

**IFAC PUBLIC SECTOR COMMITTEE
IFAC PSC MEETING – November 2004**

COUNTRY REPORT – AUSTRALIA
(Prepared 23 September 2004)

This Country Report only notes events since the last Report was prepared for the July 2004 PSC meeting. For a more comprehensive description of some of the projects on the AASB's work program, see the web site www.aasb.com.au.

Projects for which substantial progress has been made are outlined in the following.

GAAP/GFS Convergence

The AASB is continuing to implement the Financial Reporting Council's strategic direction to give urgent priority to GAAP/GFS harmonisation. The AASB has modified its plan for implementing the strategic direction (see www.aasb.com.au).

The Board confirmed its broad guiding principle that, in the interest of neutrality of standards between the public sector and the private sector, unless there are compelling reasons to do otherwise, definition, recognition and measurement requirements contained in accounting standards should be adopted as part of any GAAP/GFS convergence solution.

The Board has considered a range of financial reporting issues for the General Government Sector (GGS) in the context of providing financial information about the GGS as a sector within a whole of government general purpose financial report. In that context the Board will consider an illustrative set of financial statements reflecting the following tentative decisions:

- GGS financial information should be required to be presented as a separate column on the face of the whole of government financial statements;
- financial information about other government sectors (public non-financial corporations and public financial corporations) should be disclosed in the notes to the whole of government financial statements;
- GGS investments in controlled entities in other sectors should be required to be presented as an asset in the GGS column; measured at the GGS's proportional share of the carrying amount of the net assets of the controlled entities, updated at each reporting date;
- GGS comprehensive income (comprising all non-owner movements in equity [including direct-to-equity movements] and identified, recognised and measured in accordance with accounting standards) should be presented in the GGS column of the income statement (rather than, consistent with the requirements in AASB 101 *Presentation of Financial Statements* [which is based on IAS 1], separated in an income statement and a statement of changes in equity);
- GGS comprehensive income should be required to be split between the equivalent of profit and loss as it is described in AASB 101 and other non-owner movements in equity;
- GGS comprehensive income should not be required to be split in any other way. If a government elects to split comprehensive income in another way, it must do so on a "transactions"/"other economic flows" basis in accordance with GFS principles, showing unlabelled totals of each component; and

- GFS analytical balances (including “net operating balance” and “net lending/borrowing”) should be presented in the GGS column, together with reconciliations where definition, recognition and measurement treatments differ from the treatments used to determine amounts presented in accordance with the foregoing dot points.

The Board has also decided that the status of financial reporting by the GGS, including whether the GGS can also be considered as a separate reporting entity, (previously discussed at its 27 May 2004 meeting), should be reconsidered at a future meeting to ascertain whether there are additional arguments or alternative approaches to dealing with the issue that were not fully considered previously.

Review of AAS 27 “Financial Reporting by Local Governments”

The Board has commenced its review of submissions on ED 125 *Financial Reporting by Local Governments*. Consistent with its sector-neutral principle, the Board confirmed that issues adequately addressed in other standards should be applicable to local governments through those standards and it is unnecessary to specify them directly in a local government specific standard.

The Board commenced its detailed consideration of the proposals in ED 125 relating to revenue recognition and decided on the following:

- consistent with the proposals, the concepts of reciprocal/non-reciprocal should not be referred to, and instead guidance should address liability (asset) vs revenue (expense) recognition issues;
- the guidance should focus on principles (and avoid being rules-based), and give prominence to the more common arrangements found in practice such as in substance agreements for the provision of goods and services and in substance conditional grants;
- in relation to in substance conditional grants, the Board will consider the nature of the conditions that give rise to the initial recognition of revenue (rather than a liability) by a grantee at a future meeting; and
- the Board agreed that unconditional grants (but which have restrictions relating to purpose and/or time of use) initially give rise to an asset and an associated revenue by a grantee.

Review of AAS 29 “Financial Reporting by Government Departments”

Since the previous Country Report, the AASB made the following decisions relating to proposals to be included in an Exposure Draft on the review of AAS 29:

- Following consideration of specific issues, a decision will be made on whether:
 - (a) these issues are specifically relevant to particular types of entities (and if so, which types) for which an “industry-based” standard would be appropriate; or
 - (b) such issues can be relocated in to other generally applicable “issue-based” standards.

As a consequence, the Board will reconsider its earlier decision to expand the scope of AAS 29 to entities within the general government sector.

- In relation to the review of current requirements in AAS 29 relating to the disclosure of administered items, the Board decided that:
 - (a) due to government departments and other wholly-owned government controlled entities effectively being part of the government, these entities should recognise in their own financial reports those items that are managed on behalf of the controlling government;
 - (b) the financial statements should be presented in such a way that a user can distinguish between those items described in (a) (an appropriate description is yet to be determined) and other controlled items; and
 - (c) in distinguishing between items described in (a) and other controlled items, rather than have an accounting standard define the distinction, a controlling government should be required to designate whether an item is of the kind described in (a). The Board will consider characteristics that indicate that an item of the kind described in (a) exists, and whether those characteristics should be specified in a standard, at a future meeting.

AASB Convergence (by 2005)

On 15 July 2004, the AASB made Australian equivalents to the IASB standards that will be applicable on or after 1 January 2005, including a number of Australian standards needed to deal with the grandfathering of various treatments.

Broadly, the AASB equivalents of IASB standards adopt the IASB standards word-for-word. Specific guidance for not-for-profit entities (defined as those whose principal objective is not the generation of profit) is “embedded” in the AASB standards (for example, to address non-cash flow generating assets issues in relation to inventories, and property, plant and equipment for impairment purposes), clearly identified as only applying to not-for-profit entities. Where available and suitable in an Australian context, the not-for-profit entity text is based on relevant IPSASs. Furthermore, the AASB standards limit the options retained in some IASB standards, and also include requirements (such as disclosures) that are additional to the disclosures in IASB standards.

In relation to IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance*, the Board made AASB 120 to apply only to for-profit entities. The existing Australian revenue recognition requirements continue to apply to not-for-profit (including public sector) entities. The Review of AAS 27 *Financial Reporting by Local Governments*, (ED 125) includes proposals for commentary to clarify the existing Australian requirements relating to revenue recognition, including guidance on the accounting for government grants.

AASB 1 *First-time Adoption of Australian Equivalents to International Financial Reporting Standards*, the Australian equivalent to IFRS 1, was issued on 15 July 2004. This contains an ‘Aus’-added paragraph, interpreting in the Australian context the requirements in IFRS 1.3 for application of this Standard (to the first annual report containing an explicit and unreserved statement of compliance with IFRSs). Paragraph Aus3.1 in AASB 1 states:

“The conditions specified in paragraph 3 for the application of this Standard are satisfied when the first financial report after this Standard becomes effective contains a statement that the financial report complies with Australian Accounting Standards, in accordance with paragraph Aus13.2 of AASB 101.”

This means that AASB 1 will apply to all Australian reporting entities, not just those (for-profit) entities that are able to claim IFRS-compliance.

Employee Benefits

In July 2004, the AASB responded to the IASB's exposure draft on "Amendments to IAS 19 *Employee Benefits: Actuarial Gains and Losses, Group Plans and Disclosures*" The AASB's submission did not support the proposal to introduce an option to recognise actuarial gains and losses directly in retained earnings.

Related Party Disclosures

AASB 124 *Related Party Disclosures*, the Australian equivalent to IAS 24, was issued by the AASB on 15 July 2004. Despite the general principle that the Australian Standards equivalent to the IASB Standards should be 'sector-neutral', AASB 124 does not apply to not-for-profit non-corporate entities and the question of extension to the public sector remains deferred until the AASB has sufficient time to consider the ramifications.

Interests in Joint Ventures

In relation to the IASB's Research Project, the Joint Venture Team (led by Australia and comprising staff from the standard setters from Australia, China/Hong Kong, Malaysia and New Zealand) finalised a joint venture questionnaire aimed at identifying the structure of joint ventures worldwide. The questionnaire went online in July 2004 with an extended deadline of 30 September 2004. An analysis of responses to the questionnaire together with other issues papers is expected to be put to an IASB meeting early next year.

URGENT ISSUES GROUP (UIG)

The UIG deals with accounting issues of relevance to the private sector and/or the public sector. Following a change to the UIG's Charter in July 2004, consensus views agreed by the UIG are now subject to approval by the AASB before they can be issued. The AASB also decided in July that new or revised UIG Abstracts would be called Interpretations, to be consistent with the International Interpretations. To clarify the status of UIG Interpretations, the AASB has issued AASB 1048 *Interpretation and Application of Standards*, which lists the UIG Interpretations that are to be applicable from 1 January 2005, divided into two sets, those equivalent to IASB Interpretations and those that are not. The 'service standard' will be re-issued before 1 January 2005 (and as needed thereafter) to ensure the listing is up to date.

