Australian Government
Australian Accounting Standards Board

Staff Paper

Project:	**AASB 1049 *Whole of Government and General Government Sector Financial Reporting***	**Meeting**	AASB September 2019 (M172)
Topic:	**GAAP/GFS reconciliation requirements**	**Agenda Item:**	13.1
		Date:	17/09/ 2019
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Objective of this paper

1 For the Board to decide whether relief should be provided from AASB 1049's requirement to disclose government finance statistics (GFS) measures of key fiscal aggregates[1] and reconciliations to those measures from corresponding generally accepted accounting principles (GAAP) measures.

Reason for bringing this item to the Board at this meeting

2 Adoption of AASB 16 *Leases* (first effective for financial year ending 30 June 2020) will result in jurisdictions being unable to reliably calculate GFS measures of key fiscal aggregates and reconcile to them from corresponding GAAP measures in a timely and cost effective way (refer to Attachment 13.2 – request from HoTARAC).

3 If the Board decides to address the issue, it needs to be dealt with before May 2020.[2]

Summary of staff recommendation

4 AASB 1049 should be amended to provide relief from AASB 1049's requirements as per paragraph 1. Ideally, it would be addressed as part of the already planned

1 Refer to paragraphs 11&13 of Attachment 13.3 for the definition and examples of 'key fiscal aggregates'.

2 The Victorian Department of Treasury and Finance (VicDTF) in particular has highlighted that its budget financial statements must be prepared in accordance with accounting standards and audited. For VicDTF, these new accounting standards will impact their 2020-21 budget and 30 June 2020 financial report.

comprehensive and broader post-implementation review (PIR) of AASB 1049 within the context of the review of the public sector financial reporting framework. However the PIR is not expected to be finalised before 2019/20 financial statements. Accordingly, in the interim, a limited amendment should be made to AASB 1049 that:

- allows full optional relief from the requirement to disclose GFS measures of key fiscal aggregates (and the associated GAAP/GFS reconciliations, but only when a jurisdiction elects not to disclose GFS measures); and
- requires additional narrative (not necessarily quantitative) disclosures to help ensure users understand that the GAAP measures of key fiscal aggregates presented in the financial statements are not GFS measures, how they are calculated and how they differ from their corresponding GFS measures.

Attachments

13.2 Letter from HoTARAC (dated 30 April 2019)

13.3 Overview of AASB 1049 – History, Amendments and Current Requirements (for information only)

13.4 Extract from each jurisdiction's 2019-20 budget papers (for information only)

Structure

5 This paper is structured as follows:

- Brief background (paragraphs 6-10)
- HoTARAC's concerns, narrowly focused on the three new Standards (paragraphs 11&0)
- Taking a broader perspective: Is disclosure of GFS key fiscal aggregates and GAAP/GFS reconciliations still needed? (paragraphs 13-16)
- Relationship to other AASB projects (paragraphs 17-20)
- Staff analysis – specific questions (paragraphs 21)
- Staff Recommendation (paragraph 22)

Background

6 AASB 1049 is the Board's response to the Financial Reporting Council's (FRC's) 2002-03 broad strategic direction[3] for the Board to pursue the harmonisation of GFS and GAAP reporting so that, amongst other things, governments' outcome statements are directly comparable with the relevant budget statements. The direction was at least in part

3 Refer to paragraph 1 of Attachment 13.3.

prompted by concerns about the potential for users to be confused by the co-existence of GFS based budget reports and GAAP based financial reports, which looked very similar but adopted different underlying accounting policies.

7 It was within that context that AASB 1049 required disclosure of GFS key fiscal aggregates, GAAP/GFS reconciliations and explanations of differences between GAAP and GFS "so that users are informed about the relationship between GAAP and GFS"[4] and the macro-economic impact of each government and its sectors[5]. There was an expectation at the time AASB 1049 was being developed that any GAAP/GFS legacy differences would be resolved in due course. However, despite the ongoing efforts to harmonise GAAP and GFS and to resolve various legacy differences, the fundamentally different objectives of GFS and GAAP[6] meant that GFS and GAAP could not be perfectly aligned.

8 During a PIR of AASB 1049 in March 2010 the Board reconsidered the need for the reconciliation requirements[7] but decided they should be retained as a critical part because they provide useful information in the context of GAAP/GFS harmonisation.

