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PREFACE

Introduction

1. This preface:

   - provides some background information about the role of the Public Sector Committee (PSC), and an overview of accounting and financial reporting by governments;
   - outlines the purpose of this Study; and
   - describes the PSC's Standards Project, of which this Study is a key component.

Role of the PSC

2. International Federation of Accountants (IFAC) is a worldwide organization for the accountancy profession. Its mission is the development and enhancement of the profession to enable it to provide services of consistently high quality in the public interest. The PSC is a standing committee of the Council of IFAC formed to address, on a co-ordinated worldwide basis, the needs of those involved in public sector financial management, reporting, accounting and auditing. In this context, the term "public sector" refers to national governments, regional (e.g., state, provincial, territorial) governments, local (e.g., city, town) governments and their component government entities (e.g., agencies, boards, commissions and enterprises). The PSC has a role in identifying and addressing specific public sector accounting and auditing issues and concerns.

3. The PSC has been given authority by the IFAC Council to issue standards, guidelines, studies and occasional papers on financial reporting, accounting and auditing in the public sector. Over the period 1989 to 1996 the PSC published a range of Studies covering topics such as the definition and recognition of assets, liabilities, revenues and expenses. These Studies were descriptive in nature. They were intended to provide international comparisons of current practices and to highlight conceptual issues underlying these topics. This Study provides an overview of the issues covered in prior Studies and extends the discussion of these issues. It is a link between the previous work of the PSC, and its development of accounting standards and guidance to assist entities making the transition from cash to accrual accounting.

4. The Exposure Draft of this document was published in March 1998. At that time it was entitled "Guideline for Governmental Financial Reporting" and identified issues associated with four bases of accounting (cash, modified cash, modified accrual and accrual). Following comments from respondents on the Guideline for Governmental Financial Reporting, the Exposure Drafts of International Public Sector Accounting Standards and the *Invitation to Comment: Which Bases of Accounting*, the Committee decided to establish accounting standards for the cash and accrual bases of accounting only. This document therefore focuses on the cash and accrual bases of accounting and its title has been changed to better reflect its status.

Purpose of the Study

5. The Study aims to assist governments at all levels in the identification of issues associated with financial reporting. Although some parts of the Study may relate to national governments only, other parts are applicable to all levels of government.

6. The Study contains a detailed description of both the accrual and cash bases of accounting and provides examples of actual financial statements prepared under each basis. The document explains common practice within each basis of accounting, and provides examples of the variations within those bases. Governments wishing to change their basis of accounting or modify their accounting policies will be able to use this document as a source of information about a basis of accounting, including accounting policy issues associated with that basis and the format of financial statements prepared under that basis. This may assist governments in changing their basis of accounting and ultimately contribute to greater comparability within and between financial statements of governments.

7. Other documents published by the PSC include standards, studies and occasional papers. Standards contain individual requirements on financial reporting, accounting and auditing in the public sector. Studies provide advice on financial reporting, accounting and auditing issues in the public sector,

while occasional papers provide information that contributes to some segment of the body of public sector financial reporting, accounting and auditing knowledge.

The Standards Project

8. The PSC has embarked on the Standards Project to encourage improvements in the quality of the financial information typically provided by governments. The development of this Study is an initial phase of this medium-term project.

9. The other focus of the project is the development of a core set of Standards on accounting and financial reporting by governments — International Public Sector Accounting Standards (IPSASs).

10. The accrual standards will be developed by reviewing existing International Accounting Standards (IASs) issued by the International Accounting Standards Committee (IASC), and adapting them as appropriate for the public sector. The cash basis standard will incorporate any relevant aspects of the accrual standards. The PSC decided to use IASs as the starting point for its public sector Standards in an effort to be consistent, where possible, with existing international guidance, as well as avoiding the need to "reinvent the wheel" for the public sector. Although the public sector context is different, the overriding objective of financial reporting, which is to provide information which meets user needs, is the same across both public and private sectors. Using IASs as the basis for the PSC Standards will lead to a consistent approach to similar issues within public and private sector standards. There will, of course, be other areas where issues specific to public sector entities and governments will not have been addressed by the IASs.

11. Over time, the PSC intends to extend the scope of the Standards Project to address some of the gaps in the initial set of standards and to provide further guidance on financial reporting issues within the public sector.

Focus on Two Bases of Accounting

12. In its previous Studies the PSC described four specific bases of accounting used by governments, being the cash basis, modified cash basis, modified accrual basis and accrual basis. The four bases of accounting described in previous PSC Studies accorded with the bases of accounting used by the Committee on Accounting Standards of the International Organization of Supreme Audit Institutions in its *Accounting Standards Framework* and the associated *Accounting Standards Framework Implementation Guide – Departmental and Government-wide Financial Reporting*. This Study focuses on two bases of accounting, the cash basis and the accrual basis. It provides a detailed explanation of the accounting practices and issues associated with the cash and accrual bases and a brief description of the range of practices between these points. It incorporates discussion on other practices adopted by governments as variations to either the cash or accrual bases.

13. There are multiple points along the spectrum between cash accounting and accrual accounting and considerable diversity in the practices of governments. Given the difficulty of defining points with universal significance, the PSC has found it more appropriate to focus on setting standards for the cash and accrual bases. In recognition of the diversity that exists in practice, the PSC will develop and promulgate additional guidance for governments to assist in the transition between these two points. This additional guidance will recognize that there are a variety of different transition paths, depending upon the circumstances of each individual jurisdiction.

PART I - INTRODUCTION

CHAPTER 1

EXECUTIVE SUMMARY

Objectives of the Study

14. This Study provides a detailed description of the cash and accrual accounting bases and variations on these bases, as used by governments. The Study also provides practical examples of financial reporting under each basis. The objective of the Study is to provide information that will be a useful reference source for governments which wish to change their basis of accounting or review their accounting practices in relation to those of other governments.

15. The descriptions of the cash and accrual bases and modification to those bases are intended to:

    - facilitate the choice and adoption of a particular basis of accounting by a government; and
    - provide information to ensure that standard setters and preparers of financial statements have a common understanding of the accounting policy issues associated with that basis.

Bases of Accounting

16. The public sector financial reporting environment is characterized by a spectrum of practice between cash accounting and accrual accounting. Governments around the world adopt a variety of reporting practices along the spectrum, and may indeed combine aspects from both ends of the spectrum. The Study provides guidance on the application of the cash basis and the accrual bases of accounting, and describes variations on these bases as used by governments.

17. The Study focuses on the cash basis and the accrual basis, and the PSC intends to develop international public sector accounting standards that are structured around these two bases. However, the PSC recognizes that governments may in practice adopt modified versions of these bases and that they may follow different transition paths as they move along the spectrum from cash to accrual accounting. The PSC intends to address this issue by way of transitional provisions within individual accrual accounting standards and by developing guidance to assist entities in making the transition from cash to accrual accounting.

Scope of the Study

18. The Study is intended to assist governments at all levels in the preparation of their financial reports. Although some parts relate to national governments only, other parts are applicable to all levels of government.

19. The PSC has previously advised that Government Business Enterprises should use accrual accounting and follow International Accounting Standards (PSC Guideline 1, *Financial Reporting by Government Business Enterprises*). However, Government Business Enterprises may still find the information within this document useful.

20. This Study neither prescribes nor recommends particular accounting treatments. The main purpose of the Study is to describe and illustrate the accounting practices of governments, and to identify the accounting policy issues that arise in the context of governmental financial reporting.

21. This Study focuses on the issues that governments face in the preparation of general purpose financial reports for external users (also referred to as governmental financial reports). They are reports which are prepared for external users who are unable to require or to contract for the provision of special reports to meet their specific information needs. External users include the electorate (and its elected representatives) financial analysts/economists, lenders, suppliers and the media. These reports are often the only source of information for external users.

22. Governmental financial reports may also be used by internal users such as government decision makers (principally managers within individual government sub-entities), and government ministers (or equivalent) at both the portfolio level and the whole of government level. However, internal users are usually able to request specialized internal reports that are specifically designed to meet their

needs. In practice both types of reports are usually prepared from the same accounting system, although different classifications may be used, or a greater level of detail may be provided.

23. Special purpose financial reports are financial reports tailored to meet the specific information needs of a particular user. Examples include reports prepared for major lenders and internal reports prepared for the managers and governing body of a reporting entity. The level of disclosure and type of information presented in these reports is determined by the specific user. Internal management reports will usually contain very detailed information, particularly with respect to the items under management's control. Due to the specialized needs of internal users, the scope and content of reports prepared for internal management purposes vary enormously. It is beyond the scope of this Study to discuss the wide range of special purpose reports which may be produced.

Structure

24. The Study is in five parts:

- Part I Introduction
- Part II Cash Basis
- Part III Accrual Basis
- Part IV Measurement Bases
- Part V System of National Accounts and Government Finance Statistics

25. Parts II and III include a discussion of how well the information produced under each basis of accounting meets the needs of users, a description of the financial elements recognized under each basis of accounting, and some general recognition and measurement issues associated with these elements. The descriptions also include possible classifications of financial elements and a discussion of external financial reports produced under these bases.

Cash Accounting

26. Part II describes the elements recognized under cash accounting: cash balances, cash receipts and cash payments. The Study defines each of these elements, describes types of cash receipts and payments, and discusses the recognition, reporting, and classification issues associated with these elements. It discusses the benefits associated with cash information, such as the links between cash-based financial statements and traditional cash-based appropriations and the fact that preparers and users of cash-based information do not require any detailed accounting knowledge. It discusses the limitations of using cash accounting when more complex information is desired. It also describes the types of financial reports which are commonly prepared under cash accounting and identifies additional disclosures which may be made as part of the financial statements.

27. Many governments using the cash basis supplement the data available under this basis with additional information, such as information on commitments or government debt. In addition, some governments hold the books open for a specified period after the end of the reporting period. Refer to Part II for a discussion of common modifications to the cash basis. Although many modifications to the cash basis are observed in practice, this Study focuses on the "pure" cash basis in order to establish a base for discussion of financial reporting issues and to establish a framework for preparers and auditors as they consider the implications of various transition paths.

Accrual Accounting

28. Part III discusses the strengths and weaknesses of accrual accounting and provides an explanation of the reasons given by various countries for adopting accrual accounting. It contains a description of the elements recognized under accrual accounting: assets, liabilities, net assets/equity, revenue and expenses. For each element, the Study discusses the definition and recognition criteria, describes the types of items recognized within each element and discusses the application of the definition and recognition criteria to those items. Where appropriate, reference is made to relevant discussion in International Accounting Standards (IASs).

29. The Study discusses the types of financial statements commonly prepared under accrual accounting and describes other information that may also be disclosed in the financial statements.

30. Some governments which have moved towards the adoption of accrual accounting have decided not to

recognize particular categories of assets or liabilities. They may have made these variations from the accrual basis as part of a planned progression to accrual accounting, or because they consider that the variations represent appropriate arrangements for their jurisdiction. For example, a government may not have recognized all its physical assets. This could be because complete records of asset holdings were not available at the time, or because the government considered that certain categories of physical assets did not satisfy the recognition criteria for assets. In addition, the accounting practices of a jurisdiction may be prescribed by regulation or statute that are developed independently of the government. Common modifications to the accrual basis are discussed within Part III.

Measurement Bases

31. The Study contains a description of various measurement bases. Although it does not recommend particular measurement bases, it identifies which bases are commonly used in the measurement of certain assets and liabilities.

System of National Accounts and Government Finance Statistics

32. Governments often prepare financial information for three purposes: the compilation of governmental financial statements, national accounts in accordance with the United Nations System of National Accounts (SNA) and the International Monetary Fund (IMF) Government Finance Statistics (GFS). The Study explains the relationship between these three reporting systems and examines some of the differences between them. One historic difference between these systems has been the different measurement bases used. However, the measurement differences are already diminishing. The SNA is already on an accrual basis (with assets and liabilities at market value). The GFS is considering the adoption of the accrual basis and governmental financial reports are moving toward adopting accrual accounting (although in some jurisdictions assets and liabilities are reported at historical cost).

Appendices

33. The appendices contain a glossary of terms used throughout the Study, and examples of financial statements prepared by various governments. Readers should note that the financial statements in the appendices are for illustrative purposes only. They represent current practice, but are not necessarily representative of best practice. They are intended to facilitate understanding and to provide a context for the examples used throughout the text of the Study.

Cost/Benefits

34. The choice of a particular basis of accounting will be made by each government on the basis of the costs and benefits associated with that option. Different bases of accounting have different strengths and some may be more appropriate than others in particular circumstances (refer to Chapters 4 and 11 for a discussion of the benefits of each basis of accounting). The most appropriate basis will depend on the characteristics and nature of the entity, the type and purpose of the report and the value of the information to users. The decision may also be influenced by whether whole of government financial statements are to be prepared and, if so, the basis of accounting which will be used in such statements. It will also depend on the costs of developing and maintaining the necessary financial information systems.

35. A number of issues become more complex as entities move towards accrual accounting. These issues include the range of elements and financial performance measures which may be reported, the definition of elements and the establishment of measures for those elements. Consequently the importance of judgments concerning the transactions and events reflected in the financial statements increases with accrual accounting. Similarly, the cost of developing and maintaining accounting systems may increase. The actual costs of adopting a particular basis will depend upon the existing capacity of personnel in terms of experience and training, and the reliability and completeness of existing systems. The costs and benefits may also be influenced by the degree of political commitment and amount of resource devoted to a change in basis. A system change which has a high degree of political commitment and is adequately resourced is more likely to provide short-term benefits than a system change which occurs without such support.

36. Making such cost/benefit decisions is always difficult; the costs are borne by the reporting entity and can be determined with some precision. However, the benefits are often enjoyed by third parties as

well as the entity itself and can only be assessed subjectively. A comprehensive assessment would consider the incremental benefits that are likely to flow from moving from one basis of accounting to another and the improved decision making which is expected to result from the availability of more comprehensive financial information. They should also include consideration of whether the government has an obligation to be accountable for all the resources it controls and the result of that control. A decision not to provide certain information should take into account the opportunity cost associated with not having that information available for decision makers.

Transition between the Bases of Accounting

37. The PSC intends to explore issues associated with the transition between the bases of accounting by way of occasional papers describing the transition process within individual jurisdictions (e.g., *Perspectives on Accrual Accounting* available at www.ifac.org) and specific guidance on the transition from cash accounting to accrual accounting. This Study provides information on the definition and recognition of elements under each accounting basis, and the disclosure of information in external financial statements. It does not specifically address the process of transition from one accounting basis to another. This is for the following reasons:

- The nature of the progression may differ between governments. Some governments may choose a gradual progression along the continuum of accounting bases, while others may move directly from, say, cash accounting to accrual accounting.
- The transitional steps will be unique to each government. The nature of the transition will depend on the current accounting basis used, the quality and range of information already available, the resources allocated to the transition and the time period allowed for transition.

CHAPTER 2

OBJECTIVES OF FINANCIAL REPORTING

Introduction

38. A number of financial reporting issues are common to all bases of accounting. Regardless of the basis of accounting adopted by a government, these issues are relevant. This Chapter provides a summary of some of these issues.

39. This Chapter discusses the:

- need for objectives for governmental financial reporting and the governmental operating environment;
- needs of users of governmental financial reports;
- objectives and qualitative characteristics of financial reporting;
- ability of alternative bases of accounting to meet the objectives of financial reporting;
- relationship of governmental financial reporting to other forms of reporting;
- determination of the reporting entity; and
- preparation of consolidated financial statements.

40. Much of the material in this Chapter is drawn from PSC Study 1 *Financial Reporting by National Governments* and PSC Study 8 *The Government Financial Reporting Entity*. Readers are referred to these Studies for more detailed discussion of these issues.

The Importance of Objectives for Financial Reporting

41. The determination of the objectives of financial reporting is the first step in the process of governmental financial reporting. The objectives would then lead to the selection of a basis of accounting and the determination of the accounting policies within that basis. In practice the use of a basis of accounting by a government may have been the result of historical developments and available resources rather than an explicit decision. However, consideration of the objectives of financial reporting is an important step in deciding whether to retain a basis of accounting or to adopt a different basis, and in determining the accounting policies to be applied within that basis.

42. The overriding objective of financial reporting is to provide information that meets user needs. This Chapter therefore identifies the principal users of governmental financial reports and the types of information that they require. First though, it is helpful to consider the environment within which governmental financial reporting takes place and the purpose of governmental financial reports compared to other forms of reporting.

Governmental Operating Environment

43. The following quote illustrates some of the objectives of financial reporting within the public sector.

> *The broad issues of corporate governance, performance reporting, and comparability of financial and non-financial performance information are becoming increasingly important to users of general purpose financial reports of government entities. In the Swiss public sector, for example, we believe there is now an increasingly clear public expectation that governments and their component entities should (a) be effective and (b) be seen to be effective and the legislator is progressively introducing such logic into federal and cantonal laws. This evolution implies that financial reporting should be sufficiently transparent to ensure that financially-based performance indicators are properly and consistently reported to users of such information.* (Swiss Institute of Chartered Accountants and Tax Consultants, Submission on Exposure Draft Guideline for Governmental Financial Reporting)

44. Some of the distinguishing features of the public sector's operating environment which influence the nature of the information reported are:

- Governments do not generally exist to make a profit. Instead, a government is generally concerned with the welfare of its citizens, determining the best way of financing the goods and services that it wishes to provide to its citizens and establishing the regulatory framework within which business is conducted. Although the functions undertaken by governments vary across jurisdictions and within differing levels of government, such functions often include the provision of health, education and defense. The absence of a profit motive for most government entities (apart from business enterprises) means that a variety of financial and non-financial performance indicators may be required in order to assess performance.
- Governments as a whole tend to obtain most of their revenue from taxes and other non-reciprocal transactions. Unlike the parties to a reciprocal transaction, taxpayers have no choice about entering into the transaction and have no guarantee that they have received value for money. Even where citizens enter into reciprocal transactions with individual government entities those entities may have a monopoly on the provision of a service.
- Authorization to use public resources and the management of those resources are usually conducted by different arms of government, the legislature and the executive. The legislature has the right to hold the executive accountable for its management of financial affairs and the use of financial resources entrusted to it. Public sector entities are usually required to demonstrate that to the best of their ability and available resources, they have provided the goods and services required by citizens, at least cost. In contrast, private sector entities are usually accountable to shareholders for making a return on funds employed in a competitive environment, rather than for the nature of the goods and services that they have provided.

45. These distinguishing characteristics of the public sector have led to the development of additional forms of reporting that do not usually form part of the traditional model for private sector financial reporting such as non-financial performance reporting and compliance reporting. One of the challenges facing the public sector is the need to measure the consequences of government policy decisions and the implementation of those decisions. Some of these additional forms of reporting requirements are discussed later in this Chapter (see "Relationship Between Governmental Financial Reporting and Other Forms of Reporting").

46. The overriding objective of financial reporting is that information should meet users' needs. According to the IASC Framework for the Preparation and Presentation of Financial Statements,

> *The objective of financial statements is to provide information about the financial position, performance, and changes in financial position of an enterprise that is useful to a wide range of users in making economic decisions.* (paragraph 12)

47. Although certain differences between the private and public sectors exist, there are also similarities between the two sectors in terms of the information required to manage, or hold individuals to account for their management of entities. To the extent that public sector entities want financial information on cash flows, assets and liabilities, and changes in those assets and liabilities, the accounting models and accounting standards developed by the private sector, such as International Accounting Standards (IASs), contain much useful guidance. Although private sector standards do not address some of the issues faced by governments such as the recognition of taxation revenues, they provide guidance on many of the other issues faced by governmental accountants. Where appropriate, this Study refers to pronouncements of the International Accounting Standards Committee that contain guidance on issues discussed within this text. As part of its ongoing work program, IFAC PSC is developing a set of public sector accounting standards. The initial set of standards are largely based upon IASs but over time the PSC will also begin to address public sector financial reporting issues that are not covered by IASs.

Users

48. The principal users of governmental financial reports include:

- Legislative and other governing bodies: Legislative and other governing bodies grant authority to governments and government entities to administer public financial affairs and resources. They may use financial reports to assess the government's stewardship of resources, compliance with legislation and other authorities, and the government's financial position and financial performance.
- The public: The public includes taxpayers, electors, voters, special interest groups, and recipients of goods, services and transfers provided or made by the government. Taxpayers are required to provide resources to the government and are interested in information about how the government has used the funds received in the current and previous years. They are also interested in information on whether the government is managing to fund current goods and services out of current taxes collected.
- Investors and creditors: Investors in government securities and other creditors are entitled to information which allows them to assess whether the government is likely to be able to meet its commitments as they fall due. This category of users may also have access to special purpose reports.
- Rating agencies: Many governments obtain finance from the national and international capital markets by issuing bonds or other financial instruments. Rating agencies provide assessments of a government's creditworthiness for the capital markets using standard categories such as A, AA- etc. Rating agencies are primarily concerned with a government's ability to service debt and to repay that debt when it falls due. Rating agencies therefore consider the nature and extent of a government's other obligations, the asset backing of a government, the extent of its current and projected spending and its ability to generate the same or increased levels of tax revenue.
- Other governments, international agencies and resource providers: These users have similar information needs to investors and creditors. However, to the extent that the funding they provide may be earmarked for specific projects they may also require information on compliance with the terms of the agreement and specific performance measures in relation to that project. International agencies are interested in the comparability of the financial statements of various governments and the use of complete disclosure.
- Economic and financial analysts: Economic and financial analysts, including the media, review and analyze information on behalf of other users.
- Senior management: Although senior management are internal users and have access to more detailed internal reports, often the general external reports provide a useful overview of the financial affairs of the entity for these users.

User Needs

49. Although the users described above have a range of information needs, and some groups may place a higher or lower priority on certain types of information than other groups, the user groups also have similar information needs. The PSC considers that, taken as a collective group, users expect that governmental financial reports will help them to:

- assess the sources and types of revenues;
- assess the allocation of and use of resources;
- assess the extent to which revenues were sufficient to cover costs of operations;
- predict the timing and volume of cash flows and future cash and borrowing requirements;
- assess the government's long term ability to meet financial obligations, both short and long term;
- assess the government's or entity's overall financial condition;
- provide the public with information concerning those assets held on behalf of taxpayers, specifically information on ownership and control, composition, condition and maintenance;
- assess the financial performance of the government or entity in its use of resources;
- assess the economic impact of the government on the economy;
- evaluate government spending options and priorities;
- assess whether resources were used in accordance with legally mandated budgets and other legislative and related authorities such as legal and contractual conditions and constraints; and
- assess the government's or entity's stewardship over the custody and maintenance of resources.

Relationship Between Governmental Financial Reporting and Other Forms of Reporting

50. This Study focuses on the financial information provided in governmental financial reports. Governmental financial reports are reports which are prepared for a range of external users who are unable to require or to contract for the provision of special reports to meet their specific information needs. The reports are designed to meet the common needs of these external users. Most external users have limited access to information and rely heavily, if not exclusively on governmental financial reports. The disclosure of information in governmental financial reports may be governed by legislation, regulations or accounting standards.

51. Governmental financial reports, in common with private sector financial reports, are not intended to provide all the information needed by users. The scope of governmental financial reports is constrained in the following ways:

    - They are financial reports. Items which cannot be quantified are not included in the financial statements totals, although they may be disclosed as additional information in the notes. Users may seek other sources of information, including statistical data, demographic information, narrative assessments, and reports on general economic conditions and the political environment to meet their needs.
    - They provide information in respect of the reporting entity which has prepared the reports. The reporting entity may be an individual government department or it may be a collection of all government agencies of a certain type. The reports therefore focus on the activities of a government agency or a particular level of government. They do not usually combine information on different levels of government or information on the government and the rest of the economy. Financial information on the entire government sector and the national economy is usually produced by way of Government Finance Statistics and the System of National Accounts (or regional equivalents) respectively.
    - They provide information on financial performance rather than service performance. Performance reporting includes information on the nature, quality, quantity, cost etc of the goods and services provided by governments. Although performance reporting, and in particular information on the cost of goods and services, may be incorporated within governmental financial reports, discussion of performance reporting is outside the scope of this Study.
    - They are external reports rather than internal reports. Although senior management may use the information in governmental financial reports, management typically has access to more detailed information for decision making. For example, although the governmental financial reports may measure assets at historical cost, management reports may contain both historic cost and current market values for certain categories of assets.
    - The basis of accounting underlying the governmental financial reports may differ from that used in the preparation of the budget documents, and accordingly, certain accounting principles may differ between the two. For example, budget documents may contain authorizations for obligations or commitments. Unless obligations or commitments meet the definition of a liability under the accrual basis of accounting, they are not recognized as an element under any basis of accounting described in this Study.
    - They generally portray the effects of past events. Financial reports prepared at year-end contain information on the impact of transactions and events during the reporting period on the financial performance and position of the entity. Although governments may choose to provide prospective financial information such as forecasts of future events and transactions in their financial reports such information is traditionally found in budget reports only.
    - Compliance reporting may be incorporated in the governmental financial reports. Although reporting on compliance with budgets and appropriations is an important form of reporting for many government entities, this reporting may be included within a governmental financial report, the budget documents for the next year, or published as a separate report. Compliance reporting is discussed later in this Chapter.

52. Information on service performance may be incorporated as part of governmental financial reports or may be prepared as a separate report. Performance measures and indicators, both planned and actual, can be set out in the budget or plan. Actual results are measured using those measures and indicators. Such information can include comparisons of budgeted and actual output quantity and quality. It may also include a discussion of the relationship between outputs and outcomes. Some governments also report on general economic statistics such as unemployment, Gross Domestic Product, inflation, interest rates, balance of trade etc.

53. For example, the performance information produced by United Kingdom government departments as part of their financial reporting using the accrual basis (referred to as resource accounting) will include the costs incurred by each department in pursuit of each of its main aims and objectives; the outputs from each departmental program, and performance against objectives (*Better Accounting for the Taxpayer's Money - the Governments Proposals*, July 1995, paragraph 1.26).

Objectives of Governmental Financial Reporting

54. A number of standard-setting bodies in various jurisdictions have considered the objectives of financial reporting. Examples of such jurisdictions and/or bodies include the IASC, various accounting standard setting bodies within the United States of America, Australia, Canada and New Zealand. The IASC Framework identifies objectives of financial reporting for private sector entities. IFAC PSC Study 1 *Financial Reporting By National Governments* identified the following objectives of governmental financial reporting:

> *Financial reporting should demonstrate the accountability of the government or unit for the financial affairs and resources entrusted to it, and provide information useful for decision making by:*
>
> *a. Indicating whether resources were obtained and used in accordance with the legally adopted budget.*
>
> *b. Indicating whether resources were obtained and utilized in accordance with legal and contractual requirements, including financial limits established by appropriate legislative authorities.*
>
> *c. Providing information about the sources, allocation, and uses of financial resources.*
>
> *d. Providing information about how the government or unit financed its activities and met its cash requirements.*
>
> *e. Providing information that is useful in evaluating the government's or unit's ability to finance its activities and to meet its liabilities and commitments.*
>
> *f. Providing information about the financial condition of the government or unit and changes in it.*
>
> *g. Providing aggregate information useful in evaluating the government's or unit's performance in terms of service costs, efficiency and accomplishments.* (IFAC PSC Study 1 paragraph 63)

55. In defining the objectives of financial reporting an analysis of the costs and benefits associated with preparing financial information that meets those objectives is relevant. In principle, the benefits to users of the financial statements should exceed the costs of recording, summarizing, reporting and auditing the information. The benefits and costs also need to be considered over a reasonable time frame in order to balance the short-term costs of shifting from one basis to another. One difficulty of conducting a cost benefit analysis is that although it is usually possible to measure certain aspects of costs, benefits may be more difficult to quantify.

Qualitative Characteristics of Financial Reporting

56. The quality of the information provided in financial reports determines the usefulness of those reports to users. The qualitative characteristics of financial information discussed in the IASC Framework are:

    - understandability;
    - relevance;
    - materiality;
    - reliability;
    - faithful representation;
    - substance over form;
    - neutrality;
    - prudence;
    - completeness; and
    - comparability.

57. In addition, the IASC also notes that other characteristics such as timeliness, are important. A balancing, or trade off, between characteristics may be necessary. Different accounting bases may also score more highly on one characteristic than another. Deciding the relative importance of the characteristics in different cases is a matter of judgment. A brief description of some of these characteristics follows. Readers interested in a fuller discussion of these characteristics are referred to the IASC Framework and PSC Study 1 *Financial Reporting by National Governments*.

58. Understandability means that information is understandable, clear and precise. Information provided in financial reports should be presented simply and clearly, and should be comprehensible to users of the reports.

59. Relevance means that information must assist users in making their decisions — there must be a logical relationship between the information provided and user needs. In order to be relevant, information must also be timely and reliable.

60. Materiality is a term used to describe the significance of financial statement information to users. Materiality is a matter of judgment in the particular circumstances. It can be judged in relation to the reasonable prospect of an item's significance in users' assessments and judgments. An item may be relevant because of its nature alone, in other cases both nature and materiality are important. A material item would be expected to affect assessments of, and judgments on, government financial operations and management. In general, users are interested in financial information that has direct bearing on their assessments and decisions. Reporting immaterial items could simply impair the clarity and understandability of the financial report.

61. Reliable information faithfully represents what it purports to represent, is complete, reasonably free from bias (neutral) and verifiable. Reliability does not preclude the use of estimates within financial reports but the methods used to estimate figures must be reliable.

62. It is desirable that information be both consistent over time and comparable between government financial reports. Comparability is limited to comparisons between entities using the same basis of accounting. Accounting standards generally require changes in the basis of accounting or policies within that basis to be fully disclosed.

Relationship Between Alternative Bases and Financial Reporting Objectives

63. All bases of accounting provide information which meets some of the objectives of financial reporting, some more so than others. To the extent that the accrual basis incorporates information that is recorded under the other bases of accounting, it arguably meets more user needs than the other bases. However, objectives differ between the bases. Different bases may be more appropriate than others depending upon which objectives the reporting entity considers to be the most important. The following table summarizes how well financial reports prepared under different bases provide information (excluding supplementary information) which meets the objectives of financial reporting.

ALTERNATIVE BASES OF ACCOUNTING INCLUDING MODIFICATIONS TO THOSE BASES — ABILITY TO MEET OBJECTIVES[1]

	CASH		ACCRUAL	
	CASH BASIS	**MODIFICATIONS TO THE CASH BASIS**	**MODIFICATIONS TO THE ACCRUAL BASIS**	**ACCRUAL BASIS**
OBJECTIVES				
Compliance with legally adopted budgets[2].	Yes	Yes	Yes	Yes
Compliance with legal and contractual requirements, including spending limits.	Relating to cash requirements and limits	Cash and near cash requirements and limits	Cash and financial resources requirements and limits	Cash and economic resources requirements and limits
Sources, allocation and uses of financial resources.	Cash resources	Cash and near cash resources	Cash and financial resources	Cash and financial resources
Financing and cash requirements.	Cash resources	Cash and near cash resources	Cash and other financial requirements	Cash and other financial requirements
Ability to finance activities and to meet liabilities and commitments.	From cash	From cash and near cash	From financial resources	From economic resources
Financial condition and changes therein.	Cash position	Cash and near cash position	Financial resources	Financial and economic resources
Financial performance in terms of service costs.	Information not reported	Information not reported	Limited information reported	Provides information necessary to assess performance

Reporting Entities in the Public Sector

64. A reporting entity is an entity in respect of which it is reasonable to expect the existence of users dependent upon financial reports for information which will be useful to them for accountability and decision making purposes. The term may refer to departments or ministries of government, other entities that are part of government, as well as the whole of government. Determining the boundaries of the government reporting entity determines which entities, transactions and activities will be encompassed by a government's financial report.

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[1] The comments in each of the four columns on how well information prepared under each basis, or certain modifications to that basis, meets the objectives of financial reporting assume that the information reported is limited to that generated under that basis. However, in all cases, governments may report supplementary information which allows them to more fully meet the objectives of financial reporting.

[2] The ability of a financial report to demonstrate compliance with legally adopted budgets depends upon the basis of accounting used in each instance. Even where the basis of accounting differs between the two, reconciliations are possible.

65. There are a number of concepts or approaches which may be used to determine the boundaries of the financial reporting entity. These include the:

- authorized allocation of funds approach;
- legal entity approach;
- political accountability concept; and
- concept of control.

66. The four concepts listed are not mutually exclusive. For example, the legal entity concept may be used in conjunction with the concept of control. In addition, application of different concepts may produce similar reporting entities, particularly at lower levels. However, as a government moves towards whole of government reporting, the application of the different concepts is more likely to lead to different results. For example, legal requirements for compliance reporting may mean that a government prepares additional reports based on the authorized allocation of funds concept in addition to its financial reports. Each of the concepts listed is discussed more fully below.

67. Under the authorized allocation of funds approach it is argued that accountability and the provision of information for decision making can be met by demonstrating compliance with the authorized allocation of funds or spending mandate, for example, demonstrating compliance with expenditures authorized to be made from "consolidated revenue" or "public funds". Using this approach, the reporting entity would comprise those entities that are funded wholly or predominantly by authorized allocations of government funds. The reporting entity would therefore be consistent with the budget reporting entity. Fund accounting is one manifestation of this concept.

68. Fund accounting is based on one concept of the reporting entity. Traditionally the focus of financial reporting by government has been on identifying the purposes for which expenditure has been authorized and demonstrating that those authorizations have been complied with. The government financial reporting entity has been determined by reference to the individual funds, which may be subject to parliamentary appropriation. Fund accounting is an accounting system structured to treat restricted cash balances as a separate accounting and, in many cases, a separate financial reporting entity. On this basis, funds represent a pool of resources set aside for the carrying on of specific activities or the attainment of certain objectives in accordance with legislative or other regulatory restrictions placed on the use of those resources. By accounting for those resources on a separate or fund by fund basis, the extent to which resource usage has complied with those restrictions can be demonstrated (PSC Study 8 *The Government Financial Reporting Entity* available at www.ifac.org). While funds may meet the definition of reporting entities as outlined in PSC Study 8, funds will usually be components of a larger government entity which is itself a reporting entity. This will require the preparation of consolidated or summary financial statements for the primary government.

