for this approach.

Appendix A

Glossary of Indicators

Government Finance Statistics Reporting Guidelines

This Appendix lists examples of indicators. It is not intended to be an exhaustive list. Where an indicator includes a defined term, that term is shown in *italics* and its definition is shown after the indicators.

- **Gross debt, total:** Total gross debt—often referred to as “total debt” or “total debt liabilities”—consists of all *liabilities* that are *debt instruments*. A debt instrument is defined as a financial claim that requires payment(s) of interest and/or principal by the debtor to the creditor at a date, or dates, in the future. (Source: International Monetary Fund: *Public Sector Debt Statistics—Guide for Compilers and Users* 2011)
- **Net debt:** Net debt is calculated as gross debt minus *financial assets* corresponding to *debt instruments*. (Source: International Monetary Fund: *Public Sector Debt Statistics—Guide for Compilers and Users*: 2011)
- **Net financial worth:** Net financial worth of an *institutional unit* (or grouping of units) is the total value of its *financial assets* minus the total value of its outstanding *liabilities*. (Source: International Monetary Fund: *Public Sector Debt Statistics—Guide for Compilers and Users*: 2011)
- **Net worth:** Net worth of an *institutional unit* (or grouping of units) is the total value of its *assets* minus the total value of its outstanding *liabilities*. (Source: International Monetary Fund: *Public Sector Debt Statistics—Guide for Compilers and Users*: 2011)
- **Overall balance:** This term corresponds to the GFS 1986 terminology of “Overall Deficit/Surplus,” which is defined as revenue plus grants received less expenditure less “lending minus repayments.” The balance so defined is equal (with an opposite sign) to the sum of net borrowing by the government, plus the net decrease in government cash, deposits, and securities held for liquidity purposes. The basis of this balance concept is that government policies are held to be deficit- or surplus-creating, and thus the revenue or expenditures associated with these policies are “above the line.” Borrowing or a rundown of liquid assets, however, is deficit financing or “below the line.” It should be noted that the term **lending minus repayments** included above the line covers government transactions in debt and equity claims on others undertaken for purposes of public policy rather than for management of government liquidity or earning a return. (Source: International Monetary Fund: *Manual on Fiscal Transparency* (2007))
- **Primary balance:** The overall balance, excluding interest payments. Since interest payments represent the cost of past debt, and the determinants of future debt that are under policy control of government are other spending and revenue measures exclusive of interest payment, the primary balance is of particular importance as an indicator of the fiscal position in countries with high levels of debt. (Source: International Monetary Fund: *Manual on Fiscal Transparency* (2007))

Underlying Definitions

- **Debt instrument:** A debt instrument is defined as a financial claim that requires payment(s) of interest and/or principal by the debtor to the creditor at a date, or dates, in the future. (Source: International Monetary Fund: *Public Sector Debt Statistics—Guide for Compilers and Users* 2011)
- **Economic assets:** Economic assets are entities (i) over which economic ownership rights are enforced by institutional units, individually or collectively, and (ii) from which economic benefits may

be derived by their owners by holding them or using them over a period of time. (Source: International Monetary Fund: *Public Sector Debt Statistics—Guide for Compilers and Users* 2011)

- **Financial assets:** Financial assets consist of financial claims plus gold bullion held by monetary authorities as a reserve asset. A financial claim is an asset that typically entitles the owner of the asset (the creditor) to receive funds or other resources from another unit, under the terms of a liability. (Source: International Monetary Fund: *Public Sector Debt Statistics—Guide for Compilers and Users* 2011)
- **Institutional unit:** An institutional unit is an economic entity that is capable, in its own right, of owning assets, incurring liabilities, and engaging in economic activities and in transactions with other entities. (Source: International Monetary Fund: *Public Sector Debt Statistics—Guide for Compilers and Users* 2011)
- **Liability:** A liability is established when one unit (the debtor) is obliged, under specific circumstances, to provide funds or other resources to another unit (the creditor). (Source: International Monetary Fund: *Public Sector Debt Statistics—Guide for Compilers and Users* 2011)

