PSAB
Public Sector
Accounting Board

PUBLIC SECTOR ACCOUNTING DISCUSSION GROUP

Report on the Public Meeting

June 4, 2018

The Public Sector Accounting (PSA) Discussion Group is a discussion forum only. The Group's purpose is to support the Public Sector Accounting Board (PSAB) by enabling discussion in a public venue of issues arising from the application of the CPA Canada Public Sector Accounting Handbook (PSA Handbook), as well as emerging issues and issues on which PSAB requests advice. The Group comprises members with various backgrounds who participate as individuals in the discussion. Any views expressed in the public meeting do not necessarily represent the views of the organization to which a member belongs or the views of PSAB. The Group discussions do not constitute official pronouncements or authoritative guidance.

This document has been prepared by the PSAB staff and is based on discussions during the Group's meeting.

Comments made in relation to the application of the PSA Handbook do not purport to be conclusions about acceptable or unacceptable application of the PSA Handbook. Only PSAB can make such a determination.

ITEMS PRESENTED AND DISCUSSED

Statement of Concepts: *A Revised Conceptual Framework for the Canadian Public Sector*

PSAB asked the Group to discuss two financial statement foundations proposed in Chapter 5 of the Statement of Concepts, and to provide input on their merits.

Control

The Group appreciated the distinction between sovereign powers and control and felt the definition was generally appropriate. A number of members suggested that a key distinction at the conceptual level should be when control must be exercised to be relevant for financial statement recognition and when the ability to control exists but its exercise is not required as a condition for recognition. For example, at the standards level in Section PS 1300, *Government Reporting Entity*, the ability to control is sufficient; its exercise is not required. But in Section PS 3510, *Tax Revenue*, the power to tax alone is not enough; the power must be exercised (the tax levied) and the taxable event must have occurred for a receivable to exist. The Group suggested exploring whether the ability to control is relevant mostly to entity questions; whereas for individual transaction recognition, the exercise of control may be required. The threat of exercising control or a history of exercising control may also be factors to consider in entity questions; though this may be a standards-level consideration. The distinction between influence and control should also probably be identified.

The effect of defining control and providing related guidance should be evaluated in relation to its implications for future standards-level issues, such as leases, intangibles and other items in the recognition prohibitions. Care needs to be taken to get the concept at the right level. Further, some specific issues with applying control at the standards level were highlighted; for example, the criteria of control in Section PS 1300 are sometimes used as a checklist rather than factors to help in determining when, in substance, control exists. The control proposals in the framework should not change how control is assessed under standards.

Distinctions between political control and economic control, as well as their interaction when the resourcing of entities is in play, were suggested by a couple of members as additional areas to explore. Control over in-year processes versus control over the existence of an entity was differentiated. Further, a conceptual distinction between control and economic dependence should be made; in particular, a dependent entity's ability to say no to funding and shut down may exist, negating a perception of control.

Members asked that an evaluation be done as to whether the proposed concept of control works for all types of public sector entities, including all types of governments and all SUCH sector[1] entities.

Service Capacity

Group members reflected on the proposed concept and considered whether the concept could be narrowed to only economic resources and economic obligations for financial statements. Service capacity is future-oriented by definition, but is being used as a focus for reporting on the past. There is an overlap with the service potential of tangible capital assets. Some appreciated the link to what governments do, especially to the direct provision of services at the local level. Others recognized that the concept could show users if things were "better or worse off" after the year's activities.

Questions were raised as to whether this concept was intended to have implications for standards-level measurement decisions. For example, would fair value measurement of assets and liabilities provide a better measure of service capacity than the existing mixed-measurement model? Or, would it have implications for the accounting for impairments of assets that comprise service potential, requiring more nuanced standards to deal with reductions in service potential than what is currently in the PSA Handbook?

PSAB's intent is not to require the reporting of all of an entity's service capacity in financial statements; but financial statements help to make the broader service capacity evaluation, which would also use information from other accountability reports. It is in the public interest to understand how a public sector entity serves the public and how it manages its capacity to do so. In addition, it was noted that service delivery is more of an operations statement focus (accountability); whereas service capacity is more of a position statement focus that is more future-oriented (sustainability and setting of future tax rates/fees, etc.).

