



**INTERNATIONAL FEDERATION  
OF ACCOUNTANTS**

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**Agenda Item  
5**

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**DATE:** 13 November 2007  
**MEMO TO:** Members of the IPSASB  
**FROM:** John Stanford  
**SUBJECT:** Fiscal Sustainability

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**OBJECTIVE OF THIS SESSION:**

**To approve** the Project Brief for the project on fiscal sustainability.

**AGENDA MATERIAL**

5.1 Draft Project Brief on Fiscal Sustainability.

**BACKGROUND**

At the Montreal meeting it was decided to initiate a project on long term fiscal sustainability information. This is to be part of a three-pronged approach to accounting for social benefits, which also includes:

- ED 34, “Social Benefits: Disclosure of Cash Transfers to Individuals and Households”; and
- The Consultation Paper, Social Benefits: Issues in Recognition and Measurement.

It was also agreed that the project brief would be issued together with the ED and the Consultation Paper and that comments would be invited. ED 34 and the Consultation Paper were issued at Agenda Item 6 on 5 November 2007.

The conceptual framework project will be considering whether long-term fiscal sustainability reporting is within the scope of general-purpose financial reporting in detail. Nevertheless, the direction at Montreal was that the scope of the long-term fiscal sustainability project was to be from a general-purpose financial reporting perspective and that it should not be limited to the general-purpose financial statements.

The US Financial Accounting Standards Advisory Board (FASAB) has initiated its own project on long-term fiscal sustainability. This has a challenging target of producing an Exposure Draft in 2008 proposing requirements for the US Federal Government’s consolidated financial statements with a full Standard to follow in 2009. The FASAB project does not envisage requirements for individual agencies. There has been tentative staff-level discussion of a joint project between the FASAB and the IPSASB on fiscal sustainability. IPSASB Staff’s view is that, given the fact that FASAB has already initiated their project, the timescales for the FASAB and the fact that FASAB meets much more regularly than IPSASB, a fully-fledged joint project will be difficult. However, Staff has had considerable informal discussion and has agreed to

share agenda materials and other papers. IPSASB Staff members attended the July meeting of the FASAB, at which fiscal sustainability was a major agenda item.

FASAB staff has assembled and analyzed comparative materials on approaches to fiscal sustainability in a number of Anglophone jurisdictions. These materials and the perceptions of FASAB staff have been particularly useful to IPSASB staff in the development of these agenda item materials and Staff is very grateful to FASAB staff for their openness and assistance. The current INTOSAI member is also a FASAB member and has facilitated these links. The expertise of FASAB staff will be valuable to this project.

### **OBJECTIVES OF THE PROJECT**

The ultimate objective of the project is to produce a framework for the reporting and disclosure of information related to the long-term fiscal sustainability of governmental programs. As this is not a project directly related to the general purpose financial statements it is not feasible or appropriate to provide definitive final outputs at the initiation stage. Intermediate objectives are to produce a Consultation Paper and, dependent upon decisions following analysis of submissions on that Consultation Paper, an Exposure Draft and/or draft detailed Guidance. The Consultation Paper will highlight and analyze existing approaches in jurisdictions where fiscal sustainability reporting is a feature of governmental financial management as well as the approaches of supra-national bodies such as Eurostat and the IMF in making comparative fiscal projections.

### **ISSUES**

The key issues identified by Staff are highlighted below.

#### *i) Definitions*

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

At a very high level, fiscal sustainability involves an assessment of the extent to which service delivery can be maintained at existing levels and the extent to which governmental obligations to citizens under existing legal frameworks can be met over a pre-determined future period. The analysis of fiscal sustainability therefore takes account of both current and future beneficiaries, regardless of whether present obligations to them, determined in accordance with accrual accounting principles, exist at the reporting date.

Fiscal sustainability is sometimes coupled with the broad concept of inter-generational equity, which evaluates the extent to which future generations of taxpayers will be affected by the fiscal consequences of current policies for the delivery of goods and services. Inter-generational equity therefore considers whether, and to what extent, the cost of current government operations is likely to be met by future generations of taxpayers, and the extent to which future taxpayers will receive service provision and benefits equivalent to current levels.

The reporting of fiscal sustainability is also commonly linked to frameworks involving targets and benchmarks requiring indicators such as:

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

It will be necessary to consider which terms need to be defined and whether requirements should specify that a minimum set of indicators should be reported.