Other Sources

- **Fiscal gap:** The **fiscal gap** is the change in non-interest spending and/or receipts that would be necessary to maintain public debt at or below a target percentage of gross domestic product (GDP).⁴ More specifically, the fiscal gap is the net present value of projected spending⁵ minus projected receipts, adjusted by the decrease (or increase) in public debt required to maintain public debt at or below the target percentage of GDP for the stated projection period. (Source: US Federal Accounting Standards Advisory Board: Statement of Federal Financial Accounting Standards 36: *Comprehensive Long-Term Projections for the U.S. Government* 2009)
- **Inter-temporal budget constraint:** The inter-temporal budget constraint is satisfied if the projected outflows of the government (current public debt and the discounted value of all future expenditure, including the projected increase in age-related expenditure) are covered by the discounted value of all future government revenue. (Source European Commission: *Sustainability Report* 2009))
- **Net Debt/Total Revenues:** Net debt as a proportion of total revenues. (Source Canadian Public Sector Accounting Board (PSAB): Statement of Recommended Practice 4 (SORP 4), *Indicators of Financial Condition*: 2009)

⁴ GDP is the total market value of all final goods and services produced domestically during a given period of time. The components of GDP are: private sector consumption and investment, government consumption and investment, and net exports (exports-imports).

⁵ Since interest is factored into the present value calculation, the fiscal gap as a share of spending is expressed as a share of spending excluding interest ("non-interest spending").