Since the previous Country Report, the UIG has concentrated on developing Interpretations equivalent to SIC and IFRIC Interpretations and on revising the existing Abstracts for consistency with the Australian equivalents of IASB Standards where the Abstracts will be retained for application alongside the Australian equivalent Standards. The following UIG Interpretations have been issued:

Interp'n	Title	Intern'l Equiv.
1	Changes in Existing Decommissioning, Restoration and Similar Liabilities	IFRIC 1
107	Introduction of the Euro	SIC-7
110	Government Assistance – No Specific Relation to Operating Activities	SIC-10
112	Consolidation – Special Purpose Entities	SIC-12
113	Jointly Controlled Entities – Non-Monetary Contributions by Venturers	SIC-13
115	Operating Leases – Incentives	SIC-15
121	Income Taxes – Recovery of Revalued Non-Depreciable Assets	SIC-21
125	Income Taxes – Changes in the Tax Status of an Enterprise or its Shareholders	SIC-25
127	Evaluating the Substance of Transactions Involving the Legal Form of a Lease	SIC-27
129	Disclosure – Service Concession Arrangements	SIC-29
131	Revenue – Barter Transactions Involving Advertising Services	SIC-31
132	Intangible Assets – Web Site Costs	SIC-32
1019	The Superannuation Contributions Surcharge	–
1030	Depreciation of Long-Lived Physical Assets: Condition-Based Depreciation and Related Methods	–
1031	Accounting for the Goods and Services Tax (GST)	–
1038	Contributions by Owners made to Wholly-Owned Public Sector Entities	–
1039	Substantive Enactment of Major Tax Bills in Australia	–
1055	Accounting for Road Earthworks	–

The UIG is continuing to address the revision of a number of other Abstracts for application alongside the Australian equivalents of IASB pronouncements:

Abstract	Title
17	Developer and Customer Contributions in Price Regulated Industries
40	Non-Reciprocal Transfers within an Economic Entity for Monetary or No Consideration
42	Subscriber Acquisition Costs in the Telecommunication Industry
47	Professional Indemnity Claims Liabilities in Medical Defence Organisations
51	Recovery of Unfunded Superannuation of Universities
52	Income Tax Accounting under the Tax Consolidation System
53	Pre-Completion Contracts for the Sale of Residential Development Properties

The topic of accounting for commodity pooling arrangements, which will be relevant to public sector entities involved in the marketing of commodities, has not been advanced significantly since the previous Country Report, given the work on new and revised Interpretations under the international adoption program.

The UIG Agenda Committee has recently added two issues to the UIG's agenda:

- (1) settlement discounts and volume rebates on inventory purchases; and
- (2) recognition of levy rights.

The second issue has particular relevance in the public sector. Legislation establishing compensation, nominal insurer, and similar schemes usually enables levies to be raised to meet the costs of operating the scheme. For example, legislation establishing a scheme to meet workers' compensation claims may include powers to enable recovery from employers of amounts incurred for claims and administrative costs.

A common feature of these schemes is that the funding for the liabilities of the scheme is assured or "guaranteed". However, differences in accounting practices have arisen such that in some jurisdictions a right to receive levies to fund the costs of the scheme are recognised as an asset, being a receivable or a right to levy, when the liabilities are recognised, while in other jurisdictions an asset is not recognised at the same time as the liabilities. The issue is whether an entity should recognise the right to raise levies to fund compensation liabilities as an asset at the time the liability is recognised or whether an asset should only be recognised when the levy is imposed and the levied parties are advised of the amounts payable.

COMMONWEALTH GOVERNMENT, STATES AND TERRITORIES

Current Status

As reported in the July 2004 Country Report, most Australian jurisdictions prepare budgets and budget outcomes using an accrual GFS basis. Victoria and the ACT use GAAP. The Commonwealth uses both GFS and GAAP, but accrual GFS predominates.

In addition, the Commonwealth government prepares general purpose reports at the whole of government level and for individual reporting entities on an accrual accounting basis. All States/Territories prepare general purpose financial reports for the whole of government and for departments and agencies on an accrual basis.

Consequently, all jurisdictions seek harmonisation of GFS and GAAP.

Commonwealth Government

As reported in the July 2004 Country Report, the Commonwealth Government's Accounting Policy Branch, established within its Department of Finance and Administration, sets accounting and financial reporting policy for Commonwealth reporting entities. In addition, it is responsible for reviewing accounting policies for all GAAP and GFS reporting.

State & Territory Governments

Each State and Territory Government is autonomous and therefore has similar arrangements residing in their Departments of Treasury & Finance.

DATE: 21 September 2004
TO: Members of the Public Sector Committee
RE: Country Report – Canada

INTRODUCTION

This report contains details on the status of public sector accounting activities of the Canadian Public Sector Accounting Board (PSAB).

Generally Accepted Accounting Principles

Responses to Exposure Draft GENERALLY ACCEPTED ACCOUNTING PRINCIPLES, closed August 31, 2004. The ED is modeled off its private sector equivalent, CICA-Handbook Accounting GENERALLY ACCEPTED ACCOUNTING PRINCIPLES, Section 1100.

The most prevalent issue from respondents relates to the status of the private sector CICA Handbook-Accounting (commonly referred to as the ‘Bluebook’) when the CICA Public Sector Accounting Handbook (commonly referred to as the ‘Redbook’) is silent on an issue.

The ED’s principles-based approach does not afford the Bluebook any special status but instead ranks it equally among all other possible sources of GAAP. This runs contrary to current practice where-by practitioners consider the Bluebook the first port of call after the Redbook.

The GAAP taskforce is scheduled to meet early October to review the responses and provide PSAB with a draft final Handbook Section for approval in late November 2004.

Government Transfers

PSAB has approved an Associates’ Draft proposing new standards for accounting for government transfers by both transferring and recipient governments at all levels of government. The proposals address the input received from the October 29, 2003 Transfers Forum (see Canada country report of February 6, 2004).

The salient issue for the Forum related to the deferral vs immediate recognition in circumstances associated with pre-paid government transfers. The input received from the Forum indicated that there was wide support for the deferral in some instances. The majority of Forum attendees argued their points of view using PSAB’s new conceptual framework - confirming that any proposals would have to be consistent with it.

Therefore, the main proposal in the Associates’ Draft defines a concept called “exchange-type transfers”. A government that pays a transfer that meets the definition of an exchange-type transfer in advance of the recipient meeting the transfer stipulations acquires an asset

as a result of the transfer. That asset comprises a right to compel another party to provide services or acquire or develop service capacity in accordance with the transferor's terms.

Comment closing date is September 30, 2004.

Liabilities, Contingent Liabilities and Contractual Obligations

In June 2004, PSAB approved final Handbook Sections for each of 'Liabilities', 'Contingent Liabilities' and 'Contractual Obligations'.

The new Sections:

- No longer need "legislation to be in force" for recognizing a liability but instead focus on the substance of the transaction or event.
- Recognize that there may be occasions where a government can have a constructive or equitable obligation that meets the definition of a liability.
- Provide the characteristics of a liability and additional guidance for interpreting and applying those characteristics.
- Recognize that liabilities can exist as the result of externally restricted inflows.

Sale-Leaseback Transactions

In September 2004, PSAB released for public comment, Draft Guideline 'Sale-Leaseback Transactions – Expense Based'. The Draft Guideline proposes an accounting approach very different to existing requirements.

Current public and private sector Canadian GAAP for sale-leaseback transactions are based on the view that the terms of the sale and the lease are not able to be separated objectively ie: there is 'interdependence'. As a result, gains and losses arising on sale of the property are deferred and amortized.

The Draft Guideline introduces a new premise for accounting for these transactions called the 'components' approach. Components assumes objective separation of the sale and leaseback can be achieved by comparing each to their respective fair values (ie: fair value for both the property and the lease contract). This comparison also enables accounting for their economic substance.

The Draft Guideline does not prescribe deferrals of gains or losses but instead, under certain circumstances, allows their immediate recognition. The ultimate objective of the Draft Guideline is to report the economic substance of sale-leaseback transactions.

Comment deadline is November 30, 2004 with a final Guideline anticipated to be approved early in 2005.

Revenue

This project is leveraging and building upon the work being done on this topic by the PSC. PSAB is asking its Associates group to provide input to the PSC on the proposals in its ITC - input that will also be useful for the Canadian project.

The CICA PSA Handbook does not currently include a definition of revenue for governments though a general revenue recognition principle is included in the general standards of financial statement presentation for both senior and local governments.

The CICA PSA Handbook does have specific Sections regarding restricted assets and revenues (Section PS 3100) and government transfers (Section PS 3410 - which is currently being revised).

However, the existing standards do not specifically address many other types of government revenue, such as income and property taxes. This project will address the gap.

Comment deadline to PSAB is September 30, 2004.

Accounting in Senior Government Budgets – Research Report

The objective of this study is to provide a “state of the union” comparative and descriptive look at the accounting bases and policies used by Canadian federal, provincial and territorial governments in their budgets and appropriations as compared to their summary financial statements. The accounting relationships between these three sets of documents and how the budgets are reconciled to the financial statements in order to provide the budget to actual comparisons required by the CICA PSA Handbook would be key issues.

The information garnered from this research could be used as the basis for additional research on consolidated accrual budgeting.

A draft of the report is with study group Associates with a comment deadline of September 15, 2004. A final meeting for the project is scheduled for early October with publication expected early 2005.

Local Government Financial Statement Reporting Model

In June 2004, PSAB approved a statement of principles (SOP) for Associate comment.

The major issue for the local government model is accounting for non-financial assets, the most significant of which are tangible capital assets. At present, the reporting model for local governments states that, “financial statements should provide information about a local government’s physical assets.”

