

# **PSAB'S International Strategy Decision: Option 2 – Adapt IPSAS principles when developing future standards**

**September 2020**

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**CPA Canada Public Sector Accounting Handbook**

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*Prepared by the staff of the Public Sector Accounting Board*

## **FOREWORD**

The primary objective of a Basis for Conclusions document is to set out how the Public Sector Accounting Board (PSAB) reached its conclusions. It also sets out significant matters arising from comments received in response to the proposals exposed and indicates how PSAB has dealt with the issues raised.

These documents are intended to assist financial statement users, preparers, auditors and other parties interested in public sector financial reporting in understanding the rationale PSAB follows when developing or amending standards, or strategic decisions.

This document has been prepared by staff of PSAB. It does not form part of the PSA Handbook nor is it part of public sector generally accepted accounting principles. Basis for Conclusions documents also do not include any guidance on the application of the relevant Section or Guideline.

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## BACKGROUND

1. On May 5, 2020, PSAB voted to approve “Option 2 – Adapt IPSAS principles when developing future standards,” as described in Consultation Paper 2, “[Reviewing PSAB's Approach to International Public Sector Accounting Standards](#).” This decision resulted from extensive consultation with Canadian stakeholders. The Board initiated the project through its 2017-2021 Strategic Plan, “Review of PSAB's Approach to International Public Sector Accounting Standards.”
2. PSAB's Strategic Plan outlines the broad strategic objectives that guide the Board in achieving its public interest mandate over a multi-year period. A key strategy of the 2017-2021 Strategic Plan reflects the increasing trend toward global harmonization of accounting standards in the private and public sectors.
3. As it developed its Strategic Plan, PSAB determined that the time was appropriate to review its approach toward its international strategy and International Public Sector Accounting Standards (IPSAS), especially as more countries were adopting or adapting IPSAS. This strategy outlined that over the 2017-2021 period, the Board would:
  - (a) research the differences between Public Sector Accounting Standards (PSAS) and IPSAS;
  - (b) learn about the experiences of other jurisdictions that follow, partially follow or not follow IPSAS;
  - (c) publish a consultation paper to get stakeholders' opinions; and
  - (d) develop options that would inform the Board's approach to its future international strategy.
4. PSAB released its first of two Consultation Papers, “[Reviewing PSAB's Approach to International Public Sector Accounting Standards](#)” (Consultation Paper 1), on May 28, 2018. Consultation Paper 1 introduced stakeholders to the decision-making model that the Board would use to evaluate the international strategy decision. It asked key questions on the decision-making criteria and described the four potential options. It did not seek opinions on which option the Board should pursue.
5. PSAB received 29 written responses to Consultation Paper 1, including some joint responses representing 63 respondents. The Board also received verbal feedback during presentations and meetings with stakeholders.
6. PSAB and its [Strategic Advisory Group](#), which was formed to provide strategic direction on the International Strategy project, reviewed the feedback to Consultation Paper 1. The feedback was used to develop Consultation Paper 2.
7. Consultation Paper 2 was released on May 8, 2019. It finalized the international strategy options and sought stakeholders' feedback on which option was in the Canadian public interest.
8. PSAB received 28 written responses to Consultation Paper 2. The Board also conducted 18 interviews with stakeholders across Canada to obtain feedback. When considering joint written and interview responses, 102 respondents provided feedback. Respondents were diverse, including comptrollers, legislative auditors, local governments, First Nations groups, accounting firms, accounting organizations (both Canadian and international) and government not-for-profit organizations (GNFPOs).
9. Stakeholders' responses to both Consultation Papers shaped PSAB's final decision on its international strategy.