In developing its approach the FASAB has contrasted financial position, which is an entity-level attribute based on accrual-based principles and which is reported in the balance sheet (statement of financial position) and financial condition, which is a prospective and broader attribute that requires forward assumptions about both financial and non-financial data.

It is important to distinguish long-term fiscal sustainability and sustainability or environmental sustainability. This project is only dealing with long-term fiscal sustainability. However, there is a linkage between environmental sustainability and long-term fiscal sustainability because assumptions about environmental sustainability impact upon financial assumptions such as changes in GDP and demographic assumptions such as population growth, emigration and immigration.

*ii) Mandatory/Discretionary Nature of Proposals and Requirements*

The next question is whether the IPSASB should be developing mandatory or discretionary requirements i.e. should all entities within the scope be required to produce reports on long-term fiscal sustainability as a regular feature of their general-purpose reporting or should the scope be restricted by, for example:

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

In IPSAS 24, “Presentation of Budget Information in Financial Statements” the scope was limited to entities that make approved budgets publicly available. IPSAS 24 did not require that budgets be made publicly available. IPSAS 22, “Disclosure of Financial Information about the General Government Sector” only applies to governments that elect to disclose financial information about the general government sector in their consolidated financial statements. It does not require such disclosures to be made.

This will be the first time that IPSASB has developed requirements for any type of prospective reporting. This may suggest that, as a first step, a discretionary approach is sensible with the extension of that requirement to be considered in the future. However, the IPSASB’s view that long-term fiscal sustainability reporting is necessary to allow informed readers to assess the viability of governmental programs and to complement information in the general purpose financial statements may militate towards a mandatory approach.

The project will also examine whether requirements should apply to all entities or only to entities which have adopted the accrual basis of accounting. Long-term fiscal sustainability reporting involves the reporting of projected cash flows. Although it may be useful to be able to use items reported in the statement of financial position as a starting point in the estimation of key fiscal indicators involving net debt there is no intrinsic reason why requirements should only apply to entities already on the accrual basis. However, the range of assumptions required and the sophistication of estimation techniques militate towards excluding entities on the cash basis from the scope because of cost-benefit considerations.

*iii) Reporting Entity for Long-term Fiscal Sustainability Reporting*

The main issue is whether the requirements are to apply to all public sector entities; only government entities at the national level, to the whole-of-government level or to another level. The rationale for including all entities within the scope is that this is consistent with the entity-level approach that has characterized most IPSASB pronouncements. However, IPSAS 22 only applies to the consolidated financial statements of government, so there is a precedent for developing standards with requirements that do not apply to all public sector entities.

It is arguable that any requirements should only apply at the whole-of-government level because requiring individual entities to prepare and report information on the fiscal sustainability of operations is onerous and not proportionate to the benefit that users will derive from the information. Conversely, for nations with federalized structures, only developing requirements for part of the public sector may not satisfy user needs on the overall fiscal sustainability of the public sector: this particularly applies where the service delivery of significant public sector programs is the responsibility of entities at sub-national levels of government and where sub-national level entities have wide tax-raising powers.

This leads to the need for consideration of the linkage with statistical accounting approaches and in particular whether the general government sector (GGS) may provide the appropriate reporting boundary for fiscal sustainability reporting. The GGS encompasses all levels of government, regardless of whether control relationships exist, as well as social security funds and non-market non-profit entities controlled by government units. Under statistical accounting the public sector also comprises public financial corporations and public non-financial corporations. In contrast to the accrual basis the GGS does not consolidate controlled entities outside the GGS sector and does not therefore eliminate balances and transactions between entities in the GGS and other sectors. It treats controlling interests in entities outside GGS as investments. Statistical accounting is used as the basis for long-term fiscal sustainability reporting in a number of jurisdictions.

It will be necessary to determine the reporting entity for fiscal sustainability reporting and in so doing to analyze the advantages and disadvantages of reporting boundaries based on accrual and statistical approaches.

*(iv) Interaction with Management, Discussion and Analysis*

As indicated above, the IPSASB has decided that the project will deal with long-term fiscal sustainability from the broader perspective of general-purpose financial reporting rather than the

provision of information on the general-purpose financial statements. The IPSASB has decided to initiate a project on Management Discussion and Analysis (M, D &A otherwise known as management commentary, narrative reporting or the operating and financial review) in the first quarter of 2008. In some jurisdictions the M, D &A or equivalent is the main mechanism by which expected future trends and changing conditions to the operational environment and their potential impact on the reporting entity are highlighted for users. It will therefore be important to consider the extent to which the M, D & A should include details, and indicators of fiscal sustainability.