9 Despite the Board's expectation back in 2007 that "it is possible that the measurement differences will not be of great significance" and "over time, several of the measurement differences will be resolved"[8], as pointed out by HoTARAC[9], the adoption of AASB 1059 *Service Concession Arrangements: Grantors*, AASB 16 *Leases* and AASB 1058 *Income of Not-for-Profit Entities* will create significant new differences.

10 Within this context, the following section analyses HoTARAC's concerns from the relatively narrow perspective of the three new Standards.

HoTARAC's concerns, narrowly focused on the three new Standards

11 As noted in paragraph 9 above, HoTARAC's request is prompted by the implications of AASB 1059, AASB 16, and AASB 1058 for the AASB 1049 reconciliations. In follow-up consultations, HoTARAC has clarified that its request for exemption from GGS reconciliations under paragraph 41(a) of AASB 1049 extends to the public non-financial corporations (PNFC) and public financial corporations (PFC) sectors (and therefore paragraph 52 of AASB 1049) and the whole of government (WoG).

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4 Paragraph BC52 of the Basis for Conclusions on AASB 1049.

5 Paragraph 1(c) of the AASB 1049.

6 Refer to footnote 2 to paragraph 2 of Attachment 13.3

7 Although the reconciliation was regarded by the Board as critical to AASB 1049, it specifies other significant requirements (refer to paragraphs 18-21 of Attachment 13.3). If the Board were to decide to withdraw AASB 1049, consideration would need to be given to whether and if so which requirements should be retained and where they should be located.

8 Paragraphs BC24 of the Basis of Conclusions on AASB 1049 *Financial Reporting of General Government Sectors by Governments* (September 2006) and paragraphs BC50 of the Basis of Conclusions on AASB 1049 *Whole of Government and General Government Sector Financial Reporting* (March 2015)

9 See Attachment 13.2.

12 In relation to each new AAS:

- AASB 1059 changes the accounting for service concession arrangements (SCAs) from a 'risk and reward' to a 'control' approach. However, GFS continues to adopt 'risk and reward', and so a new GAAP/GFS harmonisation difference arises. There is a possibility that ABS will review its GFS rules on SCAs and this convergence issue could be resolved eventually[10]. However, the ABS GFS Manual is generally updated every ten years and the last update was in 2015, hence it is unlikely to change in the near future (and certainly not before 30 June 2020).

- AASB 16 significantly changes lessee accounting by removing the classification between operating and finance leases. However, GFS will maintain the classification. From our discussions with ABS, this difference might never be removed due to GFS's adherence to the counterparty symmetry principle.

  In implementing AASB 16, jurisdictions have decided not to continue maintaining the GFS operating/finance lease classification on cost/benefit grounds. Consequently, ABS has decided to run its own data collection process for GFS leasing purposes – but that information would not be available until after jurisdictions' financial reports have been finalised. As a result, jurisdictions might not have GFS lease data with which to calculate GFS measures of key fiscal aggregates (nor GAAP to GFS reconciliations) before finalisation of the financial statements.

- AASB 1058 may result in a recipient deferring its revenue recognition for certain capital grants while the grantor will continue to expense the grant immediately. However, because GFS follows the counterparty symmetry principle and recognises the capital grants upon receipt/payment for both recipient and grantor, similar to leases, this difference might never be removed.

Taking a broader perspective: Is disclosure of GFS key fiscal aggregates and GAAP to GFS reconciliations still needed?

13 Some may argue that, in light of the widening differences between GAAP and GFS, a necessary consequence of the FRC direction is that disclosure of GFS measures of key fiscal aggregates and GAAP/GFS reconciliations should continue to be mandated so that users can assess the degree of harmonisation.

14 However, our review of the nine jurisdictions' 2019-20 budgets and subsequent outreach to their preparers (eight responded[11]) provides evidence that the differences between GAAP and budget accounting policies have all but disappeared such that the main driver behind the GAAP/GFS reconciliation requirements no longer exists[12]. All

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10 Particularly given that internationally the System of National Accounts (SNA) (of which GFS is effectively a component) has identified SCAs/PPPs as a convergence issue on its research agenda – see [IPSAS-GFS Tracking Table *IPSASB Meeting (June 2019)*].