[1] Schools, universities, colleges and hospitals.

Members agreed that the concepts of control and service capacity would have implications and provide some context for future standard setting.

Further proposals from the Statement of Concepts may be discussed at the Group's November 2018 meeting.

Sections PS 3200 and PS 3300: Public Liability Claims

The submission asked the Group to discuss how a municipality should account for public liability incidents (e.g., slip-and-fall accidents) that have occurred, but are unknown to the municipality at year-end. The scenario assumed that the incident had occurred but was not yet reported to, or a claim made against, the municipality. An internal policy to cover the first $25,000 of public liability claims was agreed upon between the municipality and its insurance company, such that the $25,000 was like a deductible. The municipality's annual payments for public liability claims were assumed to be material.

Three views were discussed. Views A and B proposed liability or contingent liability recognition respectively. Both views indicated that the past event was the occurrence of the incident. However, View A asserted that the liability definition in Section PS 3200, *Liabilities*, was met because the agreement with the insurer and past practice removed its discretion to avoid the obligation. View B instead asserted that while the incident before year-end was an existing condition as required by Section PS 3300, *Contingent Liabilities*, there was still uncertainty at year-end as to whether or how many claims would be made, and the amounts could be disputed by the government; uncertainties that would only be resolved after year-end. View C asserted that the past event for recognition purposes would be the reporting of the incident to the municipality and a claim being made. Since neither of these occurred before year-end, recognition would not be appropriate.

The Group did not support View C, and was inclined more toward View B than A given the uncertainties existing at year-end. It was noted that this type of scenario is a form of self-insurance and that under either View A or B the uncertainties would be factored into recognition and measurement of a liability.

Sections PS 3100 and PS 3510: Municipal Off-Site Lot Levies

The submission asked the Group to discuss the accounting for municipal off-site levies in Alberta and whether they would be accounted for as a liability or tax revenue. Section PS 3100, *Restricted Assets and Revenues*, would require them to be accounted for as a liability until used for the specified purposes. Section PS 3510, *Tax Revenue*, would require them to be recognized as tax revenue when the levy is charged and the taxable event, the issue of the development permit, has occurred. The issue arises because Section PS 3510 excludes developer charges from its scope, referring such charges to be accounted for under Section PS 3100. But the PSA Handbook does not define developer charges; so the nature of the exclusions from the scope of Section PS 3510 is not clear.

The Group's discussion explored the nature of off-site lot levies, considering whether they were in the nature of exchange transactions and what types of capital they are intended to finance. Off-site lot levies fund capital needs outside of any particular development site. They are used for the growth-related capital needs of the municipality as a whole; for example, building a ring-road around a city or new major arterial road, or expanding the sewage system capacity to address growth demands. In contrast, on-site levies deal with capital needs of the site; for example, street lighting or links to municipal water and sewage systems from the site.

Members learned that the legislation and related regulations require the off-site lot levies to be used for capital – a very broad restriction. And there are no repayment requirements if the funds are not used for the specified purposes. It was clarified that under a Section PS 3100 conclusion, the levies would be recognized in revenue as the capital asset is acquired, not over the useful life of the related asset.

The Group agreed that the PSA Handbook is not clear and arguments were possible to support either a Section PS 3100 or Section PS 3510 accounting treatment. Two questions formed the basis for much of the discussion:

1. Are the off-site lot levies exchange or non-exchange transactions?
2. Are the restrictions on the use of the levied funds sufficient to comprise an external restriction under Section PS 3100 and thus allow for liability recognition?

Members noted that Section PS 3100 may allow the recognition of liabilities that do not meet the definition of a liability in Section PS 3200, and that Section PS 3100 is out of date. Some noted the wide variety of purposes for which levied funds can be used might be even too broad for the Section PS 3100 definition of a restriction, thus supporting recognition as tax revenue. However, if the levy could be judged as being more in the nature of an exchange transaction (in exchange for the development permit), a Section PS 3100 treatment could be justified. Except, municipalities do capital projects all the time and many jurisdictions will always have growth-related capital expenditures; so for them, there are no real restrictions on the use of the levied funds and they could probably be considered tax revenue.