69. Arguments which support the authorized allocation of funds approach include the following:

- users wish to evaluate the use of government funds compared to the allocation of public funds;
- reports which focus on the budget sector are more relevant because the two sectors are different in nature and also because users can obtain separate reports from entities outside the budget sector; and
- different bases of accounting may be used by the budget sector and other sectors. Where this occurs consolidation of the budget and non-budget sectors is more difficult.

70. However, these arguments need to be considered against the fact that the authorized allocation of funds approach results in a fairly narrow boundary for the reporting entity and does not provide a complete view of the resources and activities for which the government is accountable. For example, a municipality may provide all its public services directly to the public, or it may establish separate corporations to carry out activities such as water supply and roading. Citizens are paying for these services regardless of how the municipality chooses to deliver the services, but the authorized allocation of funds results would provide the taxpayer with two different types of reports under the two scenarios.

71. The second approach is that of the legal entity (Christiaens 1997). This approach supports the use of legislation to determine a list of entities or type of entities which must be included within the government's consolidated financial reports. This approach is often observed in practice in conjunction with other approaches. This situation arises because even where a government adopts the legal entity approach, it still needs a conceptual basis to determine which entities are included within a legislative list.

72. The third concept is the political accountability concept (CICA 1985, page 35). Political accountability suggests that an entity would report all activities and entities over which it is accountable, irrespective of the legal or organizational structures under which the activities are carried on, including activities conducted in partnership between a government and private entities or other governments.

73. The fourth concept is that of control. Under this approach the government financial reporting entity includes all those entities and transactions which the government controls. The concept of control is often used in the private sector and has increasingly been adopted by governments as well. In the public sector the concept is often referred to as control through ownership mechanisms. This precludes other concepts of control such as control associated with the power to regulate or the power arising from the government's position as a major funder or purchaser of goods and services. Under the control concept, the reporting entity includes all resources controlled by and all obligations of the reporting entity, regardless of the administrative or legal entities which have been created to manage those resources and obligations.

74. When a government uses the concept of control as the determinant of the boundaries of the reporting entity the following observations may be made regarding the financial statements:

- the government demonstrates accountability for all that it controls (in addition to any compliance reporting in relation to budgetary authority or spending mandates);
- all resources and obligations controlled by the government are included within one set of financial statements; and
- entities which the government does not control are not included in the government's financial statements.

75. Difficulties associated with the use of control as the determinant of the reporting entity include the fact that governments have a wide potential range of control. The concept therefore needs to be restricted to certain types of control and the application of the concept may require some judgment. For this reason, governments usually develop more detailed guidance to be used in the application of the concept. Examples of factors which may be used to indicate the existence of control by a government of another entity include:

- the existence of an executive power which enables the government to give directions to the governing body of that entity on its financial and operating policies;
- the government has broad discretion, under existing legislation, to remove a majority of members of the governing body of that entity; or
- the government has a majority of the votes that are likely to be cast at a general meeting of that entity.

76. If control is adopted as the criterion for establishing the boundaries of the government financial reporting entity, the following issues need to be resolved:

- the determination of the definition/characteristics of control;
- the identification of the entities which are controlled by governments; and
- the mechanism for combining all transactions.

Combination Issues

77. When governments prepare financial reports for a reporting entity which includes a number of controlled entities, it will be necessary to address the issue of how to combine the information within those reports. Options include:

- separate financial statements for each entity;
- separate financial statements for various sectors of government activity;
- consolidated financial statements with all entities fully consolidated;
- consolidated financial statements with some entities consolidated and others equity accounted; and
- combined statements with no consolidation adjustments.

78. The use of full consolidation has the advantage that it allows the overall financial position of an entity and its sub-entities to be viewed as one entity. When full consolidation is used, consolidation procedures include:

- ensuring that consistent accounting policies are used by all entities, or if they are not consistent, making appropriate adjustments to the reported figures;
- ensuring that the reporting period for all entities is comparable; and
- eliminating any inter-entity transactions and balances e.g., eliminating any loans from one entity to another and eliminating inter-entity sales of goods and services.

79. However, when the reporting entity is a government, the use of different bases by different levels of government or different types of entities creates a further consolidation issue. In some countries it is not uncommon for certain government agencies to use accrual accounting, but for higher levels of government to use the cash basis, although possibly with modifications.

80. Some of the options available to a government wishing to prepare consolidated financial statements when one or more entities use different basis of accounting are as follows:

- require all entities to adopt the same basis of accounting;
- allow the use of different bases and make adjustments at the time of consolidation to bring all the financial statements onto the same basis. This could result in the financial statements being prepared on a higher or lower basis depending upon the type of information available. For example, if most entities used a modified version of the accrual basis and a small group of entities used a modified version of the cash basis, it might be possible to make an adjustment for financial assets and liabilities of the latter group. The degree of precision required when making such adjustments would depend upon the materiality of the figures;
- prepare consolidated financial statements on a lower basis but provide note disclosure of the additional information which is available;
- prepare a group report which presents financial information for all entities within the reporting entity, but do not combine the financial statements; and
- prepare a group report which adds together the financial statements of different entities although they are prepared on a different bases. This option presents a number of difficulties both for preparers and readers. For example, if information prepared on a cash basis is combined with information prepared on an accrual basis, identical transactions will have been accounted for in different ways.

81. Where a government prepares whole of government financial statements, the reporting entity may be broader than the general government sector used in the compilation of GFS and SNA reports. A clear description of the reporting entity and whether this differs from the entity used for GFS purposes is helpful to readers using both GFS and governmental financial reports.

Compliance Reporting

82. Compliance reporting is the act of reporting actual results against budgeted or planned results. Many government reporting entities e.g., government departments, are subject to legislative controls such as appropriations over the nature and amount of their spending. These reporting entities are usually required to demonstrate compliance with appropriations both to the government entity which granted the appropriations and/or to the electorate from whom the funds were initially obtained. They may also be required to demonstrate compliance with regulations, laws or contracts relating to individual loans or grants. The discussion in this Chapter focuses on reports which demonstrate compliance with appropriations or budget authorities, particularly those compliance reports which are presented as part of the governmental financial reports. As discussed earlier, compliance reporting may take place within the governmental financial reports, the budget for the next year or a separate compliance report.

83. Compliance information may be presented in a number of ways. Options include:

- a statement with separate columns for budgeted amounts, actual amounts and amounts in excess of appropriations; or
- a statement by the management of the entity asserting that all appropriations and/or other legal authorities have been complied with. If any appropriations or authorities have been exceeded, or expenses incurred or payments made without appropriation, then such details may be disclosed by way of footnote to the relevant item within the governmental financial report.

84. When there are several additional appropriations through the year, an issue may arise as to which set of budgeted estimates to use. Best practice suggests that both the originating budget for which authorization was sought and any additional appropriations sought during the year be clearly shown.

85. For compliance and control purposes it is important that planned and actual results are reported on the same basis of accounting, and for the same reporting entity. If compliance reports are to meet their objective of providing users with a valid comparison of amounts appropriated and amounts used, then it is essential that the reports use both the same basis of accounting and cover the same budget entity as the budget statements.

86. Currently a range of practice exists both across and within jurisdictions. Some of the combinations which exist are as follows:

- appropriations are cash-based and governmental financial reports are cash-based;
- appropriations are cash-based but include certain obligations and governmental financial reports are modified accrual-based;
- appropriations are cash-based and governmental financial reports are accrual-based; and
- appropriations are accrual-based and governmental financial reports are accrual-based.

87. Some jurisdictions which have moved from the cash basis to the accrual basis for governmental financial reporting retained the use of cash-based appropriations for a number of periods following the transition. In such an environment, the accrual information is perceived as an external reporting requirement, rather than a key input to managerial decision making. Although it is possible to have cash-based appropriations and accrual governmental financial reports, the powerful incentives flowing from the appropriation process means that managers often continue to focus on the cash basis information. Using different bases of accounting for governmental financial reporting and budgeting increases the complexity of reporting and creates incentive problems for management.

88. Despite the desirability of having the budget and actual results measured using the same basis of accounting, where the bases differ, a reconciliation of the amounts provided is extremely useful to users. This may be done in a number of ways, but as a minimum approach, budget surpluses/deficits may be reconciled to the net changes in financial position reported in the financial statements.

89. The reporting entity may also vary between the budget statements and the governmental financial reports. Budgets often include only figures in relation to government entities which require cash inflows from the government during the year. Entities which are self supporting, for example, GBEs, may be outside the budget system. However, when a government prepares consolidated financial statements it will usually apply the concept of control to determine which entities form part of the external reporting entity. If the concept of control is used, and GBEs satisfy the control criteria, they

are included in consolidated financial reports. Where there are entities included in the governmental financial reports which are "off budget", a reconciliation between budgeted and actual results, showing the impact of such "off budget" entities on the reported results, is desirable.

90. The following example provides an illustration of compliance reporting.

SUB HEAD	DESCRIPTION	ORIGINAL ESTIMATE	SUPPLEMENTARY APPROVALS & VIREMENTS	APPROVED ESTIMATE	ACTUAL EXPENDITURE	MORE THAN ESTIMATE	LESS THAN ESTIMATE
		CI$	CI$	CI$	CI$	CI$	CI$
01	Personal Emoluments	98,994,848	1,992,918	100,987,766	96,720,816	272,541	4,539,491
02	Travelling & Subsistence	2,646,113	124,858	2,770,971	2,526,855	89,419	333,535
03	Supplies & Materials	8,113,908	1,130,988	9,244,896	8,116,202	-	1,128,694
04	Rent of Property	3,155,940	-9,250	3,146,690	1,891,495	112	1,255,307
06	Utilities	5,833,393	548,385	6,381,778	5,771,544	1,621	611,855
07	Other Operating & Maintenance Services	34,866,019	630,469	35,496,488	31,648,364	-	3,848,124
08	Grants, Contributions & Subsidies	27,180,749	3,165,169	30,345,918	27,692,376	420,347	3,073,889
10	Awards and Indemnities	75,000	42,000	117,000	114,971	8,252	10,281
11	Retiring Benefits – Non-Statutory	1,339,769	23,500	1,363,269	1,284,555	-	78,714
12	Inter-departmental Purchases & Services	2,083,304	104,122	2,187,426	1,707,759	-	479,667
13	Interest payments – Non-Statutory	35,000	-25,897	9,103	8,826	-	277
14	Reference Materials and Others	455,080	-2,983	452,097	296,034	-	156,063
17	Repayments & Reserve	2,375,125	10,000	2,385,125	1,806,632	-	578,493
19	Loans	952,307	0	952,307	455,449	-	496,858
21	Insurance	3,004,094	-493,356	2,510,738	1,591,563	-	919,175
	TOTAL RECURRENT EXPENDITURE	191,110,649	7,240,923	198,351,572	181,633,441	792,292	17,510,423

Example 2.1
Cayman Islands Government Accounts for the year ended 31st December 1997
Appendix IV, page 40 (CI$)

91. The following example provides an illustration of reconciliation of a reported deficit under the accrual basis with the budget surplus on a cash basis.

Reconciliation of the Excess of Net Cost over Revenue to the Unified Budget Surplus for the Year Ended September 30 (Unaudited)
(In billions of dollars)

Unified budget surplus	69.2
Veterans' compensation	(109.4)
Military and Federal employees	(39.8)
Environmental liabilities..................................	(12.8)
District of Columbia pension fund	(5.5)
Net amount of all other differences	(35.5)
Financial Report's excess of net cost over revenue	(133.8)

Example 2.2
Financial Report of the United States Government – 1998
Supplemental Table (Unaudited), page 89 (USD)

PART II – CASH BASIS

CHAPTER 3

CASH BASIS – DESCRIPTION

Introduction

92. This Part describes the cash basis of accounting and explores some of the areas where entities using cash accounting need to develop specific accounting policies. It is not prescriptive. The PSC is also developing an International Public Sector Accounting Standard (IPSAS) which will set out appropriate accounting treatments and disclosures under the cash basis of accounting.

93. The cash basis of accounting recognizes transactions and events when cash is received or paid. It measures the overall financial result for a period as the difference between cash received and cash paid. It provides readers with information about the sources of cash raised during the period, the uses to which those funds were applied and the cash balance at the reporting date. The measurement focus is cash balances and changes therein (PSC Study 2 *Elements of the Financial Statements of National Governments*). The following example illustrates the disclosure of an accounting policy for the cash basis of accounting.

> **Accounting Policies**
>
> (i) The accounts of the Government are prepared on a cash basis. Transactions are recorded only when moneys are received and paid within the given period, whether or not the receipts and payments are in respect of goods supplied or services rendered during that period and whether they relate to recurrent or capital expenditure or revenue. The Statement of Assets and Liabilities does not include fixed assets, loans, investments other than those made under Section 3(4)(a), 8(2)(b), 9(3)(a) and 10(4)(b) of the Finance and Audit Act.

Example 3.1
Annual Statements of the Republic of Mauritius for the year ended 30 June 1998
Notes to the Accounts, page 2

Cash Balances

94. The cash basis of accounting recognizes cash and near-cash balances (PSC Study 5 *Definition and Recognition of Assets*). Cash includes cash in hand, cash in transit and cash on deposit. Near-cash balances consist of temporary investments in marketable securities and bullion. All other assets are mentioned only in relation to the cash effects of their acquisition or disposal. Assets other than cash which are held but not recognized may be described by way of additional statements or notes.

Cash Receipts

95. Under the cash basis of accounting all cash receipts, regardless of type, are recognized when cash is received (PSC Study 9 *Definition and Recognition of Revenues*). Cash receipts include:

- receipts from reciprocal (exchange) transactions
  - sale of goods and services
  - cash proceeds from sale of assets or investments;
- receipts from non-reciprocal transactions
  - taxation receipts
  - issue of currency
  - grants, contributions and donations (including transfers from another entity);
- financing inflows
  - interest receipts
  - borrowings;
- capital contributions by the controlling entity or owners; and
- custodial receipts.

96. Cash receipts may be classified by source or type. Cash receipts are discussed further in Chapter 6.

Cash Payments

97. Under the cash basis of accounting all cash outflows, regardless of type, are recognized when cash is paid (PSC Study 10 *Definition and Recognition of Expenses/Expenditures*). Cash payments include:

- payments relating to reciprocal (exchange) transactions
  - purchase of goods and services
  - acquisition or construction of assets
  - investments in other entities (both loans and capital injections);
- payments relating to non-reciprocal transactions
  - government transfers
  - grants, contributions and donations;
- financing outflows
  - interest payments
  - repayment of debt; and
- custodial payments.

98. Cash payments may be classified as "current" or "capital". Payments for the acquisition of assets may be categorized as "capital" if the asset is expected to have a useful life in excess of a year. Within the class of capital expenditure, annual asset expenditures may be reported by type (land, buildings etc.) and/or function (health, defense etc.). Although this description conveys the economic reality that benefits will be received in later periods, no recognition of these benefits is included in the financial statements. Types of cash payments, including methods of classification, are discussed further in Chapter 7.

Transactions and Events not Recognized

99. By definition, cash accounting recognizes cash transactions only. Other transactions or events are not generally recognized. Non-cash transactions or events include:

- unrealized gains or losses (e.g., increases or decreases in the value of assets due to interest rate movements);
- the purchase of goods and services or long-term assets on credit or where the method of payment includes a non-cash exchange;
- the consumption of goods or services which have been paid for in previous accounting periods;
- the consumption of service potential of long-term assets; and
- the incurrence of liabilities (e.g., increases in superannuation/pension obligations).

100. Although unrealized gains and losses on cash balances held in foreign currencies are non-cash transactions, they affect the closing cash balances. They are therefore necessary to reconcile opening and closing cash balances. Refer to Chapter 5 for further discussion of this item.

Reporting Model

101. The financial statement reporting model associated with the cash basis of accounting is a Statement of Receipts and Payments or Cash Flow Statement which reconciles opening and closing cash balances. Cash balances, cash receipts and cash payments are discussed more fully in Chapters 5, 6 and 7.

CHAPTER 4

CASH BASIS – BENEFITS AND LIMITATIONS

Introduction

102. This section examines the ability of governmental financial reports prepared under cash accounting to meet the needs of users.

Financial Statements

103. Under cash accounting one main financial report is typically prepared. This shows the cash financial position as at balance date and details of cash receipts and payments for the entity during the period. Where the reporting entity consists of a number of individual reporting entities, such as funds, each reporting entity, or fund, would prepare a separate report. The wider reporting entity, e.g., the whole of government entity, would also usually prepare a consolidated report.

104. Cash-based financial reports show the sources, allocation and use of cash resources. They show the cash required to finance the activities of government, the cash raised to meet those requirements, including the level of taxes extracted during a period, and the cash position of the government. This information is useful to a range of internal and external users as follows:

- internal users:
  - legislative bodies such as Parliament in assessing compliance with amounts appropriated;
  - Ministers and senior government managers reviewing the total amount and nature of government spending;

- external users:
  - potential lenders and suppliers evaluating the government's management of cash balances; and
  - financial analysts/economists assessing the impact of the government's fiscal requirements on the economy.

Historical Perspective

105. Traditionally, government budgets and appropriations have been cash based. This was one of the factors which led to the predominance of the cash basis in government accounting. The popularity of the cash basis in government accounting arose from the need for Parliament, or other representatives of the electorate, to monitor the collection of taxation receipts and the subsequent spending of those receipts by the government each year. The cash basis focuses on the flow of cash within an accounting period and thereby provides a basis for comparison with appropriations, as discussed below.

Compliance with Appropriations

106. To the extent that budgets and other requirements are themselves cash based, cash-based financial reports are able to demonstrate compliance with legally adopted budgets and with legal and contractual requirements. Governments reporting on a cash basis typically budget on a cash basis. The inclusion of a budget column in the financial statements allows a direct comparison to be made between budgeted and actual amounts. This information is useful to the legislature and external users interested in holding a government accountable, and internal users monitoring actual spending against appropriations.

Qualitative Characteristics

107. The principles underlying the cash basis are easy to understand and easy to explain.

108. In principle, information provided under the cash basis of accounting scores highly on the qualitative characteristic of understandability. To the extent that cash flows are uniform over time, it may also have high levels of reliability and comparability. Because it is relatively easy to compile cash-based information, reports may be more timely than under other bases of accounting. However, the method

of presentation of cash based information, such as the publication of detailed lists of receipts and payments, can affect the understandability of such information.

Costs

109. It is possible to operate a cash-based accounting system and to prepare cash-based financial statements with fewer trained staff than under other bases. However, governments using cash-based systems have often used large numbers of clerical staff to approve, process and check cash payments, usually via a central accounting and control system. In addition, some jurisdictions argue that extensive accounting and financial management skills are required to operate some types of cash-based budget systems. Generally, the cost of providing cash information is thought to be lower than under alternative bases.

110. The fact that cash accounting does not require any detailed accounting knowledge has made it easy for a wide range of users to access and understand information prepared on this basis. In comparison to other bases of accounting, politicians and other general users require less assistance or training to understand cash-based information.

Limitations of Cash Accounting

111. As discussed above, cash accounting provides information on cash flows and allows both the legislature and the government to monitor spending against cash-based appropriations. Many governments have found that information on cash collected, and cash spent, meets their needs for both internal management and for external accountability. However the demands of governments and external financial statement users for more complex information have grown. Increasingly, users of governmental financial statements expect governments to provide information on assets and liabilities, and the impact of current consumption on the stock of net assets held by a government. Cash accounting is not designed to meet these information needs. Its objectives are clear: to report cash inflows, cash outflows and changes in the cash balances held. Those who have more extensive information requirements need to either maintain supplementary records, or consider moving to a different basis of accounting.

112. Cash accounting focuses solely on cash flows within the current reporting period. It ignores other resource flows which may also impact upon the ability of a government to provide goods and services now, and in the future (e.g., although some jurisdictions may keep additional records, the cash basis does not account for accumulated borrowings and other liabilities). Nor does it record the benefits obtained from assets over a number of accounting periods. For these reasons cash-based information may be less relevant for decision makers. Some jurisdictions supplement cash-based financial statements with published cash forecasts which provide an indication of whether future cash receipts will be sufficient to cover expected cash outflows.

113. The United Kingdom Green Paper on Resource Accounting noted that one of the main limitations of cash accounting is the lack of information it provides on capital (assets).

> *While the present cash accounting system has served government well over many years, there are limitations to the information which it provides on capital. With cash accounting, spending on what is used over many years is recorded only when money is spent. No subsequent account is therefore taken of whether the asset is still in use, has reached the end of its useful life, or has been sold.* (*Better Accounting for the Taxpayer's Money: Resource Accounting and Budgeting in Government,* A Consultation Paper, July 1994, paragraph 1.16)

114. Cash accounting limits the ability of the electorate to hold the government accountable for its use of resources. The provision of information only on cash flows means that governments can be held accountable for their use of cash, but there is no corresponding information available with which to hold the government accountable for its management of assets and liabilities.

115. Where a government prepares its financial statements on a cash basis it may collect and report supplementary information such as information on its assets. Such information may be collected as a preliminary step on a transitional path to the adoption of a different basis of accounting. This information may be disclosed in the published financial statements or it may be used solely for

internal management purposes. The full benefits of collecting such information are able to be realized when the information is made available for legislative or public scrutiny.

116. One of the advantages of cash accounting over other bases of accounting is that there is no need for preparers to exercise any judgment when determining the amount of cash flows for the period. To that extent it is less subjective than other bases of accounting. However, preparers still have the ability to manage the timing of cash flows by delaying receipts or payments until the next reporting period.

117. Despite the apparent simplicity of cash accounting, in practice, financial statements prepared under cash accounting may not be easy for users to understand. This is largely due to the practice of reporting receipts and payments in great detail.

CHAPTER 5

CASH BASIS – CASH BALANCES

Definition and Recognition of Cash Balances

118. The cash basis of accounting recognizes cash and near-cash balances such as temporary investments in marketable securities and bullion. All other assets are mentioned only in relation to the cash effects of their acquisition or disposal.

119. IAS 7, *Cash Flow Statements* provides the following definitions:

> *<u>Cash</u> comprises cash on hand and demand deposits.*
>
> *<u>Cash equivalents</u> are short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.* (paragraph 6)

120. IAS 7 (paragraph 7) goes on to explain that short-term highly liquid investments are held for the purpose of meeting cash commitments rather than for investment. They normally include only those investments with maturities of, say, three months or less at the date of acquisition. They exclude equity investments but could include preferred shares that are acquired within three months of the redemption date.

121. An alternative definition of cash comes from the United States of America Federal Accounting Standards Advisory Board (FASAB):

> *Cash consists of:*
> *(a) coins, paper currency and readily negotiable instruments, such as money orders, checks, and bank drafts on hand or in transit for deposit;*
> *(b) amounts on demand deposit with banks or other financial institutions; and*
> *(c) foreign currencies, which, for accounting purposes, should be translated into U.S. dollars at the exchange rate on the financial statement date.* (SFFAS No. 1)

Reporting of Cash Balances

122. Closing cash balances are determined by taking opening cash balances, then adding cash receipts and subtracting cash payments during the reporting period. Changes in cash balances due to movements in foreign currencies, being unrecognized gains/losses, should be separately disclosed. The following example illustrates the disclosure of cash balances.

3. CASH AND BANK BALANCES

These balances refer to cash in hand, in transit and balances with banks and agents, both local and overseas.

	Rs
Balances held locally	130,153,800
Balances held overseas	17,274,846
	147,428,646

Example 5.1
Annual Statements of the Republic of Mauritius for the year ended 30 June 1998
Notes to the Accounts, page 2 (Rs)

123. Cash balances may be held in domestic and foreign currencies and it is usual to disclose these separately. Cash balances held in foreign currencies are reported at the closing rate. It is also best practice to disclose the terms, conditions and method of valuation for cash equivalents such as short term securities or bullion.

124. Cash receipts may be restricted in purpose. Restrictions may be imposed by an outside agency which has donated cash for a particular purpose, or more commonly restrictions may operate when an entity has constructed separate funds for the carrying on of specific activities or attaining certain objectives in accordance with legislative or other regulatory restrictions. An entity may be required, by contract or legislation, or may have chosen to make disclosures of these restricted cash flows. Such disclosures would also include disclosure of the portion of these funds remaining in closing cash balances.

Classification of Cash Balances

125. Possible classifications of cash include:

- cash on hand;
- cash in transit; and
- demand deposits.

126. Near-cash balances may be grouped according to the type of asset, with bullion being separately disclosed. Amounts denominated in domestic currency and foreign currencies are generally separately disclosed.

CHAPTER 6

CASH BASIS – CASH RECEIPTS

Definition of Cash Receipts

127. A cash receipt is an inflow of cash to the reporting entity.

Recognition of Cash Receipts

128. Under the cash basis of accounting all cash receipts, regardless of type, are recognized when cash is received. Entities using cash accounting recognize all receipts, regardless of type, although there may be separate disclosure of different types of receipts. Where an entity operates a system of holding accounts where receipts are deposited prior to being coded, there may be a slight time delay between the time of receipt and the coding of receipts to the relevant account code. In such cases, receipts are recognized when coded.

Types of Cash Receipts

129. Receipts include:

- receipts from reciprocal (exchange) transactions
  - sale of goods and services
  - dividend and interest receipts
  - cash proceeds from sale of assets;
- receipts from non-reciprocal transactions
  - taxation receipts
  - fees, fines, licenses etc.
  - issue of currency
  - grants, contributions and donations;
- financing inflows
  - borrowings;
- capital contributions by the controlling entity or owners; and
- custodial receipts.

130. The following examples illustrate the disclosure of revenue classifications.

<u>Abstract Account of Revenue and Expenditure of the Consolidated Fund for Financial Year 1997-98</u>

	RECURRENT REVENUE *Analysis of total recurrent revenue by Heads:*	**Estimated** **Rs**	**Actual** **Rs**
Heads			
41	Direct Taxes	3,662,000,000	3,623,289,187.57
42	Indirect Taxes	12,453,400,000	12,082,202,926.98
43	Receipts from Public Utilities	276,700,000	738,402,273.66
44	Receipts from Public Services	516,842,000	548,591,832.81
45	Rental of Government Property	43,710,000	48,568,434.99
46	Interest and Royalties	1,248,727,000	1,282,782,864.60
47	Reimbursements	173,621,000	147,188,882.46
	TOTAL - RECURRENT REVENUE	18,375,000,000	18,471,026,403.07

Example 6.1
Annual Statements of the Republic of Mauritius for the year ended 30 June 1998
Statement B, page 6 (Rs)

Abstract Account of Revenue and Expenditure of the Capital Fund for Financial Year 1997-98

Heads	CAPITAL REVENUE	Estimated	Actual
	Analysis of total capital revenue by Heads:	**Rs**	**Rs**
51	Grants	110,000,000	216,498,179.29
52	Loans: -		
	A. Local Sources	1,500,000,000	2,755,397,660.00
	B. External Sources	637,000,000	530,689,772.89
53	Dividends from Investments	390,000,000	440,639,758.86
54	Miscellaneous	2,000,000	1,224,510.49
	TOTAL - CAPITAL REVENUE	2,639,000,000	3,944,449,881.53
	Excess of Revenue over Expenditure		***524,118,038.10***

Example 6.2
Annual Statements of the Republic of Mauritius for the year ended 30 June 1998
Statement C, page 8 (Rs)

131. Types of receipts, including the treatment of receipts authorized by way of appropriation, are discussed below.

Appropriations

132. For the government as a whole, appropriations are an authorization to expend funds. However, for individual entities within government, any funds paid to the entity within the reporting period which are subject to appropriations are accounted for as cash receipts. In some jurisdictions, a government department supplying goods and services to the government or to the community on the government's behalf may regard the receipt of cash authorized by an appropriation as an exchange transaction. In other jurisdictions such receipts are regarded as non-reciprocal transfers. Both types of receipts are discussed below. This discussion assumes that an entity is required to account for cash receipts from a higher level of government. Under some centralized accounting and banking systems, all cash may be held centrally and individual entities may not receive any cash from its controlling entity. In that case, entities are only required to account for cash which they have received from other sources.

Receipts from Reciprocal (Exchange) Transactions

133. These transactions include the sale of goods and services, the receipt of dividends and interest and the total proceeds of asset sales. The cash flows associated with the disposal of assets are recognized as receipts when the cash is received. Receipts from the disposal of assets are generally reported separately to highlight their non-recurring nature (e.g., as capital receipts), and their effect on the reported cash surplus or deficit for the period.

Receipts from Non-reciprocal Transactions

134. A non-reciprocal transaction is one in which the entity receives assets (including cash) or has liabilities extinguished without directly giving approximately equal value in exchange to the other party or parties to the transfer. Taxation is the major source of such inflows or economic benefits. Some jurisdictions use the term "non-exchange" transfer to refer to non-reciprocal transfers. In addition to taxation receipts, governments may also receive grants, contributions and donations from other parties. For example, national governments may receive aid or grants from other sovereign governments or from supranational authorities. Component entities of a national government may

receive transfers from the controlling government entity which, under some circumstances may be viewed as an exchange relationship with the controlling government entity, but under other circumstances may be viewed as non-reciprocal transfers.

135. Under cash accounting only those transfers which result in the receipt or payment of cash are recognized.

Receipts Derived from use of the Powers of Government

136. Governments receive involuntary transfers through the use of their powers. The types of such transfers are wide-ranging, have a variety of alternative names, and vary from one jurisdiction to another. They may include:

- income tax;
- fringe benefit tax;
- sales tax;
- value-added tax;
- payroll tax;
- property tax;
- capital gains tax;
- stamp, check, credit and debit duties;
- custom and excise duties;
- license tax;
- road-user charges and motor vehicle fees;
- levies; and
- fines.

137. Taxation receipts frequently make up the majority of a national government's receipts and are generally viewed as an important component in measuring the government's financial results during the period. The mix of taxation receipts and borrowing is also important when assessing inter-generational equity.

138. Although other levels of government may also have the right to tax or levy, taxation will not necessarily constitute the majority of their receipts.

139. Taxation receipts may be collected by government departments or statutory bodies. The circumstances surrounding the collection of taxation receipts by departments may vary. In some cases the department or statutory body may have the right to retain the receipts for its own use. In other cases the receipts are instead collected on behalf of the government or a higher level of government, in which case the entity collecting the taxation has no right to spend the receipts without further authorization. Where a department is entitled to retain receipts, the gross inflows and outflows are normally reported within the cash flows of the department. Custodial receipts are discussed separately later in this Chapter.

140. The classification of user charges as reciprocal or non-reciprocal may vary between jurisdictions. Where the user charge represents a service provided by the government and the price is set at the cost of the service, or after allowing for a reasonable rate of return on costs, then the charge may be classified as reciprocal. However, where there is an element of taxation in that the price exceeds costs (and any allowance for a reasonable return) the charge, or part of the charge, may be regarded as non-reciprocal.

141. The following examples illustrate the disclosure of various types of non-reciprocal receipts which relate to the use of the powers of government.

	Heads and Items	Original Estimate of Revenue	Actual Revenue	Over the Estimate	Under the Estimate
	41 – DIRECT TAXES	**Rs**	**Rs**	**Rs**	**Rs**
	101 – TAXES ON INCOME				
.001	Income Tax, Companies & Bodies Corporate	1,175,000,000	1,170,921,843.21		4,078,156.79
.002	Income Tax, Others	1,350,000,000	1,237,687,238.59		112,312,761.41
	201 – TAXES ON CAPITAL				
.001	Succession Duties	0	34,073.65	34,073.65	
	301 – CONTRIBUTIONS TO SOCIAL SECURITY				
.001	Retiring Allowance Scheme for Members of the National Assembly	800,000	779,732.56		20,267.44
.002	Contributions to the Civil Service Family Protection Scheme	95,000,000	100,252,477.56	5,252,477.56	
	401 –TAXES ON FINANCIAL TRANSACTIONS				
.001	Mortgages, Inscriptions and Transcriptions	10,000,000	1,399,005.66		8,600,994.34
.002	Registration Fees	775,000,000	908,093,203.33	133,093,203.33	
.003	Stamp Duties	12,000,000	12,132,492.24	132,492.24	
.004	Incorporation and Lodging Fees, Search, Duty, etc	9,200,000	9,745,569.000	545.569.00	
	501 – TAX ON PROPERTIES				
.001	Tax on Properties	235,000,000	182,243,551.77		52,756,448.23
	TOTAL – DIRECT TAXES	3,662,000,000	3,623,289,187.57	139,057,815.78	177,768,628.21
	Net amount under the Estimates				*38,710,812.43*

Example 6.3
Annual Statements of the Republic of Mauritius for the year ended 30 June 1998
Statement D, pages 9 and 10 (Rs)

	Heads and Items	Original Estimate of Revenue	Actual Revenue	Over the Estimate	Under the Estimate
	42 – INDIRECT TAXES	**Rs**	**Rs**	**Rs**	**Rs**
	101 – CUSTOMS DUTIES				
.001	Import Duties and Excise Duties on Imports	6,350,000,000	6,205,452,911.19		144,547.088.81
.003	Stamp Duty on Imports	0	1,439,351.00	1,439,351.00	
.004	Sales Tax/Value-Added Tax	2,975,000,000	2,724,596,253.07		250,403.746.93
	201 – TAXES ON COMMERCE AND INDUSTRY				
	(1) Excise Duties				
.101	Spirits, Liquors and Alcoholic Beverages	690,000,000	681,457,054.00		8,542,946.00
.102	Tobacco and Cigarettes	775,000,000	832,085,864.00	57,085,864.00	
.199	Miscellaneous	16,000,000	15,815,525.00		184,475.00
	(2) Licences				
.201	Liquor	11,000,000	10,117,259.00		882,741.00
.202	Trading and Professional	0	535,129.75	535,129.75	
.203	Company and Commercial Partnership	44,000,000	45,494,763.18	1,494,763.18	
.299	Miscellaneous	57,000,000	79,262,025.10	22,262,025.17	
	Carried forward	10,918,000,000	10,596,256,135.36	82,817,133.10	404,560,997.74
	(9) Miscellaneous				
.901	Sugar Brokerage Tax	400,000	480,947.05	80,947.05	
	301 – TAXES ON TRANSPORTATION				
.001	Road Motor Vehicle Licences	280,000,000	292,128,664.50	12,128,664.50	
.999	Miscellaneous	17,000,000	15,039,432.10		1,960,567.90
	401 – TAXES ON GAMBLING				
.001	Tax on Lotteries	28,000,000	28,624,319.78	624,319.78	
.002	Tax on Betting	275,000,000	161,358,901.17		113,641,098.83
.003	Tax on Gaming	345,000,000	368,005,445.30	23,005,445.30	
	501 – TAXES ON HOTEL, RESTAURANT AND INTERNATIONAL TRAVEL				
.001	Tax on Hotel & Restaurant Bills	590,000,000	620,309,081.72	30,309,081.72	
	TOTAL – INDIRECT TAXES	12,453,400,000	12,082,202,926.98	148,965,591.45	520,162,664.47
	Net amount under the Estimates				*371,197,073.02*

Example 6.4
Annual Statements of the Republic of Mauritius for the year ended 30 June 1998
Statement D, page 10 (Rs)

Receipts Derived from the Issue of Currency

142. Currency in the form of notes and coins is usually created and issued by a central bank, sometimes referred to as the reserve bank or federal bank. The cost of creating notes and coins is a cash payment of the central bank. When the currency is issued, the central bank receives cash equal to the face value of the currency. Although these cash receipts and cash payments are cash flows of the central bank, if that bank forms part of the government reporting entity, the cash receipts and cash payments would also be cash flows of the government as a whole and would be included in any whole of government financial statements. The following example illustrates the disclosure of cash receipts from the issue of currency.

