Introduction to International Public Sector Accounting Standards (IPSAS) Workshop Transcript Session 5: Expenses

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We will now turn our attention to the last session of the workshop, dealing with expenses.

In this session we will look at two standards,

- IPSAS 42 which provides guidance on the accounting for social benefits. And we will look at
- Appendix A of IPSAS 19 which provides guidance on collective and individual services.

The delivery of social benefits to the public is a primary objective of most governments, and accounts for a large proportion of their expenditure.

Governments also provide services, for example healthcare and defense. Such services are outside the scope of social benefits; instead they are covered by guidance on Collective and Individual Services, which can be found in Appendix A to IPSAS 19, Provisions, Contingent Liabilities and Contingent Assets.

I will now turn it over to Iman to walk us through these topics.

Iman Sheikh: Thank you Antonella. Before we begin, I wanted to highlight that IPSAS 42 is a public sector specific standard; there is no IFRS equivalent.

So what are social benefits?

Examples of Social Benefits include:

- Unemployment Benefits
- State Retirement Pensions
- Disability Pensions

More specifically, social benefits are cash transfers (including transfers in the form of cash equivalents, for example pre-paid debit cards) provided to individuals and/ or households.

Social benefits are only provided when eligibility criteria (to receive a social benefit payment when it is next paid) are met.

For example, a government may provide unemployment benefits to ensure that the needs of those whose income during periods of unemployment would otherwise be insufficient are met.

Although the unemployment benefit scheme potentially covers the population as a whole, unemployment benefits are only paid to those who are unemployed, i.e. those who meet the eligibility criteria.

The assessment of whether a benefit is provided to mitigate the effect of social risks is made by reference to society as a whole. The benefit does not need to mitigate the effect of social risks for each recipient.

An example is where a government pays a retirement pension to all those over a certain age, regardless of income or wealth, to ensure that the needs of those whose income after retirement would otherwise be insufficient are met. Such benefits satisfy the criteria that they are provided to mitigate the effect of social risks.

Social risks relate to the characteristics of individuals and/or households–for example, age, health, poverty, and employment status. The nature of a social risk is that it relates directly to the characteristics of an individual and/or household. The circumstances that lead to an unplanned or undesired event arise from the characteristics of the individuals and/or households. This distinguishes social risks from other risks, where the circumstances that lead to an unplanned or undesired event arise from something other than the characteristics of an individual or household.

For example, unemployment benefits are social benefits because the circumstances covered by the unemployment benefit arise from characteristics of the individuals and/or households – in this case a change in an individual's employment status.

By contrast, aid provided immediately following an earthquake is not a social benefit. Because the risk relates to geography rather than individuals and/or households, this risk is not a social risk.

IPSAS 42 permits two approaches to accounting for social benefits.

The general approach is expected to apply to most social benefits; and for many governments will be the only approach that they use.

The insurance approach is an optional approach, and IPSAS 42 only permits its use when specified criteria are met. Because entities will generally apply the general approach, this presentation focuses on this approach.

The general approach includes a single recognition point for all social benefits and follows the principles in the Conceptual Framework for recognizing a liability.

The key factor in determining when a liability for a social benefit arises is identifying the past event. Under the general approach, the past event that gives rise to a liability is the satisfaction by the beneficiary of all eligibility criteria for the provision of the next social benefit.
The satisfaction of eligibility criteria for each social benefit payment is a separate past event.

Antonella Risi: You mentioned eligibility criteria, what is an example of an eligibility criterion?

Iman Sheikh: Being alive at the point at which the eligibility criteria are required to be satisfied may be an eligibility criterion, whether explicitly stated or implicit. This depends on the characteristics of each individual social benefit scheme.

Other ongoing eligibility criteria may be relevant for some social benefit schemes.

For example, many unemployment benefits are only payable while the individual remains resident in the jurisdiction; residence is an ongoing eligibility criterion.

Antonella Risi: Can we look at some social benefit recognition examples?

Iman Sheikh: The recognition examples are examples of when a beneficiary may first satisfy all the eligibility criteria for the provision of the next social benefit. To continue to receive the social benefit, beneficiaries would need to continue to satisfy the eligibility criteria.
Some social benefits include a waiting period as part of the eligibility criteria.

For example, some unemployment benefits are paid after an individual has been unemployed for a set amount of time, say 14 days. Where there is this type of waiting period, the eligibility criteria are only satisfied once the individual has been unemployed for the specified period.

Antonella Risi: Great, thank you! Now that you have covered recognition, can you walk us through the measurement of these expenses?

Iman Sheikh: Sure – let's look at when expenses are recognized and when liabilities are recognized when it comes to social benefits.