Appendix B

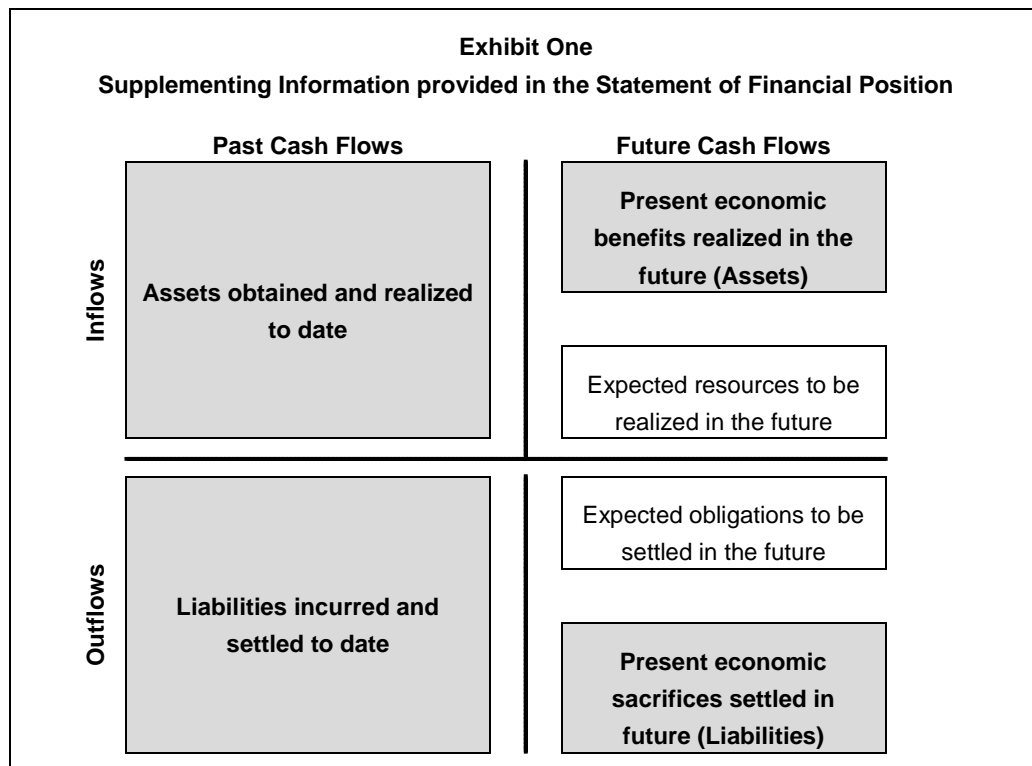
Existing Definitions in IPSASs

Term	Definition	Paragraph reference in this RPG
Assets	Resources controlled by an entity as a result of past events and from which future economic benefits or service potential are expected to flow to the entity.	2
Cash	Comprises cash on hand and demand deposits.	11
Cash equivalents	Short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.	11
Controlled entity	An entity, including an unincorporated entity such as a partnership, which is under the control of another entity (known as the controlling entity).	14
Controlling entity	An entity that has one or more controlled entities.	14
Government Business Enterprise	An entity that has all the following characteristics: (a) Is an entity with the power to contract in its own name; (b) Has been assigned the financial and operational authority to carry on a business; (c) Sells goods and services, in the normal course of its business, to other entities at a profit or full cost recovery; (d) Is not reliant on continuing government funding to be a going concern (other than purchases of outputs at arm's length); and (e) Is controlled by a public sector entity.	7
General government sector	Comprises all organizational entities of the general government as defined in statistical bases of financial reporting.	16
Liabilities	Present obligations of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits or service potential.	2
Reporting date	The date of the last day of the reporting period to which the financial statements relate.	1
Revenue	The gross inflow of economic benefits or service potential during the reporting period when those inflows result in an increase in net assets/equity, other than increases relating to contributions from owners.	11

Basis for Conclusions

Background

- BC1. The IPSASB initially launched a project on accounting for social policy obligations (subsequently re-termed social benefits) in 2002. This led to the publication of an Invitation to Comment (ITC), *Accounting for Social Policies of Governments*, in January 2004. Following an analysis of responses to that ITC, the IPSASB began to develop proposals for accounting for obligations related to different sub-categories of social benefits. In late 2006, due to failure to agree on recognition points and measurement requirements for liabilities, the IPSASB decided not to develop further proposals on recognition and measurement at that time.
- BC2. As an interim step the IPSASB developed proposals for the disclosure of amounts to be transferred to those eligible at the reporting date for cash transfers (benefits settled in cash). It expressly did not propose the disclosure of obligations and liabilities. ED 34, *Social Benefits: Disclosure of Cash Transfers to Individuals or Households* was issued in March 2008.
- BC3. The deliberations on identifying the point at which liabilities for social benefits arise had led the IPSASB to the view that the financial statements cannot provide all the information that users need on social benefits. This is illustrated in Exhibit One below where the shaded boxes indicate information provided in the financial statements. The IPSASB considered that before launching any further project it should consult constituents. Therefore the IPSASB raised this issue in a further Consultation Paper, *Social Benefits: Issues in Recognition and Measurement* and issued a Project Brief, *Long-Term Fiscal Sustainability Reporting*. Both these documents were issued at the same time as ED 34.