STATEMENT 1 – CONSOLIDATED FUND OF INDIA – REVENUE ACCOUNT–RECEIPTS	Major Head	Accounts 1997-98	Budget 1998-99	Revised 1998-99	Budget 1999-2000
B. NON-TAX REVENUE					
(a) Fiscal Services		**873.57**	**1109.94**	**1046.67**	**1265.36**
Currency, Coinage & Mint	0046	607.99	823.68	776.58	1014.51
Other Fiscal Services	0047	265.58	286.26	270.09	250.85
: :	: :	: :	: :	: :	: :
: :	: :	: :	: :	: :	: :

Example 6.5
Annual Financial Statement of the Government of India for the financial year 1997-98
Statement I – Consolidated Fund of India – Revenue Account – Receipts, page 1 (Rs. Crore)

Grants, Contributions and Donations

143. National governments may receive both non-reciprocal transfers from other governments or supranational authorities and grants, contributions or donations from the private sector. Other levels of government, including government sub-entities may receive both non-reciprocal transfers from higher levels of government and grants, contributions or donations from the private sector. This section looks at the accounting treatment of non-reciprocal transfers received by national governments. The treatment of non-reciprocal transfers made by national governments to other levels of government is discussed in Chapter 7.

144. In some countries the term “grant” is associated with a certain type of discretionary receipt and the term “transfers” is therefore used to refer to the broad range of non-reciprocal transfers including grants, shared cost agreements and entitlements. In other countries the terms may be used interchangeably. These transfers may take the form of cash, services, transfer of an asset or the reduction of an existing liability. Where these transfers take the form of cash, they will be recognized by the recipient government.

145. Restrictive conditions may or may not attach to the transfer. Both restricted and unrestricted grants, contributions and donations meet recognition criteria for the cash basis of accounting as soon as they are received. Disclosure of the different types of grants, contributions and donations, and any restrictions (e.g., grants may be specifically tagged for the purchase of assets) on cash balances remaining at the end of the reporting period may be appropriate.

146. Further discussion of non-reciprocal transfers is found in PSC Study 9 *Definition and Recognition of Revenues*.

Financing Inflows and Capital Contributions from the Controlling Entity or Owners

147. Financing inflows include all receipts from borrowings. They would also include any cash raised by discounting future expected receipts.

148. Under cash accounting, there is usually no distinction made between cash provided by a controlling government entity for operating costs, and amounts which represent the acquiring of, or an increase in, a financial interest in the entity. They are both recognized as cash receipts. Where a distinction is made, there may be separate disclosure of such receipts.

Custodial Receipts

149. Custodial receipts include taxes collected as agent for another government, contributions towards pension and welfare funds, and other receipts collected as agent for another entity. In practice custodial receipts may or may not be included as a cash receipt of the reporting entity. Custodial receipts may be separately disclosed to indicate their special nature.

Classification

150. Classification should depend on users’ needs and on how they can best be met. The following

constraints are also important:

- level of detail of the information required;
- the ability to classify the information and the reliability of the resulting numbers; and
- benefit versus cost.

151. Receipts may be classified by source or type. Alternative classification systems for receipts include:

- operating, investing, and financing, in accordance with the categories used in IAS 7, *Cash Flow Statements*;
- capital and current (also referred to as capital and recurrent);
- by activity and/or organization to which the receipt relates;
- reciprocal and non-reciprocal; and
- by function in accordance with the classifications used by the System of National Accounts (SNA) and the International Monetary Fund's Government Finance Statistics (GFS). Refer to Chapter 19 for a fuller description of these systems.

152. These classifications are not mutually exclusive. More than one type of classification may be used at the same time. An illustration of a classification system for receipts is shown below. Note that some user charges may be classified as reciprocal or non-reciprocal depending upon the nature and amount of the charge.

Receipts from Reciprocal (Exchange) Transactions
Current
Sales
Dividends (from entities other than state-owned monopolies)
Interest
Royalties
Capital
Proceeds from asset sales

Non-reciprocal Transfers – Receipts from the use of the Powers of Government
(depending on the particular jurisdiction)
Taxes on income, profits and capital gains
Sales taxes
Property taxes
Payroll taxes
Poll taxes
Social security contributions
Taxes on specific services
Excises
Customs and import duties
License, registration and permit fees
Fines

Non-reciprocal Transfers – Receipts from Issue of Currency

Non-reciprocal Transfers – Grants, Contributions and Donations
(with separate disclosure of any restrictions on use)
From other levels of government
From other governments
From supranational authorities
From the private sector

Financing Inflows

Contributions from Controlling Entities *(in the case of controlled entities)*

Custodial Receipts

CHAPTER 7

CASH BASIS – CASH PAYMENTS

Definition of Cash Payments

153. A cash payment is a cash outflow resulting from the payment of cash by the reporting entity to a party outside the reporting entity.

Recognition of Cash Payments

154. There are a range of points at which transactions which will lead to a cash payment may be recorded within an accounting system. These points include:

- approval of a budget which includes the specific item or an amount for that class of transactions;
- approval of the request to purchase within the entity;
- the placing of an order (recognition of a commitment to spend);
- receipt of the item;
- receipt of an invoice;
- approval of a payment order; and
- payment of the invoice.

155. Under commitment accounting transactions are recorded when there is a commitment to purchase an item. This allows an entity to manage its projected spending against amounts available under a budget. Commitment accounting is often used in conjunction with cash accounting as it provides additional management information. However, under the cash basis of accounting, the actual recognition of payments occurs at the time of payment.

156. Payment systems may include the use of prepayments. Prepayments may occur when a government forwards a sum of cash to one of its departments or agencies to be used as a source of ready cash, or alternatively when the government is prepaying an agency to handle transactions on behalf of the government e.g., to make social security payments. The bank accounts held for such purposes are sometimes referred to as imprest accounts. If the recipient agencies, and therefore their bank accounts, form part of the government reporting entity, the initial transfer of funds to the agency is generally not recognized as a payment in the whole of government financial statements because the funds in these bank accounts form part of the Government's opening and closing cash balances. In both cases the payments are not recognized until payment has been made and the details of the payment are recorded in the accounting system. However, where a payment system results in a series of checks being issued to social security recipients, payment would be recognized at the time that the checks are issued.

157. An alternative method of dealing with imprest accounts is to record the transfer of funds to the account as a payment, and at the end of the reporting period to transfer the funds in the bank account back to the government's bank account. It is suggested that this method is more appropriate where the imprest accounts do not form part of the government reporting entity, or where legislation requires the recording and disclosure of all payments from particular government bank accounts.

Types of Cash Payments

158. Cash payments include:

- payments relating to reciprocal (exchange) transaction;
  - purchase of goods and services
  - acquisition or construction of assets
  - investments in other entities (both loans and capital injections);
- payments relating to non-reciprocal transactions
  - government transfers
  - grants, contributions and donations;

- financing outflows
  - interest payments
  - repayment of debt; and
- custodial payments.

159. Although some transactions such as borrowing and the payment of interest may be restricted to the whole of government level, most of the above payments are made by government sub-entities.

160. These categories are not mutually exclusive: more than one classification may be applicable to a given payment (e.g., a grant to a government sub-entity may be tagged for the purchase of assets). Refer to the discussion of classification of payments later in this Chapter.

161. The types of payments made by government entities will depend upon the type of activities conducted by the entity. Entities providing mainly policy advice will spend a high proportion of their budget on personnel. Entities providing operational services to government (e.g., operating penal institutions) will have a wider range of payments including those relating to personnel, food, utilities, vehicles and buildings.

Payments made under Appropriation

162. For entities such as government departments, payments will usually be subject to some type of legislative authority or appropriation. The nature of appropriations differs between jurisdictions. Appropriations may authorize the spending of money on types of cash payments (e.g., wages and salaries) and/or for particular purposes such as programs, activities or outputs.

Purchase of Goods and Services

163. Purchases of goods and services could include payments for stationery, rent, maintenance, power, rates or taxes on land, vehicle expenses etc.

Payments for Personnel

164. Payments for personnel could include wages and salaries, payments for holiday leave, and other benefits paid to employees, or paid by the employer with respect to the employee.

Government Transfers

165. One definition of government transfers comes from IAS 20, *Accounting for Government Grants and Disclosure of Government Assistance*. This definition focuses on transfers of resources from the government to enterprises.

> <u>Government grants</u> *are assistance by government in the form of transfers of resources to an enterprise in return for past or future compliance with certain conditions relating to the operating activities of the enterprise.* (paragraph 3)

166. An alternative definition, which also encompasses transfers to individuals and intergovernmental transfers, comes from Public Sector Accounting Recommendation PSAR Section PS 3410, *Government Transfers* of the Canadian Institute of Chartered Accountants (CICA). Although the discussion in this publication is designed to provide guidance for governments using the accrual basis of accounting, some of the discussion is also relevant for governments using the cash basis of accounting.

> ***Government Transfers*** *are transfers of money from a government to an individual, an organization or another government for which the government making the transfer does not:*
> *(a) receive any goods or services directly in return, as would occur in a purchase/sale transaction;*
> *(b) expect to be repaid in the future, as would be expected in a loan; or*
> *(c) expect a financial return, as would be expected in an investment.* (PSAR Section PS 3410, paragraph .03)

167. The PSAR identifies three major types of transfers: entitlements, transfers under shared cost agreements and grants. These categories are based on a concept of a spectrum in the degree of

discretion the government has in making a transfer. Further discussion of each of these transfers is given in Chapter 15. However, not all countries make this distinction between types of transfers.

168. The payment of welfare benefits and other transfer payments (including unemployment and sickness benefits) are payments at the whole of government level. When these benefits and transfers are made by a sub-entity, they will usually be an agency or custodial payment made on behalf of the government.

Grants, Contributions and Donations

169. Grants, contributions and donations are a further class of non-reciprocal transfers. They may or may not have restrictive conditions applying. Under cash accounting all grants, contributions and donations, including loans, or contributions of capital from a higher level of government or controlling entity are recorded as cash payments. However, separate disclosure of loans and capital contributions highlights the non-recurring nature of these grants.

Acquisition or Construction of Assets

170. The annual costs of acquiring or constructing assets are shown as cash payments in the financial reports of entities using the cash basis. Such acquisitions are usually categorized as "capital" if they are expected to have a useful life in excess of a year. This distinguishes recurring operating payments required to provide ongoing services from non-recurring payments. These capital payments may also be reported by type (land, buildings, etc.) and/or function (health, defense, etc.). Assets other than cash which are held, but not recognized, may be described by note. Refer to Chapter 8: Cash Basis – External Reporting for a discussion of additional disclosures under cash accounting.

171. IAS 16, *Property, Plant and Equipment* contains a number of suggested disclosures in relation to the acquisition or construction of assets. Although this standard assumes the use of the accrual basis of accounting, many of the disclosures would also provide useful information for readers of cash-based financial statements.

172. The following example illustrates the disclosure of payments made which relate to the acquisition of capital assets. This type of expenditure is often disclosed separately as capital expenditure under the cash basis of accounting.

	Votes and Items	**Total of voted provision rendered available for the year**	**Actual Expenditure**	**Over the Provisions**	**Under the Provisions**
	022 – Police				
.001	Quarters and Barracks	1,300,000.00	1,201,179.25		98,820.75
.002	Construction/Improvement of Police Stations	5,650,000.00	5,649,041.54		958.46
.003	Improvements Renewal, and Minor Projects	4,639,000.00	4,638,087.23		912.77
.004	Vehicles, Launch, Plant, Equipment and Furniture	22,308,000.00	22,307,475.28		524.72
.005	Road Safety and Traffic Improvement	2,764,000.00	2,763,494.36		505.64
	TOTAL - POLICE	36,661,000.00	36,559,277.66		101,722.34

Example 7.1
Annual Statements of the Republic of Mauritius for the year ended 30 June 1998
Statement E1, page 100 (Rs)

Loans made to other Entities

173. Loans which result in a cash payment may be separately disclosed. The transfer of assets other than cash is not recognized as a payment, although the transfer may be disclosed in the Notes to the Financial Statements.

174. The following example illustrates the disclosure of cash payments associated with loans and advances.

	Votes and Items	Total of voted provision rendered available for the year	Actual Expenditure	Over the Provisions	Under the Provisions
	SERVICES UNDER THE CONTROL OF THE MINISTER OF LOCAL GOVERNMENT AND PUBLIC UTILITIES				
	224 – Central Water Authority				
.001	Loan to CWA for Development Programme	5,000,000.00	5,000,000.00		
.002	Loan to CWA for Port Louis Water Supplies	5,000,000.00	3,729,149.80		1,270,850.20
.003	Loan to CWA for District Water Supplies	88,406,000.00	88,405,637.60		362.40
.004	Loan to CWA for Mare aux Vacoas Water Supplies	53,181,000.00	53,180,248.76		751.24
	TOTAL – CENTRAL WATER AUTHORITY	151,587,000.00	150,315,036.16		1,271,963.84

Example 7.2
Annual Statements of the Republic of Mauritius for the year ended 30 June 1998
Statement E1, page 99 (Rs)

Capital Injections to Government Owned Entities

175. Capital injections by central government to government departments or agencies which involve a cash payment are shown as a cash payment in the financial reports of the parent entity, if such reports are prepared. If the capital contribution is specifically tagged for the purchase of assets it may be separately disclosed as a “capital” payment.

Financing Outflows

176. Interest payments are recognized as cash payments at the time of payment. Repayments of borrowings which involve cash flows are also recognized as cash payments.

177. The following example illustrates the disclosure of the payment of interest by the whole of government.

	Original Estimate CI$	Approved Estimate CI$	Actual 1997 CI$	More than Estimate CI$	Less than Estimate CI$
Statutory Expenditure:					
Public Debt Charges – Interest	4,774,181	4,774,181	4,455,569	-	318,612
Public Debt Charges – Repayments	7,944,326	7,944,326	8,710,244	765,918	-
Other Statutory Expenditure	7,551,631	7,551,631	5,307,813	-	2,243,818
Total Statutory Expenditure	20,270,138	20,270,138	18,473,626	765,918	2,562,430
Total Expenditure	255,473,399	276,969,077	246,625,711	949,385	31,292,750
Surplus/ Deficit (-) for the Year	-7,748,675	-29,244,353	-3,425,907	-	25,818,446

Example 7.3
Cayman Islands Government
Accounts for the year ended 31st December 1997
Statements of Receipts and Payments for the year ended 31st December 1997, page 3 (CI$)

Custodial Payments

178. Custodial payments include the payment of welfare benefits and transfer payments by government departments or agencies on behalf of the government, and the payment of amounts collected as agent of another entity (e.g., the transfer of employee contributions towards pension and welfare funds to those funds). In practice, the treatment of custodial payments varies between jurisdictions and they may or may not be recognized as a cash payment of the reporting entity depending upon the jurisdiction. Where custodial payments are disclosed, receipts and payments are disclosed separately.

179. The following example illustrates the deployment of cash resources to aid in the provision of training services and unemployment payments for the benefit of the unemployed. These payments are made by a government agency on behalf of the government as a whole.

Interdepartmental Transactions

180. In some jurisdictions, usually those which use a centralized accounting system for government departments, some interdepartmental transactions may be recorded as cash receipts and cash payments, although the transactions have been effected by a book entry only. These are transactions which would have been recorded as payments and receipts by the individual sub-entities if they had had their own accounting systems.

Classification

181. Classification depends upon users' needs and on how they can best be met. The constraints identified in the discussion of classification of receipts in Chapter 6 apply here also.

182. Cash payments may be classified in a number of ways, and it is common for most payments to be classified in more than one way. Under a well designed system multiple classifications can be accommodated within the same system. Methods of classification include:

- current or capital;
- economic type;
- function;
- organization or organizational unit (and appropriations for each of those units); and
- detailed type.

Classification as Current or Capital

183. An example of current and capital classifications is shown below.

APPENDIX 7

Operating Fund Account
ABSTRACT OF OPERATING AND CAPITAL EXPENDITURE
FOR THE YEAR 1997

Heads of Expenditure	Revised Estimate	Expenditure	Increase	Decrease
	$	$	$	$
	: :	: :	: :	: :
PRINTING AND STATIONERY				
Operating	1,608,050	1,592,706.73	...	15,343.27
Capital	366,150	363,474.12	…	2,675.88
VAT	176,400	156,021.11	…	20,378.89
SUPPLIES				
Operating	4,361,807	4,687,721.79	325,914.79	…
Capital	559,493	559,492.43	…	0.57
VAT	506,500	505,836.61	....	663.39
INFORMATION, TECHNOLOGY & COMPUTING SERVICES				
Operating	2,185,342	2,098,724.92	…	86,617.08
Capital	378,000	367,389.44	…	10,610.56
VAT	253,300	253,075.04	…	224.96

Example 7.4
Report on the Accounts and Finance, Parliament of Fiji
For the Year 1997, Appendix 7, page 1 (FD)

Classification by Economic Type

184. Under a cash accounting system all payments may be classified by economic type, e.g., wages and salaries, capital, and non-reciprocal transfers including grants, contributions and donations. The object classification enables an entity to exercise control at various levels of management.

185. The following examples illustrate the disclosure of payments for goods and services by economic type.

APPENDIX 8 –*(continued)*

Operating Fund Account

DETAILED STATEMENT OF OPERATING AND CAPITAL EXPENDITURE FOR THE YEAR 1997

SEG's	Heads of Service	Revised Estimate	Expenditure	Increase	Decrease
	2 – OFFICE OF THE PRIME MINISTER Programme 2-Public Service Commission Summary of Total Expenditure	$	$	$	$
1	Established Staff..	2,816,000	2,813,935.36	....	2,064.64
2	Unestablished Staff...	118,060	116,606.06	....	1,453.94
3	Travel and Communications.............................	111,200	96,962.12	....	14,237.88
4	Maintenance and Operations.............................	23,500	22,167.54	....	1,332.46
5	Purchase of Goods and Services.......................	166,500	119,819.64	....	46,680.36
6	Operating Grants and Transfers........................	1,647,090	1,331,734.66	....	315,355.34
7	Special Expenditures...	80,400	54,539.49	....	25,860.51
	Total-Operating..	4,962,750	4,555,764.87	....	406,985.13
	Net Decrease..	....	....	....	406,985.13
8	Capital Construction	1,665,000	1,069,744.01	....	595,255.99
9	Capital Purchase	213,450	199,266.02	....	14,183.98
	Total-Capital..	1,878,450	1,269,010.03	....	609,439.97
	Net Decrease..	....	....	....	609,439.97
	: :	: :	: :	: :	: :

Example 7.5
Report on the Accounts and Finance, Parliament of Fiji
For the Year 1997, Appendix 8, page 2 (FD)

3. Expenditure by standard accounts classification

		1993		1992
Salaries and wages		$3,975		$ 4,089
Employee benefits		794		838
Transportation and communication		308		291
Services		1,414		1,581
Supplies and equipment		645		704
Acquisition/construction physical assets		566		702
Transfer payments		40,583		39,124
Interest and other expenditures on provincial debt	$5,635		$4,793	
less: Interest and other investment income	342		597	
Interest on debt issued for provincial purposes		5,293		4,196
Other transactions		129		158
Total expenditure		$53,707		$51,683

Example 7.6
Public Accounts of Ontario, 1992–93
Notes to the Financial Statements, page 6 (CAD)

Classification by Function

186. A classification by function or program provides useful information on the purposes or objectives of expenses. It helps allocative decision making and the review by the legislative and executive branches of government. This information provides data which could be used to calculate expenditures per unit of activity. Most government outlays can be assigned to a specific function or broad sector of the government. Some, however, require judgment. For example, military colleges are usually classified as “defense” rather than “education”.

187. Existing functional classification systems include the United Nations’ System of National Accounts

and the International Monetary Fund’s Government Finance Statistics. These are discussed in Chapter 19. The following example illustrates the classification by function of cash payments made by the whole of government.

STATEMENT 1 - CONSOLIDATED FUND OF INDIA - REVENUE ACCOUNT-DISBURSEMENTS

(In crore of Rupees)

	Accounts 1997-98	**Budget 1998-99**	**Revised 1998-99**	**Budget 1999-2000**
A. GENERAL SERVICES	114219.68	130367.66	136161.12	149742.44
(a) Organs of State	1443.63	1424.48	1425.57	1141.09
(b) Fiscal Services	2628.63	2900.20	2954.15	3012.52
(c) Interest Payment and Servicing of Debt	65637.27	75000.00	77248.00	88000.00
(d) Administrative Services	7199.69	8223.74	8610.86	8795.79
(e) Pensions and Miscellaneous General Services	10008.35	10922.26	13691.56	14106.23
(f) Defence Services	27302.11	31896.98	32230.98	34686.81
B. SOCIAL SERVICES	11239.86	14768.39	14187.83	15416.35
C. ECONOMIC SERVICES	97979.42	95245.40	100019.86	102678.65
(a) Agriculture and Allied Activities	12875.14	15703.87	15227.35	16509.58
(b) Rural Development	4901.91	5373.23	5162.10	4969.49
(c) Special Areas Programmes	524.74	859.19	858.33	1656.02
(d) Irrigation & Flood Control	216.14	279.54	272.08	279.81
(e) Energy	15102.06	2709.32	2497.00	3032.83
(f) Industry and Minerals	9114.29	8798.26	10363.53	10870.72
(g) Transport	30769.03	33968.54	33027.39	36266.09
(h) Communications	17463.24	20383.93	21260.56	23534.83
(i) Science Technology and Environment	2627.32	3045.94	3006.47	3327.04
(j) General Economic Services	4385.55	4123.58	8345.05	2232.24
D. GRANTS-IN-AID AND CONTRIBUTIONS	53267.36	53910.79	50976.27	59745.34
Disbursements of Union territories	1025.97	1090.43	1237.23	1236.47
TOTAL - REVENUE DISBURSEMENTS	***277732.29***	***295382.67***	***302582.31***	***328819.25***

Annual Financial Statement of the Government of India for the financial year 1997-98
Statement I – Consolidated Fund of India – Revenue Account – Disbursements, pages 4 and 5 (Rs. Crore)

Classification by Organization

188. Payments can also be divided into separate sections for each ministry, department or agency. These organizations can then be held responsible for these items (e.g., Ministry of Agriculture, Ministry of Health). Such a classification is tailored to the particular structure of the government. Within each spending organization, the payments can be further classified by the type of payment or by organizational unit. They may also be further classified by appropriation category.

189. An example showing classification of payments by organizations is shown below.

APPENDIX 1V
DETAILS OF RECURRENT EXPENDITURE FOR THE YEAR ENDED 31st DECEMBER 1997

		ORIGINAL ESTIMATE	**SUPPLEMENTARY APPROVALS & VIREMENTS**	**APPROVED ESTIMATE**	**ACTUAL EXPENDITURE**	**MORE THAN ESTIMATE**	**LESS THAN ESTIMATE**
		CI$	**CI$**	**CI$**	**CI$**	**CI$**	**CI$**
	HEAD 13. PORTFOLIO OF FINANCE AND ECONOMIC DEVELOPMENT						
1.	Personal Emoluments	1,602,125	67,467	1,669,592	1,621,062	-	48,530
2.	Traveling & Subsistence	204,749	-3,900	200,849	191,590	-	9,259
3.	Supplies & Materials	26,954	12,110	39,064	34,021	-	5,043
6,	Utilities	1,122,029	1,082	1,123,111	998,437	-	124,674
7.	Other Operating & Maintenance Services	2,119,935	366,258	2,486,193	2,133,893	-	352,300
8.	Grants, Contributions & Subsidies	5,006,450	994,485	6,000,935	5,633,459	-	367,476
10.	Awards and Indemnities	75,000	-	75,000	64,720	-	10,280
11.	Retiring Benefits – Non - Statutory	1,275,009	23,500	1,298,509	1,252,720	-	45,789
14.	Reference Materials & Other	1,144	-475	669	499	-	170
17.	Repayments & Reserve	2,375,125	10,000	2,385,125	1,806,632	-	578,483
19.	Loans	952,307	-	952,307	455,449	-	496,858
21.	Insurance	2,854,094	-533,356	2,320,738	1,441,664	-	879,074
	TOTAL HEAD 13	17,614,921	937,171	18,552,092	15,634,146	-	2,917,946

Example 7.8
Cayman Islands Government
Accounts for the year ended 31st December 1997
Appendix IV, page 34 (CI$)

CHAPTER 8

CASH BASIS – EXTERNAL REPORTING

Introduction

190. This Chapter considers the types of financial reports commonly prepared by government financial reporting entities using the cash basis of accounting. Government financial reporting entities are those entities in respect of which it is reasonable to expect the existence of users dependent on financial reports for information which will be useful to them for accountability and decision making purposes. The term may refer to the whole of government, departments or ministries of government, or other entities that are part of a government.

Reporting Model

191. The financial statement reporting model (refer to definition of reporting model in the Glossary) frequently associated with the cash basis of accounting is a Statement of Receipts and Payments, also referred to as a Cash Flow Statement, which reconciles opening and closing cash balances.

192. Accordingly, information disclosed in the financial statements under the cash basis indicates whether the government has spent more or less cash than it collected during the reporting period.

193. The Statement shows the excess (or shortfall) of receipts over payments. If operating receipts and payments are disclosed separately from borrowings and repayments this provides a useful measure of whether a government has managed to meet current cash requirements from current cash receipts, and whether its net cash balance has increased or decreased. For a more detailed discussion of the benefits of the information presented under cash accounting refer to Chapter 4.

194. There is no prescribed format for a Statement of Receipts and Payments. Receipts and payments may be shown as separate categories, or alternatively, certain types of receipts and payments such as current and capital flows may be grouped together. Statements of Receipts and Payments may also be prepared for each of the main operating accounts.

Notes to the Financial Statements and Statement of Accounting Policies

195. The Notes to the Financial Statements are regarded as an integral part of the financial statements. They provide more detailed disclosure (e.g., disclosure of the amounts of specific taxation receipts collected) than is possible or desirable on the face of the main statements.

196. The Notes to the Financial Statements include a Statement of Accounting Policies. It is fundamental to the understanding and interpretation of governmental financial reports that those who use them are aware of the accounting policies on which they are based. IAS 1, *Presentation of Financial Statements* discusses the selection and disclosure of accounting policies.

> *Accounting policies are the specific principles, bases, conventions, rules and practices adopted by an enterprise in preparing and presenting financial statements.* (paragraph 21)

197. IAS 21 requires disclosure of all significant accounting policies, which is normally made by way of a Statement of Accounting Policies.

198. Under cash accounting, the principal accounting policies are the definition of the reporting entity, the point of recognition for receipts and payments and the translation of amounts denominated in foreign currency. Examples of accounting policies for the cash basis of accounting are included in Appendix 2.

Additional Disclosures

199. Governments operating under the cash basis of accounting may collect additional information and disclose it as memoranda items. Although not a product of a cash-based accounting system, such information may be regarded as having sufficient value to warrant its collection. It would be reported in addition to, rather than as part of, the financial statements.

200. The additional statements or note disclosures could include:

- items recognized under accrual accounting
  - resources (lists of physical assets and investments)
  - borrowings;
- items normally disclosed under accrual accounting
  - commitments
  - contingencies (guarantees, indemnities and securities);
- other items
  - unappropriated payments
  - tax expenditures; and
  - forecast information.

201. One benefit of disclosing asset information, even by way of supplementary schedules, is that once information about assets is formally reported, the accuracy of asset information usually improves. This allows better management of assets. Initial asset disclosures may be narrative only, with valuations gradually being added over time.

202. Although borrowings are not recognized as liabilities under the cash basis, separate schedules of borrowings are often prepared and published because of the importance of the government's level of debt for fiscal and monetary policy purposes. If borrowings are disclosed, it may also be appropriate to disclose details of securities over assets. Non-cash loans may also be disclosed.

203. Where additional records of assets and liabilities are maintained by entities using the cash basis of accounting, those entities will incur additional record keeping costs. These costs will be largely the same as the costs normally borne by entities maintaining details of assets and liabilities as part of an accrual accounting system. However, the prior collection of information on assets and borrowings may be helpful if governments subsequently adopt accrual accounting, and would help reduce implementation costs. Where such additional information is disclosed it should be both comprehensive and reliable. Inaccurate or incomplete data presents as many risks to decision makers as a complete lack of information. That is, it may be better to have a complete data set on a particular class of assets than to have a partial set of information on all assets. Where information is not complete, this should be clearly signalled to users.

204. Examples of contingencies are claims, pending or threatened litigation, guarantees of the indebtedness of others and indemnities. A commitment is an entity's responsibility for a future liability based on an existing contractual agreement. Disclosure of contingencies and commitments shows an entity's possible exposure to loss and future liabilities.

205. Where extensive disclosures of assets, liabilities and other items that are inherent to accrual accounting are made by entities using the cash basis of accounting, it may be more cost effective for those entities to adopt accrual or modified accrual accounting and thereby reap the benefits of recognizing these items within an integrated reporting system.

206. An example of additional asset and liability disclosure is shown below.

NOTE 9 TO THE ACCOUNTS

STATEMENT OF CONTINGENT LIABILITIES

DETAILS OF CONTINGENT LIABILITY	YEAR ISSUED	Currency	APPROVED LIABILITY	LIABILITY 31/12/97	CI$ VALUE 31/12/97
PORT AUTHORITY					
Guarantee of loan for developing property in the Industrial Park Area	1988	CI$	1,500,000	1,084,139	1,084,139
Guarantee of loan for land purchase 1.25 acres	1990	CI$	300,000	227,116	227,116
CAYMAN ISLANDS MUSEUM					
Guarantee of loan for renovation of the Old Law Courts Building	1988	CI$	300,000	12,695	12,695
WATER AUTHORITY					
Guarantee of loan for the Water and Sewerage Project and Red Bay Spotts Extension	1991	US$	21,850,000	18,633,111	15,527,593

Example 8.1
Cayman Islands Government
Accounts for the year ended 31st December 1997
Notes to the Accounts, page 21 (CI$)

Compliance with Appropriations

207. As discussed in Chapter 2, compliance reporting may form part of the end of year governmental financial reports, or the budget statements for the following year. Examples of compliance reporting are shown in Chapter 2.

Tax Expenditures

208. Tax expenditures are estimates of the revenue foregone because of preferential provisions of the tax structure. They are due to special exclusions, exemptions, deductions, credits, deferrals, and tax rates that depart from a 'baseline'. These exceptions are generally intended to achieve public policy objectives by providing benefits to qualifying individuals or entities or by encouraging particular activities. They also may be intended to improve tax equity or offset imperfections in other parts of the tax structure. Tax expenditures are not revenue. They are not inflows of resources to the reporting entity. (SFFAS No. 7, page 75)

209. The U.S. standards allow entities to disclose tax expenditure information that is relevant to the performance of the entity's programs but caution that this information should be appropriately qualified and explained to help the reader assess the possible impact of the specific tax expenditures on the success of related programs. In addition, with similar cautionary language, they permit the disclosure of the cost to state and local governments and to citizens of federal laws which mandate them to make expenditures or incur other types of costs, such as costs related to federal regulations that establish the characteristics of a product or the methods of production (also referred to as directed flows of resources or unfunded mandates). (SFFAS No. 7, page 28)

210. Tax expenditures represent tax receipts foregone by the government. Although tax expenditures result in fewer taxes being collected than would otherwise be the case, no government currently recognizes tax expenditures as a payment of cash. It is not accepted practice to recognize opportunity costs. However, governments may wish to disclose estimates of tax expenditures as supplementary information.

Forecast Information

211. Governments which collect taxation receipts usually prepare budget statements outlining forecasts of budgeted receipts and payments. The forecast budget documents contain details of the appropriations or legislative authorities for which approval is sought. This information may be presented in conjunction with external financial reports, but it is more commonly published as a separate document. The type of information presented in budget documents is determined by the nature of appropriations. A full discussion of forecast information is outside the scope of this Study.

CHAPTER 9

MODIFICATIONS TO THE CASH BASIS

Introduction

212. This Chapter describes various modifications to the cash basis. Under the most common modification to the cash basis the books are held open for a specified period after year end (e.g., around one month). The intention behind this modification is to overcome some of the perceived timing difficulties experienced under the cash basis whereby cash flows which relate to current year spending may not occur until after the end of the year. As well as adopting modifications to the cash basis, governments may also provide additional disclosure of certain items normally recognized under accrual accounting. The disclosure of particular items will vary from jurisdiction to jurisdiction. In addition to the items disclosed under the cash basis, there may be separate disclosure of the near-cash balances represented by receivables and payables subsequently received or paid during the specified period and various financial assets and liabilities. For example, the government of Malaysia uses a specified period within its federal annual financial statements. It also prepares memorandum accounts which disclose the following items:

- assets
  - recoverable loans
  - investments
  - subscriptions to international organizations
  - statutory deposits;

- liabilities
  - public debt
  - guarantees
  - notes payable.