*(v) Time Horizons*

In jurisdictions which make long-term fiscal sustainability reports publicly available there is currently variability of the time horizon. For example:

- in its *Intergenerational Report* the Australian Commonwealth Government uses a 40 year horizon;
- in the *Statement of New Zealand's Long-Term Fiscal Position* a time horizon of at least 40 years is required;
- in its report, *The Long-Term Sustainability of Public Finances in The European Union*, published in 2006 the European Commission, used a time-horizon up until 2050;
- in its *Statement of Social Insurance* which is within the Consolidated US Financial Statements there is a time horizon of 75 years; and
- in its *Long-term Public Finance Report*, the UK Treasury uses a 50 year time horizon.

Obviously there is a relationship between the robustness of assumptions and the time horizon: the further the time horizon is from the reporting date the more fragile assumptions become. Whilst this consideration militates towards shorter- time horizons there is conversely what FASAB has termed a “moving window”: where events and modified trends just outside the reporting horizon might have a significant impact on reported information. This problem is potentially exacerbated by shorter time horizons.

The project will explore various time horizons and consider how prescriptive requirements should be.

*(vi) Regularity of Reporting*

Publication of the general-purpose financial statements is on an annual cycle. However, it is arguable whether the same frequency of reporting should be required for long-term fiscal sustainability reporting. This is both because of the costs of reporting and the fact that the key material policy, demographic and economic assumptions are unlikely to change sufficiently rapidly within a year to justify the costs of annual reporting. For example the Australian Intergenerational report is required every five years, whilst the New Zealand Statement on the Long-Term Fiscal position is required every four years. There is a need to consider whether there should be minimum intervals between reporting or whether any requirements should be more flexible, for example requiring reporting intervals to be disclosed with any changes to those intervals since previous reports were produced.

*(vii) Assumptions and Sensitivity of Assumptions*

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

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

The term *policy assumptions* refers to the basis on which future levels of service delivery will be determined. It is tentatively proposed that such assumptions should be on the basis of current legal frameworks. This is dealt with in more detail below (see section Tensions with Current Legal Frameworks).

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

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

It is not proposed that the IPSASB develop detailed requirements as to which assumptions should be used for long-term fiscal sustainability analysis. This will depend upon the portfolio area and the program. However, the project will consider the disclosure of such assumptions. Assumptions are inherently uncertain and changes in those assumptions can have a significant impact on projections: this is reflected in the fact that much current reporting devotes considerable attention to the sensitivity of those assumptions.

Assumptions also include discount rates. In order to determine the present value of future net cash-flows discounting is necessary. The selection of a discount rate can have a major impact on the amounts reported. Potential approaches include rates:

- Reflecting the time value of money;
- Reflecting a risk-free basis;
- Based on specified instruments;
- Based on expected return on assets to be used to meet future obligations or on future operating funds; and
- Based on future predicted economic growth rates.

*(viii) Tensions with current legal frameworks*

As a general principle IPSASs have adopted the tenet that transactions and elements are evaluated and determined within current legal frameworks. Such an approach has been adopted in ED 34, “Social Benefits: Disclosure of Transfers to Individuals and Households”. The view has been that the preparers of the financial statements should not predict governmental actions and that there should be no assumption that programs will terminate unless legislation to that effect has been enacted at the reporting date. If such a principle is adopted for long-term fiscal sustainability reporting the complementary approach to taxation would be that inflows should be determined using current legal requirements and taxation rates unless changes have been effected at the reporting date.

Issues arise as to the correct approach for projections under current frameworks where different legal obligations conflict or where projections are clearly unreasonable. Examples might be where:

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

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

*(ix) Approach to Discretionary Programs*

In broad terms, discretionary programs are programs which the government is not required to maintain under current legal requirements beyond a clearly specified period. In one jurisdiction discretionary programs are contrasted with mandatory programs which involve entitlements, with authorizations for discretionary programs being renewed on an annual basis. The main issue is whether expenditure projections should extend beyond the limit of current authorizations and, if so, how such expenditure projections are to be projected for such programs. A related issue is that discretionary programs are likely to expire before the time horizons used for reporting, so it is questionable whether an assumption should be made that such programs will be renewed on expiry.