## SUMMARY OF RESPONDENTS' VIEWS

10. Consultation Paper 2 asked stakeholders which of the four international strategy options best meets the Canadian public interest.
11. Compared to the feedback received on Consultation Paper 1, responses to Consultation Paper 2 indicated that stakeholder sentiment had shifted toward adopting IPSAS. While there was some support for Option 1 (“Status Quo”), the responses indicated an acceptance of a more internationally aligned approach. Most stakeholder feedback, both written and interview, showed a preference for Option 2. While Consultation Paper 1 did not seek responses on this topic, many respondents readily voiced their preference for Option 1.
12. A shift in stakeholder opinion toward Option 2 was a major consideration for PSAB in its decision to adopt Option 2 as its international strategy.
13. In both Consultation Papers, PSAB committed to evaluating the international strategy decision according to five criteria:
  - (a) high-quality accounting standards;
  - (b) due process;
  - (c) international alignment;
  - (d) Canadian control and influence over the standard-setting process; and
  - (e) transition costs.
14. PSAB determined that all criteria would be weighted equally in its evaluation. While it considered whether certain criteria should be weighted more heavily than others, the Board decided against this approach. This was based on the small number of criteria in total, the subjectivity involved in weighting and the Board's desire that the evaluation not become a numerical exercise.

## EVALUATION OF THE OPTIONS

15. In providing their responses to which option best meets the Canadian public interest, stakeholders focused on Canadian control and influence over the standard-setting process, international alignment and transition costs. As a result, these evaluation criteria will be discussed first, followed by the remaining two criteria: high-quality accounting standards and due process.

### Canadian control and influence over the standard-setting process

16. One of the main factors in PSAB's decision to pursue Option 2 as its future international strategy was respondents' views toward Canadian control and influence over the standard-setting process.
17. In its decision-making process, PSAB noted that whichever option it pursued, it needed to maintain strong Canadian control and influence over the standard-setting process. This, along with the desire to maintain Canadian stakeholders' strong control over standards, meant that Option 1 or 2 would be most feasible. Although the Board and the respondents acknowledged that Option 1 would allow the most control and influence, Option 2 would still allow significant control and influence while enabling greater involvement in international standard setting. Stakeholders who supported Option 2 also noted this.

18. Under Option 2, PSAB and some respondents noted that the Board would continue to have full autonomy in identifying, prioritizing and determining which projects it would pursue. If the Board chose to develop a standard where an international standard already exists, the principles in that IPSAS would be used to develop the Canadian standard. The Board would still be responsible for developing the standard to ensure it meets Canadian stakeholders' needs. Further, under this option, the Board would maintain the ability to modify IPSAS principles, in accordance with approved criteria, if a Canadian need exists.
19. Some respondents expressed concern that a change in international strategy, particularly to Option 3 or 4, would result in less Canadian control and influence in standard setting. They thought Canadian control and influence would be reduced under these options as the International Public Sector Accounting Standards Board (IPSASB) agenda-setting process considers issues important to all global stakeholders. Some respondents argued that this may make it difficult to address Canadian issues in a timely manner and may result in standards being developed that do not fully meet the needs of Canadian users and preparers. With Option 2, this would not be the case. PSAB and Canadian stakeholders would continue to have full control over its agenda-setting process, and Canadian financial reporting issues would continue to be addressed as needed. All standards that are developed would be developed with only Canadian stakeholders in mind.
20. PSAB also noted that moving to Option 2 would further strengthen Canada's position as a leader in international standard setting and further enhance the Board's relationship and collaboration with the IPSASB. It would allow the Board to better influence standard setting at the international level and be a stronger voice in international public sector standard setting.
21. Some respondents who were hesitant of a change in PSAB's international strategy were concerned that IPSAS was not specific to the Canadian environment. They said a change in international strategy, particularly to Option 3 or 4, would result in standards that are less customized to the Canadian environment. They noted that IPSAS has largely been developed without Canadian input as few Canadian stakeholders have responded directly to IPSASB documents for comment in the past. These respondents added that those that do respond tend to be larger governments or Auditors General, and so are not seen as representing the entire scope of PSAB's stakeholders.
22. While it has heard these concerns, PSAB notes, under Option 2, it would continue to develop Canadian standards for its stakeholders. Therefore, this move would not result in standards less specific to the Canadian environment. While few Canadian stakeholders have responded to IPSASB documents for comment in the past, the Board's relationship with IPSASB has been close for many years. PSAB staff have taken an active approach to responding to IPSASB documents for comment, including giving Canadian-specific input for developing international standards. The Board's staff have also participated in task-based groups and provided technical support to Canada's IPSASB members. This support includes providing briefing notes related to the IPSASB agenda items with Canadian-specific context.
23. Respondents correctly pointed out that there is no guarantee of Canadian representation on the IPSASB in the future. However, PSAB believes it has developed and implemented processes to ensure IPSASB hears Canadian stakeholders' voices. When Option 2 is implemented in Canada, PSAB will promote all of IPSASB's discussion papers through its various communications channels. Canadian stakeholders will be encouraged to review and respond. The Board will also provide official responses to IPSASB documents for comment. PSAB will consult stakeholders on IPSASB projects that are highly relevant to the Canadian public sector.