Ultimately, the Group did not reach a consensus on the issue, indicating that the circumstances of the individual municipality and the terms of the levy may affect the choice of accounting treatment. It was noted that the breadth of the requirement to spend on capital and the lack of repayment requirements may have an impact on enforceability of the use of the levied funds, and accountability for such use.

Consultation Paper: *Reviewing PSAB's Approach to International Public Sector Accounting Standards*

PSAB requested that the Group discuss in a public forum three questions relating to its Consultation Paper, *Reviewing PSAB's Approach to International Public Sector Accounting Standards.*

1. Are the criteria for evaluating the international strategy options proposed in the Consultation Paper the right criteria? Are there additional criteria that should be used?
2. Should any evaluation criteria carry more weight than others?
3. Have the business cases for the options been articulated clearly, and are the distinctions between the options clear?

Responses to the Group's clarifying questions revealed the following contextual information:

- There are currently two Canadian members on the International Public Sector Accounting Standards Board (IPSASB). Retaining two seats is unlikely. In all likelihood one seat, for which the member is nominated by CPA Canada, would be retained.
- The staff complements of the IPSASB and PSAB are comparable and IPSASB staff are located on CPA Canada premises.
- For many IPSASB projects, IFRS® Standards are the starting point. But for public sector–specific standards the IPSASB would essentially start from scratch as PSAB does.
- The IPSASB has 18 members, each of whom is permitted a technical advisor. Some IPSASB observers also attend and have the right to speak at board meetings. The IPSASB holds public meetings to discuss publicly available meeting materials.
- Canada, through CPA Canada and the federal government, provides some annual funding to the IPSASB.
- The IPSASB and the Chartered Institute of Public Finance and Accountancy (a U.K. accounting body) are compiling a report to be issued in 2018, detailing countries that have converged or are considering converging to some degree with the IPSAS.

The Group provided feedback on the criteria and whether they should be weighted. Members indicated that generally, the six criteria make sense, but they provided some additions and suggested weighting.

- PSAB must consider the public interest in setting standards; it is part of its mission. So, the extent to which each option would serve the public interest, the quality of the standards that would result and the nature and extent of the due process that would support standard-setting are key factors to guide PSAB's decision as to which option is best for Canada.
- Canada has a long-standing practice of being a world player, whether it be in foreign policy, standards or other international endeavours. Canada supports global perspectives and global stability and gets involved in global initiatives. The extent to which each option is consistent with this role should be a further criterion considered by PSAB.
- The timeliness of standard setting is an issue, so the resources criteria is important. But there was some feeling that PSAB could leverage the international work to deal with this issue rather than adopting the International Public Sector Accounting Standards (IPSAS), and thus retain some influence (e.g., Option 2).
- Influence is a particular issue for sovereign governments. They already perceive their influence waning over standard setting in Canada as more public sector entities apply the PSA Handbook. This influence could be further reduced if PSAB moves to Options 3 or 4. PSAB was asked to consider this relationship with sovereign governments in making its decision.
- The two current Canadian members on the IPSASB also sit as members of the Group; by virtue of their roles and contribution to the public sector in Canada, not as a consequence of their roles as IPSASB members. They explained that the IPSASB does address Canadian interests and that

many issues for Canada are also issues for other countries and are thus raised at the IPSASB. They felt that the IPSAS could work very well for Canada. Group members and other interested individuals were encouraged to attend the IPSASB meetings when they are held in Canada, or through livestream, when that is available, to see how the board operates.

- The private sector felt similar apprehension in moving publicly accountable enterprises to IFRS Standards, but that move was successful. Two Group members reflected on the Accounting Standards Board and Auditing and Assurance Standards Board experience in moving to international standards. Canada retains influence through its technical expertise, research and outreach to gather and understand Canadian views, as well as sometimes through Canadian members on the international boards. The work of both Boards in reviewing and adopting international standards has increased.
- Influence is also an issue for Indigenous governments. They would retain some influence under Options 1 or 2, but likely none under Options 3 or 4.
- Less important criteria are transition costs, which occur only once, and international alignment, because comparability outside Canada is not as crucial to the public sector. National alignment within Canada was noted as being more important, and comparability with the United States perhaps as a secondary consideration. For some entities, bond raters and capital markets are key users of their financial statements.
- When deciding on the right option for Canada, PSAB should consider the likelihood that its stakeholders would accept its new international strategy.