213. Although the adoption of modifications to the cash basis and additional disclosures often occur together, this Chapter focuses on modifications to the cash basis — specifically the application of the specified period. The benefits of disclosing additional information under the cash basis and issues surrounding the reporting of additional disclosures are discussed in Chapter 8.

The Specified Period – Introduction

214. The specified period is usually established by government resolution and is applied to all government entities using this method of accounting. It is generally around one month in length. Receipts and payments which occur during the specified period but which originated in the previous reporting period are recognized as receipts and payments of the previous fiscal year (PSC Study 2 *Elements of the Financial Statements of National Governments*). Cash flows at the beginning of the reporting period which have already been accounted for in the previous reporting period are deducted from the current period's cash flows.

215. The recognition and reporting of cash balances, cash receipts and cash payments in conjunction with a specified period is virtually identical to the recognition and reporting of these items under the cash basis. However, the use of a specified period does lead to some differences in these elements. These are discussed below.

The Specified Period – Cash Balances

216. The modification to the cash basis refers only to the holding open of the books to recognize certain amounts received and paid during the specified period. In addition to amounts normally recognized under the cash basis, they include the net balance of amounts received and paid during the specified period which originated in the previous reporting period.

The Specified Period – Cash Receipts

217. In addition to the inflows generally recognized as receipts under the cash basis of accounting, amounts received during the specified period which originated in the previous reporting period are recognized as receipts of the previous reporting period. The recognition criteria for receipts in relation to the specified period are discussed below.

The Specified Period – Cash Payments

218. In addition to the outflows generally recognized as payments under the cash basis of accounting, payments made during the specified period which originated in the previous reporting period are recognized as payments of the previous reporting period. This extension of the reporting period applies to all categories of payments.

The Specified Period – Measurement Focus

219. The measurement focus under this method of accounting is on current financial resources and changes in those resources.

The Specified Period – Length

220. The exact length of the specified period may vary between governments. In addition, individual governments using a specified period may have used different specified periods over time or for different types of flows. Such changes make it difficult to compare results between jurisdictions or for one jurisdiction over a period of time and in some cases may provide an opportunity to influence reported results. Best practice would suggest that:

- the specified period be consistently applied from year to year;
- the specified period be the same for both receipts and payments;
- to the extent possible, the same criteria for recognition of receipts and payments during the specified period be applied to all receipts and payments;
- around one month is an appropriate specified period because accounts for goods purchased on credit are commonly settled within this period. A specified period which is any longer may make it difficult to produce timely financial statements; and
- the accounting policies used be fully disclosed.

221. The accounting policies illustrated below provide details of the modifications to the cash basis of accounting used by the Province of Ontario. This Province has since changed its basis of accounting.

> **Reporting entity**
> The financial statements, prepared using the concept of a Consolidated Revenue Fund, are designed to provide an accounting of the financial resources appropriated by the Ontario Legislature. The accounting policies and practices followed by the Province are designed to report the financial transactions of Government ministries as Consolidated Revenue Fund cash inflows and outflows. Activities of agencies of Government of Ontario are reported only to the extent to which their operations have been financed from, or have contributed to, the Consolidated Revenue Fund.
>
> **Basis of accounting**
> The cash basis of accounting used by the Province is modified to allow for an additional thirty days to pay for goods and services received during the fiscal year just ended and for certain non-cash transactions. Cash inflows, however, are closed at March 31 for cash received.
>
> Capital costs are charged to expenditure when paid.

Example 9.1
Public Accounts of Ontario, 1992 –93
Notes to the Financial Statements, page 5

The Specified Period – Recognition Criteria for Receipts

222. The main recognition criterion for receipts during the specified period is that the receipt must have originated in the preceding period. Across jurisdictions, there is no uniformity in the application of this phrase. Some governments consider that all receipts received during the specified period have originated in the preceding period. Other governments recognize only some of these receipts. The examples given below illustrate the application of the specified period to receipts. In any event, it is desirable that the criteria used by a government be consistently applied from year to year and be disclosed in the Statement of Accounting Policies.

223. Although preparers would need to exercise their own judgment, the following types of receipts received during the specified period would generally be recognized as a receipt of the prior reporting period:

- taxation receipts where the taxation was imposed on a transaction which took place or where the taxation was due to be paid in the preceding reporting period;
- receipts from the sale of goods and services where the invoice had been issued prior to the end of the preceding reporting period;
- grants, contributions and donations which were due to be received prior to the end of the preceding reporting period;
- interest receipts where the interest was earned on balances held in the preceding reporting period;
- proceeds from sales of non-current assets where the transaction has been completed (contract signed and delivery completed) and payment was due prior to the end of the preceding reporting period;
- loans made by a government which are due to be repaid at balance date but which are repaid during the specified period;
- borrowings where the loan agreement had been completed (signed) prior to the end of the preceding reporting period; and
- custodial receipts which were due prior to the end of the preceding reporting period.

224. In order to ensure that cash receipts are accounted for once only, cash receipts in the current period which are recorded as receipts of the preceding accounting period are not also recognized as receipts of the current period.

The Specified Period – Recognition Criteria for Payments

225. The consistent application and disclosure of accounting policies is also relevant to payments made during the specified period. The specified period varies between jurisdictions, but a specified period of one month is fairly common. The criteria used to determine whether payments made during the specified period are recognized in the preceding period also vary between jurisdictions.

226. The overriding criterion may be that an amount must have been appropriated in the preceding financial year in order to be recognized as a payment of that year. The following examples illustrate the application of the specified period to payments. Payments made in the specified period under the following conditions would be treated as payments of the prior reporting period:

- taxation refunds made during the specified period where the refund had been approved prior to the end of the preceding reporting period;
- the purchase of goods or services where both the invoice and the goods or services had been received prior to the end of the preceding reporting period;
- government transfers (e.g., for welfare payments) where the payment related to the preceding reporting period;
- other grants, contributions and donations made where the item had been due for payment in the preceding reporting period;
- the acquisition or construction of assets where the purchase contract had been signed or invoice received and the assets or goods and services relating to construction had been received prior to the end of the preceding reporting period;
- interest payments relating to the use of borrowed funds during the preceding reporting period;
- the repayment of any portion of debt due to be repaid at the end of the preceding reporting period;

- investments in other entities (both loans and capital injections) where the agreement to provide the investment occurred during the preceding reporting period, and where the actual payment was due in the preceding reporting period; and
- custodial payments where the amount paid had been due in the preceding reporting period.

Specified Period – Benefits and Limitations

227. The benefits of this modification to the cash basis of accounting is that it has a broader measurement focus. Instead of being on cash balances, the focus is on current financial resources (cash plus near-cash balances, with near cash being amounts recognized in the specified period). The recognition of certain receipts and payments during the specified period means that there is some information on receivables and payables. Although these are not recognized as assets and liabilities, the collection of information on the amounts and types of near-cash equivalents will allow the reporting entity to better control these amounts. One reason why a government may adopt this modification is that it allows amounts appropriated for a particular financial year to be recognized as a payment of that year, despite the fact that payment is delayed until the specified period. However, it does not recognize payments which occur beyond the specified period.

PART III – ACCRUAL BASIS

CHAPTER 10

ACCRUAL BASIS – DESCRIPTION

Introduction

228. This Part aims to assist those governments currently applying, or considering adopting, accrual accounting. Because accrual accounting provides more comprehensive information than that provided under cash accounting and is more complex than cash accounting, there are a wider range of accounting issues that governments must address. These issues concern the recognition of assets and liabilities and the associated revenues and expenses. Some of these issues are almost identical to the issues faced in the private sector, for example the recognition of assets such as office equipment and motor vehicles, and the accounting treatment required for borrowings. Other issues such as the point of recognition for taxation revenues and welfare payments have not been addressed by the private sector. Where possible this Study makes use of the extensive research and literature which has already been developed within the private sector. The Study explores some of the areas where entities using accrual accounting need to develop specific accounting policies. It is not prescriptive. The PSC is also developing a core set of International Public Sector Accounting Standards (IPSASs) which set out recommended practice in relation to accounting treatments and disclosures.

229. In the main this Study refers to the International Accounting Standards (IASs) issued by the International Accounting Standards Committee (IASC) as an authoritative and appropriate source of private sector accounting standards. The IASs provide a comprehensive and well developed framework for resolution of such issues. The PSC has decided to use IASs as the starting point for IPSASs in an effort to be consistent, where possible, with existing international guidance, as well as avoiding the need to "reinvent the wheel" for the public sector. Although the public sector context is different, the fundamental objectives of financial reporting are the same across both public and private sectors. Using IASs as the basis of the PSC Standards will lead to a consistent approach to similar issues within public and private sector standards. The IPSASs will be developed by reviewing existing IASs, and adapting them as appropriate for the public sector. In relation to issues which are specific to governments (such as the recognition of taxation revenues), or where the relative size of the assets and liabilities concerned is much greater than in the private sector (such as infrastructure assets), this Part of the Study attempts to apply the relevant principles from the IASC framework and draws upon literature from international governments.

230. This Chapter discusses the elements recognized under the accrual basis of accounting. Financial reports portray the effects of transactions and other events by grouping them into broad classes according to their economic characteristics. These broad classes are termed elements. The accrual basis recognizes transactions and events when they occur rather than when cash is paid or received. The elements recognized under the accrual basis of accounting are assets, liabilities, net assets/equity, revenues, and expenses. Although the focus of accrual accounting is on all assets, not just cash, accrual accounting records contain complete information on cash flows and a Statement of Cash Flows is an integral part of accrual financial statements.

231. The accrual basis provides users with information about such matters as the resources controlled by the entity, the cost of its operations (or the cost of providing services) and other information useful in assessing financial position and changes in it, and in assessing whether the reporting entity is operating economically and efficiently (PSC Study 1 *Financial Reporting by National Governments*, paragraph .089). The measurement focus under accrual accounting is on economic resources and changes therein (PSC Study 2 *Elements of the Financial Statements of National Governments*, paragraph 044). Two main measurement bases are used under accrual accounting — historical cost and current cost. The interpretation of information prepared under accrual accounting will differ according to which measurement base(s) has been used in the preparation of the financial statements. Measurement bases are discussed in further detail in Chapter 18.

Assets

232. The accrual basis requires recognition of all assets which meet the generally accepted definition of an asset and the recognition criteria. Assets include cash, accounts receivable, accrued revenues, physical assets and other long-term assets. PSC Study 5 *Definition and Recognition of Assets* discusses the application of the asset definition in the IASC Framework for the Preparation and Presentation of Financial Statements to assets held by governments.

233. Chapter 12 provides a detailed discussion of the definition of assets, the various types of assets which may be recognized by governments, and some asset recognition issues.

Liabilities

234. The accrual basis recognizes liabilities relating to goods and services acquired up to the end of the reporting period, including accrued salaries and wages, accrued vested vacation pay and other accrued compensated absences. In addition, all borrowings and debt are recognized, as are transfer payments due, even where no value is received directly in return. Therefore, the financial statements would report accounts payable, accrued liabilities, transfer payments payable, debt and other borrowings.

235. The issues associated with accounting for and reporting liabilities in the public sector have been addressed in PSC Study 6 *Accounting for and Reporting Liabilities*, and are discussed further in Chapter 13.

Net Assets/Equity

236. Under the accrual basis of accounting, the financial statements will include a Statement of Financial Position which discloses information about assets and liabilities. Where assets and liabilities are not equal, a residual figure for net assets/equity will be reported. Where this figure is positive it can be interpreted as the net resources that may be applied for the provision of goods and services in the future, and therefore the community's investment in the reporting entity. Where the figure is negative it may be viewed as the amount of future taxation or other revenues which are already committed to paying off debt and other liabilities. Net assets/equity can comprise some or all of the following components:

- contributed capital;
- accumulated surpluses and deficits; and
- reserves (for example revaluation reserve; foreign currency translation reserve).

237. Where any of those components is individually material, it is usually disclosed separately.

Revenues

238. Revenues reflect the amounts due or earned during the year, whether collected or not. Revenues which have been recognized but not received are accounted for as an asset: revenue receivable.

239. Revenues include:

- taxes;
- revenues from the sale of goods and services; and
- net gains on the sale of assets.

240. By comparison with the cash basis of accounting revenues do not include financing inflows, or gross proceeds from sales of assets. Nor do revenues include custodial flows where the government is merely acting as an agent of another party or where the government is acting as trustee. Custodial or agency receipts are discussed further in Chapter 14.

241. The definition of revenues and its application to revenues in the public sector have previously been discussed in PSC Study 9 *Definition and Recognition of Revenues*, and are covered in Chapter 14 of this Study.

Expenses

242. Expenses are the costs incurred during the period related to the acquisition of goods and services, whether or not payment has been made. They include amounts transferred or payable to eligible beneficiaries consistent with government policies (transfer payments). Expenses may also include the payment of grants, contributions and donations which are non-repayable. Expenses do not include repayment of debt or contributed capital.

243. Expenses include the costs associated with:

- the purchase of goods and services;
- the depreciation of physical assets;
- the net loss on sale of assets;
- non-reciprocal government transfers; and
- non-repayable grants, contributions and donations.

244. In contrast with the cash basis of accounting expenses do not include payments associated with the acquisition or construction of physical assets, the repayment of debt or investments in other entities (both loans and capital injections). Nor do expenses include custodial flows where the government is merely acting as an agent of another party or where the government is acting as trustee. Custodial or agency flows are discussed further in Chapter 14.

245. The cost of physical assets is recognized as an asset at the time of purchase. This cost is then allocated as depreciation over the life of the asset, with the exception of most land.

246. The definition of expenses and its application to expenses in the public sector have previously been discussed in PSC Study 10 *Definition and Recognition of Expenses/Expenditures*, and are covered in Chapter 15 of this Study.

Recognition Criteria

247. The IASC Framework for the Preparation and Presentation of Financial Statements describes the process of recognizing financial elements, and establishes recognition criteria as follows:

> *Recognition is the process of incorporating in the balance sheet or income statement an item that meets the definition of an element and satisfies the criteria for recognition set out in paragraph 83. It involves the depiction of the item in words and by a monetary amount and the inclusion of that amount in the balance sheet or income statement totals. Items that satisfy the recognition criteria should be recognised in the balance sheet or income statement. The failure to recognise such items is not rectified by disclosure of the accounting policies used, nor by notes or explanatory material.*
>
> *An item that meets the definition of an element should be recognised if:*
> (a) *it is probable that any future economic benefit associated with the item will flow to or from the enterprise; and*
> *(b) the item has a cost or value that can be measured with reliability.* (paragraphs 82-83)

248. These criteria have also been adopted in a number of conceptual frameworks internationally. “Probable” means that the chance of an event occurring is more likely than less likely and “measurable” means reasonably estimable.

249. It is important to consider the interrelationship between elements. An item which meets the definition and the criteria for recognition of a particular element will automatically result in both the recognition of one element, and a change in another element. For example, the purchase of an asset may result in the reduction of another asset, or the recognition of a revenue or liability.

Reporting Model

250. The financial statement reporting model frequently associated with accrual accounting is based on the preparation of a Statement of Financial Position (also known as a Balance Sheet or Statement of Assets and Liabilities), a Statement of Financial Performance (also known as a Statement of Revenues and Expenses or an Income Statement), and a Statement of Cash Flows. The Statement of Cash Flows

provides a summary of cash receipts and cash payments during the year, classified under various sub-headings. Notes to these statements or supplementary schedules may also report summary information about such matters as compliance with spending mandates and relevant performance indicators.

CHAPTER 11

ACCRUAL BASIS – BENEFITS AND LIMITATIONS

Introduction

251. This section examines the benefits which both internal and external users of governmental financial reports may obtain when these reports are prepared using accrual accounting. In previous PSC publications the term full accrual has been used. In this Study the term accrual is used to mean the same as full accrual. It is acknowledged that internal users will also have access to more detailed information and a wider range of information than that provided in governmental financial reports.

252. Governmental financial reports have both an accountability role and an informative role. In an accrual context they provide information which enables users to:

- assess the performance, financial position and cash flows of the entity;
- assess the entity's compliance with accrual budgets; and
- make decisions about providing resources to, or doing business with, the entity.

253. Accrual accounting provides users with information which:

- allows the government to demonstrate accountability for its use of all resources;
- allows the government to demonstrate accountability for its management of all assets and liabilities recognized in the financial statements;
- shows how the government financed its activities and met its cash requirements;
- allows users to evaluate the government's ongoing ability to finance its activities and to meet its liabilities and commitments;
- shows the financial position of the government and changes in financial position; and
- is useful in evaluating the government's performance in terms of its service costs, efficiency and accomplishments.

Financial Position

254. Governments require information on the overall financial position and detailed information on the current stock of assets and liabilities to:

- make decisions about the feasibility of the services they wish to provide;
- demonstrate accountability to the public for their management of assets and liabilities;
- plan for future funding requirements of asset maintenance and replacement;
- plan for the repayment of, or satisfaction of, existing liabilities; and
- manage their cash position and financing requirements.

255. Governments need to be able to assess both the impact of past decisions on the current financial position, and the impact of current decisions on the future financial position. This information is only available when details of all assets and liabilities are recognized.

256. Managers of government organizations are often entrusted with the management of significant assets and liabilities. Managers therefore need to determine the most efficient way of using the assets, controlling the liabilities, and reporting on their stewardship.

257. Accrual accounting requires organizations to maintain complete records of assets and liabilities. The discipline of collecting this information can be as useful as the final figures. In the absence of accrual accounting many organizations do not have complete asset registers, or complete details of liabilities. For example, when governments first start to compile asset registers there may be insufficient information to determine ownership of some assets. Complete information on assets and liabilities, including that relating to ownership and control, is a precursor to proper management of assets and liabilities.

Assets

258. Information on assets is required for three main reasons:

- to provide for the efficient management of assets;
- to help managers to deliver a better service; and
- to save money both through the efficient use of assets and through the disposal of surplus assets.

259. The management of public assets requires sufficient records to identify the existence of assets and the costs of holding and operating these assets. The recognition of assets in a Statement of Financial Position requires that governments undergo a rigorous process of identifying all assets, verifying ownership and placing a value on assets. While the adoption of accrual accounting is not a necessary prerequisite for this to occur, it is often the driving factor. Financial reporting deadlines require that this process be completed within a given timeframe and the review of this information by an external auditor provides assurance as to its reliability.

260. Better information regarding assets leads to better decisions on maintenance, disposal of surplus assets and replacement of decayed or obsolete assets. These decisions are particularly important in relation to major physical assets such as infrastructure assets, the replacement of which could strain the financial capacity of a government.

Current Assets

261. Significant funds may be tied up in current, or short-term, assets such as receivables and inventories. The net amount invested in current assets and current liabilities may also be referred to as working capital. Funds tied up in working capital are not available for other uses such as increasing levels of activity in a program or for debt reduction. When information on the composition and level of working capital is available, managers are able to manage working capital more efficiently.

Physical Assets

262. Accrual accounting and the compilation of information within an asset register allow the identification of the ongoing costs, such as depreciation and maintenance, of owning and operating assets. Information on these costs is needed to measure the total cost of goods and services produced. As discussed later in this Chapter, both governments as a whole and individual managers need to know the total cost of goods and services in order to determine which goods and services to provide, and the most efficient way of providing those goods and services. Both summarized and detailed asset information is useful. Total asset figures show how much government funding is tied up in asset holdings. This allows the government to make informed decisions when considering capital investment acquisitions or disposals. Detailed asset information is more likely to be of use to those Ministers or managers with responsibilities for particular government departments or agencies. The asset register is the asset database which provides the basis for the figures in the financial statements. It includes information on asset purchase prices, asset condition, expected lives. It may also include information on current replacement cost.

263. Records of maintenance costs allow managers to budget for these costs and to determine the best time to replace assets. Information on deferred maintenance is also useful as it will consume future resources and may affect the reliability of an asset. Detailed information on deferred maintenance is generally collated and used by managers who have responsibility for particular assets. It is not normally disclosed in the external financial statements unless the amount of deferred maintenance is considered material for the users of the financial statements. Appropriate selection and application of depreciation methods and regular reviews for indications of impairment ensure that the information in the financial statements is sufficient for external users.

264. Information on loss or damage through theft, accident or natural disaster is more easily identified under accrual accounting and is essential for management of these risks. Once organizations have access to information on such losses, they are then able to manage these risks, either through external insurance or self insurance.

265. By recognizing the decline in asset values through use and obsolescence, managers are encouraged to consider the costs of holding and using fixed assets. Managers are able to manage those costs, and to make informed decisions such as lease or buy decisions.

266. Citizens also rely on governments to manage natural resources and Government Business Enterprises (GBEs) and to make decisions regarding their retention or disposal. Financial reporting of assets is required to assist users to understand the current and possible future effects of such transactions. For example, the disposal of a GBE for cash consideration (at more than book value) would increase the current cash resources of the government. However, it would also reduce possible future cash flows from dividends. Information on the level of assets and changes in assets provides information on whether the resources necessary to enable continuity of services have grown, declined or have been maintained.

Liabilities

267. The main benefit of information on all liabilities is that it forces governments to acknowledge and plan for the payment of liabilities which may have accumulated over time, not just borrowings. Historically, governments have tended to focus on their outstanding debt as a primary measure of the government's liabilities or indebtedness, particularly in formulating or assessing economic policy. Liabilities can also arise as a result of the acquisition of assets or services. All liabilities, regardless of their nature, must be paid for by the government at some point in the future. Liabilities can be substantial, and just as real as market borrowing. Information that reports the extent of the financial obligations and exposure to potential liabilities is useful because it bears directly on future revenue requirements and on a government's ability to pay its obligations and finance its operations. Liabilities other than borrowings include accounts payable, accrued expenses and other long-term liabilities such as pension liabilities.

268. Reporting on a government's total liabilities at reporting date is necessary to ensure complete reporting of transactions and events, and to understand and assess demands on resources. When used with other available financial data, adequate information about the nature and terms of liabilities facilitates assessments of such matters as debt management and exposure to foreign exchange liabilities.

269. Once liabilities are recorded and reported, it is possible to allocate responsibility for their management. If liabilities are not reported, they are less likely to be taken into account when making decisions, and governments cannot exercise proper stewardship. Without full and complete information about their liabilities, contingencies and commitments, governments and other users of government financial reports cannot make realistic assessments about the government's financial condition. The risk of making poor decisions is much greater if legislators, government managers, and their advisers have incomplete or fragmented information that fails to show all that a government owes.

270. Reporting liabilities is important for both accountability and decision making. In addition to the cost of future services, governments have to meet past debts as they come due. Governments must be able to estimate realistically whether they can continue to afford the quality and quantity of services they deliver, and whether they can afford new programs and services. Governments, as well as analysts and other users of government financial reports, cannot make sound decisions on those matters without an understanding of the full nature and extent of all the government's liabilities.

271. Information on potential liabilities is also of interest to external users. Information on contingent liabilities helps users to understand the government's exposure to risk. Information about a government's commitments gives an appreciation of the extent to which the government's resources are already committed to meet certain obligations in the future. Information about contingencies and commitments also allows management to monitor these items.

Net Assets/Equity

272. Financial statements prepared under accrual accounting show the reporting entity's net assets/equity (assets less liabilities). Clear information about net assets/equity helps the government to manage debt levels, and to monitor the level of debt in relation to other liabilities and asset holdings.

273. Information on net assets/equity enables governments to make better decisions regarding the extent of

government activity and the financing of that activity. Current activities may be financed from current revenues. Alternatively to the extent that certain assets may be sold, activities may be financed by a reduction in net assets/equity. Net assets/equity may be reduced by:

- the consumption of existing assets;
- asset sales if sale proceeds are then used to finance current expenditure;
- increased borrowing; and
- the incurrence of other additional liabilities (e.g., unfunded superannuation/pension obligations).

274. Most assets (e.g., schools, hospitals and roads) held by governments are held for the purpose of delivering services to the community and are not immediately available for sale. However, governments do make choices about the level of such services (and by implication the assets that are required), the location of such assets, and in some cases the ownership arrangements for these assets. For example, governments may enter into private finance arrangements whereby a private sector entity takes over existing assets or constructs new assets and has a service contract with the government. Where current activities are funded out of net assets/equity, this will affect a government's ability to meet its liabilities and commitments in the future.

275. Accrual accounting highlights the impact of financing decisions on net assets/equity and may lead governments to take a longer term view when making financing decisions. Decisions which have long-term financial implications can be evaluated in terms of both their current and future impacts. For example, the longer term financial impact on net assets/equity of changing levels of, or entitlements to, government benefits can be evaluated.

276. Information on net assets/equity also means that governments may be held accountable for the financial impact of their decisions on both current and future net assets/equity.

277. Information on levels of net assets/equity in various government agencies may be used to introduce a system of capital charging, whereby government agencies are required to pay a sum to the Government for their use of capital, thereby making the agencies more aware of the costs associated with tying up scarce resources in assets. Various arrangements exist in different countries. New Zealand has a system of capital charging whereby central government departments are charged around 10% (reviewed annually) on the balance of net assets each year. In the Swedish Central Government, a system whereby interest is charged on both the acquisition of fixed assets (through internal loans in the National Debt Office) and for current assets or temporary cash deficits (through interest bearing accounts with the National Debt Office) has been in use for five years. The United Kingdom plans to introduce capital charging to government departments and believes that this will "focus attention throughout the financial planning cycle on the cost of holding assets as well as on new capital spending" *(Better Accounting for Taxpayer's Money – the Governments Proposals*, July 1995, paragraph 1.21). All these systems are designed to make agencies aware of the fact that funds provided to finance assets have a cost and to provide an incentive for agencies to minimize the amount of capital funding they require. Capital charges ensure that proposals for new spending are considered in light of the existing asset base and whether the purchase can be funded from that base.

Net Assets/Equity in a Government Accounting Context

278. Net assets/equity is the term given to the balance of assets less liabilities. The assets and liabilities recognized in the financial statements are restricted to those elements that meet the definitions and satisfy the associated recognition criteria. For government reporting entities there may be significant assets and liabilities that do not satisfy the recognition criteria and are therefore not recognized in the Statement of Financial Position (e.g., the power to tax and the present value of future payments under welfare schemes).

279. Accordingly, it can be argued that the figure for net assets/equity in governmental accrual-based financial statements is not a complete measure of expected future cash flows. Although this may be the case, it is nonetheless a highly significant indicator of government financial condition. Moreover, by supplementing the accounting measure of net assets/equity by disclosures on the (cash) effects of future transactions expected under current or proposed policy settings, it is possible to enhance the decision-usefulness of the figure for reported net assets/equity.

280. The various statements used to show movements in net assets/equity are discussed in Chapter 16.

Financial Performance

281. Information on revenues and expenses is important in assisting governments and other users to assess the financial condition and performance of governments. Information on revenues is essential for decision making at the whole of government level (e.g., in assessing the impact of taxation and other revenues on the government's fiscal position and in assessing the need for borrowing in the long-term). Information about expenses is important for sound decision making about the financing of future services and resource allocation. Accrual accounting allows for the measurement of the total cost of providing services on an aggregated basis, and also allows for more accurate cost measurement of specific programs and activities. It includes all revenue and expense flows, both cash and non-cash. Comparing revenues with expenses helps users to assess inter-period net assets/equity (i.e., whether current revenues are sufficient to cover the costs of programs and services provided in the current period).

282. In addition to providing information to external users, governments need information about expenses in order to assess their revenue requirements, the sustainability of their programs and their flexibility. At a more detailed level, governments need information on the cost of each good or service provided, both to decide whether to continue with that activity and also to allow for proper budgeting and control of activities.

283. Governments are usually elected on a broad range of policy issues. At some point a government must translate its general policies into specific decisions regarding the provision of goods and services through activities and programs, the use of transfer payments or legislative measures. Ideally these resource allocation decisions would be based on an assessment of the costs and benefits of each proposal, and the relative importance of competing proposals. By providing improved financial information to users, accrual accounting has the potential to alter resource allocation to, and within, the public sector. This may occur directly or via voting behavior.

284. Although the wider social costs and benefits of proposals can be difficult to assess, the specific cost of pursuing policy objectives through the provision of services by a particular government organization can be identified. The costs include not only the cost of goods and services produced or purchased and paid for during the accounting period but also the cost of using long-lived assets and other non-cash costs.

285. Governments need to know the total costs of their activities so that they can decide:

- which policy objectives to pursue;
- how best to meet these policy objectives;
- whether to fund the production of services within government sub-entities, or whether to purchase goods and services directly from non-government organizations; and
- whether user fees cover the costs associated with a service.

286. Governments at various levels make decisions regarding both the type and level of government services, and the best way of providing those services. They therefore need information about the cost of providing these services in order to make rational decisions about the viability and desirability of specific programs and activities, and to assess the performance of the government sub-entities responsible for the provision of these services through activities and programs.

287. Some jurisdictions have provided incentives for greater efficiency within the public sector by creating competition between private and public sector suppliers. Effectively, the government is facing a make or buy decision. Comparisons between public sector and private sector suppliers can only take place when information on the full cost of both options is available.

288. Once the government has determined the activities and programs it would like its sub-entities to pursue, it then needs financial information to ensure that the sub-entities are delivering the specified services, and delivering them within agreed budgets. Accrual accounting can be used to provide this information. The same information, at a more detailed level, can also be used within sub-entities for the management of activity and program costs.

289. Once costs are identified it is then possible to delegate the authority to manage those costs. An accounting system can be established to produce both external financial reports and internal management reports. The level of detail in internal management reports and the extent to which authority to manage costs is delegated is determined by each reporting entity.

290. Accrual accounting allows an organization to record the total costs, including depreciation of physical assets, of carrying out specific activities. The recognition of all costs, regardless of whether a cash transaction has taken place, generally provides more accurate measures of operating costs than other accounting bases. By accruing accounts receivable and accounts payable it spreads the impact of the actual timing of cash flows on reported results. By recognizing depreciation as an expense it removes the large cash flow impact of asset purchases by allowing the cost of the asset to be recognized each year that it is in use. It is the only basis of accounting which recognizes as an expense the cost of allowing the current stock or value of physical assets to decline.

291. Accrual accounting also allows an organization to recognize all employee-related costs, even if the cash flows associated with these costs do not arise until a future accounting period. For example, decisions to offer government employees future pension benefits instead of current salary or other current benefits may shift the cash flows to future years. Accrual accounting means that the actual cost will be recognized in the year in which it occurs. The clear identification and reporting of the actual costs of remunerating employees allows managers to compare the cost of various types of employment or remuneration options.

292. Managers within sub-entities need financial information to determine the most efficient way of producing their outputs and of managing the resources over which they have been delegated authority. This may involve choices regarding the location of activities; in-house provision or the use of external contractors; renting or leasing buildings and equipment. Managers also need to monitor actual costs against budgeted costs and actual cash flows against budgeted cash flows. They need regular financial reports for internal monitoring of actual spending against budget, and reporting to governments and the electorate.

293. Government sub-entities supplying goods and services to other parties also need accurate and complete cost information for pricing purposes. Accrual accounting helps to identify the effective government subsidy where goods and services are supplied at less than cost. Explicit identification of such subsidies allows governments to examine the level and existence of such subsidies in the light of competing spending proposals.

Cash Flows

294. Reporting of cash flows is an important and integral part of accrual accounting. A Statement of Cash Flows is one of the main external statements prepared under this basis. Accrual accounting does not diminish the information available under the cash basis of accounting and may actually lead to better information on cash flows, and therefore to better cash management. Because accrual accounting accounts for all revenues and expenses, whether or not they involve cash flows in the current reporting period, more complete and systematic information on future cash flows is recorded. For example, under accrual accounting detailed records of accounts receivable, accounts payable, long term liabilities and the current state of physical assets are recorded. This additional information may allow more accurate cash budgets to be prepared. Under accrual accounting managers are usually responsible for the management of not only revenues and expenses but also cash flows.

295. A United Kingdom paper commented on the use of accrual accounting (which it refers to as resource accounting) in managing cash flows as follows:

> *Resource accounting will require a more systematic approach to recording debtors and creditors, which will allow departments to plan and control cash flow more effectively than under a purely cash-based accounting system. At present, cash flow is mostly controlled at the end of the payment process; more comprehensive information on debtors and creditors should help departments to forecast cash flow difficulties, and to take remedial action well in advance (for example by rescheduling purchases).* (*Better Accounting for the Taxpayer's Money: Resource Accounting and Budgeting in Government, A Consultation Paper, July 1994,* paragraph 2.20)

Benefits of Accrual Accounting in Practice

296. Although relatively few governments currently use accrual accounting, there is a growing trend towards accrual accounting as part of wider financial management reforms (Scott, 1996). At present, governments using accrual accounting include:

- Australia (state, federal and local government);
- Canada (target date for reporting on a full accrual basis at whole of government level is fiscal year 2001-2002);
- Finland (government agencies and whole of government);
- France (local government);
- Germany (some government organizations);
- Iceland (agencies and whole of government);
- Ireland (pilot project for selected government departments);
- Italy (local government);
- Malaysia (local government);
- Netherlands (agencies and local government);
- New Zealand (national and local government);
- Sweden (central government agencies and local government);
- Switzerland (local government);
- Tanzania (local government);
- United Kingdom (all local authorities, executive agencies and health service trusts); and
- United States (federal government).

297. The federal government of Malaysia is considering introducing the accrual basis. In the Netherlands some Ministries currently using cash accounting are considering the introduction of accrual accounting. The central government in Tanzania, which currently uses cash accounting, intends to move to accrual accounting. The benefits anticipated or actually experienced by some of the countries using or intending to use accrual accounting are discussed below.

Benefits – New South Wales, Australia

298. New South Wales was the first jurisdiction in Australia to publish accrual-based financial reports on both the State Public Sector and the Budget Sector. A number of other jurisdictions have since followed this lead. In common with New Zealand, New South Wales has introduced legislation — the General Government Debt Elimination Act 1996 — which sets out fiscal principles and targets. These principles and targets are "directed at achieving a strong, sustainable budget position, a stable tax regime, a gradual reduction of debt and service delivery costs as well as the enhancement of the net worth of the General Government Sector". (Public Accounts of the NSW Budget Sector 1995–96)

299. The principles and targets include references to operating surpluses, levels of net debt and net assets/equity, the funding of superannuation/pension liabilities, the maintenance of physical assets, constraints on the relative growth of costs, the management of financial risks and the level of taxes. The use of accrual accounting has provided information on each of these targets.