A further issue is the appropriate assumption for making expenditure projections for discretionary programs. Such assumptions might include:

- use of 5-10 year trend information for extrapolation purposes;
- same projected growth rate as for GDP;
- a general or specific inflation index.

*(x) Comprehensiveness of Reporting*

The issue is whether all governmental programs should be considered or whether the scope should be restricted to only certain programs e.g. contributory programs or social insurance programs.

**Action Requested:** Confirm the key issues highlighted by Staff and **identify** any further issues that need to be added to the project brief.

## COMMUNICATION

Staff has been impressed by the emphasis on communication in the FASAB project. A key component of the FASAB project has been to make information accessible understandable and meaningful to the public, using as a criterion the average citizen who has a reasonable understanding of governmental activities and is willing to study that information with reasonable diligence. The rationale is that there is already considerable and highly detailed information produced by a variety of bodies such as Office for Management and Budget, the Congressional Budget Office and the Government Accountability Office: developing requirements that simply lead to the provision of further detailed information or the reformulation of existing requirements in formats that are not easily comprehensible will not satisfy user needs.

This leads to the issues of whether a separate Communications Plan is required for this project and whether in conjunction with the issue of a Consultation Paper it would be worthwhile to hold forums or roundtables, which might include a variety of constituents including concerned citizen groups.

**Action Requested: Provide** views on whether a separate Communications Plan should be developed and preliminary views on whether a Roundtable should be planned in conjunction with the publication of Consultation Paper.

## ARRANGEMENTS FOR OVERSIGHT AND DEVELOPMENT OF PROJECT

Staff considers that a Task Force comprising seven to nine members would be the appropriate way of progressing this project. It is important that the Task Force reflects both geographical balance and expertise from accounting standard-setters, preparers, statistical accounting, budget development and auditing. Whilst the main expertise for progressing the project is within the Board and its Technical Advisors and Observers consideration should be given to the appointment of external members. Staff has suggested that, in view of the FASAB project, it would be worthwhile to include a FASAB Staff Member in the Task Force. The project brief proposes the following composition:

- Two public sector standard-setters, one of which will have a current project in this area;
- One government entity preparer of general-purpose financial statements;
- Two statistical accountants with experience of preparation of long-term fiscal sustainability projections;
- One preparer of government budget reports;
- One legislative auditor;
- Two surrogates for users of financial statements (e.g. from the IPSASB Observer group, academics, member of legislative assembly).

It is envisaged that the Task Force will communicate generally by electronic means. Two face-to-face meetings are likely to be necessary: one during the Consultation Paper development stage and one during the stage to develop and ED and/or draft guidance. Task force membership will be determined by the Chair and Technical Director.

**TIMETABLE**

A detailed timetable is provided in the project brief. The main milestones are:

**Consultation Paper to be approved:** February 2009

**Exposure Draft of Standard/Draft Guidance to be approved:** June 2010

**Final Standard/Final Guidance:** June 2011



**DRAFT**  
**INTERNATIONAL PUBLIC SECTOR  
ACCOUNTING STANDARDS BOARD**  
**PROJECT BRIEF AND OUTLINE**

**1. Subject**

Reporting on and making disclosures about the long-term fiscal sustainability of governmental programs.

**2. Project Rationale and Objectives**

During the development of its project on social benefits the IPSASB has formed a view that, regardless of the approach that is taken to the point at which a present obligation for different sorts of social benefits occurs and the view as to the extent of those present obligations and the resultant liabilities, the financial statements cannot satisfy all the needs of users in assessing the future viability of programs providing social benefits. The information in the financial statements needs to be complemented by information on the long-term fiscal sustainability of those programs.

a) Objectives to be achieved

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

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

This is not a project directly related to the general purpose financial statements. It is therefore not feasible or appropriate to provide definitive final outputs at the initiation stage. Dependent upon decisions following analysis of submissions on a Consultation Paper, an Exposure Draft of a Standard and/or detailed Guidance will be developed.

b) Link to IFAC/IPSASB Strategic Plans

*Link to IFAC Strategic Plan*

Issuing requirements and guidance on public sector financial reporting issues is a primary role of the IPSASB. The development of such requirements and guidance supports IFAC's mission of

servicing the public interest by contributing to its aim of becoming the international standard-setter for governmental financial reporting.