- BC4. In October 2008 the IPSASB reviewed responses to all of the above documents. In the light of these responses, it was decided not to develop ED 34 into an IPSAS. The IPSASB also noted that a large majority of respondents agreed that the financial statements cannot convey sufficient information to users about the long-term financial implications of governmental programs providing social benefits.⁶ In light of this view the IPSASB decided to initiate a project on long-term fiscal sustainability (subsequently re-termed "Reporting on the Long-Term Sustainability of Public Finances"). This led to the issue of a Consultation Paper, *Reporting on the Long-Term Sustainability of Public Finances*, in November 2009. Drawing on existing practice the Consultation Paper put forward the case for reporting long-term fiscal sustainability information, made suggestions on how such information might be presented and sought the views of constituents. The majority of respondents to the Consultation Paper favored the continuation of the project, although many said that they preferred the IPSASB to develop guidelines rather than requirements.
- BC5. Further work on proposals for the recognition and measurement of liabilities arising from obligations to deliver social benefits is progressing indirectly in Phase 2 of the *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities* project. This phase deals with elements, and includes the development of the definition of a liability and other relevant issues such as whether the power to tax is an asset. This work is likely to influence the approach to recognizing and measuring liabilities related to social benefits.
- BC6. In light of the responses to the Consultation Paper, the IPSASB developed Exposure Draft (ED) 46 Recommended Practice Guideline (RPG), *Reporting on the Long-Term Sustainability of a Public Sector Entity's Finances* which was issued in October 2011. This ED proposed non-authoritative guidance for public sector entities reporting long-term fiscal sustainability information.
- BC7. The IPSASB has further developed its thinking on reporting long-term fiscal sustainability information in the course of its project on *The Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities*. Chapter 2: Objectives and Users of General Purpose Financial Reporting reflects the view that, although the financial statements are at the core of financial reporting, a more comprehensive scope is necessary to meet the needs of users. That scope includes prospective financial information. The IPSASB has also noted that projected outflows relating to obligations as a result of past decisions and projected inflows related to sovereign powers and taxation powers may not be recognized or may only be partially recognized in the statement of financial position and the statement of financial performance. Therefore, in order to meet the objectives of accountability and decision-making, users need information on prospective inflows and outflows in order to supplement information on the entity's financial position in the financial statements.
- BC8. The IPSASB acknowledges that the rationale for reporting long-term fiscal sustainability information in paragraph BC7 might indicate that for some entities such reporting should be required. However, the IPSASB concluded that it would be premature to issue an

⁶ Further work on proposals for the recognition and measurement of liabilities arising from obligations to deliver social benefits is progressing indirectly in Phase 2 of the *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities* project. This phase deals with elements, and includes the development of the definition of a liability and other relevant issues such as whether the power to tax is an asset. This work is likely to influence the approach to recognizing and measuring liabilities related to social benefits.

authoritative pronouncement, because reporting long-term fiscal sustainability information in general purpose financial reports (GPFRs) is an area where practice is developing and the IPSASB wishes to encourage innovative and flexible approaches. Consistent with the views of the majority of respondents to the Consultation Paper, the majority of respondents to ED 46 supported the voluntary application of this guidance.

Scope

- BC9. The IPSASB considered whether the scope of the RPG should be limited to the consolidated national and whole-of-government levels. The IPSASB acknowledged that reporting long-term fiscal sustainability information is particularly relevant at these levels, but concluded that there might be significant user demand for such information at sub-national levels. The IPSASB therefore concluded that a narrow scope limited to the national and whole-of-government levels is not justified.

Definitions

Long-Term Fiscal Sustainability

- BC10. The Consultation Paper noted that there is no universally accepted definition of long-term fiscal sustainability and included a working definition that long-term fiscal sustainability is “the ability of government to meet its service delivery and financial commitments both now and in the future.” The IPSASB acknowledged the view that this definition is insufficiently rigorous and that a definition should be adopted that provides users with a clearer indication whether an entity's current economic position is sustainable. Such an approach might involve (a) linking current service delivery levels and the settling of obligations relating to entitlement programs to the maintenance of current taxation levels and (b) focusing on projected debt paths. An entity that can only maintain current service delivery levels and meet entitlement obligations and financial obligations by increasing taxation or current debt levels is identified as being in an unsustainable position. Macro-economists tend to adopt this more rigorous approach and focus on “explosive” debt paths, which is a term that connotes that existing service levels and existing benefits from entitlement programs cannot be sustained without major increases in levels of indebtedness.
- BC11. The IPSASB decided to retain the definition of long-term fiscal sustainability used in the Consultation Paper for ED 46 except for widening the scope to reflect that it can apply to all public sector entities (except Government Business Enterprises) rather than limiting it to governments. In coming to this conclusion the IPSASB noted the need for governments and public sector entities to both (a) provide services and meet obligations relating to entitlement programs and (b) meet financial obligations, principally debt servicing. The IPSASB also noted the sovereign power of government to legislate for new taxation sources and to vary the levels of existing taxation, while acknowledging that in a global environment the ability to increase taxation might be practically constrained by a number of considerations. The IPSASB took the view that, provided an entity gives appropriate attention to the dimensions of debt capacity and service capacity, as highlighted in paragraphs 31–36, users will be given adequate information that an entity cannot maintain existing service levels, meet obligations to the current and future beneficiaries of entitlement programs and meet financial obligations without increasing revenue from taxation and other sources or increasing borrowing.