Amongst other things, the SOP is attempting to broaden the applicability of Section PS 3150 TANGIBLE CAPITAL ASSETS to include local governments. By doing so will require local governments to record and amortize those assets in its financial statements.

It is anticipated that upon completion, the local government reporting model will in all material respects resemble the full-accrual expense-based reporting model which was approved by PSAB for Federal, Provincial and Territorial Governments in October 2002 (applicable from April 1 2005).

Financial Instruments

The purpose of the project is to develop accounting standards for the recognition, de-recognition, measurement, presentation and disclosure of financial instruments in government financial statements. The standard should establish principles that will guide the development of appropriate accounting policies for existing financial instruments as well as the new variations that will undoubtedly be created in the future.

The first step in this project will be a survey to ascertain the nature, extent of, and reporting practices for, the financial instruments of Canadian governments.

Staffing for this project has been finalized and is expected to commence in October/November 2004.

Performance Reporting

The project is designed to develop a set of basic principles that will guide the future development of performance reporting including a framework for identifying performance indicators.

The first step will be to develop an Introduction to Public Performance Reporting which will establish the context for and outline the framework for this type of reporting.

The next step will focus on the nine principles established by the Canadian Comprehensive Auditing Foundation (CCAF) as set out in its publication entitled "Reporting Principles - Taking Public Performance Reporting to a New Level".

The project will use the nine principles as overarching principles and develop more specific guidance for each.

Segmented Reporting

This project focuses on disclosure of additional information about segments of the government reporting entity in their summary financial statements. The objective of the disclosures is to help users better understand the different types of activities that governments engage in.

An SOP is being prepared for approval by PSAB in November 2004 adopting a hybrid approach to determining segments. The hybrid will adopt a mix of the 'management approach' applied in CICA Handbook-Accounting, Section 1701 SEGMENT DISCLOSURES and the 'distinguishable activities' approach used in IPSAS 18 SEGMENT REPORTING.

The project is very sensitive to balancing 'costs vs benefits' of providing segmented information. Therefore the SOP will examine different formats for presenting segmented information and also explore if the information needs of users of government financial statements impact the volume/nature of information disclosed.

STATE OF ISRAEL
MINISTRY OF FINANCE - ACCOUNTANT GENERAL'S OFFICE

September 22, 2004

Re: **Country Report**

Section I: Standard Setting Overview

As mentioned in our Country Report (Agenda Item 7.21-7.24, on June's PSC meeting in N.Y.) Israel has already formulated the following accounting standards for the public sector:

1. Regulation No. 1: Supports and Grants
2. Regulation No. 2: Fixed Assets
3. Regulation No. 3: Inventories and Emergency Inventories
4. Regulation No. 4: Liabilities, Commitments and Engagements
5. Regulation No. 5: Investments
6. Regulation No. 7: Revenues from Barter Transactions
7. Regulation No. 8: Recognition of Revenues from Unilateral Transactions
8. Regulation No. 9: Projects Executed Under Contract
9. Regulation No. 10: Credit and Loans
10. Regulation No. 11: Employee Benefits
11. Regulation No. 13: Intangible Assets

In addition, following are Accounting Regulations in Final Stages of Approval:

1. Regulation No. 6: Accounting for Leases and BOT Projects
2. Regulation No. 12: Consolidation of Entities, Proportionate Consolidation and Equity Method
3. Regulation No. 14: Provisions, Contingent Liabilities, Contingent Assets and Discontinued Operations
4. Management Discussion and Analysis
5. Ministry, Accountant General and Consolidated Financial Statements

Those regulations were formatted by a committee appointed by the Accountant General. The committee role was to formulate the accounting regulations and to assist in their adoption in the government ministries.

Since last PSC meeting in N.Y. the committee was granted a legal status and become a board.

The board's current name is the Israeli Public Sector Accounting Standard Board (IPSASB).

The composition of the new board is as follows:

- 3 members from the Accountant Generals Office (including the Chair).
- A member from the Israeli Securities Authority.

- A member from the Institute of CPAs in Israel.
- A member from the Financial Accounting Standards Board.

Chair of the board: C.P.A. Alroy Ron, the Chief Accountant at the Accountant Generals Office.

Technical director of the board: C.P.A. Ran Tal, Advisor to the Chief Accountant.

The board has prioritized adoption of all IPSASs. In addition, the board will now establish work procedures equivalent to those of the PSC and IASB so to provide maximum transparency of it's deliberations to the public.

Since a large part of the board, at it's previous shape, was done before all current IPSASs had been published and was based on PSC studies and American Standards than available, the board is now in process of adjusting previously published regulations to their IPSAS equivalents were needed, adopting IPSASs on topics not yet dealt with and withholding regulations published which are now being considered by PSC (for example: Non Exchange Revenue Recognition).

As a result, the following regulation, some not yet effective or approved (see above), will be comprehensively changed in order to comply with relevant IPSAS:

- Regulation No. 2: Fixed Assets
- Regulation No. 4: Liabilities, Commitments and Engagements
- Regulation No. 10: Credit and Loans
- Regulation No. 12: Consolidation of Entities, Proportionate Consolidation and Equity Method

In addition, the following Israeli Regulations do not currently have an equivalent under current IPSAS and so the board is awaiting further developments in the PSC with regard to them:

- Regulation No. 1: Supports and Grants
- Regulation No. 8: Recognition of Revenues from Unilateral Transactions
- Regulation No. 6: Accounting for Leases and BOT Projects
- Regulation No. 11: Employee Benefits

The following list of IPSASs will be part of the adoption schedule that would be approved by the new board in the near term as its working agenda.

- IPSAS 1: Presentation of Financial Statements
- IPSAS 2: Cash Flow Statements
- IPSAS 3: Net Surplus or Deficit for the Period, Fundamental Errors and Changes in Accounting Policies
- IPSAS 4: The Effects of Changes in Foreign Exchange Rates
- IPSAS 5: Borrowing Costs
- IPSAS 10: Financial Reporting in Hyperinflationary Economies
- IPSAS 14: Events After the Reporting Date
- IPSAS 15: Financial Instruments: Disclosure and Presentation

- IPSAS 16: Investment Property
- IPSAS 18: Segment Reporting
- IPSAS 19: Provisions, Contingent Liabilities and Contingent Assets
- IPSAS 20: Related Party Disclosures

Following is a list of IPSAS of which guidelines has already been incorporated in current and not yet effective Israeli regulations (only minor changes might be needed in order for a full adoption) and therefore considered by us as already been adopted:

- IPSAS 6: Consolidated Financial Statements and Accounting for Controlled Entities
- IPSAS 7: Accounting for Investments in Associates
- IPSAS 8: Financial Reporting of Interests in Joint Ventures
- IPSAS 9: Revenue from Exchange Transactions
- IPSAS 11: Construction Contracts
- IPSAS 12: Inventories
- IPSAS 13: Leases
- IPSAS 17: Property, Plant and Equipment

Section II: Government Financial Statements Overview

A first step towards publishing a full set of accrual basis financial statements has been achieved by the submission to publication of this years "Information about Assets and Liabilities of the Government of Israel as at 31, December 2004".

Since this report is regarded as a transitional report (from cash basis to accrual basis) it was decided to put an emphasis on the current gaps between current reporting and the requirement of the abovementioned (See standard Setting Overview) Regulations and on relevant IPSASs where needed.

We continue implementation of a new ERP system that will enable us to improve our nation's financial reporting. In 2004, implementation has been completed in the Ministry of Justice (2003: Ministry of Finance and Ministry of Science). Implementation is now being carried in the Courts Management, Water Commissionership, Ministry of Environment, Ministry of Immigration, Fountain of Religious Studies, Institute of Agricultural Studies, Ministry of Health, and Ministry of Housing. Till the end of 2006 the implementation process in all government offices would be completed.

The ERP system allows a more comprehensive reporting within offices that already implemented the system and work in the new ERP and accounting environment. The ERP project, together with the new accounting standards and the accrual accounting, create a revolution in accounting and disclosure which has already started in this recent report.

A major part of Israel's government real-estate (office buildings and governmental districts) were acquired/constructed/received decades ago (even prior to the formation of the Israeli state), and no historical cost data exists with regard to them. Many different methods of evaluating were considered, including: execution of individual appraisals

for each property, registration of the assets at a symbolic value, and the gathering of old information with regard to old properties.

Finally, it was decided that a survey of the 5,200 building in over 1,000 different real-estate locations would be carried out. The survey data was used in a "fair value model"- an appraisal model which allows the user to put a price tag on each property based on different factors of the property such as it's: location, area, age, construction materials, construction method and many other factors. Also, different coefficients were determined to adjust the value for factors that effect the value of the property such as deductions for large scale buildings and so. The model was statistically tested and was found valid and accurate. With regard to governmental districts constructed in the last decade, cost data exists and therefore it was used.

However, the model dose not include the value of the land on which the property rests. Also, no similar (or other) model was established to measure the value of lands owned by the government and not being used as office buildings or governmental districts, heritage assets, public accommodations, infrastructure assets, military assets and more. As a second step, all of these assets will be dealt with in an appropriate manner as part of their registration on the new ERP system and implementing different accounting standards.