*Link to IPSASB Strategy*

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

### **3. Outline of the Project**

#### **a) Project Scope**

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

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

- all governmental programs should be within the scope; or
- whether the scope should be restricted to only certain programs e.g. contributory programs or social insurance programs.

This project is only dealing with long-term fiscal sustainability and not environmental sustainability. However, there is a linkage between environmental sustainability and long-term fiscal sustainability, because assumptions about environmental sustainability impact upon financial assumptions such as changes in Gross Domestic Product (GDP) and demographic assumptions such as population growth, emigration and immigration. The project will acknowledge those linkages.

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

##### *i) Definitions*

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

At a very high level, fiscal sustainability involves an assessment of the extent to which service delivery can be maintained at existing levels and the extent to which governmental obligations to citizens under existing legal frameworks can be met over a pre-determined future period. The analysis of fiscal sustainability therefore takes account of both current and future beneficiaries,

regardless of whether present obligations to them, determined in accordance with accrual accounting principles, exist at the reporting date.

Fiscal sustainability is sometimes coupled with the broad concept of inter-generational equity, which evaluates the extent to which future generations of taxpayers will be affected by the fiscal consequences of current policies for the delivery of goods and services. Inter-generational equity therefore considers whether, and to what extent, the cost of current government operations is likely to be met by future generations of taxpayers, and the extent to which future taxpayers will be provided with services and benefits equivalent to current levels.

The reporting of fiscal sustainability is also commonly linked to frameworks involving targets and benchmarks involving such indicators as:

- Net Debt
- Net Debt/GDP
- Fiscal Gap
- Fiscal Imbalance

The project will consider which terms need to be defined and whether requirements/guidance should specify or recommend that a minimum set of indicators should be reported.

*ii) Mandatory/Discretionary Nature of Proposals and Requirements*

The project will consider whether the IPSASB should be developing requirements and if so, whether such requirements should be mandatory or discretionary i.e. should all entities within the scope be required to produce reports or disclosures on long-term fiscal sustainability as a regular feature of their general-purpose reporting or should the scope be restricted by, for example:

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

The project will also examine whether requirements should apply to all entities or only to entities which have adopted the accrual basis of accounting.

*iii) Reporting Entity for Long-term Fiscal Sustainability Reporting*

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

It is arguable that any requirements should only apply at the whole-of-government level because requiring individual entities to prepare and report information on the fiscal sustainability of operations is onerous and not proportionate to the benefit that users will derive from the information. Conversely, for nations with federalized structures, only developing requirements for part of the public sector may not satisfy user needs on the overall fiscal sustainability of the sector: this particularly applies where the service delivery of significant public sector programs is the responsibility of entities at sub-national levels of government and where sub-national level entities have wide tax-raising powers.

The project will consider statistical accounting approaches and in particular whether the general government sector (GGS) may provide the appropriate reporting boundary for fiscal sustainability reporting. The GGS encompasses all levels of government, regardless of whether control relationships exist, as well as social security funds and non-market non-profit entities controlled by government units. Under statistical accounting the public sector also comprises public financial corporations and public non-financial corporations. In contrast to the accrual basis the GGS does not consolidate controlled entities outside the GGS sector and does not therefore eliminate balances and transactions between entities in the GGS and other sectors. It treats controlling interests in entities outside GGS as investments. Statistical accounting is used as the basis for long-term fiscal sustainability reporting in a number of jurisdictions.

It will be necessary to determine the reporting entity for fiscal sustainability reporting and in so doing to analyze the advantages and disadvantages of reporting boundaries based on accrual and statistical approaches.

*(iv) Time Horizons*

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

*(v) Regularity of Reporting*

Publication of the general-purpose financial statements is on an annual cycle. However, it is arguable whether the same frequency of reporting should be required or recommended for long-term fiscal sustainability reporting. This is both because of the costs of reporting and the fact that material policy assumptions, demographic assumptions and economic assumptions are unlikely to change sufficiently rapidly within a year to justify the additional costs of annual reporting.

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

*(vi) Assumptions and Sensitivity of Assumptions*

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

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

The term *policy assumptions* refers to the basis on which future levels of service delivery will be determined. It is tentatively proposed that such assumptions should be on the basis of current legal frameworks. This is dealt with in more detail below

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

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

The very preliminary view at the onset of the project is that the IPSASB should not develop detailed requirements as to which assumptions should be used for fiscal sustainability analysis. This will depend upon the portfolio area and the program. However, the project will consider the disclosure of such assumptions. Assumptions are inherently uncertain and changes in those assumptions can have a significant impact on projections: The project will also address the sensitivity of assumptions.