300. The State of New South Wales reports on each of these fiscal targets in its State and Public Accounts. Two examples of such reporting are given below.

> *Commonwealth Grants increased from $8,348 million in 1995–1996 to $8,480 million in 1996–97, i.e. 1.6%. However, after adjusting for an increase in CPI of 1.4% and population growth, Commonwealth Grants on a per capita basis decreased by 1.1%. This is in line with* ***Fiscal Principle No.5 – Net Cost of Services*** *which is to keep growth in net cost of services and outlays below the growth in inflation and population (i.e. zero growth in per capita terms).* (Consolidated Financial Statements of the NSW Public Sector 1996–97, page 9)
>
> *Net assets of the Budget Sector were $22,953 million at 30 June 1997, an increase of 20.2% ($3,858 million) on the level at 30 June 1996. This was due to an increase in total assets of $3,775 million and a $83 million reduction in total liabilities. The increase in Budget Sector net assets is in*

accordance with Fiscal Principle No. 2, which is to maintain or increase net worth (ie net assets) of the General Government sector in real terms. (Consolidated Financial Statements of the NSW Public Sector 1996–97, page 14)

Benefits – New Zealand

301. New Zealand has experienced the benefits of accrual accounting, both at the whole of government level in terms of financial management and at a sub-entity level in terms of better management information and better performance.

302. New Zealand was facing an economic crisis prior to its financial management reforms.

> *In the late 1980s New Zealand faced a deteriorating fiscal situation. The government was concerned that large deficits would lead to a sharp rise in public debt, and damage prospects for growth and incomes. If interest rates rose and exchange rates fell, there could have been concerns about New Zealand's ability to service its overseas debt. The root cause of the persistent fiscal problem was the steady rise in expenditure as a percentage of Gross Domestic Product. The government was advised that the solution for improved economic performance was to contain government spending and reduce pressures on the tax system.* (The Treasury 1990)

303. Concerns about its fiscal position and economic performance led the New Zealand Government to introduce a series of reforms, including accrual accounting. The requirement for government departments and the whole of government to use accrual accounting was included in the Public Finance Act 1989. A further reform occurred in 1994 when the Fiscal Responsibility Act established requirements for the government to report on its forecast fiscal position using generally accepted accounting practice (GAAP) including disclosure of expenses, revenues, the surplus (deficit), debt, and net worth. The government is also required to set targets for its fiscal objectives. The outcome of these reforms is described below.

> *A series of reforms, including accrual accounting, were instituted in the central government sector in 1989. The results have been startling. In each of the years 1992-1994, New Zealand's system of government was rated as being the most effective performer among the 22 OECD countries (World Competitiveness Report). On an accrual basis, New Zealand government expenditures over the period 1990 to 1995 remained broadly stable in nominal terms, implying a sharp reduction in expenditure as a percentage of GDP.* (Cangiano 1996, page 24)

304. Over the period 1985-94, the fiscal balance shifted from a deficit of about 9% of GDP to a surplus of 3%, while gross public debt declined substantially (Cangiano 1996).

305. Accrual accounting also held advantages for Ministers making resource allocation decisions.

> *The new focus on outputs brought about by the (Public Finance) Act became especially apparent. The new focus on outputs brought about by the Act meant ministers had genuinely meaningful information about the services produced by their departments and were in a position to make informed trade-offs between competing priorities.* (Richardson 1995, page 104)

306. The benefits of accrual accounting were not confined to the upper levels of government. A study of senior public service managers rated accrual accounting as "the undisputed success story" and ranked it as more successful than all other reforms (Stace and Norman 1995).

307. Participants in the Stace and Norman study generally agreed that:

- *(there is) "better financial reporting in my organization" and "at the government level".*
- *"The clear separation of capital from operational expenditure allows more rational decision making in the financial field."*
- *The more open financial reporting allows the public to better "assess the financial performance and position of government."*
- *(there is) "greater financial discipline and checks on unnecessary activity"(as a result of user pays).* (Stace and Norman 1995, page 6)

308. As mentioned earlier in this Chapter, the clear identification of costs means that authority to manage those costs may be delegated. The benefits of this delegation have also been seen in New Zealand. Cangiano (1996) reports that since the introduction of the financial management reforms in New Zealand, there has been a widespread tendency to underspend budgeted allocations. This is attributable to an increased capacity on the part of departments and agencies to manage their own budgets and resources independently.

Benefits – Switzerland

309. In Switzerland, accrual accounting is widely used at a cantonal level but not yet at the federal level. In 1978 the Conference of Cantonal Finance Ministers published a manual on the so-called "New Accounting Model" (now referred to as "Harmonized Accounting Model"), recommending that the cantons should introduce this system of double-entry accounting as soon as possible. Today, nearly all the cantons and municipalities have introduced the accrual accounting model: only the Confederation is still based on the principle of cash or modified cash accounting. This widespread use of the model allows sensible financial comparisons not least in the sense of benchmarking and is the starting point for new cost information systems.

310. The model consists of asset accounting and profit and loss accounting and is therefore largely modeled on private sector accounting. The profit and loss account is subdivided into a current account and a capital account which is a specialty of the public sector not commonly used in the private sector, The capital account contains all expenses and receipts that are capital in character and which exceed SFr 100,000, and the corresponding receipts. Their balance, net investment, is transferred to the asset account as capital appreciation on the closing of accounts and then, in the following year, written off with the other assets according to standard rates. Expenses below SFr 100,000 are not transferred to the asset account; they pass directly to the profit and loss account and are therefore entirely written off in the same year. Whereas financial assets are free assets, administrative assets are operating assets.

Benefits – United Kingdom

311. The Government introduced accrual accounting (referred to as resource accounting) across government during 1998. The first year for which resource accounts will be published will be 1999–2000. Resource budgeting will be implemented in 2000 for the plans for 2001–2002 onwards. The perceived benefits of resource accounting (as described in the White Paper on resource Budgeting and Accounting in Government) are as follows:

> *After consultation and further work, the Government has concluded that a fully resource based system of public expenditure planning and control would achieve improved management and value for money by the taxpayer by:*
>
> - *making decision makers focus more on resources consumed and not just on cash spent;*
> - *treating capital and current expenditure in a way which better reflects their different economic significance; and*
> - *encouraging a greater emphasis on outputs and the achievement of aims and objectives.*
>
> (*Better Accounting for Taxpayer's Money – the Governments Proposals*, July 1995, paragraph 1.1)

Benefits – United States

312. The United States (U.S.) federal government prepares accrual consolidated financial statements that have been subjected to an audit by the Comptroller General of the United States. The 1997 Consolidated Financial Statements of the United States Government were the first such set of statements prepared. These statements were based on, although not in full compliance with, the accounting standards created by the Federal Accounting Standards Advisory Board (FASAB). This section outlines the background to FASAB accounting standards and the move towards accrual accounting in the U.S..

313. During the late 1980s and into the 1990s, several audits by the General Accounting Office identified sloppy record keeping, inaccurate financial reports, and a basic lack of internal control in many federal agencies. This situation, compounded by financial management scandals, aroused the Congress to deal with the poor state of federal financial management. The Chief Financial Officers Act of 1990 was the first of several pieces of legislation aimed at improving financial management and included a

requirement for audit of several pilot agencies. The success of these pilots led to an expansion of these requirements in 1994 to require all major agencies of the federal government's executive branch to have agency-wide financial statement audits beginning with fiscal year 1996 and consolidated federal financial statement audits for the executive branch of the United States Government beginning with fiscal year 1997.

314. Agency management and congressional leaders have found that good financial information has become critical to making informed decisions, especially as efforts to bring down the budget deficit have increasingly constrained budgetary resources. This increased emphasis on good financial information, in turn, led to a major effort to develop a new set of accounting standards. The FASAB was created to consider and recommend accounting standards and principles for the Federal Government to improve the usefulness of federal financial reports.

315. The resulting federal accounting standards are based on a set of objectives centered around providing information on budget integrity, operating performance, stewardship, and systems and controls. Previous standards based on accrual accounting standards for commercial enterprises were judged to be inadequate. The current set of U.S. federal standards provide information about:

- budgetary resources made available, obligations incurred, and outlays; and a reconciliation of budgetary obligations incurred to the net cost of operations;
- net cost of agency operations (total cost of operations less earned revenues) and appropriations and taxes used to finance the net cost of operations;
- operating assets such as receivables, inventories, and property, plant, and equipment; and operating liabilities which include pensions and other post-employment benefits earned by governmental employees; and
- stewardship resources and obligations which include most heritage and military assets, certain investments in the nation's well-being such as investments in human capital (education and training programs financed by the federal government for the benefit of the general public), and social insurance obligations.

316. Under these standards, only the dollar values of operating assets and liabilities are reflected in the Balance Sheet. Stewardship resources and obligations are required to be reported as part of the financial statements, albeit as supplementary stewardship information. Thus, all accountabilities are reported, but they are reported separately. The U.S. believes that the consumption of service potential of stewardship resources such as military assets cannot be reliably measured through depreciation. For this and other reasons it has elected to exclude these assets from the Balance Sheet and treat the annual expenditures on them as a separate element of cost in the operating statement. Extensive stewardship reporting is also required on physical quantities, conditions and costs of these resources. The U.S. also believes that for various reasons, including the fact that social insurance benefits and the related payroll taxes are subject to change, that the actuarial valuations of social insurance obligations are not operating liabilities. Nevertheless, the future effects of the obligations involved in programs for Social Security, Medicare, etc. need the type of ample disclosure that stewardship reporting can provide. As a result, various measures of the economic sustainability of social insurance programs are required to be reported.

317. The emphasis on accrual accounting has been spurred on by Congressional interest in measuring performance results, which includes the cost of outputs and outcomes. As a result, the "bottom line" of the operating statement is the agency's net cost of operations and the components of it provide information about the cost of the major programs and activities for which the agency is responsible. To aid in this endeavor, the FASAB has also established cost accounting standards that require agencies to measure the full costs of goods and services they provide. Such full costs will reflect all related costs incurred by the government regardless of which agency actually makes the expenditures.

318. Even the U.S. budget, which is essentially cash based, has moved to the use of accrual accounting for some programs, most notably being credit programs: direct loans and loan guarantees. The use of the cash basis accelerated the budget impact when direct loans were made and it delayed the impact when a guarantee was made. Because of this, more programs began using guarantees, which made it more difficult to control the cost of credit programs. Accrual accounting has proven to be a better method for planning and controlling the use of resources for these programs and is now being considered for federal insurance programs.

319. U.S. federal government accrual accounting standards, which have been developed using "due process" procedures similar to those used by the private sector standard setters, have the force of law in the U.S..

Costs of Adopting and Operating Accrual Accounting Systems

320. The costs of introducing accrual accounting include the costs of:

- identifying and valuing existing assets;
- developing accounting policies;
- establishing accounting systems, including the purchase of computer systems and pilot testing the system;
- development of skills and training for both the preparers and users of financial information.

321. Some costs, such as the cost of purchasing computer systems, are easily identified. Other costs such as the development of accounting skills in personnel may be more difficult to identify. The actual costs of adopting a particular basis will depend on the existing capacity of personnel in terms of experience and training, and the reliability and completeness of existing systems. In some jurisdictions the development of institutional capacity may be an essential and major step in the implementation of accrual accounting. In other jurisdictions this may be much less important due to existing skills and knowledge. The adoption costs will also be influenced by the nature of the accounting system. If the accounting system is intended to collect information for both internal and external reporting then it will need to be more extensive.

322. Adoption costs can be minimized by making use of accounting policies used by other, similar entities, and by having a staged transition to full accrual reporting. The transition may be staged by organization, or even by financial element within organizations. For example, financial assets could be recognized initially with physical assets being recognized over subsequent accounting periods. Difficult asset valuation issues may be deferred until other more easily valued assets have been accounted for. Infrastructure assets are one group of assets which are generally more difficult to value than other assets (there are also variations in the definition of infrastructure assets between jurisdictions). One option for a country adopting accrual accounting is to delay valuation of this class of assets so as to thereby allow time for implementation issues to be resolved, and also to spread the cost of the change.

323. Despite the advantages of a staged transition, there are also drawbacks. It may be difficult for users to make comparisons over time and to understand the extent of changes made during the period. When a range of bases is used by various entities or when the classes of assets recognized change from one year to the next it may be difficult to interpret the information provided during the transitional period. Full disclosure of any changes made during the year is desirable and, where possible, comparative information on the same basis should be available.

324. The benefits of accrual accounting depend, in part, upon how extensively accrual information is used for budgeting and management purposes. For example, both the Commonwealth Government of Australia and some of the state governments have recently moved to accrual-based budgeting and believe that this generates additional benefits which are not realized when accrual accounting is used solely for external reporting purposes.

325. A higher level of training and accounting skills are required to operate an accrual accounting system than a cash-based system. This may result in increased personnel costs. However, New Zealand is one jurisdiction which considers that the accrual accounting systems are not necessarily more expensive when all the ancillary costs associated with its previous cash accounting system were included. It points to the fact that commercial software may be able to be used by a number of entities, that integrated recording systems streamline the processing of certain transactions and the need for multiple reconciliations can be minimized and major savings can be achieved. In New Zealand, although the need for more qualified people increased as a result of the reforms, the total number of people associated with transaction processing actually decreased.

326. Each jurisdiction would need to analyze both the costs and benefits of adopting accrual accounting and the capability of the jurisdiction to effectively implement such a change, before making a decision to adopt this basis of accounting. Political commitment and the adequacy of existing systems are

factors which can affect the success of a change in accounting basis. Jurisdictions which have made the change are often strongly in favor of accrual accounting.

Conclusion

327. The accrual basis provides users with financial information about such matters as the resources controlled by the entity, the cost of its operations (cost of providing goods and services), enhanced cash flow information, and other financial information useful in assessing financial position and changes in financial position, and in assessing whether the reporting entity is operating economically and efficiently.

328. Accrual accounting is essential if financial reporting is to provide information useful in evaluating the government's performance in terms of service costs, efficiency and accomplishments. It can assist users by providing better information for decision making and accountability and by changing the way managers think and operate.

CHAPTER 12

ACCRUAL BASIS – ASSETS

Introduction

329. PSC Study 5 *Definition and Recognition of Assets* considers issues associated with the definition and recognition of assets in the public sector. This Chapter builds on the material in Study 5. It provides a definition of assets, and outlines the recognition criteria for assets. It then describes various types of public sector assets which meet the definition of an asset, discusses recognition issues associated with these types of assets and provides examples of classification systems commonly used in the disclosure of assets.

Definition of Assets

330. The accrual basis of accounting reports on the economic resources or service potential (assets) and obligations (liabilities) of the entity, and changes therein. It requires the capitalization of outlays on the acquisition of all capital assets and the depreciation of those assets as their service potential is consumed or lost.

331. PSC Study 2 Elements of the Financial Statements of National Governments states:

> *... the fundamental characteristics of an asset are:*
> *(i) the existence of service potential or future economic benefits;*
> *(ii) the service potential or future economic benefits must arise from past transactions or events (that is, 'future' assets cannot be recognized in the financial statements); and*
> *(iii) the service potential or future economic benefits must be controlled by the reporting entity as at the reporting date.* (paragraph .065)

332. These characteristics flow from the definition of an asset in the IASC Framework for the Preparation and Presentation of Financial Statements, which states:

> *An asset is a resource controlled by the enterprise as a result of past events and from which future economic benefits are expected to flow to the enterprise.* (paragraph 49)

333. The IASC definition refers only to future economic benefits. The PSC, in common with a number of other public sector standard setters, considers that the definition of an asset needs to incorporate both economic benefits and service potential. Service potential is the capacity of an asset, singly or in combination with other assets, to contribute directly or indirectly to an entity's objectives in the public sector.[3] Some jurisdictions use only the term "future economic benefits" to cover both concepts. This is illustrated in the following excerpt from the Australian Statement of Concepts No. 4, *Definition and Recognition of the Elements of Financial Statements*.

> *The expression 'service potential' has been omitted from the definition and recognition criteria. As is noted in paragraph 18 of this Statement, the characteristic of future economic benefits is synonymous with the notion of service potential, a term which is used more commonly in respect of not-for-profit entities. The expression 'future economic benefits' has sometimes been used in accounting texts to signify access to future cash inflows. However, the term is used in the Statement with a broader meaning – namely, the capacity to provide goods and services in accordance with the entity's objectives, whether those objectives are the generation of net cash inflows or the provision of goods and services of a particular volume and quality to beneficiaries. This amendment has been made so as to simplify the expression used in the Statement, and does not change the intended meaning of the definitions and recognition criteria.* (paragraph A10(a), SAC 4)

[3] Adapted from "Crown Accounting Policies for External Financial Reporting", Crown Assets, paragraph 2a, page 27, New Zealand Treasury, November 1991.

Recognition of Assets

334. Under the accrual basis of accounting, all assets that meet the definition and recognition criteria for an asset are reported in the Statement of Financial Position.

335. Under the IASC Framework for the Preparation and Presentation of Financial Statements an asset should be recognized when it is probable that the future economic benefits will flow to the enterprise and the asset has a cost or value that can be measured reliably (paragraph 89).

336. The first half of the recognition criteria, that of probable future economic benefits or service potential, may be relatively easy to apply. However, reliable measurement of public sector assets may initially be more difficult. Cost records, valuation methods, accounting standards and/or market values may not exist for some public sector assets. For physical assets which are acquired or constructed, relevant costs may include the purchase price, import duties and transport, handling and other costs directly attributable to the acquisition of the item. IAS 16, *Property, Plant and Equipment* contains a discussion of this issue.

337. Where cost records are unavailable or the cost of acquisition (if any) no longer has any relevance to users because of subsequent changes in values, an initial valuation of assets is often required. Where an active market for an asset class exists (e.g., the market for certain financial instruments), then the task of achieving sufficient reliability to justify recognition can follow established practice. Markets for a specific service may often exist outside the particular jurisdiction; for example, certain utilities, such as water or electricity supply, are privately operated and shares in the operating entities may be traded elsewhere. The values attributed to these private sector operating entities can provide some benchmark in considering the value of public sector operations in the same field. If there are no cost records or market values available for assets, then estimates may be required. Quite frequently, when a government first adopts accrual accounting, estimates will be required. Where assets are recognized class by class, over a period of time, additional disclosure of unrecognized assets may be appropriate (a discussion of disclosure of unrecognized assets is included in this Chapter).

338. Particular problems may be experienced with the reliable measurement some assets such as and taxation receivable. These assets are all discussed separately in this Chapter. Where the lack of a reliable measurement precludes the recognition of these assets, additional note disclosure may be provided. Conflict between the qualitative characteristics of relevance and reliability is unavoidable, and it is a matter of judgment to assess the balance which best meets the needs of users.

339. In addition to establishing recognition criteria, most entities also specify asset recognition thresholds. Assets less than a certain monetary value are treated as an expense. Only assets above the recognition threshold are recorded as assets in the financial statements. The recognition threshold varies from entity to entity and depends upon the size of the entity — larger entities usually adopt a higher recognition threshold. Refer also to the discussion of physical assets later in this Chapter.

Types of Assets

340. Types of assets generally held in the public sector may be classified using the following headings:

- Financial assets;
- Physical assets; and
- Intangible assets.

Each of these categories is discussed below.

Financial Assets

341. The definition of financial assets given in IAS 32, *Financial Instruments: Disclosure and Presentation* is:

A financial asset is any asset that is:

(i) cash;

(ii) a contractual right to receive cash or another financial asset from another enterprise;

(iii) a contractual right to exchange financial instruments with another enterprise under conditions that are potentially favourable; or

(iv) an equity instrument of another enterprise. (paragraph 5)

342. Financial assets can include some of, or all the following:

- cash and temporary investments;
- revenues receivable;
- loans and advances to other governments;
- other loans and advances;
- investments;
- derivatives; and
- prepayments.

343. A more detailed discussion of some of these categories of financial assets is given below. (Note that under some modifications of the accrual basis the definition of financial assets is broader and includes inventories held for sale in the ordinary course of operations and land held for resale.)

344. Financial assets have clear future benefits and their value may normally be measured with reliability. They therefore meet the criteria for recognition. Under a historical cost accounting model, foreign exchange assets are commonly carried at closing rates and short- and long-term loans are carried at face value. Under hyperinflationary conditions, financial asset balances are converted to current values. IAS 39, *Financial Instruments: Recognition and Measurement* provides guidance on the measurement and disclosure of financial assets and liabilities.

Financial Assets – Cash

345. Cash in the form of money in the bank clearly has the three characteristics of an asset. IAS 7, *Cash Flow Statements* (paragraph 6) contains the following definitions:

> *Cash comprises cash on hand and demand deposits.*
>
> *Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.*
>
> *The term "other monetary assets" may also be used to describe near-cash assets such as bullion and cash in transit.*

Financial Assets – Investments

346. Financial investments in the private sector are assets held for capital growth or investment income. This concept also applies in the public sector to investments such as shares in companies. In the public sector, investments may also include the government's ownership interest in other government entities such as ministries, departments, and agencies. Many of these investments are held because the government has decided that ownership of activities is the best way of providing services to the public. Investments in government entities generally meet the definition and recognition criteria to be recognized as assets, although only to the extent that the investments are recoverable. Similarly, additional capital injections to government-owned entities are only be recognized as an addition to an asset to the extent that they are recoverable. Capital injections which are made for the purpose of supporting an entity in financial distress are not likely to be recoverable and would therefore be recorded in the Statement of Financial Performance as an expense.

347. Under accrual accounting, an initial value is required for each investment recorded in the accounting system. For some investments such as investments in government departments or agencies, there will be no acquisition price (or construction cost) or known market value for the investment as a whole. In the absence of this information, the value of the investment may be determined by valuing all the assets and liabilities represented by the underlying investment. The book value of an investment may also be reassessed periodically for evidence of impairment or to support a revaluation of the investment.

348. The definition of the reporting entity is also relevant when it comes to the recognition of investments within financial statements. Where the concept of control determines the reporting entity, only those investments which are controlled by the reporting entity would be included in its financial statements. Where consolidated financial statements are prepared, investments in controlled entities are removed from the financial statements and replaced with information on the individual assets and liabilities of those entities.

349. Examples of accounting policies for financial investments and note disclosure of investments follow.

Investments

Marketable securities held for trading purposes

Marketable securities held for trading purposes are recorded at net current value.

Equity investments

Equity investments (other than those forming part of the reporting entity) are recorded at the lower of cost and net current value.

Other investments and marketable securities held for investment purposes

Other investments, including marketable securities held for investment purposes, are recorded at the lower of cost and net current value.

Investments held for hedging purposes are recorded on the same basis as the item being hedged.

Example 12.1
Financial Statements of the Government of New Zealand
for the year ended 30 June 1999
Statement of Accounting Policies, pages 61 and 62

Investments

Investments are valued at cost or market valuation.

Example 12.2
Consolidated Financial Statements of the NSW Public Sector 1996–97
NSW Budget Sector, Notes to and forming part of the Financial Statements, page 66

NOTE 28. INVESTMENTS

	1997 $m	1996[1] $m	1997 $m	1996 $m
	Total Asset Value		**Market Value** (where applicable)	
GOLD HOLDINGS	1,757	3,825	1,757	n/a
DEPOSITS	5,657	4,098	3,784	n/a
GOVERNMENT SECURITIES	21,183	14,387	20,590	n/a
DEBENTURES	56	-	1	n/a
SHARES				
Shares in associated entities	202	216	149	n/a
Shares in companies	336	855	95	n/a
Shares in international financial institutions	714	1,551	71	n/a
Total shares	**1,252**	**2,622**	**315**	**n/a**
INTERNATIONAL MONETARY FUND QUOTA	4,448	4,306	-	n/a
ASSOCIATED ENTITIES	332	4,119	-	n/a
OTHER INVESTMENTS	946	1,115	-	n/a
Total investments	**35,631**	**34,472**	**26,447**	**n/a**

Investment maturity schedule

	1997 $m	1996[1] $m
Not later than one year	13,600	13,160
Later than one year and not later than 2 years	1,619	1,566
Later than 2 years and not later than 5 years	2,699	2,611
Later than 5 years	17,713	17,135
Total investments by maturity	**35,631**	**34,472**

[1] Trial and unaudited.

Example 12.3
Financial Statements of the Commonwealth Government of Australia
for the year ended 30 June 1997
Notes to and forming part of the financial statements, page 61 (AUD)

Financial Assets – Loans Outstanding

350. Loans owing to a government meet the definition of an asset. Any interest owing on such loans would meet the definition of revenue and would be a revenue receivable until received. Loans receivable may require adjustment from the amount provided to the recipient where particular conditions of interest concessions or terms for forgiveness reduce the value of the loan to below its original cost. Accounts receivable or debtors are shown at book value less a provision for doubtful debts.

351. An example of an accounting policy for loans outstanding is shown below.

Note 1. I. Loans and Interest Receivable

Loans are accounted for as receivables after the funds have been disbursed. For loans obligated after the effective date of the Credit Reform Act, October 1, 1991, the amount of the Federal loan subsidy is computed. The loan subsidy includes estimated delinquencies and defaults net of recoveries, the interest rate differential between the loans rates and Treasury borrowings, offsetting fees, and other estimated cash flows associated with these loans. The value of loans receivable is reduced by the present value of the expected subsidy costs. For loans obligated prior to October 1, 1991, principal, interest and penalties receivable are presented net of an allowance for estimated uncollectible amounts. The allowance is based on past experience, present market conditions, an analysis of outstanding balances and other direct knowledge relating to specific loans. Note 8 provides additional information concerning loans receivable.

Example 12.4
U.S. Department of the Interior
FY 1998 DOI Annual Accountability Report
Notes to Principal Financial Statements
as of September 30, 1998 and 1997, page 67

Financial Assets – Accounts Receivable

352. This category could include moneys owing on goods and services provided to third parties, and moneys owing from a higher level of government or other parties where grants or appropriations have been recognized as revenues but which have not yet been received.

353. Examples of the accounting policies and note disclosure of accounts receivable are given below.

Receivables and advances

Receivables and advances are recorded at the amounts expected to be ultimately collected in cash.

Example 12.5
Financial Statements of the Government of New Zealand
for the year ended 30 June 1999
Statement of Accounting Policies, page 61

Note 1.F. Accounts Receivable

Accounts Receivable consist of amounts owed to Interior by other Federal agencies and the public. Federal accounts receivable arise generally from the provision of goods and services to other Federal agencies and, with the exception of occasional billing disputes, are considered to be fully collectible. Receivables from the public generally arise either from the provision of goods and services or from the levy of fines and penalties resulting from Interior’s regulatory responsibilities. An allowance for doubtful accounts is established for reporting purposes based on past experience in the collection of accounts receivable and analysis of outstanding balances. Note 4 provides additional information concerning accounts receivable.

Example 12.6
U.S. Department of the Interior
FY 1998 DOI Annual Accountability Report
Notes to Principal Financial Statements
as of September 30, 1998 and 1997, page 66

Receivables

Receivables are recorded at the amounts expected to be ultimately collected in cash and are therefore net of provisions for doubtful debts.

Example 12.7
Consolidated Financial Statements of the NSW Public Sector 1996–97
NSW Budget Sector, Notes to and forming part of the Financial Statements, page 66

4. RECEIVABLES	**96-97 $m**	**95-96 $m**
Current Receivables		
Debtors		
• Sale of Goods and Services	248	*
• Asset Sales	194	77
• Taxation	172	275
• Crown Land leases	16	16
Amounts owing by Non-Budget Sector Agencies		
• Dividends	948	660
• Tax equivalents	113	323
• Corporatisation adjustments	-	33
Advances Receivable	57	57
Other	113	443
	1,861	1,884
Less Provision for Doubtful Debts	(65)	(220)
	1,796	1,664

Example 12.8
Consolidated Financial Statements of the NSW Public Sector 1996–97
NSW Budget Sector, Notes to and forming part of the Financial Statements, page 71 (AUD)

Financial Assets – Taxation Receivable and Accrued Taxation

354. When a government exercises its powers to levy taxes it recognizes the ensuing cash receipts as taxation revenue. In addition, it may need to recognize additional amounts of taxation revenue relating to taxation receivable and accrued taxation. Taxation receivable is usually recognized when assessments have been issued by the taxation authority in relation to income earned during the current financial year and the amounts are due to be received. Apart from any disputes over the amount of the assessment, such amounts are reasonably certain to be received by the taxation authority. Where taxation receivables are the subject of a dispute which will be settled by an administrative body or by judicial decision, both the definition and recognition criteria need to be carefully applied. Such receivables may meet the definition of an asset but may not meet the criteria for recognition. Taxation receivable is recognized only when there is a reliable and binding assessment of the taxpayer's liability as at the end of the financial year. Taxation receivable would not be recognized in relation to taxes where the taxpayer's liability has not been assessed at the end of the financial year.

355. By contrast with taxation receivable, accrued taxes are amounts which are not yet due to be received by the taxation authority, but where the individual or entity has earned income in the current financial year on which taxes will be payable in the near future. Accrued taxes are calculated only in circumstances in which the government has reliable information on both the levels of income earned and the amounts of taxation historically collected in relation to such income. The recognition of accrued taxes will depend upon both the reliability of information available and the nature of the particular power to tax. The justification for recognizing accrued taxes is that the taxes are to be received by the government in the future. Many items of taxation receivable will meet the definition of an asset in that they represent future economic benefits arising from past events which are controlled by the reporting entity. However, future tax receipts relating to income earned in future periods rather than past periods would not generally meet the definition of an asset.

356. Uncertainties surrounding the estimation of taxes and the level of associated doubtful debts may mean that some taxes are not recognized until returns are filed or the actual payment is received. This will often be the starting point for jurisdictions which have adopted accrual accounting. As more information is collected over a number of accounting periods, it may be possible to adopt recognition points prior to receipt. All taxation receivables that meet the definition and recognition criteria are recognized, and then, if necessary, a provision is made for any portion which is not expected to be recovered. Although only the net amount may be reported in the financial statements, the accounting records would contain details of both total taxes receivable and the provision for bad debts. The recognition of taxes is discussed in Chapter 14.

357. An example of an accounting policy for, and note disclosure of, taxation receivable is shown below.

Note 1.E. Taxes Receivable

"Taxes receivable" primarily consist of uncollected tax assessments, penalties and interest when tax payers have agreed the amounts are owed, or a court has determined the assessments are owed. This Financial Report does not include unpaid assessments when neither taxpayers nor a court has agreed that the amounts are owed (compliance assessments) and the Government does not expect further collections due to factors such as the taxpayer's death, bankruptcy or insolvency (write-offs). Taxes receivable are reported net of an allowance for the estimated portion deemed to be uncollectible.

Note 4. Taxes Receivable

Taxes Receivable as of September 30

(In billions of dollars)

Gross taxes receivable	82.9
Allowance for doubtful accounts	55.8
Taxes receivable, net as of September 30, 1998	27.1

Example 12.9
Financial Report of the United States Government – 1998
Notes to the Financial Statements, pages 64 and 67 (USD)

Financial Assets – Prepayments

358. At the end of the reporting period the entity may have paid for some services in advance of receiving or using the services. For example, rent may be paid every two months — one month in arrears and one month in advance. The month's rental paid is advance is termed a prepayment. Prepayments are often immaterial in relation to other assets and may be reported in the financial statements together with other current assets such as receivables.

359. In the public sector some transfers for welfare benefits are paid in advance. Such prepayments may meet the definition and recognition criteria for assets. Chapter 13 includes a discussion on a related issue; i.e., the treatment of transfers payable and when they would meet the definition of liabilities.

Physical Assets

360. The term “physical assets” is used to classify assets other than financial or intangible assets. Physical assets, excluding inventory, are usually referred to as non-current assets or long-term assets unless they have been classified as “current” because of imminent disposal. Inventories are normally classified as current physical assets.

361. Long-term physical assets include :

- property, plant and equipment;
- infrastructure assets;
- investments;
- heritage assets;
- defense or military assets; and
- natural resources.

362. Assets may belong in one or more of these categories. Any category of physical assets which constitutes a significant proportion of total asset holdings may be separately disclosed.

363. The recognition of physical assets occurs only under the accrual basis. Where an asset has been recognized in the Statement of Financial Position and is disposed of in the subsequent period, there will usually be a difference between the proceeds of disposal (if any) and the carrying amount included in financial report. Such residuals are recognized in the period of disposal.

364. Reporting entities may choose to recognize assets only in excess of a minimum financial amount. This minimum level may be determined in relation to the value of fixed assets held by the organization. The Annual Report of the West Sussex County Council 1997/98 states *“A de minimis level of £15,000 has been applied generally, except for vehicles, so as to exclude individual assets or works below this figure from the asset registers.”* (page 33) Similarly the New Zealand Defence Force Annual Report for the year ended 30 June 1999 states *“Fixed asset additions costing $5,000 are capitalised and recorded at historical cost.”* (page 114)

365. Some entities may operate a policy with two recognition thresholds: a minimum level below which assets cannot be capitalized, a band where discretion may be exercised by the preparer, and an amount above which assets must be capitalized. Where individual assets fall below the threshold but the value of the asset class as a whole is above the threshold, assets may be pooled and recognized as a class. Another practice for categories of assets which are renewed regularly e.g., renewable equipment, is to recognize the initial purchase of the asset as a fixed asset but to treat all replacements as an expense. Changes to the value of the recorded asset would only occur if a major increase or decrease in quantity or value occurs.

366. Governments may follow the generally accepted accounting principle of historical cost as a basis for the recognition of assets. Alternatively, they may adopt modified historical costs where certain assets are periodically revalued to amounts which do not exceed their recoverable amounts. (This option is specifically prohibited in some jurisdictions.) Where a revaluation has taken place, there must be appropriate disclosure of asset measurement policies and valuation methods. Some jurisdictions may also adopt current cost models. Refer to Chapter 18 for a discussion of measurement bases.

367. Consumption of an asset’s service potential is treated as an expense in the period in which it occurs. Refer also to Chapter 15.