Projection

BC12. Several respondents to ED 46 suggested that the relationship between projections, budgets and forecasts should be clarified. Given that there are no universally accepted definitions of these terms, the IPSASB decided to develop a definition of projection to clarify the characteristics of information that should be used in calculating the projections. The IPSASB considers that the key characteristics of a projection is that it:

- (a) Is prospective financial information;
- (b) Should be based on current policy assumptions (as that term is explained in paragraphs 42–48 of the RPG); and
- (c) Should be based on assumptions about economic and other conditions such as demographic conditions.

Determining Whether to Report Long-Term Fiscal Sustainability Information

BC13. As discussed in paragraph BC9 the IPSASB concluded that the scope of the RPG should not be limited to particular levels of government. However, the IPSASB acknowledged that reporting long-term fiscal sustainability information might not be appropriate for all entities. The IPSASB considered this issue at length.

BC14. The Consultation Paper questioned whether reporting long-term fiscal sustainability information is appropriate for individual controlled entities. This reservation was based on a tentative view that (a) the cost of producing the information for such entities is likely to be greater than the benefits to users, (b) the production of separate reports and disclosures by individual entities within an economic entity might be confusing to users and (c) it could be misleading if entities with limited tax-raising powers and a dependency for resources on entities at other tiers of government provide projections that are contingent on taxation decisions over which they have little or no control. Some respondents to the Consultation Paper challenged this view and suggested that there are cases where users for long-term fiscal sustainability information of controlled entities can be identified. The example of a local government entity controlled by a state or provincial government was cited. These respondents proposed that the test for whether an entity reports long-term fiscal sustainability information should be to assess which potential users exist for this type of information. The IPSASB was persuaded by these arguments and the RPG reflects these views in paragraphs 12–14.

BC15. The IPSASB acknowledged that direct evidence of the existence of users of long-term fiscal sustainability information might not be readily available. The IPSASB considered what proxies might indicate the existence of users. The IPSASB concluded that there are likely to be users for long-term fiscal sustainability information for entities with one of more of the following characteristics:

- (a) Significant tax and/or other revenue raising powers;
- (b) Powers to incur significant debt; or
- (c) The power to determine the nature, level and method of service delivery including the introduction of new services.

BC16. The IPSASB believes that reporting long-term fiscal sustainability information is likely to be relevant at the whole of government level, consolidated national level, and for major sub-

national entities such as regions, provinces, states and large local government entities (for examples, cities), which have tax raising powers enabling them to generate a significant proportion of their total revenues. The IPSASB remains of the view that reporting long-term sustainability information is unlikely to be appropriate for individual government departments. This is because often they do not have tax raising powers, their expenditure is controlled through appropriations, and they do not have powers to incur debt.