Assumptions also include discount rates. In order to determine the present value of future net cash-flows discounting is necessary. The selection of a discount rate can have a major impact on the amounts reported. The principles governing the selection of discount rates for long-term fiscal sustainability reporting will be explored.

*(vii) Tensions with current legal frameworks*

As a general principle IPSASs have adopted the tenet that transactions and elements are evaluated and determined within current legal frameworks. The view has been that the preparers of the financial statements should not predict governmental actions and that there should be no assumption that programs will terminate unless legislation to that effect has been enacted at the reporting date. If such a principle is adopted for long-term fiscal sustainability reporting the complementary approach to taxation would be that inflows should be determined using current legal requirements and taxation rates unless changes have been effected at the reporting date.

Issues arise as to the correct approach for projections under current frameworks where different legal obligations conflict or where projections are clearly unreasonable. Examples might be where:

- there is a legal requirement for a balanced budget and that requirement cannot be met under existing expenditure projections unless expenditure is reduced, benefits changed, contributions and taxation raised or through extensive disposals of assets: should balanced budget requirements take precedence over entitlements determined under existing legal frameworks or predicted growth trends?;

- where a program is operated on a segregated fund basis and benefits cannot be paid once the fund's earmarked assets have been exhausted and exhaustion is projected within the time horizon of the reporting framework; should the exhaustion of the fund be reflected in projections of outflows of benefits?; or
- projections require taxation levels or debt levels that are not "reasonably" feasible in a global environment, acknowledging that deterring "reasonableness" is highly problematic and risks questioning governmental policy intentions.

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

*(viii) Approach to Discretionary Programs*

Discretionary programs are programs which the government is not required to maintain under current legal requirements beyond a clearly specified date. Discretionary programs may be contrasted with mandatory programs which involve entitlements. Authorizations for discretionary programs may be renewed on an annual basis.

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

A further issue is the appropriate assumption for making expenditure projections for discretionary programs. Such assumptions might include:

- use of 5-10 year trend information for extrapolation purposes;
- same projected growth rate as for GDP; or
- a general or specific inflation index.

#### **4. Implications for Specific Groups**

a) IASB

There is an indirect relationship with the IASB's Conceptual Framework project, although this is primarily addressed through the IPSASB's own Conceptual Framework project. The IASB also has a project on Management Commentary and issued a Discussion Paper in late 2005. The IASB will consider whether a project on Management Commentary should be added to its active agenda in December 2007. Whilst this project will primarily have an influence on the planned IPSASB project on Management's Discussion and Analysis it will be relevant indirectly to this project. In its Discussion Paper the authors of the IASB Discussion Paper proposed that in addition to taking a historical perspective the Management Commentary should take a prospective view in considering the main trends and factors likely to affect an entity's future development, performance and position.

b) Relationship to other IPSASB projects in process or planned

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

(i) *Social benefits*

The IPSASB has an ongoing project on social benefits. The IPSASB's deliberations on social benefits have been catalysts in the decision to initiate this project. The approach in ED 34, "Social Benefits: Disclosure of Transfers to Individuals and Households" is a bridge between accrual approaches and the development of fiscal sustainability information.

(ii) *Conceptual Framework*

A project to develop a public sector conceptual framework is underway. This is led by the IPSASB and carried out in collaboration with the national standard-setters. The components of this Project dealing with the scope of financial reporting, the reporting entity and the objectives of financial reporting are relevant to this project.

(iii) *Management's Discussion and Analysis*

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

c) Other

Reports on the long-term fiscal sustainability of governmental programs are made publicly available in a number of jurisdictions and supra-national bodies also make comparative analyses of the financial condition of nation states available.

Globally a number of public sector standard-setters are considering or developing requirements for narrative reporting in the public sector.

The Financial Report of the United States Government includes a Statement of Social Insurance (SOSI) which adopts a 75 year time horizon for specified programs. The US Financial Accounting Standards Advisory Board (FASAB) has a Standard, SFFAS 17, "Accounting for Social Insurance (Revised 2006)", which provides requirements for the SOSI. FASAB is also developing a Standard providing requirements for broader fiscal sustainability reporting.