368. Examples of accounting policies for and note disclosures of various fixed assets are shown in the extract below.

Note 1.H. Property, Plant and Equipment

General Purpose Property, Plant and Equipment

General purpose Property, Plant and Equipment consists of buildings, structures, and facilities used for general operations, power, irrigation, fish and wildlife enhancement, and recreation; land acquired for general operating purposes; equipment, aircraft and vehicles; and construction in progress. In general, buildings and structures are capitalized at acquisition cost and depreciated using the straight-line method over a useful life of from 20 to 50 years with the exception of dams and certain related property which is depreciated over useful lives of up to 100 years. Equipment is capitalized at acquisition cost and is depreciated using the straight-line method over the useful lives generally ranging from 5 to 20 years. Capitalization thresholds are determined by the individual bureaus and generally range from $50,000 to $500,000 for real property and from $5,000 to $15,000 for equipment.

: : : : : : : : : : : : : :

Example 12.10
U.S. Department of the Interior
FY 1998 DOI Annual Accountability Report
Notes to Principal Financial Statements
as of September 30, 1998 and 1997, page 66 (USD)

Capital Assets

9. Apart from some small exceptions, all expenditure on the acquisition of capital assets, or expenditure which adds to the value of existing assets, is capitalised as fixed assets, provided that the fixed assets yield benefit to the Authority for a period of more than one year.

10. The Authority has, however, adopted a de minimis value of £10,000 for equipment and plant, and £50,000 for other assets, below which assets will not be capitalised. The de minimis limit does not apply to assets used by statutory DSOs, and no formal de minimis limit applies to land and buildings or to infrastructure.

11. Fixed assets are stated in the Consolidated Balance Sheet at current value, net of depreciation where appropriate. All expenditure (exceeding routine repairs and maintenance) on fixed assets with a benefit to the Authority of more than one year, has been capitalised on an accruals basis.

12. Fixed assets have been valued on the basis recommended by CIPFA and in accordance with the Statement of Asset Valuation Principles and Guidance Notes issued by the Royal Institute of Chartered Surveyors (RICS). Fixed assets are classified as operational assets those presently used by the Authority for the delivery of public services, or for support tasks) and non-operational assets (surplus property awaiting sale, or investment property, or assets under construction). Assets are further categorised into land and buildings, vehicles, plant, furniture and equipment, infrastructure and community assets.

13. Assets have been valued at the lower of net current replacement cost and net realisable value as stated in the RICS Guidance Notes subject to the following exceptions:

- short lived operational assets (i.e. vehicles, plant and equipment) are valued at historic cost (less depreciation where appropriate) as a proxy for current replacement cost.
- infrastructure assets are included in the Consolidated Balance Sheet at net historic cost (where known).
- uncompleted building works are included in the Consolidated Balance Sheet at historic cost.

Example 12.11
Surrey County Council
Statement of Accounts 1997/98
Accounting Policies, page 9 (GBP)

ASSETS

Non-Current Physical Assets

Capitalisation and Initial Recognition

In general, non-current physical assets with a value greater than $5,000 are capitalised except for computer equipment which is normally capitalised irrespective of the $5,000 threshold where it is considered to be part of a network of assets.

Assets are initially recognised at their acquisition cost. Cost is determined as the fair value of the assets given as consideration plus other costs incidental to the acquisition.

Assets acquired at no cost or for nominal consideration are initially recognised as assets and revenues at their fair value at the date of acquisition. Fair value means the amount for which an asset could be exchanged between a knowledgeable, willing buyer and a knowledgeable, willing seller in an arm's length transaction.

The cost of non-current physical assets constructed for own use includes the cost of materials, direct labour, attributable interest, other financing costs and foreign exchange gains and losses arising during construction as well as an appropriate proportion of variable and fixed overhead costs that can be reliably attributed to the assets.

Valuation of Land

Land held for continued use that would be replaced because of a government policy is valued at the greater of current market buying price for that land in its existing use and current market selling price based on feasible alternative use. However, for most public sector land assets, there is no prospect of alternative use because there are natural, legal or socio-political restrictions on their use and disposal. Such land is valued at "value in use".

Land held for continued use but not to be replaced given the existing government policy is valued at the greater of the present value of future net cash flows and current market selling price based on feasible alternative use.

Surplus land is valued at market selling price.

Undeveloped Crown land is currently not recognised pending the completion of an extensive valuation program. Land under roads and within road reserves which has been recognised in the financial report of the Roads and Traffic Authority (at $14.7 billion), has not been recognised in the State's Consolidated Financial Statements as there is currently no methodology available to reliably determine the value.

Example 12.12
Consolidated Financial Statements of the NSW Public Sector 1996–97
The NSW Public Sector, Notes to and forming part of the Financial Statements, pages 28 and 29 (AUD)

Valuation of Plant and Equipment, Infrastructure Systems and Buildings

Plant and equipment, infrastructure systems and specialised buildings that are held for continued use and would be replaced because of government policy are valued at depreciated current cost. Current cost is the minimum cost of replacing the remaining service potential of an asset with a modern equivalent asset (eg current market buying price, current reproduction cost or current replacement cost).

Non-specialised buildings are valued at market selling price.

Assets held for continued use that would not necessarily be replaced because of government policy are valued at the greater of the net present value of the cash flows and the current market selling price.

Surplus assets are valued at market selling value.

Infrastructure systems include assets such as roads, bridges, sewerage systems, water supply and reservoirs, power generation plants and transmission lines.

Revaluation Policies

All physical non-current assets are revalued at least every five years to current value. Revaluation increments are credited directly to the asset revaluation reserve unless they reverse any previous decrements which have been charged to the Operating Statement.

Assets acquired or constructed since the last valuation are valued at cost.

Non-current assets used by profit-seeking agencies are revalued downward when their carrying amount is greater than their recoverable amount. The recoverable amount test is not applied to non-current assets of not-for-profit agencies whose service potential is not related to the generation of net cash inflows.

Example 12.13
Consolidated Financial Statements of the NSW Public Sector 1996–97
The NSW Public Sector, Notes to and forming part of the Financial Statements, page 29 (AUD)

NOTE 13: FIXED ASSETS

30/06/98 $000		30/06/99 $000
	Land	
9,016	At cost	9,016
114,528	At valuation	111,290
123,544	*Land – net current value*	***120,306***
	Buildings	
47,762	At cost	64,152
647,428	At valuation	635,127
(53,959)	Accumulated depreciation	(88,844)
641,231	*Buildings – net current value*	***610,435***
	Specialist Military Equipment	
495,704	At cost	1,190,728
743,299	At valuation	593,848
(259,397)	Accumulated depreciation	(356,046)
979,606	*Specialist Military Equipment – net current value*	***1,428,530***
	Plant & Equipment	
114,814	At cost	123,167
67,818	At valuation	63,040
(82,215)	Accumulated depreciation	(90,316)
100,417	*Plant & Equipment – net current value*	***95,891***
	Office & Computer Equipment	
27,452	At cost	32,682
26,094	At valuation	2,841
(42,881)	Accumulated depreciation	(23,695)
10,665	*Office & Computer Equipment – net current value*	***11,828***
	Capital Work in Progress	
16,890	At cost	14,664
16,890	*Capital Work in Progress – net current value*	***14,664***
	Total Fixed Assets	
2,310,805	At cost and valuation	2,840,555
(438,452)	Accumulated depreciation	(558,901)
1,872,353	**Total Carrying Amount of Fixed Assets**	**2,281,654**

All Fixed Assets in each asset class were valued for the purpose of the opening Mode B Statement of Financial Position as at 1 January 1991 by independent Registered valuers, except for Specialist Military Equipment which was valued by representatives from the single Services.

Valuations of Land (as at 30 June 1994) and Buildings (as at 30 June 1997) are at net current values determined by independent valuers. Major vessels, aircraft and other items of Specialist Military Equipment are held at their internally assessed valuation as at 30 June 1997.

Substantially all the title to, or interest in land remains in the name of the Crown, although equitable ownership rests with NZDF. In certain cases, in the event of land being sold, potential claims may be lodged under the Treaty of Waitangi Act 1985. The effect on the valuation of Land and Buildings, if any, resulting from such potential claims cannot be quantified.

Example 12.14

Annual Report of the New Zealand Defence Force
for the year ended 30 June 1999
Notes to the Financial Statement, page 128 (NZD)

369. Inventories are defined in IAS 2, *Inventories* as assets which are:

- held for sale in the ordinary course of business;
- in the process of production for such sale; or
- in the form of materials or supplies to be consumed in the production process or in the rendering of services.

370. These categories may also be applied to governments, although in the public sector inventories are more often held for use in the rendering of services than for production and sale.

371. The classification of inventories as physical assets, rather than financial assets, is in accordance with the generally accepted use of the term "financial assets" under accrual accounting. However, under some modifications to the accrual basis of accounting a distinction may be made between inventories for sale which are regarded as financial assets, and the remaining two categories which are regarded as physical assets (PSC Study 5 *Definition and Recognition of Assets*, Figure 3.3). Inventories may be classified in various ways on the face of the financial statements or they may be shown as one figure, with more detailed note disclosure.

372. Examples of accounting policies for and note disclosures of inventories are given below.

Inventories

Inventories are valued at the lower of cost or net realisable value. Cost is calculated using the average cost or the "first in first out" method.

Example 12.15
Consolidated Financial Statements of the NSW Public Sector 1996–97
The NSW Public Sector, Notes to and forming part of the Financial Statements, page 29

Inventories
Inventories are not held for resale and are comprised mainly of munitions, technical spares in support of fixed assets and consumable items.

Inventories are recorded at weighted average cost. Appropriate allowance has been made for obsolescence.

Example 12.16
Annual Report of the New Zealand Defence Force
for the year ended 30 June 1999
Statement of Accounting Policies, page 114

8. INVENTORIES	96-97 $m	95-96 $m
Current		
Raw Materials	231	172
Work in Progress	84	145
Finished Goods	57	49
Forestry	62	59
Consumable Stores	269	395
Land Held for Resale	140	175
	843	995
Non-Current		
Forestry	1,403	1,274
Land Held for Resale	495	464
Work in Progress	54	97
Other	27	57
	1,979	1,892

Example 12.17
Consolidated Financial Statements of the NSW Public Sector 1996–97
The NSW Public Sector, Notes to and forming part of the Financial Statements, page 35 (AUD)

NOTE 31. INVENTORIES	1997 $m	1996[1] $m
INVENTORIES HELD FOR SALE		
Raw materials and stores	88	2,177
Work in progress	78	63
Finished goods	1,972	494
Land held for sale	224	151
Total inventories held for sale	**2,362**	**2,885**
INVENTORIES NOT HELD FOR SALE		
Consumable stores	3,794	3,632
Total inventories not held for sale	**3,794**	**3,632**
Total inventories	**6,156**	**6,517**

[1] Trial and unaudited.

Example 12.18
Financial Statements of the Commonwealth Government of Australia
for the year ended 30 June 1997
Notes to and forming part of the Financial Statements, page 66 (AUD)

Note 1.F. Inventories and Related Property

"Inventories" are valued at historical cost. Historical cost methods include first-in-first-out, weighted average and moving average. Estimated repair costs reduce the value of inventory held for repair. Excess, obsolete and unserviceable inventories are valued at estimated net realizable values.

Example 12.19
Financial Report of the United States Government – 1998
Notes to the Financial Statements, page 64

Note 5. Inventories And Related Property

"Inventories and related properties" consist of the categories listed below, net of allowance for obsolete and unserviceable inventory, as of September 30, 1998.

"Operating materials and supplies" are comprised of tangible personal property purchased for use in normal operations.

"Materials and supplies held for future use" includes tangible personal property not readily available in the market or held because there is more than a remote chance that they will eventually be needed.

"Inventory held for sale" is tangible personal property held for sale, net of allowances.

"Seized monetary instruments" comprise only monetary instruments. These monetary instruments are awaiting judgment to determine ownership. The related liability is included in "Other liabilities." Other property seized by the Government, such as real property and tangible personal property, is not included as a Government asset. It is accounted for in agency property-management records until the property is forfeited, returned or otherwise liquidated.

"Forfeited property" is comprised of monetary instruments, intangible property, real property and tangible personal property acquired through forfeiture proceedings; property acquired by the Government to satisfy tax liability; and unclaimed and abandoned merchandise.

"Stock pile materials" are strategic and critical materials held for use in national defense, conservation or national emergencies due to statutory requirements.

"Commodities" are items of commerce or trade that have an exchange value used to stabilize or support market prices.

"Other related property" includes all other related property not included above (for example, property acquired through military base closings).

Inventories and Related Property as of September 30

(In billions of dollars)	Defense	All Others	Total
Inventory held for sale ……………………………………	69.4	0.5	69.9
Stockpile materials ………………………………………..	4.3	37.7	42.0
Operating materials and supplies ………………………	31.1	2.6	33.7
Materials and supplies held for future use ……………..	20.3	0.1	20.4
Commodities ………………………………………………	-	0.3	0.3
Seized monetary instruments ……………………………	-	0.2	0.2
Forfeited property …………………………………………	-	0.2	0.2
Other related property ……………………………………	0.1	-	0.1
Total inventories and related property ………………	125.2	41.6	166.8

Example 12.20
Financial Report of the United States Government – 1998
Notes to the Financial Statements, pages 67 and 68 (USD)

Physical Assets – Property, Plant and Equipment

373. According to IAS 16, Property, Plant and Equipment,

> *Property, plant and equipment are tangible assets that:*
> *(a) are held by an enterprise for use in the production and supply of goods or services, for rental to others, or for administrative purposes; and*
> *(b) are expected to be used during more than one period.* (paragraph 7)

374. Investment properties may be accounted for either as property under IAS 16, or as long-term investments in accordance with IAS 25, *Accounting for Investments*. All buildings and plant etc. are regarded as having the characteristics of an asset unless they are shown to have no future economic benefits or service potential.

Physical Assets – Infrastructure Assets

375. The term infrastructure assets is sometimes used to describe the following types of assets:

- road networks, including bridges, kerbs, channels and footpaths
- sewer systems
- water supply systems
- drainage systems
- landfill sites
- flood control works
- power supply systems
- communication networks
- recreation reserves.

376. This list of examples is not exhaustive. Infrastructure assets generally have the following characteristics:

- long lived. In some cases it is difficult to define the life of the asset, particularly if a regular maintenance program is consistently applied to the asset;
- components may be replaced periodically over the asset's useful life. For example, the visible part of a road, the road surface, may be replaced several times before any work is carried out on the road pavement. Associated drainage assets may significantly outlive the road pavement before being replaced; and
- fixed in place. Parts of the network may be extended or no longer used, but the overall asset remains intact and serviceable.

377. Implicit in many definitions of the term is the idea of a network. For example, a length of road derives its service potential and future economic benefits from being part of a roading system. Infrastructure assets typically have very large values when considered as single systems; they are important to users both for their economic value and the essential services they provide. It can therefore be argued that there is benefit in separately displaying infrastructure assets in the Statement of Financial Position.

378. Infrastructure assets will usually meet the definition of an asset. In terms of the recognition criteria, the benefits from these assets will usually be probable. However, reliable measurement of infrastructure assets may be more difficult due to the absence of cost data or inactive markets. The remaining approaches to measurement derive from current cost, that is, measuring the asset at the current cost of replacing the service potential embodied in the asset. For a fuller discussion of measurement issues refer to Chapter 18.

379. An infrastructure system can be considered as a single asset or more usefully as a collection of assets; for example a water supply system could be a collection of individual assets in classes such as land, buildings, plant, and pipe networks. The individual assets may be measured in terms of their individual historical cost (if available) or their replacement cost adjusted for age and obsolescence in relation to each asset's role in the water supply system as a whole. Some jurisdictions consider that estimates of current replacement cost provide significantly more useful information for decision-making about resource allocation than historical cost data.

380. For a discussion of the recognition of the loss of service potential of infrastructure assets, refer to Chapter 15.

381. Excerpts from financial statements showing note disclosure of infrastructure assets are given below.

Notes to the Financial Statements *(continued)*
as at 30 June 1999

Forecast 1998 Budget $m	Forecast Estimated Actual $m		Actual 30 June 1999 $m	30 June 1998 $m
		NOTE 13: State Highways		
		Cost or Valuation		
8,406	8,359	Opening balance	8,359	8,210
224	158	Net additions	148	153
-	-	Net revaluations	263	(4)
8,630	**8,517**	**Total Cost or Valuation**	**8,770**	**8,359**
		Accumulated Depreciation		
69	-	Opening balance	-	-
71	81	Depreciation charged for the period	81	80
-	-	Net revaluations	(81)	(80)
140	**81**	**Total Accumulated Depreciation**	**-**	**-**
8,490	**8,436**	**Net State Highways**	**8,770**	**8,359**

The State highways comprise the land, formation works, road structure, drainage works and traffic facilities of the roads, plus bridges, culverts, tunnels, stock and pedestrian underpasses, protection works and retaining structures. The land was valued on a net current value basis while other elements of the state highways were valued on the basis of depreciated replacement cost.

Replacement costs were determined by estimating the costs of new construction of the network by the most appropriate method of construction. The methodology applied used information from the road assessment and maintenance management (RAMM) database and the bridge inventory held by Transit New Zealand. This information was supplemented by the local knowledge and expertise of the valuers. Land, formation works, and 30% of the road structure have not been depreciated as it is considered that the service potential of these components does not reduce over time.

The valuation is updated annually through the use of price indices. In addition, the state highway regions of New Zealand are subject to an in depth valuation review on a cyclic basis at an interval not exceeding seven years. In 1998/99 two state highway regions were the subject of a detailed valuation review.

After allowing for new works and depreciation during the year to 30 June 1999, the depreciated replacement cost is assessed at $8,770 million (30 June 1998: $8,359 million).

Only those highways clearly owned by the Crown are included in the Statement of Financial Position. Urban state highways (excluding motorways) are not included in the Statement of Financial Position, as these assets are owned by local authorities.

Example 12.21
Financial Statements of the Government of New Zealand
for the year ended 30 June 1999
Notes to the Financial Statements, page 83 (NZD)

Physical Assets – Investments

382. Governments may hold physical assets either for use or as investments. Physical assets which are commonly held as investments include land, buildings and forests. It is usual to identify investments separately.

383. Investments may be recognized in the financial statements of a government at historical cost or at a revalued amount.

Physical Assets – Heritage Assets

384. Public sector entities are often charged with the custody of culturally significant resources, such as works of art, historic documents, areas of land of historic, scientific or environmental significance, monuments and culturally significant buildings. Such resources are sometimes described as heritage assets. Descriptions of heritage assets follow:

> *In general usage, the term "heritage assets" refers to physical assets that a community intends preserving because of cultural, historic or environmental associations.* (Rowles 1992)
>
> *The term "heritage assets" [is used] to refer to fixed assets that a government intends to preserve indefinitely because of their unique historical, cultural or environmental attributes. A common feature to most heritage assets is that they cannot be replaced. Examples of heritage assets are monuments, art and museum collections, wilderness preserves, battlefields and buildings designated for preservation.* (CICA 1989, Chapter 3, paragraphs 34–40)

385. Implicit in the use of the term is the idea that the government or government body is acting as custodian of the asset in question. The ownership and care of culturally prized assets is politically sensitive. For this reason, and because heritage assets can entail considerable amounts of expense and investment in their protection and preservation, it may be useful to users for heritage assets to be displayed separately from other assets.

386. It is possible to argue that heritage assets are not readily distinguished from other physical assets and should not be classified separately. However, where preparers believe this information is useful, the separate disclosure of heritage assets may be appropriate.

387. The probable future benefits of a heritage asset relate to its unique historical, cultural or environmental attributes. It could be argued that the decision by a government to preserve a heritage asset is proof of its future benefit. There has been considerable debate over the measurability of heritage assets.

388. This Study acknowledges that there may be some difficulty placing a monetary value on the historical, cultural or environmental attributes of some heritage assets. However, accrual accounting requires the recognition of all assets which meet the recognition criteria. If measurement difficulties prevent the recognition of heritage assets in a particular jurisdiction, additional disclosure of these assets may be appropriate (refer to the discussion of unrecognized assets later in this Chapter). If heritage assets as a class are not recognized, this represents a modification to accrual accounting which it is appropriate to comment on in the Statement of Accounting Policies.

389. It is worth noting that there is no use of the term "heritage assets" in the private sector, notwithstanding that many private sector institutions own and hold similar assets for similar reasons. Recognition and measurement difficulties do not prevent the private sector from buying, selling, taxing, insuring or transferring by inheritance etc. various works of art, historic buildings and rare documents. Values often need to be established for insurance purposes. Similarly, it is possible to establish a transfer price when such assets pass from public to private ownership and vice versa, as occurs routinely. Instances of illegal export and looting of collections of cultural treasures confirm that when the opportunity is afforded, rare items of cultural interest can be readily traded, even where it is illegal.

390. In general, the selection of a measurement base for particular heritage assets should be made to provide users of financial reports with an understanding of the economic costs of holding that heritage asset. As with other assets, a range of measurement bases may be used to value heritage assets including historical cost, market value, replacement cost and value in alternative use. Where a jurisdiction is still in the process of determining values for heritage assets, symbolic values such as $1 may be used to alert readers to the existence of such assets.

391. In many instances heritage assets are subject to general restrictions on disposal (for example, statutory prohibitions on the export of culturally significant items) or to restrictions specific to the asset(s) recognized. Such restrictions should be disclosed in the narrative to the financial statements. Where there are legal restrictions on the sale of an asset, that asset may be measured as if the legal restriction had been removed or at a value which discounts market prices for similar assets by a factor to reflect

the restriction. In general, financial reports prepared using the going concern assumptions will be more useful if the values recognized reflect the current and actual legal position of the entity.

392. If a heritage asset is recognized at cost or market value and the asset suffers loss of service potential, then the loss of service potential of the heritage asset is recognized. Many heritage assets will have physical deterioration identical to other physical assets. However, it is possible that if particular heritage assets are maintained, restored as necessary by skilled professionals and have a long life, then their depreciation will be so small as to be immaterial.

393. An extract from an asset valuation accounting guideline on heritage assets follows. This extract illustrates the application of the concept of deprival value. Under the concept of deprival value a method of valuation or measurement base may be selected depending upon the reaction of the entity if it were deprived of that asset.

4.15. The following table summarises the application of deprival value to particular classes of assets.

Measurement Bases to be Applied Under these Guidelines to Particular Categories of Physical Non-Current Assets

Asset Category	*Where service potential would be replaced if an Agency was deprived of the asset*	*Where service potential would not (or could not) be replaced if an Agency was deprived of asset*
Asset Held for Continued Use		
: :	: :	: :
Heritage assets	Current market buying price, current replacement cost or current reproduction cost, as applicable, of the gross service potential utilised by the Agency if the service potential would otherwise be acquired by the Agency	Greater of net present value and current market value (selling price)
Surplus Assets		
All such assets	Not Applicable	Current market value (selling price)

Example 12.22
Commonwealth Government Accounting Guidelines, Australia
Accounting Guideline A 1. Asset Valuation, page 13

Physical Assets – Defense or Military Assets

394. Defense or military assets include weapons, munitions and support infrastructure. If these assets are a significant category of physical assets, they are usually shown as a separate category. The separate classification of assets used for defense purposes indicates that although non-current, such assets could be consumed at short notice in the event of hostilities. The expenses arising from the destruction of military assets in the event of hostilities or for any other reason can be recognized at the time of consumption.

395. For an example of disclosure of military assets, refer to Example 12.14.

396. The System of National Accounts classifies some military assets as capital expenditure (assets) and some as current expenditure (expenses).

> *Outlays for military purposes are however, considered to be current expenditures, except for outlays by the military authorities on land and certain items for civilian use such as schools, hospitals, and family-type housing, and in some cases roads when for civilian use. 'Military purposes' are construed in terms of final use; they include the military airport, but not the bulldozer used in constructing the airport.* (Inter Secretariat Working Group on National Accounts, 1993)

397. The Study acknowledges that it would be desirable to have consistent treatment of such assets in both SNA reports and external financial statements. As previously mentioned, accrual accounting under the IASC Framework for the Preparation and Presentation of Financial Statements requires the recognition of all assets which meet the recognition criteria. If measurement difficulties prevent the recognition of military assets in a particular jurisdiction, additional disclosure of these assets may be appropriate (refer to the discussion of unrecognized assets later in this Chapter). If military assets as a class are not recognized, this represents a modification to accrual accounting which it would be appropriate to comment on in the Statement of Accounting Policies.

398. Examples of accounting policies for military assets from both whole of government financial statements and the statements of a defense department are shown below.

> **Specialist military equipment**
>
> Specialist military equipment is recorded at depreciated replacement cost. Valuations have been obtained through specialist assessment by New Zealand Defence Force advisers.

Example 12.23
Financial Statements of the Government of New Zealand
for the year ended 30 June 1999
Notes to the Financial Statements, page 62

> Specialist military equipment with unit values of over $100,000 is valued every three years, internally, and is stated at depreciated current replacement cost after due allowances for technological change. Some aircraft rotables, in the absence of replacement costs, are valued based on latest purchase price.

Example 12.24
Annual Report of the New Zealand Defence Force
for the year ended 30 June 1999
Statement of Accounting Policies, page 114 (NZD)

Physical Assets – Natural Resources

399. A government may have control of natural physical resources (e.g., control of the continental shelf or other parts of the sea bed, geothermal resources).

400. A description of natural resources is:

> *Natural resources are economic resources in their natural undeveloped state. They can be further categorized as renewable or depletable. Renewable resources are those natural resources that can be developed and managed to produce a sustained yield for an indefinitely long period. Examples of renewable natural resources are farm land, forests, fish stocks and water for electricity generation, irrigation, recreation and consumption. Depletable resources are such natural resources as*

petroleum and mineral deposits that will diminish to the point of exhaustion over the period of their production. If not managed to provide a sustainable yield, renewable resources can also be depleted. (CICA 1989, paragraph 48)

401. In order to meet the definition of an asset, natural resources must have future economic benefits or service potential which are under direct government control. Many natural resources do meet these criteria.

402. Examples of natural resources which may meet the definition and recognition criteria for assets include:

- a state-owned coal mine's coal reserves;
- off-shore oil extraction operations; and
- repurchased fishing rights.

However, the state's general rights over minerals underground or areas of sea within the government's jurisdiction would not normally be recognized as an asset. Undiscovered mineral resources do not usually meet the definition and recognition criteria for assets. Where rights to natural resources are not recognized, the existence of these assets may be acknowledged by way of narrative disclosure.

403. In conclusion, natural resources must meet both the definition and recognition criteria for assets before they are included in the financial statements of the government. Some natural resources may not meet the recognition criteria because of measurement difficulties.

Intangible Assets

404. In private sector accounting practice, intangible assets are held to be recognizable rights to future economic benefits. Examples include patent rights, databases and goodwill arising on purchase. The scope of intangible assets is potentially much broader in the public sector due to the wide scope of the powers of government.

405. Where the state creates and delegates powers by creating rights to fishing quota, rights to prospect, rights to use parts of the radio spectrum etc., it is creating assets which may be sold or transferred to other parties. A right available for issue by the state may often have the required characteristics of an asset. As with any intangible asset, there may be difficulties in recognition and measurement.

406. Intangible assets may be classified as identifiable or non-identifiable. Although many intangible assets will meet the definition of an asset, the recognition criteria for assets means that in practice only identifiable intangible assets are likely to be recognized. For example, the power to tax would not be recognized as an intangible asset. Some jurisdictions only allow identified intangibles or purchased goodwill to be recognized as assets. In such cases unidentified intangibles may not be recognized, even where market values are available (e.g., internally generated goodwill).

For accounting policy purposes intangible assets are classified into identifiable and non-identifiable intangible assets.

Identifiable intangible assets are those intangible assets which can be sold or acquired separately from other assets. They include rights that are created by virtue of legislation but are unconnected to natural resource use, patents, databases and concessions.

Non-identifiable intangible assets are all other intangible assets. These assets cannot be sold separately. They include goodwill, human resources and the power to tax. (New Zealand Treasury, Crown Accounting Policies for External Financial Reporting, Assets, paragraph 10, page 35, June 1995)

407. The basis of measurement of intangible assets may be historical cost or by reference to the market value of the future benefits. Loss of service potential may be assessed in relation to changes in market value of the intangible asset. An example of an accounting policy for intangible assets is shown below.

Intangible assets

Intangible assets which can be sold or acquired separately from other assets are recorded at net current value if a foreseeable future benefit exists. Otherwise, intangible assets are not recognised.

Example 12.25
Financial Statements of the Government of New Zealand
for the year ended 30 June 1999
Statement of Accounting Policies, page 62

Assets not Recognized

408. Users of financial reports prepared under the accrual basis will have the expectation that all significant assets are recognized. However, significant assets may be unreported for a variety of reasons, including:

- pragmatic reasons (classes of assets may be recognized progressively over a number of reporting periods);
- recognition criteria, particularly that of reliable measurement, may not be met; or
- the jurisdiction's policy of not recognizing certain classes of assets.

409. Some jurisdictions have chosen not to recognize certain classes of assets such as heritage and defense assets. For example, the U.S. federal government chooses not to recognize certain classes of military equipment (referred to as national defense PP&E)[4] or heritage assets in the Statement of Financial Position. It considers that the consumption of military assets' service potential through depreciation cannot be reliably measured and that the valuation of heritage assets in dollars is not objective or meaningful.

410. As previously discussed, the System of National Accounts classifies some military assets as capital expenditure (assets) and some as current expenditure (expenses). The PSC intends to conduct further work on the recommended accounting treatment for both these classes of assets.

411. Where significant assets are unrecognized, the Statement of Accounting Policies would disclose this fact, and provide narrative details of these assets. The narrative disclosures may describe the state of repair and include related operating costs. Excerpts from U.S. federal accounting standards describing required disclosures for such assets (referred to as supplementary stewardship information) are shown below.

Military Assets (National Defense Property, Plant and Equipment)

At a minimum, the following information shall be reported:

- *A description of the major types of national defense PP&E by the holding entity and the values assigned under the valuation method used.*
- *The value of national defense PP&E added and withdrawn during the year, the increase or the decrease in value resulting from revaluations of assets held to latest acquisition cost, year and the end-of-year value for each major type of property using the entity's valuation method.*
- *A description of the methods of acquisition and withdrawal of national defense PP&E. This should be reported at the major program or category level; individual transactions, unless significant, need not be reported.*
- *Condition of the assets unless it is already reported in a note to the financial statements in which case a reference to the note will suffice.*
- *A reference to the applicable note to the financial statements if deferred maintenance is reported*

[4] National defense PP&E consists of: (1) the PP&E components of weapons systems and support PP&E owned by the Department of Defense or its component entities for use in the performance of military missions, and (2) the vessels held in a preservation status by the Maritime Administration's National Defense Reserve Fleet. Space exploration equipment is treated as general PP&E. Source: SFFAS No. 11 Amendments to Accounting for Property, Plant, and Equipment – Definitional Changes October 1998.

for the assets. (SFFAS No. 8, Supplementary Stewardship Reporting, Effective: FY 1998, paragraph 68, pages 25 and 26 as amended by SFFAS No. 11 Amendments to Accounting for Property, Plant, and Equipment)

Heritage Assets

The following are examples of information that should be considered for presentation:

- *Description of each major category of heritage asset.*
- *The number of physical units added and withdrawn from the heritage asset records during the year and the end-of-year number of physical units for each type of heritage asset. Heritage assets consist of (1) collection-type heritage assets, such as objects gathered and maintained for exhibition, for example, museum collections, art collections, and library collections; and (2) noncollection-type heritage assets, such as, parks, memorials, monuments, and buildings.*
- *Description of the methods of acquisition and withdrawal of heritage assets.*
- *Condition of the assets unless it is already reported in a note to the financial statements in which case a reference to the note will suffice.*
- *A reference to a note to the financial statements if deferred maintenance is reported for the assets.* (SFFAS No. 8, Supplementary Stewardship Reporting, Effective: FY 1998, paragraph 50, page 19)

412. Refer also to Chapter 16 for a discussion of additional disclosures in the financial statements.

413. Examples of the disclosure of assets not recognized are shown below.

> 1.40 Certain collection assets such as library, museum and archival collections and other heritage assets, such as national parks, have either not been recognised and/or revalued as reliable measurement of these assets is not available at this time.

Example 12.26
Financial Statements of the Commonwealth Government of Australia
for the year ended 30 June 1997
Notes to and forming part of the Financial Statements, page 40

U.S. GENERAL ACCOUNTING OFFICE
ANNUAL STEWARDSHIP INFORMATION
AS OF SEPTEMBER 30, 1998

Heritage assets are property, plant, and equipment (PP&E) possessing one or more of the following characteristics: historical or natural significance; cultural, educational, or aesthetic value; or significant architectural characteristics. In general, the cost of heritage assets is not often relevant or determinable, and the useful life of heritage assets is not reasonably estimable for depreciation purposes. Rather, the most relevant information about heritage assets is their existence and condition. Therefore, heritage assets are required to be reported only in terms of physical units. However, in the case of the GAO building, its value is known as described below.

On October 28, 1988, Public Law 100-545 transferred control of the General Accounting Office building and land in Washington, D.C., from the General Services Administration to GAO without a monetary exchange. At the time of transfer, the depreciated value of the building was $15,664,000, and the book value of land was $1,191,000. GAO recorded the building and the land as assets at the values stated above.

The GAO building is listed in the National Register of Historic Places as a symbol of a new age in federal office design. The building holds historical significance as the first structure erected exclusively for occupancy by the General Accounting Office. It was one of the first federal office buildings to be completely air-conditioned and artificially lit; and it was the first modern, block-type building to be constructed for the federal government. Its construction marked a distinct departure from the “fish-bone” type of office building, which used either interior courts or a series of wings branching from a central spine in order to provide both air and light.

Statement of Federal Accounting Standards Nos. 6 and 8 require that heritage assets be reported in a separate stewardship reporting section and not on the SOFP. GAO removed the building and land from the SOFP with the preparation of its 1996 principal statements.

Since acquiring control of the building, GAO has expended considerable resources for renovation and improvement of the building, including asbestos abatement, major redesign of office space, installation of communication wiring for local area network, upgrading of fire alarm system, and renovation of the parking garage—all to enhance use of the building for operating purposes. The costs of these projects have been capitalized as general PP&E and depreciated over their expected useful lives. Building improvement for operational efficiency is expected to continue.

Maintenance of the building has been kept on a current basis, and the expense is recognized as incurred. There is no significant deferred maintenance cost.