Regarding options in the Consultation Paper, the Group offered the following:

- Members suggested some further distinctions between Options 2 and 3:
    - Under Option 2, PSAB drives the technical agenda. Under Option 3, the IPSASB would be the driver.
    - Under Option 2, the PSA Handbook conceptual framework would apply. But under Option 3, the IPSASB conceptual framework would be the touchstone for standard setting and resolving issues for which standards do not exist.
    - Option 2 represents a shift from Option 1 because it would require that IPSASB be used as the starting point and PSAB would have to develop ‘rules of the road’ for when departure from the IPSAS is appropriate. Rules of the road would be required for Option 3 too, with less likelihood of departure.
    - There was some feeling that over time, Option 2 would become more like Option 3 and all Canadian standards would be based on the IPSAS. Over time, the prospective versus retroactive distinction in relation to the adoption of IPSAS would no longer hold. It is a question of “taking the Band-Aid off quickly or slowly.”

- Perhaps no one option meets the needs of all Canadian public sector entities and PSAB may have to consider differential reporting. But such an approach would add complexity to generally accepted accounting principles. An exploration of differential reporting will be considered for Consultation Paper 2. Consultation Paper 1 introduces stakeholders to the chosen decision model.
- One Group member requested that Consultation Paper 2 consider the need for a Canadian body to answer Canadian questions and address local concerns under Options 3 and 4.

Statement of Principles: *A Revised Reporting Model for the Canadian Public Sector*

Two issues were proposed for Group discussion:

1. The relocation of net debt indicator from the Statement of Financial Position to its own statement and the removal of the requirement to prepare a Statement of Change in Net Debt.
2. A revenue or expense of a period may not be recognized in the surplus/deficit of that period but instead initially recognized directly in a component of net assets/net liabilities.

Only Issue 1 was discussed. Issue 2 was deferred for discussion at the Group's November 2018 meeting.

In response to some clarifying questions it was noted that:

- There is nothing in the proposals to prevent an entity from continuing to provide the Statement of Change in Net Debt. However, given PSAB's concerns with the understandability of that statement and possible confusion with the Statement of Surplus/Deficit if a direct presentation approach is used, the accountability objective may not be met if the Statement of Change in Net Debt is retained.
- The comparison of actual to budget capital expenditures currently provided in the Statement of Change in Net Debt is proposed to become a disclosure requirement in Section PS 3150, *Tangible Capital Assets*.

The Group provided feedback on the proposals in the Statement of Principles regarding net debt. Members were generally supportive of the net debt indicator. Some members were in favour of the proposals relating to net debt. Others expressed concerns.

- Having the net debt indicator on the Statement of Financial Position and being able to see it in relation to the magnitude of non-financial assets provides valuable accountability information.
- While the proposed Statement of Net Debt might provide an opportunity to explain volatility in net debt, it would not address the issue that for financial instruments held to maturity, this volatility is artificial.
- Issues supporting the proposed move of net debt from the Statement of Financial Position to its own statement could be addressed in other ways. For example, endowments restricted in perpetuity could be reported with non-financial assets, rather than financial assets, given the

restrictions in their use. Performance obligations could be addressed in another way too, so they are excluded from liabilities included in the net debt calculation.

- The inclusion of deferred capital contributions in the net debt indicator of some government not-for-profit entities renders the indicator meaningless. The proposals address this issue.
- PSAB could consider requiring the same accounting principles for all entities but different presentations or different financial statements in the financial statement package of different types of entities.
- PSAB could consider developing criteria for when net debt can be reported on the Statement of Financial Position and when a Statement of Net Debt is required. Not all entities will have a need to exclude items from net debt.