24. PSAB has noted that concerns of reduced Canadian control and influence over the standard-setting process were raised during the transition in Canada to both International Financial Reporting Standards (IFRS) and International Standards of Auditing. To mitigate these concerns, the Accounting Standards Board (AcSB) and the Auditing and Assurance Standards Board (AASB) implemented processes that focused on influencing the development of international standards to ensure Canadian stakeholders' voices were heard. Almost 10 years after implementation, AcSB's and AASB's influence on the international standard-setting process is strong. Canada's experience with both private sector accounting and auditing demonstrates that it is possible to effectively influence international standard setters to Canadian stakeholders' benefit. The Board is currently developing a multi-faceted process to ensure IPSASB hears Canadian public sector perspectives.

## International alignment

25. In addition to meeting stakeholders' current needs, it is the responsibility of all effective standard setters to be forward-looking, to anticipate and to address stakeholders' future needs. PSAB thinks being comparable to international public sector organizations will become increasingly important to Canadian public sector organizations in the coming years. Moving to Option 2 will gradually increase the alignment with international standards.
26. Under Option 2, all future PSAS would be developed using IPSAS principles when an existing IPSAS exists. This will increase comparability between Canadian and international public sector organizations. PSAB will still have the ability to modify the IPSAS principles if a Canadian need exists.
27. Some respondents were not persuaded that international comparability should be a rationale for changing PSAB's approach toward its international strategy. They noted that Canadian public sector organizations compare themselves to other similar provincial and national organizations when needed. They did not see a strong need to change Canada's international strategy to make these comparisons.
28. Although international comparability may not have been important in the past, PSAB thinks that it is becoming increasingly important, especially as more Canadian public sector organizations compete internationally. This is especially true for certain public sector organizations, such as the federal government, post-secondary institutions and specific types of GNFPOs such as research hospitals and museums. Users and the general public are increasingly making comparisons between the Canadian federal government and other national governments. For GNFPOs, being internationally comparable is becoming increasingly important in qualifying for and receiving donations, research funding and enrolment. Moreover, it is becoming more common for public sector organizations to seek capital market financing.
29. While international alignment may not be important or relevant to all public sector organizations at this time, PSAB does not consider this a valid reason to stay with Option 1. It believes it has a responsibility to anticipate and consider its stakeholders' future needs.
30. Other respondents shared this view. Option 2 would allow for better buy-in from stakeholders and improve comparability and understandability for users in the private and public sectors. This may result in more active engagement from those familiar with private sector standards in reviewing public sector organizations' financial statements. These respondents also noted that this will also likely result in greater understanding of public sector statements.
31. With regards to comparability, some respondents had concerns over how PSAB selected countries (i.e., Australia, New Zealand, the United States and the United Kingdom) to compare with Canada in Consultation Paper 1. A few respondents noted that many countries looking to adopt IPSAS are not comparable to Canada. They are less developed than Canada economically and use different methods of accounting, such as the cash basis. These respondents commented that the nature of these economies means that financial statement users are not likely to make a direct comparison between these countries and Canada.

32. PSAB focused on these countries because most Canadian stakeholders are likely to compare Canada with other G7 countries. While it is true many of the countries looking to adopt IPSAS are smaller and may be less mature, many of Canada's comparators have a close relationship with IPSAS: New Zealand follows IPSAS. The United Kingdom follows IFRS® Standards with modification for the public sector, which have been found to be 95 per cent compliant with IPSAS. Australia follows IFRS Standards, on which IPSAS is based, with modifications for the public sector. With many of these countries using IFRS Standards or IPSAS as their core financial reporting framework, the Board noted that it is difficult to justify continuing with the status quo.
33. A small minority of respondents noted PSAS is not consistently applied across Canada and this should be improved before PSAB looks at moving toward international standards. The Board agrees there are opportunities to improve consistent application of PSAS across Canada. These concerns are likely to continue to exist, whether the Board changes its international strategy. It is aware of this issue and will consider this as it implements Option 2.