Sincerely,

Zvi Chalamish, C.P.A.
Senior Deputy to the
Accountant General,
Accountant General's Office,
Ministry of Finance,
State of ISRAEL

Ron Alroy, C.P.A.
Chief Accountant,
Accountant General's Office,
Ministry of Finance,
State of ISRAEL



DATE: 1 October 2004

MEMO TO: MEMBERS OF THE IFAC PUBLIC SECTOR COMMITTEE

FROM: Greg Schollum
NEW ZEALAND REPRESENTATIVE

SUBJECT: **UPDATE ON RECENT DEVELOPMENTS IN NEW ZEALAND**

Introduction

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

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

Generally Accepted Accounting Practice

Adoption of International Standards in New Zealand

The Financial Reporting Standards Board (FRSB) continues working to adopt a suite of New Zealand equivalents to IFRS/IAS. The “stable platform” is almost complete with only a handful of standards now requiring final consideration and approval by the Accounting Standards Review Board. A list of all exposure drafts issued for comment is included on the ICANZ website (www.icanz.co.nz).

Once standards have been tentatively approved by the Accounting Standards Review Board (ASRB) they are issued as Pending Standards/Interpretations on the Institute and the ASRB web sites.

New exposure drafts issued by the IASB are issued concurrently in New Zealand, and once approved by the IASB will be approved and adopted in New Zealand incorporating any adaptations considered appropriate for New Zealand.

Early Adoption of IFRS

Entities will be required to comply with the New Zealand equivalents to International Financial Reporting Standards for annual reporting periods commencing on or after 1 January 2007.

Entities may elect to adopt these standards for annual reporting periods commencing on or after 1 January 2005.

The Financial Reporting Standards Board (FRSB) has become increasingly concerned that the present absence of an applicable FRS in New Zealand addressing both share-based payments and employee benefits is causing a deficiency in NZ GAAP that will remain until at least 2007 for those entities not electing to adopt the New Zealand equivalents of IFRS early.

As a result the FRSB has recently issued two exposure drafts:

- ED-94 Transitional Arrangements for the Early Adoption of the New Zealand equivalent to IAS 19 Employee Benefits. ED-94 proposes transitional arrangements to assist entities in voluntarily applying NZ IAS 19 for reporting periods prior to complying with NZ IFRS 1 First-time Adoption of New Zealand International Financial Reporting Standards.
- ED-95 Application of NZ IFRS 2 Share-based Payment prior to the Adoption of NZ IFRS 1 First Time Adoption of New Zealand Equivalents to International Financial Reporting Standards. ED-95 proposes to require the application of the New Zealand equivalent to IFRS 2 *Share-based Payment* (NZ IFRS 2) by all entities for annual reporting periods beginning on or after 1 January 2005.

Proposed NZ IAS 41 Agriculture

The FRSB recently approved the proposed NZ IAS 41 (with no changes or additions to the underlying IAS 41) for submission to the ASRB. Respondents raised a number of concerns regarding the adoption of the requirements of IAS 41 in New Zealand, including:

- basis of measurement of bearer assets (e.g. grapevines in the wine industry);
- the costs (particularly for smaller entities) of determining fair values;
- the potential tax implications of measuring biological assets and agricultural produce at fair value; and
- the current lack of differential reporting exemptions under the New Zealand equivalents to IFRSs.

The FRSB will forward a comprehensive submission to the IASB on the widespread concern expressed by many New Zealand constituents and plans to offer its assistance to the IASB regarding any future changes to be made to IAS 41.

Proposed New Zealand Framework

The FRSB recently considered the proposed New Zealand Equivalent to the IASB *Framework for the Preparation and Presentation of Financial Statements* (NZ Framework).

The IASB *Framework* (developed for profit-oriented entities with an emphasis on financial statements) has a narrower focus than the current New Zealand *Statement of Concepts for General Purpose Financial Reporting* (which is sector neutral and incorporates guidance on non-financial information). It has proved difficult to adapt the IASB *Framework* to provide integrated guidance equivalent to that currently found in the *Statement of Concepts for General Purpose Financial Reporting*.

However, the adoption of IFRS means that the FRSB is required to develop a New Zealand equivalent to the IASB *Framework* for 2005 adopters that integrates financial and non-financial information. The FRSB has agreed, as an appropriate interim position, to issue a NZ *Framework* that focuses on financial statements (as per the IASB *Framework*), but which also acknowledges the existence of additional information in financial reports, e.g. sustainable development reporting or other non-financial performance reporting. Such additional information will be acknowledged in the proposed NZ *Framework* but not dealt with extensively.

The proposed NZ *Framework* will require that the quality of the information presented in non-financial and supplementary information be considered with regard to the qualitative characteristics and constraints on those qualitative characteristics discussed in the NZ *Framework*.

The FRSB also decided to review the NZ *Framework* in the second half of 2005 with the aim of developing a more integrated solution and at that time to consider any developments leading to changes to the IASB *Framework*.

Guidance for Public Benefit Entities (PBEs)

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

To address these concerns the Institute has announced a new initiative to ensure New Zealand retains high quality and workable financial reporting standards for the public and not-for-profit sectors (together forming Public Benefit Entities) that are based on international financial reporting standards.

Draft guidance for public benefit entities on determining fair value required for compliance with NZ IAS 16 *Property, Plant and Equipment* will be considered by the FRSB at its next meeting. Further guidance for PBEs on applying other standards will be developed over the next few months.

Not-for-Profit Taskforce

The Institute has recently established a Not-for-Profit Taskforce which over the next six months will be working to identify practical measures that the Institute should undertake to help the sector meet its accountability objectives.

The eight-person Taskforce will address a number of issues which are relevant to the Institute, including:

- impending increased reporting requirements (e.g. as proposed in the Charities Bill and the Review of the Financial Reporting Act);
- adoption of IFRS, which may not address issues of particular concern to the sector;
- relatively insufficient resources, capability and incentives within the sector to deal with these challenges; and
- increasing risks such as increased regulatory requirements (e.g. health and safety regulations), increased demands for accountability (e.g. in relation to public funding), and increased reporting requirements.

Prospective Financial Information

New Zealand currently has on issue FRS-29 covering Prospective Financial Information. The FRSB has recently established a Prospective Financial Information Working Group to review FRS-29. Prospective financial information is of particular importance in the local government sector as the Local Government Act 2002 requires local authorities to prepare a long term council community plan every three years covering a period of not less than 10 consecutive financial years.

Prospective financial information included in that plan is required to be prepared in accordance with generally accepted accounting practice. In addition, from 2006, such plans are required to contain a report from the local authority's auditor on—

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

Puttable Options

Institute staff have been requested by the IASB to draft an amendment to IAS 32 *Financial Instruments: Disclosure and Presentation* regarding accounting for puttable options. This is an important issue for New Zealand as it affects the treatment of co-operative shares redeemable at fair value. This is a major concern to a number of large co-operatives in New Zealand, such as Fonterra, as IAS 32 as currently drafted will require co-operative shares to be recognised as a liability rather than equity. A project report will be presented to the IASB in November.

IASB Projects - Management Commentary

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

The first task for the IASB Working Group is to produce a discussion paper for the IASB outlining how an international financial reporting standard for Management Commentary could

be developed. This paper outlines some of the issues the working group is considering, and early thoughts on the subject, including:

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

Trans-Tasman Accounting Standards Advisory Group

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

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

The Institute is committed to working with Australia on eliminating differences between our respective financial reporting requirements. This is in line with the Trans-Tasman initiatives. A detailed comparison between Australian standards and New Zealand standards has been undertaken and the FRSB will continue to work with the AASB to eliminate these differences as appropriate.

Review of the Financial Reporting Framework

As previously reported, in March 2004 the Ministry of Economic Development (MED) released a discussion paper containing a joint proposal of the Accounting Standards Review Board (ASRB) and the Institute of Chartered Accountants setting out a three tier reporting framework.

Some constituents expressed concern with the proposed scope of tier two. MED officials are now looking at this and certain other aspects of the proposal. The Institute has been assisting the MED with this work. A revised proposal is planned for release later this year.

This should not affect those entities seeking to adopt IFRS from 2005 as we do not expect many Tier 2 entities (if any) to early adopt IFRS. The current framework is sufficiently flexible to enable early adoption. In addition it is likely that entities that will become subject to the Financial Reporting Act 1993 as a result of the review will not be affected immediately. These entities will have a suitable transition period and some will not be required to produce reports until 2009.

Small and Medium-sized Entities (SMEs)

In June 2004 the IASB issued a Discussion Paper *Preliminary Views on Accounting Standards for Small and Medium-sized Entities*. The FRSB has responded to this proposal. In summary,

the FRSB considers that the project is more akin to differential reporting than to accounting by SMEs, is supportive of the IASB developing IASB Standards for SMEs but does not agree with the approach proposed by the IASB.

The proposed approach outlined in the IASB Discussion Paper would involve developing a separate series of standards applicable to small and medium-sized entities. This contrasts with the approach currently adopted in our *Framework for Differential Reporting* which provides reporting concessions from financial reporting standards for qualifying entities. In addition, we have significant concerns over the concept of public accountability within the IASB discussion paper as it would result in many small public sector entities (e.g. schools) having to comply with full IFRS.

This is an important project for many New Zealand reporting entities and it will overlap to a certain extent with the review of the Financial Reporting Framework being undertaken by the MED.

Auditing and Professional Standards

Adoption of International Standards on Auditing (ISAs)

The Professional Practices Board (PPB) of the Institute is continuing its work towards adopting ISAs in New Zealand. The PPB has agreed to seek the views of the key constituents on the proposal to adopt ISAs in New Zealand. In addition, the detailed analysis of the impact of adopting ISAs in New Zealand has started.