Presenting Projections of Prospective Inflows and Outflows

- BC17. The Consultation Paper considered three models for reporting long-term fiscal sustainability information and suggested that (a) the provision of additional statements providing details of projections and (b) summarized projections in narrative reporting were appropriate. Some respondents suggested that, although the Consultation Paper acknowledged that these reporting approaches were not mutually exclusive, the IPSASB should highlight that reporting long-term fiscal sustainability information just by displaying projections in statements is insufficient to meet user needs and that other presentation methods need to be deployed. The IPSASB was persuaded by this view and it is reflected in paragraph 18.
- BC18. The IPSASB considered whether it should recommend time horizons for projections for entities at particular levels of government. It acknowledged the view that standard time horizons for particular types of public sector entity might enhance comparability. The IPSASB decided that such benchmarks would be over-prescriptive and impractical. The scope of the RPG is such that standard time horizons would have to be determined for a wide range of entities, including single-purpose entities.⁷ In addition the fiscal autonomy of entities at the same level of government can differ markedly between jurisdictions. The IPSASB concluded, however, that it is good practice for entities to explain the reason for the time horizons that they select. The IPSASB considers that the extent of an entity's dependency on other entities for funding will have an impact on time horizons; the higher the level of dependency, the higher the likelihood of shorter time horizons.
- BC19. The Consultation Paper included illustrative examples of tabular statements showing 75 year projections for key programs and activities. The IPSASB noted the view of some respondents that a focus on the position at the end of the time horizon may obscure events between the reporting date and the end of the time horizon. The IPSASB accepted this view and included guidance on the need to balance the qualitative characteristics of understandability and relevance in displaying projections in paragraph 23.

Addressing the Dimensions of Long-Term Fiscal Sustainability

- BC20. The IPSASB considered that providing a flexible framework for the disclosure of information might help entities to organize the way in which they communicate information and ensure that information is a faithful representation of an entity's long-term fiscal sustainability information.
- BC21. ED 46 included three dimensions of long-term fiscal sustainability. The vulnerability definition was derived from the definition of vulnerability in Statement of Recommended Practice 4 (SORP-4), *Indicators of Financial Condition* issued by the Canadian Public Sector Accounting Board. The definition in SORP-4 is "the degree to which a government is dependent on

⁷ For example, such entities might include school boards or bodies responsible for water and drainage.

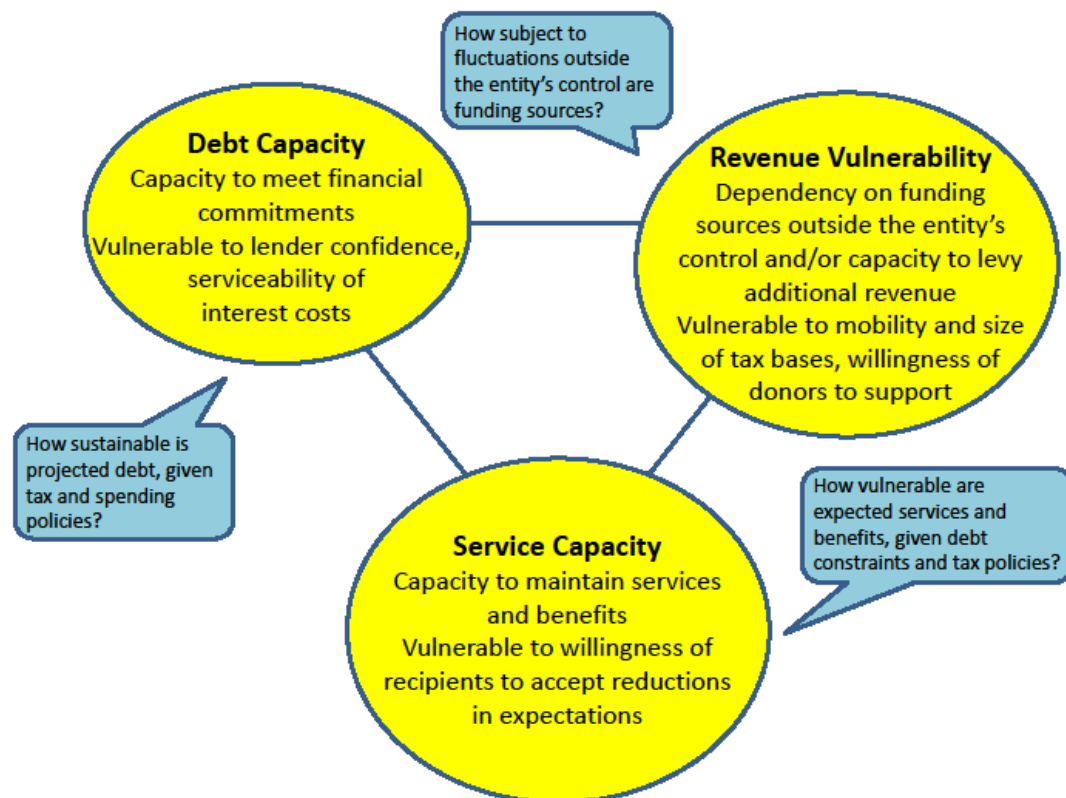
sources of funding outside its control or influence or is exposed to risks that could impair its ability to meet its existing financial obligations both in respect of its service commitments to the public and financial commitments to creditors, employees and others.” The IPSASB considered that a variant of this notion is particularly important for entities at sub-national levels which have limited taxation powers and are therefore exposed to decisions, over which they have no or very limited control, taken by other entities at other levels of government.