## Transition costs

34. A large factor in PSAB choosing to pursue Option 2 over Option 3 or 4 were respondents' concerns over transition costs. Respondents were clear in outlining their hesitance to pursue an option that would result in significant transition costs.
35. Respondents expressed concern that a change in international strategy to an option that requires retrospective adoption, such as Option 3 or 4, may result in the costs to transition outweighing the potential benefits. They highlighted the many costs associated with a retrospective adoption of a new framework: time and resources, system and technology modifications and staff education, among other things. Respondents highlighted that many public sector organizations, especially small organizations, may not have the resources or technical knowledge to retrospectively adopt IPSAS. As a result, a change in financial reporting frameworks could divert tax dollars and resources away from public sector mandates and into administration. They noted that the high potential costs of retrospective adoption call into question whether a change to Option 3 or 4 best serves the Canadian public interest.
36. Some respondents noted that there may also be significant implementation challenges around Option 3 or 4, particularly as it relates to differences in accounting treatment. One example provided was the difference in accounting for government business enterprises (GBEs). Under PSAS, GBEs are accounted for using the modified equity method of consolidation. IPSAS requires a more involved line-by-line consolidation.
37. As a result of these concerns, many respondents noted that they preferred Option 2 over Option 3 or 4. Under Option 2, the change in international strategy is prospective in nature and, as such, results in low or no transition costs. They noted this would result in minimal disruption to public sector organizations and would continue to allow public sector organizations to direct their resources toward their mandate.
38. PSAB acknowledges that a change in international strategy requiring retrospective adoption may result in high transition costs for its stakeholders. Option 2 provides a gradual alignment with international standards, while maintaining a high level of Canadian control and influence, with minimal immediate transition costs to stakeholders.

## High-quality accounting standards

39. PSAB has noted that IPSAS and PSAS are high-quality financial reporting frameworks.
40. In Consultation Paper 2, PSAB defined high-quality accounting standards as standards that allow financial statements users to analyze a public sector organization's financial situation. The Board



believes that understandability is a key component. It debated whether moving to Option 3 would increase understandability of financial reporting even more than Option 2. However, the Board understood that, based on responses to Consultation Paper 2, stakeholders were not yet ready for such a big change.

41. Moreover, PSAB also defined high-quality accounting standards as being responsive and relevant to stakeholders and addressing the diverse financial reporting requirements various public sector organizations face. As the standard setter for all public sector organizations in Canada, the Board is responsible for setting standards for a diverse stakeholder group. Some of the largest groups that follow PSAS include GNFPOs, other government organizations (OGOs) and government partnerships (GPs). Any Board decision with regards to its international strategy must be made with these stakeholders in mind.
42. A large factor in PSAB's decision to move to Option 2 in its international strategy was that it would continue to develop standards that meet its stakeholders' needs, including GNFPOs, OGOs and GPs.
43. Respondents noted IPSAS is a framework primarily responsible for providing guidance to governments and government entities. They noted that it would be difficult to meet GNFPOs' needs under Option 3 or 4. Many respondents follow GNFPO-specific standards that have no equivalent under IPSAS. Some respondents noted similar concerns existed for OGOs and GPs because IPSAS lacks guidance for these types of organizations.
44. These respondents noted that following Option 2 would allow PSAB to better cater to the needs of these types of organizations, as it maintains the ability to provide specific guidance for GNFPOs, OGOs and GPs. This guidance would not exist under Option 3 or 4 and would result in a significant change for these stakeholders.
45. Some respondents suggested that additional guidance may be developed to supplement IPSAS if PSAB moved to Option 3 or 4. Other respondents noted that PSAB could explore the possibility of having differential reporting for GNFPOs, OGOs and GPs where the full suite of IPSAS may not be necessary. While it evaluated these options, the Board did not want to pursue them at this time.