11 We assured the nine jurisdictions confidentiality for information that is not publicly available.

12 Although it cannot be certain that this will continue to be the case, from our discussion with jurisdictions there is evidence to suggest it will continue for the foreseeable future.

jurisdictions follow the Uniform Presentation Framework (UPF), which is largely consistent with AASB 1049 **presentation** requirements[13]. In terms of **recognition** and **measurement** (R&M), seven out of the nine seem to be fully aligned with GAAP and intend to continue to do so.[14] The other two state they adopt a mixed (but very GAAP dominated) budget framework. Only a handful of items are determined on the GFS basis.[15] The 2019-20 budget paper of the jurisdiction that has yet to respond to our outreach indicates it has been prepared in a manner consistent with AASB 1049.

15 Furthermore, all eight respondents are either not aware of any users (other than potentially ABS) of the published information in the GAAP/GFS reconciliations or question whether such users still exist under current circumstances.[16] To the extent ABS is regarded as a general purpose user of financial statements, our consultations with jurisdictions and ABS confirm that ABS no longer collect budget GFS data nor does it use the GAAP/GFS reconciliations for its GFS reporting purpose[17].

16 We acknowledge there is a basis for HoTARAC's concerns, particularly in relation to AASB 16. Therefore, together with our analysis from a broader perspective, we are of the view that the FRC's direction can now be better achieved without mandating disclosure of GFS measures of key fiscal aggregates and GAAP/GFS reconciliations. Relevant information can be better conveyed through budget vs actual reporting (AASB 1055 *Budgetary Reporting*), and assessment of the macro-economic impact of a government or its sectors would arguably be better met through the published 'official' ABS GFS measures of key fiscal aggregates.

Relationship to other AASB projects

17 Due to the nature of AASB 1049, and the frequency with which it has been subject to amendments[18], it is a relatively 'high maintenance' Standard. In that context, the Board has previously decided it is time to undertake a fundamental review of whether the retention of AASB 1049 (not just its reconciliation requirements) can be justified. In May 2017, in response to stakeholders' feedback expressing particular concerns about the benefits of AASB 1049's fair value asset measurement requirements, the Board decided to add to its 2017-2019 work plan a project "to obtain an external party to perform a cost/benefit analysis of AASB 1049".

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13 Refer to paragraphs 23 of Attachment 13.2

14 Although one indicated it has yet to finalise its assessment of the impact of AASB 1059 and the appropriate recognition of AASB 1058 in a budget context.

15 These include (a) discount rate used in calculating defined benefit liabilities (both adopted GFS); (b) revaluation of loans (one adopted GFS, the other adopted GAAP); (c) dividends to GGS from PNFC and PFC entities (one adopted GFS, the other we have yet to confirm); and (d) deferred taxes (one adopted GFS and the other adopted GAAP). Only (a) and (b) may have a material impact on GGS and WoG. (c) and (d) only impact PNFC and/or PFC entities.

16 In developing this paper we have not consulted directly with users. That would occur as part of any due process the Board decides to undertake in response to HoTARAC's request, and, in any event, would occur as part of the impending more comprehensive PIR.

17 ABS rely on its own data collection process, its own adjustments, assumptions and modelling tools.

18 Refer to paragraphs 5-9 of Attachment 13.3

18 Furthermore, since its introduction, AASB 1049 has been subject to the criticism that the Standard has minimal benefits in practice but significant costs to prepare and is without international precedent. This is consistent with the finding of AASB Research Report No 6 *Financial Reporting Requirements Applicable to Australia Public Sector Entities* (May 2018),[19] which identified that of the countries reviewed, Australia is the only country that requires GAAP/GFS reconciliations. Outside Australia, GAAP/GFS issues are being dealt with in a different way. For example, the International Public Sector Accounting Standards Board's (IPSASB's) policy paper *Process for Considering GFS Reporting Guidelines during Development of IPSASs* (February 2014) merely requires that in revising and developing IPSASs, unnecessary GFS/IPSASs differences should be avoided[20], and IPSASB maintains a tracking table showing GFS/IPSASs differences and highlighting areas where an IPSAS policy choice allows alignment[21]. However, IPSAS 22 *Disclosure of Financial Information about the General Government Sector*[22]remains unchanged (and does not require GAAP/GFS reconciliations).

19 With both the domestic research findings and the international approach in mind, the Board concluded that reform of the Australian public sector financial reporting framework is required. As part of that reform, the AASB released a Discussion Paper (DP) *Improving Financial Reporting for Australian Public Sector* in June 2018, intending to help establish the principles that would underpin a better public sector framework, and outline potential options for change. The reform will be largely driven by the public sector itself. Accordingly, the issue that is the subject of this paper should be addressed having regard to the broader work on the public sector financial reporting framework, including the already planned comprehensive PIR of AASB 1049.