- BC22. When developing ED 46 into the RPG the IPSASB changed the name of the vulnerability dimension to “revenue vulnerability” to emphasize that this definition relates to changes in revenues while retaining its original aim of including a dimension that highlights the degree to which an entity is dependent on, and therefore vulnerable to, sources of funding outside its control or influence.
- BC23. The other two dimensions in ED 46 were derived from the US Governmental Accounting Standards Board’s (GASB)⁸ definitions of “fiscal capacity” and “service capacity.” The GASB define fiscal capacity as “the government’s ability and willingness to meet its financial obligations as they come due on an ongoing basis” and service capacity as “the government’s ability and willingness to meet its commitments to provide services on an ongoing basis.”
- BC24. When developing ED 46 into the RPG, the IPSASB noted that the inclusion of the term “revenue” in the revenue vulnerability dimension has implications for the name of the fiscal capacity dimension because the dictionary definition of “fiscal” includes revenue.⁹ The definition of fiscal capacity relates to the ability of the entity to meet financial commitments, in other words, its ability to maintain and service its debt. Therefore the IPSASB decided that the name of the dimension should be changed to debt capacity to more closely reflect the definition.
- BC25. The relationship between these three dimensions can be illustrated in Diagram 1 below.

⁸ *Preliminary Views of the Governmental Accounting Standards Board on Major Issues related to Economic Condition Reporting: Financial Projections.* (Governmental Accounting Standards Board: Norwalk, CT, USA, November 2011)

⁹ The definition of fiscal is “of or relating to taxation, public revenues, or public debt” (Webster’s Ninth New Collegiate Dictionary, 1984).

Diagram 1: Relationship between the Dimensions of Long-Term Fiscal Sustainability



BC26. The IPSASB noted that the approach taken by these standard setters had similarities to the "dimensions" developed by Allen Schick¹⁰ and discussed in the Consultation Paper.

BC27. One of the dimensions that Schick discussed was "economic growth." The IPSASB considered that explicitly introducing a dimension of economic growth was inappropriate because the determinants of economic growth are complex and not under the control of the reporting entity. However, assumptions about economic growth will be critical to the development of projections and are likely to feature heavily in sensitivity analyses.

Principles and Methodologies

BC28. The Consultation Paper discussed the principles that should be adopted for the inclusion of programs and activities in reporting long-term fiscal sustainability information and methodological approaches central to the outcome of projections. The areas addressed included whether projections should be based on current or future policy, the approach to revenue inflows, the approach to age-related and non-age-related programs and the approach to sensitivity analysis. The IPSASB considered whether, in order to meet the qualitative characteristic of comparability, the IPSASB should make firm recommendations on good practice.

BC29. The IPSASB did not consider it appropriate to make firm recommendations on good practice because (a) the scope of the RPG includes all public sector entities and practice that is

¹⁰ Allen Schick, *Sustainable Budget Policy Concepts and Approaches* (OECD: Paris, 2008)

appropriate at one level of government may not be suitable elsewhere in the public sector, (b) while reporting long-term fiscal sustainability information has become a feature of financial management in an increasing number of jurisdictions it is at an early stage of development and (c) it is not the intention of the IPSASB to usurp the role of other professional groups with expertise in this area. In some cases the IPSASB has considered it appropriate to express a view on a preferred high level approach such as those projections are likely to be most useful when based on current policy assumptions and when they encompass both inflows as well as outflows. The IPSASB also noted that, at the national level, the Organisation for Economic Cooperation and Development has recommended that projections should be updated on an annual basis.