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

a) Development process

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

The initial output will be a Consultation Paper. Following analysis of submissions on the Consultation Paper a decision will be made on whether to develop an Exposure Draft of

Reporting Requirements and/or Guidance. An Exposure Draft and/or Guidance will also be subject to formal due process, including a consultation period of at least four months.

**Project timetable**

<b>2007</b>	
November	Project proposal approved
December	Task Force selected and confirmed
<b>2008</b>	
January-September	Task Force develops Consultation Paper
March	Update to Meeting of IPSASB
June	Update to Meeting of IPSASB
October	IPSASB reviews first draft of Consultation Paper
<b>2009</b>	
February	IPSASB reviews second draft of Consultation Paper and approves for publication
March	Publication of Consultation Paper
March-July	Exposure period for Consultation Paper
August-September	Staff analysis of submissions to Consultation Paper
October	IPSASB considers analysis of submissions to Consultation Paper and adopts approach for final stage of project
<b>2010</b>	
February	IPSASB reviews first draft of Exposure Draft (ED) and/or guidance
June	IPSASB approves ED and/or guidance
July	ED and/or guidance issued
July-November	Exposure period for ED and/or guidance
<b>2011</b>	
February	IPSASB considers analysis of submissions to ED/Guidance and provides directions for finalization of final stage outputs
June	IPSASB approves IPSAS and/or Guidance

b) Project output

The initial output will be a Consultation Paper. As indicated above definitive final outputs will be determined following analysis of submissions on the Consultation Paper. It is likely that the final output will be an Exposure Draft of a Standard and/or detailed Guidance.

**6. Resources Required**

a) Task Force

A task force is proposed with a membership of nine (including Chair) – a task force of this size is necessary to reflect a broad cross section of IPSASB constituents and to enable a range of points of view, technical expertise and discussion for the development of this project. However, a larger Task Force might prove unmanageable. Geographical representation is also important to ensure that insights and experience from all with experience of long-term fiscal sustainability reporting are obtained. It is likely that the Task Force will include both IPSASB representation-Members, Technical Advisers and Observers- and external members. The following approximate composition is envisaged:

- Two public sector standard-setters, one of which will have a current project in this area;
- One government entity preparer of general-purpose financial statements;
- Two statistical accountants with experience of preparation of long-term fiscal sustainability projections;
- One preparer of government budget reports;
- One legislative auditor;
- Two surrogates for users of financial statements (e.g.: from the IPSASB Observer group, Consultative Group, academics, members of legislative assemblies).

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

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

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

b) Staff

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

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

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

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

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

Prepared by John R. Stanford  
(Senior Technical Manager IPSASB)

Date 12 November /2007

The following should be completed after board or committee approval and after revising the project proposal form to reflect any changes by the board or committee.

Approved by \_\_\_\_\_

Date \_\_\_\_\_

(Chair IPSASB)

## **COMMENTS BY TECHNICAL MANAGERS**

The comments of Technical Manager from each technical area are required before this Project Proposal is considered by the board or committee proposing to undertake the project.

### **Technical Manager to the Compliance Advisory Panel**

[Insert comments (prompts – views on importance of project, other matters wished to be communicated)]

Signed \_\_\_\_\_

Date \_\_\_\_\_

### **Technical Manager to the DNC**

[Insert comments (prompts – views on importance of project, other matters wished to be communicated)]

Signed \_\_\_\_\_

Date \_\_\_\_\_

### **Technical Manager to the SMPC**

[Insert comments (prompts – views on importance of project, other matters wished to be communicated)]

Signed \_\_\_\_\_

Date \_\_\_\_\_

### **Technical Manager to the IESBA**

[Insert comments (prompts – views on importance of project, other matters wished to be communicated)]

Signed \_\_\_\_\_

Date \_\_\_\_\_

**Technical Manager to the IAASB**

[Insert comments (prompts – views on importance of project, other matters wished to be communicated)]

Signed \_\_\_\_\_

Date \_\_\_\_\_

**Technical Manager to the PAIB Committee**

[Insert comments (prompts – views on importance of project, other matters wished to be communicated)]

Signed \_\_\_\_\_

Date \_\_\_\_\_

**Technical Manager to the IAESB**

[Insert comments (prompts – views on importance of project, other matters wished to be communicated)]

Signed \_\_\_\_\_

Date \_\_\_\_\_

**Technical Manager to the Transnational Auditors Committee**

[Insert comments (prompts – views on importance of project, other matters wished to be communicated)]

Signed \_\_\_\_\_

Date \_\_\_\_\_