Compilation Engagements

The PPB agreed to commence a project to revise CS-1 *Statement of Compilation Engagement Standards* and CG-1 *Guideline on Performance of a Compilation Engagement - Financial Statements*.

A number of queries have been received recently from members, particularly in relation to disclaimers and letters of engagement. CS-1 and CG-1 were issued in 1989 and are in need of revision.

The PPB will consider an issues paper at its meeting in November 2004.

Assurance Engagements over Prospective Financial Information

The PPB has agreed to consider a project to develop guidance on providing assurance over prospective financial information. Assurance engagements over prospective information are required by the Securities Regulations and by the Local Government Act 2002.

The PPB also noted that the FRSB is currently reviewing FRS-29 *Prospective Financial Information*, and that any assurance standard would need to take into consideration the revision of FRS-29.

This is likely to be a complex project as it involves prospective information which is inherently uncertain and is prepared for a range of purposes, and any professional requirements will interact with various legislative requirements. The first step will be to identify the matters that a standard on this issue will need to address. The PPB will consider a draft issues paper at its next meeting.

Central Government

The two key parts of public sector reform in New Zealand (the Public Finance Act 1989 and the State Sector Act 1988) are currently under review. It is expected that a new Act, the Public Finance (State Sector Management) Act will be enacted before the end of 2004.

The new Act is intended to enhance responsible fiscal management, allow Ministers more flexibility in managing appropriations, enhance departmental reporting and expand this to also cover Offices of Parliament and the Reserve Bank, and make the Controller function (performed by the Controller and Auditor-General) a more effective check on spending.

The new Act is also designed to extend the mandate of the State Services Commissioner, in order to provide stronger leadership and guidance and improve the integration between crown entities and the rest of the State sector.

Local Government

Local authorities are currently preparing their first annual reports (including separate summary annual reports) in accordance with the new reporting requirements outlined in the Local Government Act 2002. This includes the requirement to report on progress towards the achievement of outcomes as included in local authority Long-Term Council Community Plans (10 year strategic plans).

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

Greg Schollum
NEW ZEALAND REPRESENTATIVE

*PSC. Country Report: United Kingdom
PSC November 2004

IFAC COUNTRY REPORT: UNITED KINGDOM

FINANCIAL REPORTING COUNCIL

Accounting Standards Board Developments

The Accounting Standard Board (ASB) has issued the following pronouncements and exposure drafts since the last UK Country Report:

- FRED 33, *Financial Instruments: Disclosures*
- FRED 34, *Proposal on Life Assurance*
- Draft UITF Abstract, *Retirement Benefits with a Promised Return on Contribution*
- Third Supplement to FRED 30, *Financial Instruments: Disclosure and Presentation & Recognition and Measurement*
- Draft UITF Abstract on Co-operative Entities

These pronouncements have few implications for the public sector.

FRED 33 updates the disclosure requirements in FRED 30, *Financial Instruments: Disclosure and Presentation & Recognition and Measurement*. In FRED 30 the ASB proposed that the UK requirements on financial instrument disclosures should be brought into line with the IASB's requirements through the implementation of a UK standard based on IAS 32, *Financial Instruments: Disclosure and Presentation*. Since FRED 30 was issued, the IASB has made further proposals in ED7, to amend IAS 32's requirements.. FRED 33 proposes that these amended requirements should be implemented in the UK.

The aim of FRED 34 is to produce substantial improvements in the clarity and transparency of the financial statements of entities with life assurance business, for the benefit of both policyholders and shareholders. FRED 34 will apply to all such entities but will be particularly significant for the larger life assurance groups as well as banks and other non-insurance groups that have material life assurance subsidiaries. FRED 34 is in part a response to the concerns raised by the Penrose Report, which considered problems in Equitable Life, one of the UK's largest life assurance providers.

The draft Urgent Issues Task Force (UITF) Abstract on *Retirement Benefits with a Promised Return on Contribution* provides proposed guidance on how a reporting employer applies the requirements of FRS 17, *Retirement Benefits* to certain retirement benefit schemes that promise employees a specified return on contributions. The draft Abstract, which is closely allied to IFRIC Interpretation D9 on IAS 19, *Employee Benefits* clarifies that such schemes should be accounted for as defined benefit schemes rather than defined contribution schemes. It proposes that normal defined benefit accounting principles apply, except for benefits that depend on future asset returns. The liability for such benefits should be measured at the fair value of the assets upon which the benefit is specified. When the benefit combines a guaranteed fixed return and future asset returns, the liability is the higher of the liabilities for each element.

FRED 30 Third Supplement, *Further Amendments to the Proposed Standards on Financial Instruments* sought views on four Exposure Drafts issued by the IASB, considering the following topics:

- The fair value option
- Transition and initial recognition of financial assets and financial liabilities
- Cash flow hedge accounting of forecast intra-group transactions
- Financial guarantee contracts and credit insurance

The draft UITF Abstract on *Co-operative Entities* addresses questions about how IAS 32's classification principles apply to financial instruments issued by co-operative and other entities that give the holder the right to request redemption. Again it is closely linked to IFRIC Interpretation D8. The issue of a final UK Abstract is conditional on a UK standard based on IAS 32 being implemented by the ASB.

The ASB has also issued for comment the International Accounting Standards Boards' Discussion Paper, *Preliminary Views on Accounting Standards for Small and Medium-sized Entities (SMEs)*. Whilst this paper has very limited impact on the public sector, it has provoked considerable interest, because the approach differs considerably from that in the ASB's own Financial Reporting Standard for Smaller Enterprises (the FRSSSE).

Statements of Recommended Practice (SORPs)

Developments related to the Local Government and Charities Statements of Recommended Practice (SORPs) are covered in the sections of this report devoted to those components of the UK Public Benefit Sector.

Interpretation of Statement of Principles for Public Benefit Sector

The Public Sector and Not-for-profit Committee of the ASB has now completed its revision of the proposed *Interpretation of the Statement of Principles for the Public Benefit Sector*. A further exposure draft of the interpretation is likely to be issued later in 2004.

New Chair of ASB

Ian Mackintosh, formerly Chairman of the IFAC PSC, assumed the position of Chairman of the ASB on 2 August 2004.

Auditing Practices Board Developments

The APB has issued for public comment proposed International Standard on Auditing (UK and Ireland) 300, *Planning an Audit of Financial Statements*, which will supersede Statement of Auditing Standards (SAS) 200, *Planning*.

In June 2004 the APB issued for public comment exposure drafts of 28 proposed International Standards on Auditing (UK and Ireland) (ISAs (UK and Ireland)), and indicated that, when finalised, these standards will replace existing SASs. In the Consultation Paper

for that exposure, the APB explained that a proposed ISA (UK and Ireland) on planning the audit was not included as the underlying ISA was being revised by the International Auditing and Assurance Standards Board (IAASB). The IAASB has now completed the revision of ISA 300, *Planning an Audit of Financial Statements* and that ISA, with a few additions to clarify aspects of its application in the UK and Ireland, forms the proposed ISA (UK and Ireland) 300.

The proposed ISA (UK and Ireland) 300 revises the standards and guidance on planning the audit to align them with the proposed new audit risk model that is integrated into the other proposed ISAs (UK and Ireland).

In August the Auditing Practices Board (APB) published a draft Bulletin that provides auditors with interim guidance on issues that may arise when companies (and other entities that are subject to audit) undertake the transition from UK GAAP to IFRS.

RESOURCE ACCOUNTING AND BUDGETING/WHOLE OF GOVERNMENT ACCOUNTS

Resource Accounting: Report of Financial Reporting Advisory Board

The Financial Reporting Advisory Board (FRAB), an independent body that advises on the application of financial reporting principles and standards for government, has issued its seventh report. The report covers the period from April 2003 to March 2004 and is addressed to the House of Commons Committee of Public Accounts (PAC) and Treasury Select Committee.

The report notes that, with the exception of a new Application Note on revenue, Application Note G to FRS 5, *Reporting the Substance of Transactions*, the ASB issued no new accounting standards during the period to which the report relates. The report focuses therefore on the way in which UK GAAP has been adopted, on other financial reporting issues and on corporate governance. Amongst the issues addressed are:

- Review of projects financed by the Private Finance Initiative
- Alignment of resource accounting and budgeting boundaries
- Disclosure of senior staff remuneration
- Discount rate for retirement benefit liabilities
- Convergence with international GAAP

Review of projects financed by the Private Finance Initiative (PFI)

In its last report FRAB noted inconsistencies in the accounting treatment being adopted by the private and public sectors in individual PFI projects. The report notes that Treasury has provided the FRAB with full details of the accounting treatment adopted in 21 of the 23 projects selected by the FRAB for review.

FRAB asserts the general expectation that a PFI asset should be on the balance sheet of either the operator or the public sector entity granting the concession. In 4 cases the asset was on both balance sheets, whilst in 3 cases the asset was recognised on neither balance sheet. Analysis of a further 25 projects drawn for local government and the health sector found a

much higher number of cases where the fixed assets were on neither balance sheet. This treatment appears to be driven by a belief that the assets must be off-balance sheet for the public sector body if the PFI scheme is to proceed and that this may be reflected in departmental guidance. The research shows how important it is that decisions whether or not to proceed on PFI schemes should be taken on value-for-money grounds and not on the basis of accounting treatment.