Option A: Current Legislation or Regulation with Specific Exceptions (see AP 4.1)

Current and Future Policy Assumptions

- BC29A. Paragraphs 40–42 of ED 46 explain that an entity can depart from using current policy to calculate its projections (a) where there is a conflict between current policy and legal obligations and (b) where a policy has “sunset provisions.” A respondent to ED 46 raised a concern that the concept of current policy should be broader than that proposed in the ED to deal with issues such as fiscal drag.
- BC29B. Fiscal drag refers to the phenomenon that income tax inflows grow faster than the income it is levied on because, as an individual's income grows, an increasing proportion of it is taxed at a higher rate. Fiscal drag occurs if the rates and thresholds for the taxation of individuals are not adjusted over time. Not addressing fiscal drag has the potential for an entity to overstate revenue inflows from taxation which would not reflect an entity's long-term fiscal sustainability position in a representationally faithful manner.
- BC29C. The IPSASB considered permitting an additional departure from current policy where a policy has been changed in a consistent direction over time, to address the issue of fiscal drag. However, the IPSASB concluded that this exception to current policy would enable entities to have wide discretion over the number of departures from current policy thereby potentially enabling the calculation of projections to be subject to political interference. This could result in the projections presenting a misleading view of the entity's long-term fiscal sustainability.
- BC29D. The IPSASB introduced the term “current policy assumptions” to clarify that current policy is assumed to continue (except for the three departures listed in the RPG) for inflows or outflows that are individually projected. Current policy assumptions means current legislation or regulation with departures from this being limited to: (a) where changes to current legislation or regulation have been enacted before the reporting date which have a specific implementation date within the time horizon of the projections, (b) where the provisions in current legislation or regulation are internally inconsistent (in ED 46 “a conflict in legal obligations”) and (c) where current legislation or regulation has “sunset provisions.”
- BC29E. The IPSASB noted that an entity could present a baseline projection using current legislation or regulation and also present adjusted projections which show what policy proposals, such as those addressing fiscal drag, would do to the projections if they were enacted.

Option B: Current Legislation or Regulation with Departures where Appropriate (see AP 4.1)

Current and Future Policy Assumptions

BC29F. Paragraphs 40–42 of ED 46 explain that an entity can depart from using current policy to calculate its projections (a) where there is a conflict between current policy and legal obligations and (b) where a policy has “sunset provisions.” A respondent to ED 46 raised a concern that the concept of current policy should be broader than that proposed in the ED to deal with issues such as fiscal drag.

BC29G. Fiscal drag refers to the phenomenon that income tax inflows grow faster than the income it is levied on because, as an individual's income grows, an increasing proportion of it is taxed at a higher rate. Fiscal drag occurs if the rates and thresholds for the taxation of individuals are not adjusted over time. Not addressing fiscal drag has the potential for an entity to overstate revenue inflows from taxation which would not reflect an entity's long-term fiscal sustainability position in a representationally faithful manner.

BC29H. The IPSASB introduced the term “current policy assumptions” to clarify that current policy means current legislation or regulation with departures where appropriate for inflows or outflows that are individually projected. The RPG gives examples of where a departure may be appropriate.

BC29I. The IPSASB noted that the issue of fiscal drag does not need to be explicitly addressed in the core text of the draft RPG because an entity can depart from current legislation or regulation where appropriate. This approach means that where an entity considers that current policy will be changed in a specific direction, such as the increase in the thresholds for the application of progressive taxation, it can adjust its projections accordingly. The IPSASB also notes that paragraph 56(e) recommends that any departures from current legislation or regulation are disclosed together with the reasons for such departures.