Example 12.27
Comptroller General’s 1998 Annual Report, United States General Accounting Office (GAO)
Annual Stewardship Information, pages 77 and 78 (USD)

Administered Assets

414. A government entity will normally recognize only those assets which it controls. However, government entities may administer assets on behalf of another level of government, or another entity (e.g., trust accounts which the entity does not control, and advances of funds received by the entity with respect to administered transfers). Where administered assets are not regarded as being within the control of the reporting entity, accountability for the management of such assets may be demonstrated by disclosing information in either the Notes to the Financial Statements or a separate Schedule. However, there are a range of practices associated with the reporting of administered assets and some entities include such funds as both assets and liabilities in the Statement of Financial Position. This latter practice usually occurs where the money held in trust is not distinguishable from other funds or in bank accounts.

> *"Different models of administrative arrangements in different jurisdictions mean that the manner in which administered transactions are displayed in the financial report may vary from jurisdiction to jurisdiction."* (AAS 29, 1996, paragraph 13.9.4)

415. Refer also to Chapters 13, 14 and 15 for a discussion of administered liabilities and administered transactions.

416. Examples of disclosure of administered assets are shown below.

18. TRUST FUNDS	**96-97 $m**	**95-96 $m**
Budget Sector	119	37
Non Budget Sector	1,424	1,114
	1,543	1,151
Trust monies are held by the trustee on behalf of beneficiaries. Therefore, these monies are not included in the consolidated financial statements assets.		
Budget Sector trust monies mainly comprise various forms of unclaimed monies and Supreme Court trust funds held in statutory accounts as follows:		
Health Department	82	-
Attorney General's Department	10	19
Others	27	18
	119	37
Trust monies held by Non Budget Sector agencies include: -		
Protective Commissioner	726	612
NSW Treasury Corporation	174	340
Rental Bond Board (see Note 1 Change in Accounting Policy)	363	-
Others	161	162
	1,424	1,114

Example 12.28
Consolidated Financial Statements of the NSW Public Sector 1996–97
The NSW Public Sector, Notes to and forming part of the Financial Statements, page 41 (AUD)

Note 18. Indian Trust Funds

The Indian Trust Funds differ from other dedicated collections reported in Note 17.

The Department of the Interior (Interior) has responsibility for the assets held in trust on behalf of American Indian Tribes and individuals. Trust funds are held in accounts for approximately 315 tribes, 317,000 individual Indian Accounts and other funds, including the Alaska Native Escrow Fund. The assets held in trust for Native Americans are owned by the trust beneficiaries and are not Federal assets. Therefore, these amounts are not reflected in the Balance Sheet or Statement of Net Cost.

Indian Trust Fund balances presented below do not include trust land managed by the Government.

U.S. Government as Trustee for Indian Trust Funds
Held for Indian Tribes and Other Special Trust Funds
Statement of Changes in Trust Fund Balances as of September 30
(Unaudited)

(In millions of dollars)

Receipts …………………………………	521.7
Disbursements …………………………………	(465.4)
Receipts in excess of disbursements …………………	56.3
Trust fund balances, beginning of year …………………	2,403.7
Trust fund balances, end of year …………………	2,460.0

U.S. Government as Trustee for Indian Trust Funds
Held for Individual Indian Monies Trust Funds
Statement of Changes in Trust Fund Balances as of September 30
(Unaudited)

(In millions of dollars)

Receipts	313.6
Disbursements …………………………………	(354.1)
Disbursements in excess of receipts …………………	(40.5)
Trust fund balances, beginning of year …………………	519.7
Trust fund balances, end of year …………………	479.2

Example 12.29
Financial Report of the United States Government – 1998
Notes to the Financial Statements, page 81(USD)

Classification

417. Classification depends upon users' needs and on how best they can be met. The following constraints are also important:

- level of detail of the information required;
- the ability to classify the information and the reliability of the resulting numbers; and
- benefit versus cost.

418. Common classifications of assets include classification by liquidity and classification by function. These classifications are discussed below. The System of National Accounts and the Government Finance Statistics also have classification systems for assets. These are discussed in Chapter 19.

Classification – Broad Order of Liquidity

419. Assets may be classified and disclosed according to the broad order of their liquidity. The main basis for deciding the number of classes and the content of each is the purpose of the Statement of Financial Position, which helps users to assess the nature, amounts, and liquidity of available resources and their function in use. Alternatively, reporting which distinguishes assets by function may assist users to estimate the amounts, timing and uncertainty of future cash flows. For example, assets held for sale may be reported separately from assets held for use in production, because of the potential effects of each in the timing of future cash flows. In addition, assets may be grouped according to the relative certainty of their valuation.

420. Assets may also be classified as current or non-current. It is unusual for a government to be assessed in terms of its continued existence as a going concern, and the categorization of assets and liabilities as current will at best usually only provide indications of short-term funding requirements. However, the distinction informs users about the entity's acquisition of current assets and its intentions to dispose of certain assets and is considered to be useful in some jurisdictions. Information using both types of classification may be provided as in the following example. In this example information on all asset and liability types has been shown in the financial statements together with a brief summary of current and non-current assets and liabilities at the foot of the statement.

ASSETS AND LIABILITIES
as at 30 June 1997

	Note	1997 $m	1996[1] $m
	: :	: :	: :
FINANCIAL ASSETS			
Cash	**2(b)**	3,203	3,788
Receivables	**27**	33,251	31,203
Investments	**28**	35,631	34,472
Accrued revenue	**29**	26,010	23,594
Other financial assets	**29**	936	179
Total financial assets		**99,031**	**93,236**
NON-FINANCIAL ASSETS			
Land and buildings	**30**	20,345	26,540
Infrastructure, plant and equipment	**30**	52,468	47,336
Intangibles	**30**	2,284	251
Inventories	**31**	6,156	6,517
Other non-financial assets	**32**	1,503	1,885
Total non-financial assets		**82,756**	**82,529**
Total assets		**181,787**	**175,765**
Current liabilities		58,824	52,253
Non-current liabilities		197,518	195,345
Current assets		54,722	56,866
Non-current assets		127,065	118,899

The above statement should be read in conjunction with the accompanying notes.
[1] Trial and unaudited.

Example 12.30
Financial Statements of the Commonwealth Government of Australia
for the year ended 30 June 1997
Assets and Liabilities, page 24 (AUD)

Classification – Financial and Non-financial

421. Assets may be classified as financial and non-financial. Non-financial assets may be further classified as physical assets and intangible assets. An example of the financial/non-financial classification is shown in Example 12.30.

Classification – Restricted, Unrestricted, Secured Assets

422. Secured assets are those specific assets which have been identified as being reserved to a lender in the event of default. It is accepted practice in private sector financial reporting that where assets are disclosed, secured assets are disclosed separately from unsecured assets in the Notes to the Financial Statements. The term restricted assets is applied where assets are disclosed but are subject to restrictions as to disposal of the asset or income derived from its use; such assets are often those donated to the entity for a specific purpose (CICA 1989). Other restrictions may be imposed by statute, as in a restriction of the right to dispose of reserve land or national parks. External restrictions on assets may also arise as a result of an agreement with external parties to set aside assets for a specific purpose, such as sinking funds set aside to retire debt or unspent debenture proceeds of a local government earmarked for specific capital works. The disclosure of restrictions relating to revenues and assets is discussed in CICA PS 3100.

423. Assets may also be classified by legal conditions accepted by government as part of the appropriation process or obligations to lenders, including lenders at a higher level of government.

CHAPTER 13

ACCRUAL BASIS – LIABILITIES

Introduction

424. The issues associated with accounting for and reporting liabilities in the public sector have been addressed in PSC Study 6 *Accounting for and Reporting Liabilities*, and are discussed further in this Chapter. The Liabilities Study considered the application of the liability definition and liability recognition criteria in the public sector. It concluded that the IASC definition and recognition criteria are generally appropriate for the public sector, although there may be some unique issues in the public sector, such as the treatment of some government obligations. This Chapter discusses the types of liabilities in the public sector, and the recognition and classification of these liabilities.

Definition of Liabilities

425. The IASC Framework for the Preparation and Presentation of Financial Statements defines a liability as:

> *…a present obligation of the enterprise arising from past events, the settlement of which is expected to result in an outflow from the enterprise of resources embodying economic benefits.* (paragraph 49)

426. The fundamental characteristics of liabilities identified by the IASC are:

- the existence of a present obligation arising from past events. That is, a transaction or other event in the past has given rise to a "duty or responsibility" to a third party, which has not yet been satisfied; and
- that liabilities have adverse financial consequences for the reporting entity. That is, the entity is required to incur additional liabilities, or dispose of cash or other assets to one or more entities, to settle the obligation.

427. PSC Study 6 reviewed the definitions of liabilities used by governments in a variety of countries and found that most of these definitions were consistent with the fundamental characteristics described above.

Recognition of Liabilities

428. Liabilities should be recognized when they meet both the definition of a liability and the recognition criteria for liabilities. The recognition criteria, as given by the IASC Framework for the Preparation and Presentation of Financial Statements, are:

> *…it is probable that an outflow of resources embodying economic benefits will result from the settlement of a present obligation and the amount at which the settlement will take place can be measured reliably.* (paragraph 91)

429. Before liabilities may be recognized in the financial statements they must both :

- meet the definition of a liability; and
- satisfy the recognition criteria.

430. All liabilities which meet the definition and recognition criteria should therefore be recognized. Two items which often do not meet the definition and recognition criteria are commitments and contingencies. If these items meet the definition and recognition criteria then they are recognized as liabilities and included within the financial statement totals. However, where they do not meet the definition and recognition criteria then information concerning them is usually shown in the Notes to the Financial Statements.

431. As financial statements attempt to capture liabilities, some of which will be settled well into the future, measurement difficulties arise. Many liabilities have to be estimated. The fact that amounts to be paid involve an estimate would not be sufficient reason to defer recognition of a liability. Provided that the measurement technique chosen is an accepted method, an estimate of a large liability is preferable to ignoring the existence of the liability. For example, various methods have become accepted for the estimation of future insurance claims or pension liabilities.

Types of Liabilities

432. The types of liabilities that governments may report include:

- accounts payable arising from the purchases of goods and services;
- accrued interest payable;
- accrued salaries and wages;
- accrued vested vacation pay or other accrued compensated absences;
- employee pension obligations and other accrued employee benefits, including any accrued termination benefits;
- amounts payable under guarantees and indemnities where sufficient evidence is available to indicate that it is more likely than not that the amounts will be payable;
- liabilities relating to unearned revenues;
- transfer payments payable;
- currency issued;
- lease obligations related to finance leases;
- bank loans and other short-term borrowings;
- long-term debt (both to the private sector and to other government entities);
- environmental liabilities; and
- obligations under accident compensation schemes.

433. Most of these liabilities are similar to those of business enterprises and do not pose unique accounting or reporting issues for governments. Government liabilities include transfers payable and currency issued. Government transfers payable arise from entitlements, shared cost agreements or grants where there is not a direct exchange relationship with the recipient. In concept, liabilities associated with transfer payments are not significantly different from other accounts payable. The main difference between these payables and other accounts payable is the lack of a direct exchange relationship. As there is no point of exchange, a different recognition point must be identified.

434. Occasionally the issue arises as to which entity should recognize certain liabilities, particularly where there are two levels of government involved. For example, environmental liabilities may be due to past actions of the government as a whole although the liability is associated with the property of a particular government agency. The liability will usually be recognized by the party with the legal responsibility for clean up costs, although any compensating contributions from other levels of government may be recognized as a receivable if the contributions meet the recognition criteria for receivables.

435. Receipts of unearned revenues are only recognized as liabilities if they meet the recognition criteria for liabilities. The recognition criteria would be met if there are clearly defined obligations relating to the revenue which would result in a sacrifice of future economic benefits by the reporting entity, such as the requirement to deliver goods and services in the future. Where there was no clearly defined future obligation, such receipts would not meet the recognition criteria.

436. The definition of a liability may also be applied to current and potential future obligations. At one extreme, legally enforceable obligations, such as those arising from binding contracts, clearly meet the definition of a liability. Such obligations may exist as a result of reciprocal or “exchange” transactions (e.g., purchases of goods or services), or unpaid amounts due under non-reciprocal or “non-exchange” transactions (e.g., grants or entitlements). It can be argued that, in the government context, the existence of a present obligation arising from past events occurs only when there is a legal

obligation. The legal obligation could be the result of contracts, agreements or legislation that commit the government to:

- repay borrowings;
- pay for goods and services acquired or provided prior to the accounting date;
- provide services or use resources in a specified way; or
- make transfer payments, even where no value is received directly in return (e.g., entitlements, shared cost agreements or grants).

437. Usually, an external party has a legal right of recourse if the government fails to meet the terms of the contracts, agreements or legislation.

438. In addition to legally enforceable obligations, most governments have established programs to fulfill many of the general needs of the public, and often assume responsibilities for which they have no prior legal obligation. Examples of items which may or may not meet the definition of liabilities include:

- moral or equitable obligations to provide relief to victims of natural disasters;
- the announcement of a new program or spending initiatives; and
- future obligations under current policies.

439. It is necessary to consider these equitable or constructive obligations more carefully to see whether they meet the definition of a liability. They are discussed in later in this Chapter (Future Obligations under Current Policies). Some accounting standard setting bodies have already considered this issue in the context of their own jurisdiction. For example, Australian Accounting Standard AAS 31 *Financial Reporting by Governments* states that "The intention of a government to make payments to other parties, whether advised in the form of a budget policy, election promise, or statement of intent, does not of itself create a present obligation which is binding on the government. A liability would be recognized only when the government is committed in the sense that it has little or no discretion to avoid the sacrifice of future economic benefits." (paragraph 12.1.2)

440. Two additional criteria which may be useful in assessing the difference between legal obligations and policy decisions are:

- whether or not the government has the discretion to avoid the obligation; and
- whether or not the government can vary its liability in the normal course of events without the consent of the party affected.

441. Another useful perspective is to consider whether the other party or parties involved could reasonably be considered to have a corresponding asset.

442. Although contingencies and commitments may result in sacrifices of future economic resources, they may not meet either or both of the definition or recognition criteria for liabilities. These items are both discussed in more detail later in this Chapter.

443. The following sections discuss definition, recognition and measurement issues associated with particular public sector liabilities.

Payables and Accrued Liabilities

444. Accounts payable (sometimes referred to as trade creditors) are usually amounts owing to a creditor, arising from the purchase of goods or services. At the end of the accounting period an invoice for these items would generally have been received. In the public sector payables can also include transfers payable which are the amounts actually owed, as at the end of the accounting period, to recipients of non-reciprocal transfers (discussed later in this Chapter). Payables differ from accrued liabilities in that the amounts concerned are due and payable at the end of the accounting period. In contrast accrued liabilities represent an estimate of a liability that is not supported by an invoice or a request for payment at the time the financial statements are prepared. The accrued liability is in relation to an expense which has been incurred by the end of the accounting period but which is not due for payment until a future date. An example of an accrued liability would be an estimate of rent expense owed at the end of the accounting period when rent is paid in arrears.

Transfers Payable

445. The recognition of various types of government transfers and the liabilities associated with those expenses are discussed in Chapter 15 under Government Transfers.

446. Chapter 15 states that when determining the amount of the expense and any associated liability to be accrued in the current financial statements for those receiving entitlements in the current period, only those amounts already owed, but not yet paid, meet the definition and recognition criteria for liabilities. Amounts are "owed" by the government when the external beneficiary has satisfied the conditions for the transfer during the reporting period. Potential obligations arising from an existing policy, but relying on a future event (e.g., a person becoming or remaining unemployed next year) are not considered to be "owed" at the present time and are therefore not recognized as liabilities. However, in some jurisdictions liabilities for future obligations under current policies may be recognized (refer also to the more detailed discussion later in this Chapter). Where future obligations do not meet the recognition criteria a description of the item and an actuarial valuation of the possible amount may be disclosed in the notes to the financial statements.

447. Generally the estimated, unpaid portion of incurred eligible expenditures owed to recipients pursuant to a shared cost agreement would meet the definition and recognition criteria for liabilities.

448. A survey reported in PSC Study 6 *Accounting for and Reporting Liabilities* shows the following accounting practices regarding transfer payments:

Transfer payments payable (e.g., grants, entitlements)

Australia	Obligation is recognized and measured on the basis of the best estimate of the amount payable as at the reporting date.
Canada	Recorded in the financial statements at estimated amount ultimately payable, as long as terms and conditions, if any, have been met.
France	Recorded in the financial statements at commitment specified by laws.
Italy	Recorded in the financial statements at commitment specified by laws.
Netherlands	Recorded in the financial statements at historical cost.
New Zealand	Recorded in the financial statements at estimated obligation to pay (for benefit applications accepted where eligibility criteria have been met).
Taiwan	Recorded in the financial statements based on approved budget.
United Kingdom	Recorded in the financial statements at actual amounts due but unpaid.
United States	Recorded in the financial statements at amounts due but unpaid.

(PSC Study 6, Appendix 1, page ii)

449. When the amounts involved are not material, transfers payable may be reported together with other accounts payable.

Transfers Received

450. Governments which receive transfers from another level of government or a supranational body may need to consider whether transfers received meet the definition and recognition criteria for liabilities. Where there are restrictions on the use of funds until certain obligations have been met, and those obligations are clearly specified, then they may meet the definition and recognition criteria for liabilities. This issue is discussed further in Chapter 14.

Currency Issued

451. Where the reserve or federal bank forms part of the government reporting entity, currency issued is recorded as a liability. This treatment is similar to banks recording deposits as liabilities. The interest earned on the proceeds of currency issued is accounted for in the same way as other interest revenue. Such interest may be referred to as seigniorage.

452. Under accrual accounting, only the consideration received from the issue of currency is recorded as an asset. The power to create money in the future does not meet the definition and recognition criteria for an asset. Examples of accounting policies for currency issued are shown below.

> **Australian currency on issue**
> 1.43 Australian currency issued represents a liability of the Reserve Bank of Australia in favour of the holder. Currency issued for circulation including demonetised currency is measured at face value. When the Reserve Bank issues currency notes to the commercial banks, it receives in exchange funds equal to the full face value of the notes issued.

Example 13.1
Financial Statements of the Commonwealth Government of Australia
for the year ended 30 June 1997
Notes to and forming part of the Financial Statements, page 41

> **Currency issued**
>
> Currency issued represents a liability in favour of the holder. Currency issued for circulation, including demonetised currency, is recognised at face value.
>
> Unissued currency stocks are reported as inventory and expensed when issued.

Example 13.2
Financial Statements of the Government of New Zealand
for the year ended 30 June 1999
Statement of Accounting Policies, page 63

Long-Term Debt and Borrowings

453. Long-term debt and borrowings will constitute the largest liability of many governments. Liabilities denominated in foreign currencies are normally valued at the closing rate. The treatment of foreign currency gains and losses is discussed more fully in Chapters 14 and 15.

454. Information to describe the nature and terms of a government's liabilities for borrowing would include:

- the amounts outstanding, interest rates and sinking fund amounts;
- the amounts payable on demand, within each of the next five years and appropriate description of other long-term borrowing payment dates and amounts;
- the amounts payable in foreign currencies, the currency in which such amounts are payable, the reporting currency equivalent and the basis of translation; and
- the terms and conditions of financial swap agreements.

455. Information to describe the nature and terms of a government's liabilities to other governments would include, at least, the amounts outstanding, interest rates, the amounts payable within a year and appropriate description of amounts payable after one year.

456. The main issue regarding domestic currency liabilities is whether they should be measured at face value or current market values. A common practice is to use face value in the financial statements but to disclose market values in the notes, where this information is available. Normally market information is readily available, as it is usual to mark-to-market when managing a debt portfolio. The measurement of financial assets and liabilities has been considered by the IASC in IAS 39, *Financial Instruments: Recognition and Measurement.* In summary, IAS 39 requires that:

- financial liabilities should be initially measured at cost;
- most financial liabilities should subsequently be measured at initial recorded cost amount less principal repayments and amortization; and
- derivatives and liabilities held for trading are remeasured to fair value.

457. The Financial Statements of the Government of New Zealand provide an analysis of borrowings by book value and by nominal and market value. They also include a maturity profile for borrowings, and movements during the year. Each analysis provides details of New Zealand-dollar debt and foreign currency debt. An example of the Statement of Borrowings is located in Appendix 2. Examples of note disclosure of borrowings follow.

12. BORROWINGS	**96-97 $m**	**95-96 $m**
Current	6,085	4,449
Non current	22,605	24,279
	28,690	28,728
Borrowings comprise:		
Liability to Commonwealth Government	3,641	4,097
Domestic and foreign borrowings	23,959	23,984
Bank overdraft	776	420
Finance leases[(a)]	314	227
	28,690	28,728
The maturity profile of borrowings at current capital value (1995-96 at face value):		
Not later than one year	6,085	4,700
Between one and two years	2,137	5,398
Between two and five years	11,469	6,816
Later than five years	8,999	13,207
	28,690	30,121
[(a)]Finance leases liabilities are payable as follows:		
Not later than one year	54	35
Between one and two years	53	62
Between two and five years	130	90
Later than five years	527	294
Minimum lease payments	764	481
Less: Future finance charges	(450)	(254)
Finance lease liability	314	227

Example 13.3
Consolidated Financial Statements of the NSW Public Sector 1996–97
The NSW Public Sector, Notes to and forming part of the Financial Statements, page 37 (AUD)

9. External Borrowing

External borrowing is used, within limits set by the government, to finance capital expenditure. Loans held at the year end were:

		31.3.98		31.3.97	
		£000		£000	
Total external borrowing at 31 March		**140,567**		122,133	
Less loans repayable on demand or within 12 months		**14,312**		16,474	
Total external borrowing at 31 March not repayable within the next 12 months		**126,255**		105,659	
Made up of	- Public Works Loans Board	**96,379**		70,659	
	- European Investment Bank	**24,876**		25,000	
	- Commercial Bank	**5,000**		5,000	
	- Nationalised Industries	**0**		5,000	
		126,255		105,659	
These loans mature as follows …		**£000**	**%**	£000	%
Repayable within	- one to two years	**10,529**	**8.3**	5,124	4.9
	- two to five years	**27,522**	**21.8**	32,379	30.6
	- five to ten years	**34,292**	**27.2**	28,963	27.4
	- over ten years	**53,912**	**42.7**	39,193	37.1
		126,255	**100.0**	105,659	100.0

Example 13.4
Surrey County Council
Statement of Accounts 1997/98
Consolidated Balance Sheet Notes, page 34 (GBP)

Lease Obligations Relating to Finance Leases

458. IAS 17, *Leases* (paragraph 12) requires private sector entities which purchase assets by way of finance lease to recognize both a liability and an asset. This prevents entities from obtaining assets without showing the corresponding liability for future lease repayments. Where government entities enter into finance leases they too face similar asset and liability recognition issues. The types of arrangements which governments enter into may range from straightforward finance leases to arrangements which encompass both the purchase of an asset and the services associated with that asset (e.g., a hospital and the building maintenance or cleaning services for it). Where such contracts include an identifiable finance lease then the guidance in IAS 17 may be relevant.

Employee Entitlements (including Superannuation/Pension Liabilities)

459. Leave accrual ensures that personnel costs are shown in the period in which they occur. It also provides information about the future obligations facing the government as an employer. The presentation and disclosure of the accounting policies adopted in relation to recognition of expenses is essential.

460. Types of leave which are commonly accrued include:

- annual leave;
- long service leave;
- retirement leave; and
- special leave entitlements.

461. Other types of leave are not accrued because they are taken on the basis of need, rather than vesting in the employee or providing an absolute entitlement. Therefore no liability exists until the specified event occurs.

462. The nature of a government's obligation to employees under superannuation/pension schemes will vary across jurisdictions. Some schemes may be fully funded, with both the government and the employee making regular contributions which are sufficient to cover the final employee benefits. Other schemes may operate on a pay-as-you-go basis. In such schemes the employee may make a regular contribution to the scheme, but the government contributes only the amount required to pay the amounts currently owing to retired employees. In some cases it may be possible for a government to unilaterally change employees' entitlements, and in other cases this may not be possible. Despite these differences between jurisdictions, the process for ascertaining and recognizing superannuation/pension liabilities remains the same.

463. Preparers of financial statements should determine first whether the government's obligation to employees meets the definition of a liability, and then whether the obligation meets recognition criteria. The extent to which a government is able to change the future benefits to employees will affect the probability of future payments being made and would need to be assessed at this point. Such liabilities may be legally enforceable or equitable or constructive. The fact that a liability is equitable or constructive does not mean that it does not meet the definition of a liability, but the likelihood of the obligation resulting in a future payment would need to be considered. For example, this point has been considered in the Australian SAC 4: *Definition and Recognition of the Elements of Financial Statements*. In many cases the government's obligation will meet both the definition and recognition criteria.

464. Each year, as current employees earn an entitlement to future benefits, the total cost (both cash and non-cash) of providing these future superannuation/pension benefits is recognized as an expense by the employing government. If regular payments equal to this expense are made to the superannuation/pension scheme the scheme is referred to as a funded scheme. Where payments are less than the expense the scheme is referred to as an unfunded, or a partially funded, scheme. The unfunded component of superannuation/pension benefits may be shown as an accumulating liability on the Statement of Financial Position. When payment for the liability is finally made in future periods, the payment is offset against the liability. As the expense has been previously recorded there is no need to recognize the payment as an expense at that point. Not all jurisdictions follow the practice of recognizing these amounts as liabilities in the Statement of Financial Position. Instead, some jurisdictions provide note disclosure of these amounts.

465. The size of the accumulated liability will depend, in part, upon the type of scheme operating in a jurisdiction. If superannuation/pension schemes are fully funded then the accrued liability may be non-existent or negligible. However, in an unfunded, or pay-as-you-go scheme, this liability may be substantial and may significantly alter the ratio of net assets/equity to Gross Domestic Product.

466. An example of the relative size of this liability is illustrated by the following figures taken from the Financial Statements of the Government of New Zealand for the year ended 30 June 1999.

	$m
Total assets	58,223
Total liabilities (including pension liabilities)	52,201
Pension liabilities	8,524

467. Reliable valuations of the future liability may be performed by an actuary. Examples of accounting policies for, and note disclosure of, employee entitlements and superannuation/pension liabilities are shown below.

Pension liabilities

Pension liabilities in respect of the contributory service of superannuation scheme members are recorded at the latest actuarial value of the Crown's liability for pension payments, net of the schemes' assets.

Compensated absences

Liabilities for annual leave are recognised as they accrue to employees. Provision is also made for expected payments of long-service and retiring leave obligations to employees.

Example 13.5
Financial Statements of the Government of New Zealand
for the year ended 30 June 1999
Statement of Accounting Policies, page 63

Employee Entitlements

Wages and Salaries, Annual Leave and Sick Leave

Liabilities for wages and salaries, annual leave and vested sick leave are recognised and are measured as the amount unpaid at balance date at current pay rates in respect of employees' services up to that date.

Non-vested sick leave is generally not recognised as future sick leave taken is not expected to exceed future entitlements accruing.

Long Service Leave

A liability for long service leave is recognised. It is measured at either the present value of expected future payments to be made in respect of services provided by employees up to the balance date or by applying the 'nominal method'. The 'nominal method' is an estimation technique which is considered to be adequate in reliably measuring the liability in certain circumstances. It is calculated by applying the current remuneration rates to the entitlements at year end for all employees with five or more years of service.

Major Non Budget agencies and Area Health Services have applied the present value basis. In doing so, consideration is given to expected future wage and salary levels., experience of employee departures and periods of service. Estimated future payments are discounted to present values. All other agencies have continued to apply 'the nominal method'.

Superannuation

An unfunded superannuation liability is recognised in respect of the defined benefit schemes. It is measured as the difference between the present value of employees' accrued benefits at balance date and the net market value of the superannuation schemes' assets at that date. The liability is assessed annually by the Government Actuary based on data maintained by the Superannuation Administration Authority. It is calculated based on the latest actuarial triennial assessment adjusted for any subsequent material movements in value.

The present value of accrued benefits is based on expected future payments which arise from membership of the fund to balance date in respect of the contributory service of current and past government employees. Consideration is given to expected future wage and salary levels, expected future investment earning rates, growth rate in the Consumer Price Index, experience of employee departures and periods of service.

Example 13.6
Consolidated Financial Statements of the NSW Public Sector 1996–97
The NSW Budget Sector, Notes to and forming part of the Financial Statements, page 67 (AUD)

13. EMPLOYMENT ENTITLEMENTS	96-97 $m	95-96 $m
Current	2,295	2,545
Non current	14,512	16,785
	16,807	19,330

Employee Entitlements comprise:

	96-97 $m	95-96 $m
Unfunded superannuation	12,789	15,435
Long service leave and other leave entitlements	3,642	3,628
Other salary related liabilities	376	267
	16,807	19,330

Unfunded Superannuation Liability

The Public Sector's unfunded superannuation liability for the various defined benefits schemes is assessed each year by the Government Actuary based on data maintained by the Superannuation Administration Authority. It is based on the latest triennial actuarial assessment adjusted for any subsequent movements in value.

These calculations are generally based on actual data up to 30 June 1997. The underlying demographic assumptions are consistent with the 1994 triennial valuation of the Pooled Fund Superannuation Schemes. However, the economic assumptions contained in the 1994 valuation have been revised to reflect prevailing economic conditions and to be consistent with the requirements of Australian Accounting Standard AAS25 "Financial Reporting by Superannuation Plans".

The key economic assumptions as at 30 June 1997 underlying the unfunded liabilities are:

	1997-98	1998-99	1999-2000	Thereafter
Earning rate	7.0%pa	7.0%pa	7.0%pa	7.0%pa
Salary growth rate	3.7%pa	4.0%pa	4.5%pa	5.0%pa
CPI growth rate	2.1%pa	2.5%pa	3.0%pa	3.5%pa

Unfunded superannuation liabilities as at 30 June 1997 have decreased by about $2.6 billion compared to the previous year.

The bulk of the reduction resulted from a number of major positive adjustments to employee reserves that were brought to account by the Superannuation Administration Authority in 1996-97. These adjustments related to the allocation to employer reserve accounts of Pooled Fund tax credits, State Superannuation Scheme Contributors' Reserves, amount arising from corrections to employers' annual statements and additional interest earnings.

The balance of the decrease in unfunded liabilities was due to an adjustment made by the Government Actuary to the value of accrued benefits to recognise changes in fund membership and valuation assumptions to reflect current actuarial factors.

The unfunded superannuation liability is composed of:	96-97 $m	95-96 $m
Pooled Fund		
• State Authorities Superannuation Scheme	2,214	2,075
• State Authorities Non Contributory Superannuation Scheme	876	654
• State Superannuation Scheme	6,287	9,013
• Police Superannuation Scheme	2,495	2,800
Judges' Pension Scheme	194	147
Parliamentary Contributory Superannuation Scheme	70	65
State's share of University superannuation liabilities	652	678
Other	1	3
	12,789	15,435

Example 13.7
Consolidated Financial Statements of the NSW Public Sector 1996–97
The NSW Public Sector, Notes to and forming part of the Financial Statements, pages 37 and 38 (AUD)

Note 10. Federal Employee and Veteran Benefits Payable

The Government offers its employees, both civilian and military, retirement benefits, life and health insurance, and other benefits.

The Federal Government administers more than 40 pension plans. The largest are administered by the Office of Personnel Management (OPM), for civilian employees, and by DOD, for military personnel. The Government has both defined benefit and defined contribution pension plans. The largest are defined benefit plans.

Federal Employee and Veteran Benefits Payable as of September 30

(In billions of dollars)	Civilian	Military	Total
Pension liability ………………………	996.4	650.5	1,646.9
Health benefits payable ……………..	181.8	223.4	405.2
Veterans compensation and burial benefits …………………	-	578.1	578.1
Liability for other benefits ……………	34.1	20.8	54.9
Total Federal employee and veteran benefits payable …….	1,212.3	1,472.8	2,685.1
: :	: :	: :	: :

Significant Assumptions Used in Determining Pension Liability and the Related Expense

(In percentages)	Civilian	Military
Rate of interest …………………………	7.0%	6.5%
Rate of inflation…………………………	4.0%	2.1%
Projected salary increases ……………	4.3%	2.8%

Example 13.8
Financial Report of the United States Government – 1998
Notes to the Financial Statements, page 72 (USD)

Note 13. Other Liabilities

: : : : : :

"Accrued wages and benefits" consist of the estimated liability for civilian and commissioned officers' salaries and wages earned but unpaid. It also includes funded annual leave and other employee benefits that have been earned but are unpaid.

: : : : : :

Other Liabilities as of September 30

(In billions of dollars)

: : : :	: :
Accrued wages and benefits	11.1
: : : :	: :

Example 13.9
Financial Report of the United States Government – 1998
Notes to the Financial Statements, page 76 (USD)

Land Claims by Indigenous People

468. Governments in some countries are subject to land claims by indigenous people. These land claims may be in respect of land still owned by the government or land initially taken over by the government but now owned by private individuals. Liabilities may be settled by negotiation or through the legal system. Prior to any acceptance of liability or a decision by the courts, a contingent liability may exist. Once an agreement has been reached, or judgment obtained through the legal system, then a liability exists which meets the recognition criteria. Land claims may be settled by way of monetary compensation or by transfer of land. If the liability is to be settled by transfer of land, the liability will reflect the value of the land. An example of recognition of a land claim as a contingent liability is shown under the discussion of contingent liabilities in this Chapter.

Moral or Equitable Obligations to Provide Relief to Victims of Natural Disasters

469. Governments may have open-ended obligations for natural disasters. Preparers of financial statements need to determine the point at which transfer payments and the associated liability to rectify such damage should be recognized. In the case of a natural disaster the clean up costs etc., do not meet the definition of a liability until the government accepts responsibility for them. This would be the case where the government has a clear and formal policy regarding compensation or clean up costs. At this point, assuming that the costs are both probable and measurable, the liability would then be recognized.

Environmental Liabilities

470. Although a relatively recent category of liabilities, environmental liabilities may nonetheless be significant. Many countries now have environmental laws and regulations which place responsibility for damage to the environment onto the party causing the damage or onto the present owner of property. In some cases the government may be the party which has either caused the damage and/or be the current owner of the property. When determining how to report environmental liabilities in the financial statements it is necessary to consider whether the event giving rise to a liability has occurred and whether the ensuing liability is both probable and measurable. For example, if the government damages property and is liable to provide compensation under existing laws, then the government has incurred a liability.