Alignment of resource accounting and budgeting boundaries

FRAB has, for some time, questioned the approach to drawing the boundary for resource accounting on the basis that this is driven by budget considerations and is not sufficiently underpinned by accounting concepts. In particular, FRAB notes that the definition of the boundary for Central Government Accounts, the intermediate step en route to Whole of Government Accounts, is not fully GAAP compliant as, although non-departmental public bodies are within the boundary, trading funds and public corporations are not included. The report notes a Treasury consultation process on this issue and looks forward to reporting an improvement in GAAP compliance in its next report.

Disclosure of senior staff remuneration

FRAB has consistently argued that the level of salary and pension disclosures in central government and related sectors should be the same as for the private sector to the extent that they are relevant. The ability of individuals to prevent disclosures in reliance on data protection legislation has been a complicating factor in the past. Whilst statutory changes requiring the adoption of GAAP appear to have removed these complications for the central government sector the position is less clear for many other entities, including health bodies. Parliamentary time to bring in the necessary legal clarification is not available until 2005-06 and this means that the requirements for disclosure of senior managers' remuneration will not be applicable until 2006-07 at the earliest. In forthright comments FRAB deplores the length of time that is being taken to resolve this issue and considers that "the delay has resulted in some public sector accounts not attaining the high standards that FRAB has a duty to promote."

Discount rate for retirement benefit liabilities

FRAB had previously expressed reservations about the use of a discount rate for pension scheme liabilities determined by the Government Actuary's Department (GAD) and based on long-term returns from a basket of long-dated gilts, rather than the AA corporate bond rate specified in FRS 17, *Retirement Benefits*. However, FRAB accepted the use of the GAD rate (3.5% real) for accounting periods up to 2005-06. FRAB now notes that, based on the yields of AA corporate bonds with maturity dates of more than 15 months measured over a 3-month period, the rate to be used from 2005-06 for discounting pension provisions is 2.8 per cent real and that this will be used for Central Government Accounts for 2005-06. The use of a lower discount rate will, of course, lead to an enhancement of the carrying value of the pensions liability.

Convergence with international GAAP

FRAB reports Treasury's view that there is no legal barrier to the immediate adoption of International Financial Reporting Standards (IFRS), rather than UK Generally Accepted Accounting Practice (GAAP). It discusses some difficulties in the immediate adoption of international GAAP, including the fact that at present there is no international equivalent of FRS 5, *Reporting the Substance of Transactions*, which underpins the accounting treatment of PFI, and continuing uncertainties over the completeness of the adoption of IFRS by the European Commission. Whilst recognising the soundness of the Treasury's analysis the FRAB "is disappointed that the Treasury does not feel the time is right to move to IFRS alongside the listed company sector." Nevertheless the FRAB welcomes the Treasury's commitment to adopting IFRS in the medium term.

Other Issues

The report acknowledges the IFAC PSC's Invitations to Comment on *Accounting for the Social Policies of Governments* and *Accounting for Non-exchange Transactions (including taxes and transfers)* and states that the two areas are of "paramount importance in the development of accounting standards for the government sector."

As noted in the last UK Country Report reviews have been commissioned of the format and content of resource accounts and the format and content of accounting guidance. The latter review is starting from the stance that the separate guidance for different components of the central government sector should be consolidated. Furthermore, accounting guidance should comprise 2 elements - a body of high level principles and standards supported by detailed worked examples.

Whole of Government Accounts

HM Treasury has issued a further communication in its Dear Consolidation Manager (DCM) series. DCM 06/04 applies to all designated bodies that are required to submit financial data for the preparation of consolidated central government accounts for 2003/04, apart from those which have already submitted data. It provides a checklist to assist designated bodies and their external auditors and provide them with assurance over the completeness and integrity of data. The letter and accompanying checklist can be downloaded from the whole of government accounts website at www.wga.gov.uk.

LOCAL GOVERNMENT

The 2004 edition of the *Code of Practice on Local Authority Accounting in the United Kingdom (the Local Government SORP)* has been issued following the approval of the ASB's Public Sector and Not-for-profit Committee and the full Board. The SORP governs reporting requirements for accounting periods beginning on or after 1 April 2004.

As highlighted in previous UK Country Reports the 2004 SORP substantially changes the requirements in relation to group accounts. The revised requirements are consistent with FRS 2, *Accounting for Subsidiary Undertakings* and FRS 9, *Associates and Joint Ventures*. Local

authorities (and other entities reporting under the SORP) are required to consider all their interests (including those in other statutory bodies) and to prepare a full set of group financial statements where they have material interests in subsidiaries, associates and joint ventures. These statements comprise (with appropriate disclosures):

- Group Income & Expenditure Account
- Group Balance Sheet
- Group Cash Flow Statement
- Group Statement of Total Movement on Reserves

The statements replace the provision in previous SORPs, which required the preparation of summarised group accounts as supplementary information, where interests in subsidiaries, associates and joint ventures were material in aggregate. The previous requirement had been interpreted inconsistently and the widening diversity of service delivery vehicles used by local authorities and the emphasis on the importance of the concept of control in the ASB's Discussion Paper, *Statement of Principles for Financial Reporting-Proposed Interpretation for Public Benefit Entities* were further drivers for change.

The SORP includes transitional arrangements. These arrangements allow authorities to report under the requirements of the 2003 SORP thereby delaying introduction of the revised group accounts requirements by one year. There is a strong encouragement for local authorities to implement the revised requirements in 2004/05 if possible. Authorities choosing to adopt the transitional arrangements will be required to provide comparatives in 2005/06, which basically means that they will need to prepare group accounts on a memorandum and unpublished basis with a longer timescale.

As a result of the inclusion of these transitional arrangements the ASB has qualified the negative assurance statement that it includes on SORPs. This qualification notes that "compliance with the transitional arrangement is not sufficient to secure compliance with FRS 2 and FRS 9." As the transitional arrangements last for one year only it seems likely that this qualification will not be applied to the next edition of the SORP.

There are a number of other changes reflected in the 2004 SORP. These include:

- changing the discount rate for discounting defined benefit pension liabilities from a rate determined annually by the Government Actuary's Department to the AA corporate bond rate specified in FRS 17, *Retirement Benefits*
- requiring that the minority of local authorities that have issued capital instruments that are listed or publicly traded to provide the disclosures required by FRS 13, *Derivatives and Other Financial Instruments*
- renaming certain line items in the Balance Sheet (Statement of Financial Position) to denote that they are not reserves
- a refinement of the definition of operational and non-operational assets to clarify that property being used in pursuit of the service objectives of the authority should be categorised as an operational asset and clarifying the criteria to be met for an asset to be classified as an investment property

- strengthening the SORP's provisions in relation to the definition and measurement of finance leases in line with SSAP 21, *Accounting for Leases and Hire Purchase Contracts* and FRS 5, *Reporting the Substance of Transactions* and, in particular, adding explicit disclosure requirements for local authorities acting as lessors
- deleting the term "deferred charge", which is largely derived from the statutory capital finance system, as a line item from the Balance Sheet and clarifying that unamortised "deferred charges" carried in the Balance Sheet must correspond to a recognised asset category such as an intangible asset in the case of computer software

Ant exposure draft of the 2005 edition of the *Local Government SORP* was on the agenda for the ASB's Public Sector and Not-for-profit Committee (PSNC) on 5 October. Subject to the approval of the PSNC and the full Board this will be issued for consultation in November 2004. Most of the changes are minor and relate to recent changes in legislation. However, the consultation will include an invitation to comment on the removal of the notional interest element of capital charges for operational fixed assets. A fuller discussion of the proposals for the 2005 SORP will be included in the March 2005 UK Country Report.

AUDIT COMMISSION FOR LOCAL AUTHORITIES AND THE NATIONAL HEALTH SERVICE IN ENGLAND & WALES

The Audit Commission has issued its annual report on *Stewardship & Governance*, which reviews the work of the Commission's appointed auditors in 2003 in local government, and related areas such as criminal justice and fire, and for National Health Service (NHS) bodies.

There are some trenchant criticisms of the promptness and quality of reporting in both the local authority and NHS components of the public sector. In the NHS the Commission reports the view of appointed auditors that the 2002/03 financial reporting performance was "the worst they have experienced in recent years" with particular problems at newly created entities. The report highlights that just under a third of health bodies failed to produce auditable accounts in accordance with the deadlines specified by the responsible central government ministry, the Department of Health, and notes that, for 2003/04, reporting deadlines are to be accelerated by two weeks. On a more positive note there were no qualifications of the accounts of NHS bodies, although auditors qualified the opinion on 16 regularity statements. Regularity statements assert that resources have been spent in accordance with Parliament's wishes and other statutory authorities.

The report is less critical of local government's performance in meeting statutory reporting deadlines, which are less rigorous than in the NHS. Only 4 per cent of English and Welsh local authorities failed to meet the statutory deadline of 30 September 2003 for approval of the annual financial statements (6 months after the end of the reporting period), whilst 6 per cent failed to publish the statements by the statutory deadline of 31 December 2003. The report, however, notes that approval and publication deadlines are being brought forward by 3 months on an incremental basis over a 3 year period ending in 2005/06 and that the revised deadlines will prove challenging to many authorities. In local government an issue of greater concern to the Commission is the fact that nearly 20% of accounts had to be resubmitted for approval by elected members because of discrepancies identified by auditors.