20 In addition to the above, staff have been monitoring the International Accounting Standards Board's (IASB's) Primary Financial Statement project, which aims to achieve targeted improvements to the primary financial statements with a focus on the statement(s) of financial performance[23]. An Exposure Draft is expected at the end of 2019. IASB's tentative decision on Management Performance Measures (MPMs)[24] could have particular implications for paragraphs 16-18D of AASB 1049. This is because many of the fiscal aggregates (including key fiscal aggregates) are GFS concepts[25].

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19 As part of a larger project by the AASB and Auditing and Assurance Standards Board (AUASB) to assist in reviewing the financial reporting framework in Australia for all sectors.

20 IPSASB's Policy Paper: *Process for Considering GFS Reporting Guidelines during Development of IPSASs*, paragraph 2.

21 https://www.ifac.org/system/files/uploads/IPSASB/Alignment%20of%20IPSASs-v1.pdf.

22 IPSAS 22 prescribes disclosure requirements for governments that elect to present information about the GGS in their consolidated financial statements.

23 https://www.ifrs.org/-/media/project/primary-financial-statements/supporting-materials/pfs-project-overview-sept-2018.pdf.

24 IASB's tentative decisions on MPMs include (a) entities are allowed to present MPMs in the notes, (b) MPMs complement subtotals or totals specified by IFRS Standards, (c) no specific constraints on the calculation of MPMs, (d) disclose a reconciliation in the notes between the MPM and the most directly comparable subtotal or total specified by IFRS Standards, and (e) describe why the MPMs provide management's view of performance and how they have been calculated.

25 Fiscal aggregates are referred to as "analytical balances that are useful for macroeconomic analysis purposes, including assessing the impact of a government and its sectors on the economy" on page 13 of the UPF.

However the fiscal aggregates disclosed in financial statements are not measured in accordance with GFS but are measured on the GAAP basis in accordance with paragraph 16 of AASB 1049. Consistent with the direction of the IASB's project, staff are concerned that removing the GAAP/GFS reconciliation requirement altogether without requiring some clarifying disclosures could mislead users (particularly users who are not familiar with Australian public sector financial reporting requirements) into thinking they are (pure) GFS measures.

Staff Analysis – Specific questions

What are the options available to the Board and which would be the best option?

21 Staff have attempted to cover a wide spectrum of possibilities.[26] The following table summarises these options and their respective advantages and disadvantages. Once the Board gives us an idea of its preferred option, we will proceed to consider in greater detail how it could be implemented.

Options	Advantages	Disadvantages
Option 1 – No immediate action until completion of PIR 1. the PIR should be undertaken as a high priority in the context of the review of the public sector financial reporting framework.	1. a deeply considered outcome within the context of the big picture. 2. unambiguously continues to comply with FRC's direction.	1. may not result in a timely outcome that addresses the concerns raised by HoTARAC. 2. the concern that the main driver behind the GAAP/GFS reconciliation requirement no longer exists will not be addressed until after the PIR is completed.
Option 2A – Partial relief with specific exemption (consistent with HoTARAC's request) 1. require numerical reconciliations, but exempt quantification of the GAAP/GFS differences to the extent they arise from at least AASB 16 (and perhaps AASB 1059 and AASB 1058), and instead require narrative disclosure of such convergence differences; and *2.* require disclosure that the resulting key fiscal aggregates reconciled to from GAAP in this manner are neither GFS or GAAP measures.	1. provides an opportunity to quantify and itemise the GAAP/GFS differences where practicable, and explain individual differences narratively when quantification is impracticable. 2. retains the bulk of AASB 1049 intact and thereby minimises the risk of preempting the outcome of the impending PIR.	1. reconciling GAAP measures of key fiscal aggregates to arguably ill-defined non-GAAP non-GFS numbers may mislead/confuse users. 2. does not address the concern that the main driver behind the GAAP/GFS reconciliation requirement no longer exists. 3. maybe perceived as non-compliance with FRC's direction (accordingly if this option is preferred by the Board, staff suggest some discussion with the FRC would be appropriate).
Option 2B – Partial relief without reconciliation 1. require an itemised list of quantified differences between GAAP and GFS (where practicable); and	1. provides meaningful information about each of the causes of the differences between GAAP and GFS.	Same as points 2 and 3 under Option 2A.