## Due process

46. Consultation Paper 2 defined "due process" as the mechanisms, procedures and processes in place that result in the development of high-quality accounting standards. PSAB believes that moving to Option 2 would result in greater efficiency and economy in standard setting.
47. In the past, stakeholders noted that the existing Canadian standard-setting process can, at times, be lengthy. This affects Canadian stakeholders' ability to get timely and relevant guidance to the issues they are currently facing. As a standard setter responsible for developing standards to address issues arising for its stakeholders in a timely manner, PSAB is constantly looking for ways to improve time to market for the development of PSAS. The Board feels that moving to Option 2 would result in standards being developed more quickly and would allow it to better meet its stakeholders' needs. Under Option 2, the Board could use the principles already developed by another reputable standard setter when developing future PSAS.
48. Many respondents agreed. They noted that a change in international strategy would likely result in standards being developed more quickly to address current stakeholder and business needs. They said that timelier standards would be in the Canadian public interest and contribute to high-quality and relevant standards. A few respondents even suggested that moving to Option 3 would achieve this outcome.
49. At the same time, standard-setting resources are limited. There is a constant need to develop standards addressing new and emerging issues in the Canadian public sector environment. By moving forward with Option 2, PSAB noted that it could use standards already developed by another

standard setter. This would allow the Board to reduce duplicating work efforts, deploying its limited resources to high-value areas where there are no existing national or international standards.

50. Some respondents noted that Option 1 (Status Quo) does not preclude PSAB from using IPSAS when developing PSAS. They noted the Board may not need to change its international strategy to use other standard setters' work. If the Board's due process needs improvement, those changes can be addressed independently without a change in accounting framework. The Board acknowledges that this approach was possible but thinks it would be beneficial to consult with stakeholders and formalize the process of using IPSAS principles when developing PSAS standards.

## OTHER FEEDBACK FROM STAKEHOLDERS

51. In addition to the feedback received above, PSAB received other points to consider in its international strategy evaluation. What follows is a discussion of some of the most common "other" comments received to Consultation Paper 2. It is not an exhaustive list of all the other feedback.
52. Some respondents had concerns about how applying Option 2 would vary in practice, depending on the stringency of the Criteria for Modifying and Reviewing Principles in IPSAS document. Respondents noted that overly stringent criteria may result in an option closer to Option 3, while less-stringent criteria might result in an option closer to Option 1. They said it would be difficult to contemplate the options' merits if these criteria have not been developed. PSAB agrees with this feedback and notes that it developed and considered a draft of the criteria for Options 2 and 3 before it decided on the strategy. The Board is finalizing the Criteria for Modifying and Reviewing Principles in IPSAS document and will share it publicly once it is formally approved.
53. Respondents also highlighted that regardless of the option PSAB chooses, PSAS and the due process involved in developing the standards need to be maintained in both French and English. These respondents noted it was important that exposure drafts be available in both official languages. PSAB agrees it is important to maintain the development of standards in both English and French. With Option 2, the Board will continue its consultation process in both official languages. This includes its documents for comment, exposure drafts and bases for conclusions. The Board will also be responsible for formally responding to IPSASB documents for comment and may consult with both French and English stakeholders before doing so.
54. Other respondents had concerns that a change in international strategy would introduce private sector concepts and volatility into PSAS. They noted that IPSAS is based on IFRS Standards, a for-profit framework, and would not appropriately meet the needs of the Canadian public sector and its users. These respondents explained that public and private sector objectives are inherently different and that fair value accounting may lead to poor long-term decision making by governments, which are often risk adverse. PSAB acknowledges the respondents' concerns. However, many countries including Australia, New Zealand and the United Kingdom, use IPSAS or IFRS Standards effectively in their financial reporting for public sector organizations. Moreover, Option 2 provides the Board with the ability to modify IPSAS principles that are not appropriate for application in Canada.
55. A few respondents highlighted that a change in international strategy may result in less acceptance of standards, particularly under Option 3 or 4, and, therefore, more instances of legislated accounting in Canada. PSAB recognizes there is a risk of legislated accounting under all options as some governments may feel that IPSAS or IPSAS principles are less suited to the Canadian environment. Legislated accounting not only reduces international comparability but also comparability within Canada.

## **CONCLUSION**

56. As it begins to implement its new international strategy, PSAB wishes to thank its stakeholders for their active involvement and engagement in the consultation process. The Board worked hard to understand and meet the needs of its diverse group of stakeholders in coming to an international strategy decision.
57. PSAB hopes that this change in international strategy will improve its standard-setting process, allowing the Board to better serve its stakeholders and to better anticipate their future needs.

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