Although the report provides little detail, amongst the significant areas of non-compliance with the Local Authority SORP are:

- valuation of tangible fixed assets
- classification of reserves and provisions
- impairment
- disclosures of pension assets and liabilities under the second year implementation of FRS 17, *Retirement Benefits*
- disclosure of related party transactions
- compilation of and publication of assurance statements on systems of internal financial control

Despite the significant number of authorities that had to resubmit their statements for approval, there were fewer qualified audit reports. Only 6 principal local authorities (of around 450) received qualifications compared with 14 in 2001/02. Issues giving rise to qualifications included impairments, provisions, and the inadequacy of asset registers.

CHARITIES

The UK Charity Commission, the regulator for the charities sector, issued an exposure draft (ED) of *Accounting and Reporting by Charities (the Charities SORP)* in June 2004. The changes proposed include:

- a restructuring of Trustees' Annual Report
- changes to the format of the Statement of Financial Activities (the performance statement) with the aim of producing greater clarity over the source of funds and the purpose for which funds have been generated
- combining the costs of grant-making and direct service provision so that the full cost of pursuing an activity or objective can be shown clearly
- a substantial rewrite and expansion of the sections on the recognition of incoming resources and resources expended
- introduction of the term "heritage assets" to describe assets of historical, artistic or scientific importance that are held to advance the preservation, conservation and educational objectives of charities
- clarifying the treatment of fundraising costs incurred in setting up a new source of future funding with reference to FRS 15, *Tangible Fixed Assets*, FRS 10, *Goodwill and Intangible Fixed Assets* and UITF Abstract 24, *Accounting for Start-up Costs*
- removing references to cash based reporting for smaller charities from the SORP. In future guidance for smaller charities reporting on the cash basis will be provided outside the SORP

Volunteer Input

There has been a great deal of discussion within the charities sector about the valuation of volunteer input, an issue which was, of course, also addressed in the PSC's Invitation to Comment, *Non-Exchange Revenue (including Taxes and Transfers)*. The UK Country Report for April 2004 highlighted the views of the Charity Finance Directors' Group in the report, *Inputs Matter*, that volunteer input should be consistently recognised and measured. The

Exposure Draft notes the concerns of the SORP Committee over how volunteer input can be assessed and measured reliably. These concerns are similar to those of the IFAC PSC Steering Committee. At this stage the Charity Commission does not intend to mandate the recognition of volunteer input in the Statement of Financial Activities (the performance statement). However, the exposure draft does propose fuller and more informative disclosure of the contribution made by volunteers within the Trustees' Annual Report.

Recognition of grants and donations

The ED provides more detailed guidance on the recognition of grants and donations, which is underpinned by the concept of control. In relation to grants payable, a liability and hence expenditure is recognised when the recipients right to receive the benefits falls outside the control of the donor.

The most interesting area of this part of the ED is the discussion of the approach to multi-year funding commitments. It is noted that there have been inconsistent practices, particularly where the conditions attaching to a grant commitment involve an annual review process.

For multi-year grants the ED proposes, that, where evidence exists from past practice of the operation of the condition, through an annual review process, then initially a liability should be recognised for only the first year of the funding commitment. Where operation of an annual review cannot be demonstrated then a liability for the full amount of the multi-year funding commitment should be recognised. The commentary to the ED notes that some constituents hold a more stringent alternative view that evidence of a review is, of itself, insufficient to demonstrate the operation of such a review condition and that full recognition should take place unless evidence exists of annual reviews actually having led to the rescinding of future funding. However, the ED takes the view that the operation of a review condition is evidenced by the review process rather by the outcomes of such reviews.

Heritage assets

In its discussion of heritage assets the commentary on the exposure draft notes a number of the issues inherent in this area and the difficulty of reconciling different perspectives. In particular it is noted that “ a concern exists amongst some charities that users of accounts get a distorted view of the financial position of the reporting entity if the values of heritage assets are included within the balance sheet”.

Some preparers also have concerns about the “partial recognition” issue. “Partial recognition” is an approach where only recently acquired heritage assets are included on-balance sheet and previously acquired heritage assets are not recognised on cost/benefit grounds: the argument being that the cost of obtaining a reliable valuation exceeds the benefit of resulting information to the users of the financial statements. The downside of this approach is that the recognition of similar assets depends on their acquisition date. However, expensing additions to heritage assets to the performance statement is conceptually problematic and could distort the reporting of financial performance. In the light of these conflicting considerations the ED proposes maintaining the current position, allowing cost/benefit rules to be applied where reliable cost information is unavailable and conventional valuation approaches either lack sufficient reliability or involve significant costs outweighing benefits to users.

The SORP Committee wishes to use the consultation to explore these issues in more detail. It outlines an alternative approach. This approach, whilst accepting that capitalisation is conceptually correct, would recognise that an alternative accounting treatment might be appropriate where a charity does not recognise a significant part of its existing collection on cost/ benefit grounds. In such cases, a consistent policy of non-capitalisation may be appropriate, with new acquisitions and the proceeds of disposals presented within a distinct section of the performance statement so that operational results are not distorted. Balance sheet disclosures might provide relevant information such as the nature of the collection and estimated or indicative values.

PUBLIC AUDIT FORUM

The Public Audit Forum, which brings together the United Kingdom's four national audit agencies, is about to start work on a project on the audit of non-financial performance information. In the United Kingdom auditors have historically focussed on reviewing and reporting on the underlying systems and processes for recording, preparing and publishing non-financial performance information, rather than the reported 'numbers' themselves. One of the objectives of this project is to clarify the role of auditors in the audit of such information and to thereby narrow the "expectations gap".

However, for many stakeholders this 'fine' distinction is lost and it tends to be assumed that any audit activity in relation to performance information means that the performance indicators have been audited and are thus 'accurate'. This misunderstanding gives rise to a significant 'expectations gap', which in turn potentially exposes auditors and the audit agencies to significant risks. The reporting of non-financial performance information has become an area of growing significance as freedoms from central government controls have increasingly been linked to performance against pre-determined targets and the position of senior management in public sector entities has become increasingly linked to attainment of those targets. This has given rise to the term "aggressive performance management" as an equivalent of "aggressive earnings management" in the private sector.

John Stanford, UK Technical Adviser

**THE FRENCH PUBLIC SECTOR ACCOUNTING STANDARDS UNDER THE
ACCRUAL BASIS OF ACCOUNTING**

I am pleased to send you attached the French Public Sector accounting standards, which have been recently translated in English.

These accounting standards have been issued by the French Public Sector Accounting Standards Committee (FPSASC) which has been set up after the law organizing the new Budget procedures was passed in August 2001.

The FPSASC has issued :

- a conceptual framework,
- 13 accounting standards.

The conceptual framework and the standards can be downloaded on www.minefi.gouv.fr/moderfie/architecture/index_presentation with a click at the end of the page on « *version anglaise* ».

The approach followed by the Public Sector Accounting Standards Committee is :

- (i) to retain the accrual basis of accounting,
- (ii) to focus on issues specific to the public sector. It means that when a problem is not dealt by a public sector accounting standard, the private sector accounting standards should be applied.

The main points of interest for comparative purposes with the IPSAS appear to be :

- the conceptual framework, especially the users of the financial information (§ I), the reference to the IPSAS (§ I), the use of fair value for fixed assets (§ III-5).
- the accounting standard # 3 on « sovereign » revenues (non exchange revenues).
- the accounting standard # 5 on intangible assets.
- the accounting standard # 6 on fixed assets which provides that long life assets should be valued at market value or depreciated replacement cost.



16th International Colloquium on Financial Management for National Governments

Frank Mordacq
Director of Budgetary Reform
France

UN NOUVEAU CADRE
BUDGÉTAIRE POUR
RÉFORMER L'ÉTAT

The Constitutional Bylaw on Budget Acts : the reform of public management in France

- A constitutional text passed on Parliament's initiative in 2001
- A text that reaches a consensus among the political parties
- An ambitious budgetary, accounting and public management reform
- A reform applicable in January 2006

2

The two basic aims of the reform



IMPROVE TRANSPARENCY

- More active Parliamentary role in expenditure authorisation and control
- Transparency of budget information



IMPROVE PUBLIC MANAGEMENT EFFICIENCY

- Greater autonomy and accountability for administrations
- Performance-related budgets

3

A greater role for Parliament

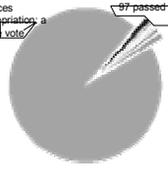
- **Consideration of appropriations**
 - First euro appropriation justification
 - Voting at public policy level
 - Extended powers of amendment reallocating appropriations among programmes
 - Assessment of the budget based on public policy goals and results
 - A budget policy debate in the spring
- **Control over government action**
 - Greater investigative and hearing powers
 - Opinions on regulatory movements of appropriations
 - Stronger links between budget execution and parliamentary authorisation

4

A richer and modernised budget policy debate

Up to 2005

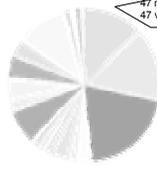
Current services appropriation, a single vote



New measures for each ministry: 97 passed in 2005

94% of appropriations are renewed virtually automatically from one year to the next (current services appropriation) without being brought into question. Most of the debates focus on just 6% of the general budget.