When it comes to the Measurement of Expenses……

An entity recognizes an expense for a social benefit scheme, measured at the amount of the next payment following satisfaction of the eligibility criteria. Discounting of the expense will not be required for most social benefits, because the next payment will usually be made within twelve months.

Where the entity makes a social benefit payment prior to all eligibility criteria for the next payment being satisfied, it measures the payment in advance (or expense recognized where the payment is irrecoverable) at the amount of the cash transferred.

When we talk about the Measurement of Liability ……

Under IPSAS 42, the liability for a social benefit scheme is measured at the best estimate of the costs that the entity will incur in fulfilling the present obligations represented by the liability.

In this context, "costs" means the social benefit payments to be made (i.e., the cash transfers). The costs do not include other elements such as administrative costs and bank charges.

Because the satisfaction of eligibility criteria for each social benefit payment is a separate past event, the liability is for the next payment only. Consequently, liabilities in respect of social benefits will usually be short-term liabilities. As a result, an entity will often know the amounts involved without needing to make estimates. Similarly, because liabilities in respect of social benefits will usually be short-term liabilities, discounting will not be required for most social benefits.

Where a liability has yet to be settled, the liability is reviewed at each reporting date, and adjusted to reflect the current best estimate of the social benefit payment required to fulfill the liability.

As with all other transactions, there are disclosure requirements related to social benefits. Some of these requirements are listed on the slide, and include

- Characteristics of social benefits;
- demographics,
- economic and other external factors that influence the level of expenditure,
- the total expenditure related to a social benefit scheme, and
- a description of any significant amendments to social benefit schemes,

Amongst other requirements.

Antonella Risi: Thank you Iman for taking us through IPSAS 42, Social Benefits. Now we will take a look at collective and individual services

Iman Sheikh: Let me provide a bit of background first.

When IPSAS 19, Provisions, Contingent Liabilities and Contingent Assets, was first issued, provisions and contingent liabilities arising from social benefits were excluded from the scope of the Standard. IPSAS 42, Social Benefits, amended IPSAS 19, to bring within the scope of IPSAS 19 collective and individual services. A key issue addressed by the amendments to IPSAS 19 is whether a provision arises in respect of those transactions.

Let's take a closer look at collective services – shall we?

The provision of a collective service to one individual does not reduce the amount available to other individuals; there is no rivalry in the consumption of collective services. Consumption of collective services is usually passive and does not require the explicit agreement or active participation of those benefiting from the service.

Antonella Risi: can you provide some examples of a collective service?

Iman Sheikh: Sure!

Examples of collective services include defense and street lighting.

Antonella Risi: Thank you. And can you give us an example of individual services?

Iman Sheikh: Examples of individual services include universal health care and education.

The provision of an individual service to one individual may reduce the amount available to other individuals, or may delay the receipt of those services by some individuals. Consumption of individual services requires the explicit agreement or active participation of those benefiting from the service. Goods or services provided by a public sector entity on commercial terms do not address the needs of society as a whole, and therefore do not satisfy the definition of individual services.

This slide provides a quick summary of what we discussed. Key point to note is that social benefits involve a cash transfer, whereas collective and individual services involve the provision of services.

Antonella Risi: Now that we have looked at what collective and individual services are, can you walk us through how collective services and individual services are accounted for?

Iman Sheikh: Sure.

The key point here is that collective and individual services are considered to be ongoing activities of the public sector entity that delivers the services. Paragraph 26 of IPSAS 19 states that “no provision is recognized for costs that need to be incurred to continue an entity’s ongoing activities in the future”. Consequently, no provision is recognized for the intention to deliver collective services or individual services in the future. Expenses are recognized as the services are delivered, in accordance with other IPSAS.

In delivering collective services, a public sector entity acquires resources and incurs expenses through contractual and other binding arrangements. Examples include the salaries paid to defense staff, the electricity used in delivering street lighting, the acquisition of non-current assets used in delivering those services, and the purchase of collective services from a third-party provider.

Similarly, the delivery of individual services is an ongoing activity of the public sector entity that provides the services. The delivery of individual services results in the public sector entity acquiring resources and incurring expenses through contractual and other binding arrangements.

For both, collective services and individual services, contractual and other binding arrangements would be accounted for in accordance with other IPSAS. These arrangements may give rise to a liability, but the liability arises from the contract or binding arrangement, not the promise to provide collective services. The public sector entity uses the resources acquired to deliver individual services. Where individuals access these services, the entity may have a number of future obligations relating to the delivery of these individual services. However, these obligations are not present obligations and do not give rise to a liability.

As with collective services, no provision is recognized for the intention to deliver individual services prior to individuals and/or households accessing the services.

And that is the end of my presentation on the two expense standards.

Antonella Risi: Thank you Iman for taking us through these very interesting standards.