26 We have excluded a conceivable option of prohibiting disclosure of GFS measures of key fiscal aggregates and GAAP/GFS reconciliations as we do not regard it as a viable alternative.

Options	Advantages	Disadvantages
2. require a narrative explanation of each unquantifiable difference.	2. avoids the downside of reconciling GAAP to an arguably meaningless Option 2A number.	
Option 3A – Full relief with no additional requirements – silent on it being optional 1. undertake a comprehensive PIR of AASB 1049 as a high priority within the context of the review of the public sector financial reporting framework; 2. delete paragraphs 41(a)(i)&(ii) and 52(b)(ii)&(iii), add no additional requirements, and be silent on whether such disclosures are optional; and 3. consequently amend the other paragraphs and illustrations relating to those paragraphs.	1. addresses the concern that the main driver behind the GAAP/GFS reconciliation requirement no longer exists. 2. similar to point 2 under Option 2A, albeit not to the same extent.	In addition to point 3 of Options 2A and 2B: 1. there is a risk that the big picture public sector financial reporting review including PIR could conclude in favour of retaining the reconciliation requirements[27]. 2. removing GAAP/GFS reconciliation requirements without requiring some clarifying disclosures could mislead users into thinking the disclosed key fiscal aggregates are (pure) GFS measures.[28]
Option 3B – Full optional relief with no additional requirements[29] 1. point 1 of Option 3A above; 2. allow but not require disclosure of GFS measures of key fiscal aggregates; and 3. retain the current requirements[30] when a jurisdiction elects to disclose non-GAAP measures of key fiscal aggregates, including the quantified GAAP/GFS reconciliation requirements.	In addition to point 1 of Option 3A: 1. explicitly allows voluntary disclosure of GFS measures of key fiscal aggregates (which must be accompanied by GAAP/GFS reconciliations) where a jurisdiction assesses that would be useful information for its users. 2. compared with Option 3A, retains more of AASB 1049 intact.	In addition to point 1 of Option 3A and point 3 of Option 2A: 1. there is a risk of that users may be misled about the measures of key fiscal aggregates where GFS measures of key fiscal aggregates and GAAP/GFS reconciliation are not disclosed.
Option 3C – Full optional relief with additional requirements 1. points 1-3 of Option 3B; 2. require disclosure of: • the fact that the disclosed key fiscal aggregates are GAAP not GFS measures;[31] and	In addition to the advantages identified for Option 3B – reduces the risk of Option 3B of users being misled about the measures of key fiscal aggregates.	Same as point 1 of Option 3A and point 3 of Option 2A.

27 However, from the feedback we have received to date, we think this is unlikely to be the case.
28 However, paragraph QC32 of the *Framework for the Preparation and Presentation of Financial Statements* rebuts this concern to some extent. It states "Financial reports are prepared for users who have a reasonable knowledge of business and economic activities and who review and analyse the information diligently. …"
29 Instead this Option would be relying on paragraph 41(a)(iii) of AASB 1049, paragraphs 15, 17(c), 55 and 112(c) of AASB 101 *Presentation of Financial Statements* (December 2017) and paragraph 6(f) of AASB 1055 to provide relevant information for users.
30 Consistent with, for example, paragraphs 16-18D, 41(a) and 52(b)(ii)&(iii).
31 Fiscal aggregates presented in financial statements are calculated using GAAP concepts in accordance with paragraph 16.

Options	Advantages	Disadvantages
• explanations of key technical terms used[32] including explanations of how each fiscal aggregate is calculated and how it differs (not necessarily quantitatively) from its corresponding GFS measure; 3. consequently amend other paragraphs[33] and illustrations relating to those requirements; and 4. rely on the current requirement in paragraph 6(f)[34] of AASB 1055 to provide relevant information for users.		

STAFF RECOMMENDATION

22 On balance, staff recommend Option 3C.

Question to the Board:

With all of the above in mind, what is the most appropriate way for the Board to proceed?

32 AASB 1049 paragraph 41(a)(iii), explained in paragraph 46.
33 Including paragraphs 16-18D.
34 This approach could be implemented in a number of ways: (a) add an explicit requirement into that paragraph specifying that, when relevant, GAAP/GFS accounting policy differences must be disclosed and quantified; (b) add some commentary to AASB 1055 to that effect; or (c) leave AASB 1055 unamended and allow practice to develop. In relation to (c), there is evidence to suggest that practice has developed to provide useful information to users about differences in budget vs actual accounting policies.