As of 1 January 2006



47 missions, 47 votes

100% of the appropriations are debated in Parliament, for each mission.

5

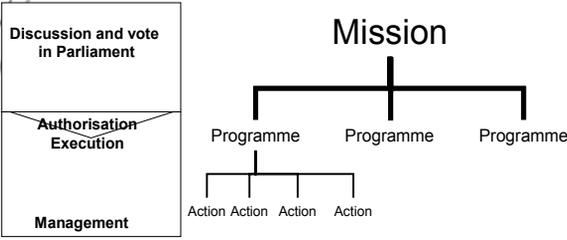
1. A new State budget presentation

2. A new performance-based management

3. A new State accounting system for improving transparency

6

1. The new State budget presentation : a programme budget structural on important political aims

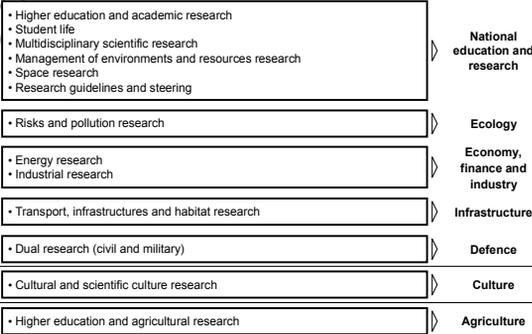


The mission: the expression of policy choices

34 missions for the State budget

- The mission is Parliament's voting unit
 - It covers a set of programmes,
 - Parliament may reallocate appropriations between programmes in the same mission.
- The mission may be ministerial or interministerial
 - 10 interministerial missions,
 - For example, the Research Mission concerns seven ministries

The Research and Higher Education Mission 13 programmes – 7 ministries



The programme: implementing public policies

132 State budget programmes

- The programme covers the appropriations needed to implement an action or a comprehensive set of actions (580)
- It concerns just one ministry and requires steering that calls for new managerial tasks
- It is tied in with performance goals and indicators
- Its credits are globalised for more flexible management (with capped payroll)

Example of globalisation Ministry of Justice

Then: 30 budget subheads

Class III – Service resources

- Personnel – service pay
- Retired personnel – pensions and allowances
- Active and retired personnel – social security charges
- Department equipment and administration
- Operating subsidies
- Sundry expenditure

Class IV – Government operations

- Political and administrative operations
- Social programmes – aid and solidarity

Class V – State investment

- Administrative and other facilities

Class VI – Investment subsidies granted by the State

- Cultural and social facilities

Now: 6 programmes

Administrative jurisdiction

The judicial system

Prison and correctional administration

Young offenders institutions

Free access to justice and legal aid

Backing for judicial policy and related organisations

An improved presentation of appropriations

Programme National police	Class Personnel	Class Current services	Class Investment	Class Subsidies
Actions		Overall	control total	
* Public order and protection of sovereignty				
* Public security				
* Road safety				
* Immigration officials and international transport safety				
* Criminal investigation police and assistance to the justice system				
* Command, training and logistics				

2. Performance-based management

- **A selection of performance goals and indicators representative of the programme priorities:**
 - **Goals** to meet the expectations of citizens, users and taxpayers: a political choice
 - **Indicators** to measure the achievement of the goals set
- **Goals and indicators:**
 - To clarify the policies will be presented to Parliament in **annual performance plans**
 - Will be used for **in-house management**
 - Will give **meaning to the staff's work**
- **Performance guide drawn up with Government, Parliament and the State Audit Office**

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Performance-based management

- **About 5 goals per programme**
- **2 performance indicators per goal**

Standpoint	Goal	Sample goal	Sample indicator
Citizen	Socio-economic effectiveness	Improve the employability of young graduates	% of graduates with a job six months after graduating
User	Quality of services provided	Speed up judicial decisions	Average decision lead time; average hearing time
Taxpayer	Management efficiency	Reduce the tax management cost	Tax cost per taxpayer

14

New responsibilities under the minister's authority

- **National steering: the Programme Manager**
 - Following arbitration headed by the Director of Financial Affairs
 - He is granted appropriations, which he distributes for internal management needs,
 - He is accountable to Parliament for performance: the **Annual Performance Plan** (appended to the budget act)
 - He reports to Parliament: the **Annual Performance Report** (appended to the budget review act)
 - **Appointed in June 2004**
- **Management: the Operational Budget Programme Manager**
 - He is granted an operational budget programme.
 - He is accountable and reports to the Programme Manager by means of the management dialogue.

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3. A new State accounting system

Two systems for the accounts

- **Cash-basis accounting system (comparison with the cash basis budgeting system)**
- **Accrual-basis accounting system in line with corporate accounting rules:**
 - To ensure the transparency of the State's financial situation,
 - To provide the elements needed to calculate costs (revenue and expenditure attached to the fiscal year, valuation of assets, etc.)

16

Implementing the State accounting system

1. The Book of Accounting Standards

- 13 draft standards drawn up by the **Standards Committee** (for financial statements, budget obligations, fixed assets, debts, etc.)
- April 2004: **approval by the French National Accounting Board**
- 21 May 2004: **approval by order of the Minister of Finance**

2. Preparation of the opening balance sheet

- Inventory and **valuation of the stock of real property**
- **Other tangible assets** and stocks (use of surveys of ministries)

17

2004-2005 milestones

■ **Parliamentary milestones for the 2005 budget**

- Presentation of the budget based on the new indicative budgetary system (September 2004)
- Presentation of the first performance goals and indicators

■ **Early 2005**

- Globalisation pilot tests

■ **September 2005**

- Vote on the budget based on the new rules

■ **January 2006**

- Budget execution and new accounting system

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COUNTRY REPORT FOR THE IFAC PSC

SOUTH AFRICA

OCTOBER 2004

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1. Accounting Standards Board (ASB)

Since the last country report, the ASB approved for issue the following exposure drafts:

- Consolidated and Separate Financial Statements*
- Investments in Associates*
- Interest in Joint Ventures*
- Segment Reporting**

Board Members: Mrs M Brown, Mr R Cottrell (Chairperson), Ms B Hogan,
Mr S Kana, Dr L Konar, Mr I A Mamoojee, Mr M J N Njeke, Mr T Nombembe, Mr I Sehoole
Chief Executive Officer: Ms E L Swart

The comment period for the exposure drafts and requests for comments close on (*) 31 October 2004 and (**) 15 December 2004 respectively.

The changes made by the IASB to IAS arising out of the improvements project, and the consequences of any IFRICs that have been issued since the development of the equivalent IPSASs have been taken into account.

Work has also commenced on the drafting of two invitations to comment, and it is hoped that the ASB will approve these for publication before the end of the year:

- Intangible assets, and
- Heritage assets.

An accounting guide on public-private partnerships (PPP) is also in the pipeline to supplement the PPP manual issued by the National Treasury. The PPP manual is available electronically on www.treasury.gov.za

2. Auditing and Assurance Standards Board

On 1 January 2005 the Auditing and Assurance Standards Board (AASB) of the Public Accountants' and Auditors' Board (PAAB), will adopt the entire suite of auditing pronouncements issued by the International Auditing and Assurance Standards Board (IAASB) of the International Federation of Accountants (IFAC) for use in South Africa. The pronouncements to be adopted will replace the existing South African Auditing Standards (SAAS). The international pronouncements, which include practice statements (hereafter referred to as IAASB Standards) to be adopted include:

- International Standards on Auditing (ISAs),
- International Standards on Review Engagements (ISREs),
- International Standards on Assurance Engagements (ISAEs),
- International Standards on Related Services (ISRSs),
- International Standards on Quality Control (ISQC); and
- the International Framework for Assurance Engagements.

3. South African Institute of Chartered Accountants (SAICA)

The following exposure drafts are open for comment:

<i>Title</i>	<i>Comment Date:</i>
ED 188 Financial Instruments: Disclosures	8 October 2004
ED 189 Preliminary Views on Accounting for Black Economic Empowerment (BEE) transactions	23 November 2004

South African Statements of GAAP are fully harmonized with IFRS. The international text is used and a South African wrap around is added.

4. Ministerial Panel for the Review of the Draft Accountancy Profession Bill

The Minister is expected to make some announcements on the Draft Accountancy Profession Bill in the next few weeks, after going through a redrafting process by the National Treasury, taking into account comments made by the Minister (see May 2004 country report) and other relevant legislation affected by the review. The legislation is aimed at a comprehensive restructuring of the accountancy and auditing profession in South Africa and the regulation thereof.

5. Corporate Law review

The Department of Trade and Industry is performing a review of corporate law with the aim of modernising legislation affecting companies in line with international trends and to accommodate the changing environment for business, both in South Africa and globally.

The objectives of the review are to:

1. Encourage entrepreneurship and enterprise diversity by simplifying the formation of companies and reducing costs associated with the formalities of forming a company and maintaining its existence, thereby contributing to the creation of employment opportunities;

2. Promote innovation and investment in South African markets and companies by providing a predictable and effective regulatory environment and flexibility in the formation and the management of companies;
3. Promote the efficiency of companies and their management;
4. Encourage transparency and high standards of corporate governance, recognising the broader social role of enterprises;
5. Ensure compatibility and harmonisation with best practice jurisdictions internationally.

The invitation to comment is available on www.dti.gov.za