471. One of the difficulties associated with environmental liabilities is assessing the extent to which damage has been done, and the cost of rectifying the damage or complying with existing laws. Where it is not possible to quantify the amount of an environmental liability then the liability would not be recognized within the financial statement totals, but the existence of the liability and a description of the extent of the potential liability could be provided by way of additional note disclosure.

472. The potential size of environmental liabilities are illustrated in the following excerpts from the financial statements of the United States Government.

> Another liability, which will likely require substantial future budgetary resources to liquidate, is related to environmental clean-up costs. As of September 30, 1998, the cost of cleaning up environmental contamination was estimated to be $224.5 billion.

Example 13.10
Financial Report of the United States Government – 1998
Management's Discussion and Analysis, page 9 (USD)

Note 11. Environmental Liabilities

Environmental Liabilities as of September 30		
(In billions of dollars)		
Energy:		
Environmental management and legacy waste …………………………….	145.1	
Active facilities …………………………………	19.6	
High-level waste and spent nuclear fuel…….	10.7	
Pipeline facilities ………………………………	7.8	
Other ……………………………………………	3.2	
Total Energy ………………………………..		186.4
DOD ………………………………………………		34.0
All other agencies ………………………………		4.1
Total environmental liabilities …………….		224.5

During World War II and the Cold War, the United States developed a massive industrial complex to research, produce and test nuclear weapons. The nuclear weapons complex included nuclear reactors, chemical processing buildings, metal machining plants, laboratories and maintenance facilities. The costs associated with removing, containing and/or disposing of hazardous waste from the properties comprise the resulting environmental liabilities. "Environmental liabilities", in this report, apply only to required cleanup costs from Federal operations known to result in hazardous waste resulting from approved Federal, State or local statutes and/or regulations.

Energy incurred operating and capital expenditures totaling $6.3 billion in fiscal 1998 to remediate legacy waste. This includes nuclear material and facility stabilization as well as waste treatment, storage and disposal activities at each installation.

"Environmental management and legacy wastes" include costs for environmental restoration, nuclear material and facility stabilization, and waste treatment, storage and disposal activities at each installation. They also include costs for related activities such as landlord responsibilities, program management and legally prescribed grants for participation and oversight by Native American tribes, and regulatory agencies. "Active facilities" represent anticipated remediation costs for those facilities conducting ongoing operations that ultimately will require stabilization, deactivation and decommissioning.

DOD is responsible for cleaning up and disposing of hazardous materials in facilities it operates or has operated. The Department has recorded a $34.0 billion liability for these costs. DOD has not currently recorded any liability for national defense assets (primarily weapon systems like aircraft, ships and submarines) and ammunitions (primarily hazardous materials).

Projects with no current feasibility remediation approach are excluded from the estimate. Significant projects not included are:

- Nuclear explosion test areas (for example, Nevada test sites).
- Large surface water bodies (for example, the Clinch and Columbia rivers).
- Most ground water (even with treatment, future use will be restricted).
- Some special nuclear material (for example, uranium hexafluoride).

Example 13.11
Financial Report of the United States Government – 1998
Notes to the Financial Statements, page 75 (USD)

Obligations Under Accident Compensation Schemes

473. A number of jurisdictions, e.g., Australia, Canada, USA and New Zealand, have operated motor vehicle or workers' compensation type insurance schemes through legally separate public sector bodies. At present, the accounting approach for such schemes is not uniform. The main issue is whether the claims notified to, and accepted by the scheme, but which not be paid until future financial years, will be recognized as a liability in the financial statements of the scheme. If they are, then they will flow through to the consolidated financial statements of the government controlling the scheme. At present some schemes do not recognize such liabilities. The recognition of these items will depend on the nature of the legislative arrangements in place in each jurisdiction. Where such liabilities are not recognized, actuarial estimates of the discounted present values of the cash flows associated with such future liabilities may be presented as additional information in the financial statements.

474. Another issue is whether potential obligations which have not yet been notified to the scheme should be recognized as a liability. The recognition of these items will depend upon whether there is sufficient information regarding their probability and measurability. An example of the recognition of such liabilities is shown below.

> All policies have been applied on a consistent basis during the period except for a change to the accounting policy in relation to the Accident Rehabilitation and Compensation Insurance Corporation (ARCIC).
>
> Up until 30 June 1999 the Crown incorporated ARCIC on the basis of the accounting policy of recognising revenue and expenses on a pay-as-you-go basis. The future costs of past claims were not recognised in ARCIC's or the Crown's financial statements, but instead were accumulated as an unfunded liability and disclosed as a note to the financial statements.
>
> As at 30 June 1999, ARCIC has recognised the ACC outstanding claims obligation (future cost of past claims) in its financial statements, and from 1 July 1999 the future costs of new claims will be recognised. Revenue will also be recognised on a consistent basis. The impact of this is to significantly reduce the Crown's investment in its State-owned enterprises and Crown entities by the amount of the liability recognised, net of an adjustment for revenue recognition alignment.

Example 13.12
Financial Statements of the Government of New Zealand
for the year ended 30 June 1999
Statement of Accounting Policies, page 64

The Announcement of a New Program or Spending Initiative

475. The intention of a government to undertake a new program or spending initiative which will result in the payments to other parties, whether advised in the form of a budget policy or election promise, does not of itself create a present obligation which is binding on a government. A liability would be recognized only when the government is committed in the sense that it has little or no discretion to avoid the sacrifice of future economic benefits or service potential. Where a new program or spending initiative has been supported by enabling legislation, it is possible a liability may exist. However, an obligation for such future spending would be more likely to be disclosed as a commitment in the notes. Future spending which is within the normal scope of operations is not normally classified as a liability or a commitment.

Future Obligations under Current Policies

476. Where the future obligations have already been incurred then they may meet the definition of a liability. For example, long-term liabilities relating to employees' current contracts generally meet the definition and recognition criteria for liabilities in the period in which the obligation arises.

477. The point of recognition for welfare payments can be determined by applying the definition and recognition criteria. A liability does not exist until the government acknowledges an obligation to the recipient for the welfare payment. Governments do not normally acknowledge any liability for welfare payments until someone applies for a welfare payment, and eligibility criteria have been satisfied. If the government makes payment to the recipient prior to the eligibility criteria being met, the government would not expense the payment, but would record it as a financial asset until the transferee meets the eligibility criteria.

478. Once it has been established that someone is eligible for a welfare benefit, it is necessary to decide how much of the government's future obligations should be recognized within the current reporting period. If welfare payments are made on a regular basis it is normal practice to recognize as a liability only that portion of the welfare payment which falls due at each payment date. If a one-off lump sum is due, then it would be recognized once the eligibility criteria have been satisfied, regardless of date of payment. Future welfare benefits do not meet the definition of an expense and would not be

recognized as a liability within the current reporting period. At any point in time the government is only obliged to pay for amounts owed to the individual at that particular time. Only these amounts are recognized as expenses (refer to the discussion of Entitlements in Chapter 15). The nature of each benefit and the determination and timing of entitlement will determine whether it is appropriate to accrue a liability at the end of the reporting period. This will vary from jurisdiction to jurisdiction. For example, where entitlement does not occur until the date of payment of a benefit, then there is no liability in relation to that benefit.

479. Some jurisdictions prefer to provide information on certain types of future commitments, by way of disclosure, rather than by recognition in the financial statement totals. The U.S. federal government has adopted this approach for the reporting of social insurance obligations, principally because of the *"significant, vexing, theoretical and practical problems"* associated with these obligations. (SFFAS No. 8 page 49) Refer also to the separate discussion of provisions and contingent liabilities in this Chapter. However, the U.S. has accrued unpaid amounts due for social insurance as of the reporting date (refer to the example below).

> **Note 1.K. Social Insurance**
>
> A liability for social insurance programs (Social Security, Medicare, railroad retirement, black lung and unemployment) is recognized for any unpaid amounts due as of the reporting date. No liability is recognized for future payments not yet due. For further information, see the Stewardship Information section on social insurance.

Example 13.13
Financial Report of the United States Government – 1998
Notes to the Financial Statements, page 64

480. Information on the government's future obligations under welfare programs (e.g., projections of general obligations and resources to cover them) may be reported in budget documents and/or financial statements.

481. In the absence of a clear legal responsibility, the existence of an obligation for which the government may have a liability must be assessed on the basis of available evidence. In situations such as these, estimates may be necessary in determining not only the amount to be paid in settlement of an obligation, but also the expectation that payment will be made.

Provisions and Contingent Liabilities

482. Provisions and contingent liabilities may arise when there is uncertainty as to amount or timing of future payments or as to the likelihood of the payment occurring. The classification of such items as provisions (recognized as liabilities) or contingent liabilities (not recognized as liabilities) is discussed in this section.

483. IAS 37, *Provisions, Contingent Liabilities and Contingent Assets* deals with the relationship between provisions and other liabilities, and between provisions and contingent liabilities. It defines provisions and contingent liabilities as follows:

A provision is a liability of uncertain timing or amount. (paragraph 10)

A contingent liability is:

(a) a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the enterprise; or

(b) a present obligation that arises from past events but is not recognised because:

(i) it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation; or

(ii) the amount of the obligation cannot be measured with sufficient reliability. (paragraph 10)

484. Provisions meet both the definition of, and recognition criteria for, liabilities. Contingent liabilities however, meet either the definition of or the recognition criteria for, liabilities but not both. Items which are recorded as contingent liabilities in one financial period may meet the definition and recognition criteria for liabilities in a subsequent period. This may occur when a previously uncertain event becomes certain e.g., a court case is decided and damages awarded against the government, or when additional information allows for the reliable measurement of a liability.

485. IAS 37 also explains the application of the recognition criteria to provisions. It notes that present obligations include both legal and constructive obligations. The Appendix to IAS 37 contains a comparison of provisions and contingent liabilities.

486. The distinction between a provision and a contingent liability is complex for both governments and business enterprises. One of the key issues is whether a present obligation exists. This depends on the individual circumstances. Examples of situations when either a provision or a contingent liability may arise within the public sector include possible obligations to:

- clean-up contaminated land;
- pay redundancy costs and other one off costs associated with an administrative restructuring;
- meet the indebtedness of others by way of guarantee;
- meet a new health and safety building code; or
- pay amounts awarded as a result of pending or threatened litigation.

487. In all of these cases, depending on the probability of the liability occurring, there may be no liability, a need to recognize a provision or a need to disclose a contingent liability.

488. As more information on the probability of events occurring becomes available, items which have previously been disclosed as contingent liabilities may meet the definition of a liability. For the purposes of comparative reporting, the notes to the financial statements should indicate that an item has been removed from the list of contingent liabilities and why it has been removed.

489. Examples of accounting policies for contingent liabilities follow, including an extract from financial statements disclosing land claims as a contingent liability.

CONTINGENCIES
1.48 In these consolidated financial statements contingencies are conditions, situations, or circumstances that: exist at the end of the reporting period, create uncertainty as to the possible gain or loss to an entity and will be confirmed only on the occurrence or non-occurrence of one or more uncertain future events.

Example 13.14
Financial Statements of the Commonwealth Government of Australia
for the year ended 30 June 1997
Notes to and forming part of the Financial Statements, page 41

Note 1.L. Liabilities and Contingent Liabilities

Liabilities represent the amount of monies or other resources that are likely to be paid by Interior as the result of a transaction or event that has already occurred. The financial statements should be read with the realization that the Department of the Interior is a component of a sovereign entity, that no liability can be paid by the Department absent an appropriation of funds by Congress, and the payment of all liabilities other than for contracts can be abrogated by the sovereign entity. Liabilities for which an appropriation has not been enacted are, therefore, classified as liabilities not covered by budgetary resources, or unfunded liabilities, and there is no legal certainty that the appropriations will be enacted.

Contingent liabilities are those where the existence or amount of the liability cannot be determined with certainty pending the outcome of future events. Interior recognizes contingent liabilities when the liability is probable and reasonably estimable. In accordance with Federal accounting guidance, the liability for future clean-up of environmental hazards is "probable" only when the government is legally responsible for creating the hazard. Thus, expected future payments for the clean-up of environmental hazards caused by others are not recognized as liabilities by Interior. Rather, these payments arise out of Interior's sovereign responsibility to protect the health and safety of the public, and are recognized in the accounting records as remediation work performed. See Note 13 for additional information regarding contingent liabilities.

Example 13.15
U.S. Department of the Interior
FY 1998 DOI Annual Accountability Report
Notes to Principal Financial Statements
as of September 30, 1998 and 1997, page 67

NOTE 13. CONTINGENT LIABILITIES

The U.S. Department of the Interior is party to various administrative proceedings, legal actions, and tort claims which may ultimately result in settlements or decisions adverse to the Federal government. Interior has accrued liabilities where losses are determined to be probable and the amounts can be estimated. Other significant contingencies exist where a loss is reasonably possible, or where a loss is probable but an estimate cannot be determined. In some cases, once losses are certain, payments may be from the Judgment Fund maintained by Treasury rather than from amounts appropriated to Interior for Departmental operations.

A. Environmental Hazards

The U.S. Department of the Interior is subject to Federal, state, and local environmental laws and regulations regarding air, water, and land use, the storage and disposal of hazardous materials, and the operations and closure of facilities at which environmental contamination resulted. The major Federal laws covering environmental contamination as related to Interior are the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA) and the Resource Conservation and Recovery Act (RCRA). Responsible parties, including Federal agencies, are required to clean up releases of hazardous substances.

Interior is the Federal agency with oversight responsibility for the Nation's national parks, wildlife refuges, and public domain lands, which comprise approximately one-fifth of the Nation's land mass. In this role, Interior is faced with many hazardous waste clean-up situations. The hazards include, among others, chemical hazards such as drums of toxic chemicals and soil and water contaminated by chemicals, and physical hazards such as open mine shafts.

Interior has an active program to find and monitor its hazardous sites, secure the affected areas, and begin clean-up of priority areas. However, the vast expanse of Interior lands prevents an acre by acre review, so the exact total number of sites and a firm statement of cleanup costs are not determinable. Once a site has been identified, it may take several years to perform an evaluation of the site and determine the potential cost of remediation.

In 1998 and 1997, Interior recognized an estimated liability of $275 million and $223 million, respectively, for sites where the Department either caused contamination or is otherwise related to it in such a way that it may be legally liable for cleanup of the hazard, and the environmental cleanup liability is probable and reasonably estimable. This estimate includes the expected future clean-up costs, or for those sites where future liability is unknown, the cost of study necessary to evaluate cleanup requirements. Interior's total contingent liability for environmental cleanup of sites, including those where liability is considered probable and reasonably estimable, may be over $338 million. The estimated liability excludes estimates of future mineral site restorations, discussed below, for which Interior will voluntarily undertake remediation without legal responsibility to do so.

In addition to the limited number of cases discussed above where Interior may have created or contributed to the hazards, other hazardous conditions exist on public lands for which the Department might fund clean up. These costs, which are not included in contingent liabilities, may result from:

- legal mining activities by others over the past two centuries and prior to current strict environmental clean up and restoration laws;
- legal mining activities subject to current standards, but where the responsible party cannot be found, has declared bankruptcy, or otherwise cannot be compelled to remove the hazard;
- illegal activities, including active and abandoned narcotics laboratories, hazardous materials dumping, and illegal mining; and
- transportation spills, landfills, pipelines, and airports.

Example 13.16
U.S. Department of the Interior FY 1998 DOI Annual Accountability Report
Notes to Principal Financial Statements
as of September 30, 1998 and 1997, pages 80 and 81 (USD)

TABLE 10.8
STATEMENT OF CONTINGENT LIABILITIES
AS AT MARCH 31, 1999—*Continued*

	Authorized limit (where applicable)[1]	Contingent liability[2]	Percentage of expected losses to outstanding guarantees (where applicable)[3]
	$	$	%
Other explicit guarantees			
Guarantees under the *Prairie Grain Advance Payments Act*	1,500,000,000	241,100,000	6.4
Guarantees under Section 19 of the *Canadian Wheat Board Act*			(18)
Guarantees to holders of mortgages insured by the Mortgage Insurance Company of Canada and GE Capital Mortgage Insurance Co. (Canada)..........................		147,451,608	
Guarantees under the *Agricultural Products Cooperative Marketing Act*		21,766,158	
	1,500,000,000	*410,317,766*	
Total gross guarantees	35,368,866,889	47,744,914,110	
Less: allowance for losses		4,090,000,000 (19)	
Net exposure under guarantees		43,654,914,110	
INTERNATIONAL ORGANIZATIONS........................		18,340,282,846 (2)(10)(20)(25)	
CLAIMS AND PENDING AND THREATENED LITIGATION		14,143,561,075 (10)(20)	
COMPREHENSIVE NATIVE LAND CLAIMS		742,000,000 (22)	
Subtotal (23)		76,880,758,031	
CONTINGENT LIABILITIES OF CONSOLIDATED CROWN CORPORATIONS		91,570,000 (24)	
TOTAL........................		76,972,328,031	

: : : : : : : :

(22) The Government has 69 comprehensive aboriginal land claims either under negotiation, accepted for negotiation or under review. Of the 69 comprehensive claims, 7 claims relating to the Council for Yukon Indians and 5 pertaining to the Dene-Metis are in the final stages of negotiation. Should negotiations be ratified, the Government would be liable to pay financial compensation over a number of years as follows:

	(in millions of dollars)
Council for Yukon Indians....................	109
Portion of the Dene/Metis claim....................	197
Nisga'a....................	190
	496
Implementation costs	246
Total....................	742

The remaining 57 comprehensive claims have not yet been quantified.

Example 13.17
Public Accounts of Canada, 1998-99
Section 10 Other Information Related to the Financial Statements (CAD)[3]

[5] The complete Statement of Contingent Liabilities from which this extract is taken may be viewed at http://www.pwgsc.gc.ca.

Commitments

490. A commitment is generally acknowledged as the government's responsibility for a future liability, based on an existing contractual agreement[4]. Although there may be a contractual agreement, the contract does not yet give rise to a present obligation. This is because no exchange has yet taken place or, in the case of a non-reciprocal transaction, the payment is not yet due. The obligation, and therefore the liability, normally arises on delivery of the goods and services. For example, when an entity enters into a commitment to purchase or construct a capital asset in the future, an obligation normally arises only when the asset is delivered or the entity enters into an irrevocable agreement to acquire the asset. The difference between commitments and liabilities is usually clear for contractual obligations. Classification may be more difficult when obligations are embodied in legislation and some judgment may be required.

491. Commitments differ from contingent liabilities in that there is generally certainty that the liability will occur, but the present obligation will not occur until a future reporting period. The obligation is not dependent upon the outcome of an uncertain future event. At the point at which the present obligation does occur, the item ceases to be a commitment and is recognized as a liability.

492. Commitments may be disclosed in the notes or in a separate schedule. They are not accrued as liabilities in the financial statements. Various international accounting standards require the disclosure of commitments. IAS 1, *Presentation of Financial Statements* requires business enterprises to disclose amounts committed for future capital expenditure. IAS 17, *Leases* is an example of a standard that expands on the general disclosure requirement in IAS 1. It requires the disclosure of commitments for minimum lease payments under finance leases and under non-cancelable operating leases with a term of more than one year in summary form, showing the amounts and periods in which the payments will become due.

493. Governments can readily report the types of commitments that businesses report such as those related to purchase of goods and services to be provided as set out in existing contracts, agreements or legislation.

494. An argument can be made that a government's entire budget, once approved, can be considered an expenditure commitment by the government. But disclosure of that "commitment" would be of little use in the government's financial statements. The amounts allowed for in a government's annual budget would be recognized as expenses by the end of the annual reporting period.

495. Generally obligations arising from ongoing social programs would not be disclosed as commitments as there is no legal obligation to make the payments in the future (although this may vary between jurisdictions). Information on the government's future obligations under ongoing social programs is needed to assess future borrowing requirements and taxation levels and the resulting impact on the economy; the long-term viability of social programs; and policy options available to control or reduce spending or deficit levels. This information may be disclosed in budget documents and/or financial statements.

496. Another alternative is to disclose information about only those commitments that are abnormal in relation to the government's financial position or normal course of "business", or that will have a significant effect on the need for revenue in the future.

497. Information about employment agreements is not disclosed as a commitment because such agreements are in the normal course of business. Similarly, it could be argued that ongoing social programs are in the normal course of the government's business and need not be highlighted unless there is a new program commitment or a significant change to expand existing programs.

498. Some governments (e.g., the U.S. federal government) are required by law to project future expenditure levels on the basis of existing policy and disclose this information.

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[4] In this Study the term commitment is used to refer to items which are not liabilities, but which an entity will be required to pay in the future. The meaning of the term may vary across jurisdictions.

499. Examples of accounting policies for commitments, including some which show the treatment of equally unperformed obligations, are shown below.

> **COMMITMENTS**
>
> 1.50 Commitments are obligations or undertakings to make future payments to other entities that: exist at the end of the reporting period and have not been recognised as liabilities in the Statement of Assets and Liabilities.

Example 13.18
Financial Statements of the Commonwealth Government of Australia
for the year ended 30 June 1997
Notes to and forming part of the Financial Statements, page 41

> ***Private Sector Financed Infrastructure Assets***
>
> There is currently no Australian Accounting Standard which specifically addresses the accounting for private sector financed infrastructure assets. Treasury has adopted the following policies pending the development of an accounting standard.
>
> Agreements Equally Proportionately Unperformed arising from private sector financed infrastructure arrangements are generally not recognised as assets or liabilities because there is significant uncertainty as to whether the definitions and recognition criteria in SAC 4 Statement of Accounting Concepts "Definition and Recognition of Elements of Financial Statements" would be satisfied. Instead, the payments under these agreements are expensed systematically over the term of the agreements. Further, the commitments for future payments under these agreements are disclosed as "Commitments" in the notes to the financial statements.
>
> However, certain private sector financed infrastructure arrangements provide for a private sector entity to design, construct, operate and maintain certain infrastructure for a specified concession period, after which the infrastructure is transferred back to the agency.
>
> The interest of the agency in such arrangements is recognised as an asset, being the emerging interest in the remaining service potential to be transferred to the agency. The emerging interest is valued by reference to the agency's emerging share in the current cost of the asset at the date of transfer. The emerging interest is progressively recognised from the date of completion of construction over the period of the concession agreement.

Example 13.19
Consolidated Financial Statements of the NSW Public Sector 1996–97
The NSW Public Sector, Notes to and forming part of the Financial Statements, pages 29 and 30

> **Commitments**
>
> Future expenses and liabilities to be incurred on contracts that have been entered into at balance date are disclosed as commitments to the extent that there are equally unperformed obligations.

Example 13.20
Annual Report of the New Zealand Defence Force
for the year ended 30 June 1999
Statement of Accounting Policies, page 115

Administered Liabilities

500. A government entity will recognize only those liabilities which meet both the definition and recognition criteria. It will not recognize liabilities unless they involve a future sacrifice of its own revenues or assets. However, government entities may administer liabilities on behalf of another level of government, or another entity (e.g., a government department may manage the central government debt portfolio). In order to demonstrate accountability for the management of such liabilities, information on the liabilities may be disclosed in either the Notes to the Financial Statements or in a separate Schedule. However, in practice there are a range of practices regarding the reporting of administered liabilities, and some entities recognize such liabilities in the Statement of Financial Position. Refer also to the discussion of administered assets and administered transactions in Chapters 12, 14 and 15.

Liabilities not Recognized

501. Where liabilities do not meet definition and recognition criteria they are not recognized in the financial statements. However, they may be separately disclosed in the Notes to the Financial Statements. For example actuarial valuations of social security (welfare) obligations under current law could be provided as a note to financial statements. An example of note disclosure of liabilities not recognized in the financial statements is shown below.

NOTE 35. LIABILITIES NOT RECOGNISED

	1997 $m	**1996[1] $m**
ON THE BASIS OF PROBABILITY		
Details of liabilities not recognised, as the sacrifice of future economic benefits is not considered probable, are as follows:		
Off balance sheet interest rate financial instruments	3,077	2,904
Cross currency and other derivatives	3,712	-
Underwriting facilities	271	-
Direct credit substitutes	153	-
Credit enhancement	730	-
Other	-	95
Total liabilities not recognised on the basis of probability	**7,943**	**2,999**
ON THE BASIS OF RELIABLE MEASUREMENT		
Details of liabilities not recognised, as the sacrifice of future economic benefits can not be measured reliably, are as follows:		
Off balance sheet interest rate financial instruments		

[1] Trial and unaudited.

Example 13.21
Financial Statements of the Commonwealth Government of Australia
for the year ended 30 June 1997
Notes to and forming part of the Financial Statements, page 70 (AUD)

Classification of Liabilities

502. Classification depends upon users' needs and on how they can best be met. The constraints identified in Chapter 12 (Classification of Assets) apply here also. A possible classification of liabilities is:

- accounts payable and accrued liabilities;
- employee pension obligations or entitlements;
- liabilities relating to unearned revenue;

- debt; and
- loans and advances from other governments.

503. Liabilities may also be grouped by nature or function. The SNA and GFS functional classifications shown in Chapter 19 could also be used.

504. Governments may want to distinguish between those liabilities that will probably be met in the next budget period, and those that will be met in subsequent periods. As discussed in Chapter 12 this could be done by disclosing liabilities in broad order of liquidity or by using the current and non-current classification. When liabilities are classified according to order of liquidity, payables and provisions tend to be at one end of the spectrum with borrowings and pension liabilities at the other end of the spectrum.

505. Because of the nature and size of government borrowings, debt is usually highlighted. It is also important to distinguish debt payable in foreign currency whenever the amount is significant, so that readers are able to assess the impact of foreign exchange movements.

CHAPTER 14

ACCRUAL BASIS – REVENUES

Introduction

506. PSC Study 9 *Definition and Recognition of Revenues*, considered the extent to which the IASC definition of income and revenues applies to revenues in the public sector. The Study concluded that although some government transactions are identical to those in the commercial or for-profit sector, many forms of government revenues are non-reciprocal transfers which require additional consideration. Study 9 focused on the definition and recognition issues associated with non-reciprocal transfers. This Chapter describes the types of revenues received by governments and discusses the extent to which the IASC definition of revenues applies. It gives examples of revenues and discusses recognition issues associated with these revenues, particularly non-reciprocal transfers.

Definition of Revenues

507. The IASC Framework for the Preparation and Presentation of Financial Statements defines income as follows:

> *Income is increases in economic benefits during the accounting period in the form of inflows or enhancements of assets or decreases of liabilities that result in increases in equity, other than those relating to contributions from equity participants.* (paragraph 70)

508. The IASC Framework goes on to explain that income encompasses both revenues and gains.

> *The definition of income encompasses both revenue and gains. Revenue arises in the course of the ordinary activities of an enterprise and is referred to by a variety of different names including sales, fees, interest, dividends, royalties and rent.* (paragraph 74)
>
> *Gains represent other items that meet the definition of income and may, or may not, arise in the course of the ordinary activities of an enterprise. Gains represent increases in economic benefits and as such are no different in nature from revenue. Hence they are not regarded as constituting a separate element in this framework.* (paragraph 75)

509. The PSC, in common with a number of public sector standard setters, has chosen to use the term revenues to apply to both revenues and gains as defined by the IASC.

Recognition of Revenues

510. The accrual basis of accounting recognizes the effects of transactions and other events in the period during which they occur, regardless of the timing of associated cash receipts. This means decisions need to be made regarding the timing of recognition of revenue. The IASC Framework for the Preparation and Presentation of Financial Statements gives the following criteria for recognition of elements:

> *(a) it is probable that any future economic benefit associated with the item will flow to or from the enterprise; and*
> *(b) the item has a cost that can be measured with reliability.* (paragraph 83)

511. "Probable" means that the chance of an event occurring is more likely than less likely and "measurable" means reasonably estimable. Often revenue may be measured with a high degree of reliability. However, in other cases, estimates of the amount may be required. The point of recognition for different types of revenue is discussed later in this Chapter.

Types of Revenues

512. Government revenues include:

- Non-reciprocal revenues
  - direct and indirect taxes
  - duties
  - fees and fines
  - other non-reciprocal transfers
- Reciprocal (or exchange) revenues
  - sales of goods or services
  - dividends
  - interest
  - net gains arising from the sale of assets
- Other gains

513. This list is not exhaustive. A fuller list is provided towards the end of this Chapter in the discussion on Classification. Exchange revenues are derived from exchanges in a similar manner to the private sector, whereas non-reciprocal revenues are usually derived from the use of the powers of government.

514. Governments may derive revenues from all these sources, although the mix will depend upon the type or level of entity. National or federal governments will normally derive most of their revenue from exercising their power to tax or levy. They may also receive grants, contributions and donations from other governments, supranational authorities or from the private sector.

515. Government departments typically have two main sources of revenue: exchange revenues from other government entities or the private sector, and revenues from central government which may be classified as reciprocal or non-reciprocal depending upon the jurisdiction. Government departments or agencies may also collect revenues on behalf of the government or other entities, known as custodial or agency receipts. The treatment of custodial receipts is discussed in Chapter 14.

516. Local government revenue may come from a variety of sources. It may include rates or polls levied on domestic or business dwellings, grants from other levels of government, and revenue from trading activities or services provided on a cost recovery basis.

517. There are a wide variety of other government reporting entities. Government Business Enterprises (GBEs) would, by definition, normally receive most of their revenue from trading activities. Other organizations may receive a mixture of exchange revenue and grants, contributions and donations.

518. Financing inflows, notably borrowings, do not meet the definition of revenue because they result in an equal change in both assets and liabilities and have no impact on net assets/equity. Financing inflows are taken directly to the Statement of Financial Position and added to the balances of financial assets and financial liabilities. For a discussion of the treatment of these items refer to Chapters 12 and 13.

Appropriations

519. For the government as a whole, appropriations are an authorization by the legislature to expend funds. For the individual entities of government which receive funds under appropriation, it is necessary to determine whether the appropriation meets the definition of revenue, and if so, whether it should be classified as reciprocal or non-reciprocal. Depending on the types of appropriations that may be made within a jurisdiction, and the characteristics of the appropriation in question, appropriations may be:

- revenue;
- a capital contribution being a direct and permanent increase in the resource base of the entity similar in nature to an equity injection to private sector entities or GBEs;
- a loan; or
- custodial receipts for transfer to third parties.

520. Under the accrual basis of accounting, appropriations representing a direct and permanent increase in the resource base of a governmental entity may be classified as capital contributions by the controlling entity where the parent government is viewed as the "owner". The recognition of such amounts as contributions of capital and loan funds would depend on the nature of the appropriation system and the framework within which government entities operate. Such recognition may be appropriate where government entities have been corporatized or a purchaser-provider (or similar) model for the delivery of services of the government departments has been adopted such that the relationship between the entity and the government replicates that between owners and private sector or other government entities. Refer to Financial Assets – Investments in Chapter 12 for a discussion of the accounting treatment in the financial statements of the entity making such a contribution.

521. If the funds are provided in order to finance operating activities in the reporting period they are revenue in nature. The legislative and administrative arrangements surrounding appropriations for operating activities vary considerably from one jurisdiction to another. In some countries (such as New Zealand) which operate under the accrual basis and have explicit agreements between the government and its agencies specifying the goods and services to be produced, the funds received under appropriation for the production of outputs may be accounted for as exchange revenue. In other jurisdictions, the funds received under appropriation may be regarded as non-reciprocal revenues (refer to the discussion of Non-reciprocal Revenues later in this Chapter).

522. Appropriations may be restricted or unrestricted. Where appropriations restrict the use of funds to a particular purpose, the entity receiving the funds must consider the appropriate point of recognition. Refer also to the discussion of Restricted Transfers later in this Chapter. The point of recognition is also affected by the certainty of receiving and keeping the funds specified in the appropriation. This will vary between jurisdictions. Revenues which have been authorized by appropriation but which have not yet been received, may be recognized as revenue if they are more likely than not to be received by the entity. Where there is some uncertainty regarding the receipt of the funds, recognition may be deferred.

523. In general, unexpended appropriations are not be treated as revenue where they must be returned to the parent government because there is not a legal entitlement to the resources. If agencies are permitted to carry-over unexpended appropriations, or some portion of them, that amount may be treated as revenue.

524. The United States views appropriations as a financing source recognized by the entity when the appropriation is used, rather than when the related costs are incurred. Appropriations are recognized as used to finance operations when an entity acquires goods and services, or when benefits and grants are provided that are authorized to be paid by the appropriations. The remaining amount of appropriations enacted into law, but not yet recognized as "appropriations used", are reflected as "unexpended appropriations" in the equity section of the entity's Balance Sheet. (SFFAS No.7, paragraphs 69 and 70)

525. An alternative treatment is that adopted in New Zealand. Parliament appropriates a variety of types of expenses and expenditures, including the purchase of outputs from departments and other providers, the funding of benefits and other unrequited transfers paid by departments on the government's behalf, and the purchase or development of capital assets. In the case of the purchase of outputs, the amounts received by the provider pursuant to an appropriation are accounted for as revenue in accordance with generally accepted accounting practice.

526. Some examples of accounting policies for revenues subject to appropriation are shown below.

Revenue

The Department derives revenue through the provision of outputs to the Crown, for services to third parties and interest on funds held in bank accounts. Such revenue is recognised when earned and is reported in the financial period to which it relates.

Example 14.1
Annual Report of the New Zealand Defence Force
for the year ended 30 June 1999
Statement of Accounting Policies, page 113

NOTE 5. NET FINANCING SOURCES

GAO's financing sources, other than reimbursable services, consist of appropriations used and imputed financing, less transfers-out. Appropriations are considered used as a financing source when goods and services are received or benefits are provided. This is true whether the goods, services, and benefits are paid prior to the reporting date or are payable as of that date, and whether the appropriations are used for items that are recorded as expenses or are capitalized. Imputed financing is the offset to the federal employee retirement benefit costs paid by OPM and imputed to GAO that are reported on the Statement of Net Cost. Transfers-out represent the book value of capitalized assets transferred from GAO to other federal agencies without reimbursement.

Example 14.2
Comptroller General's 1998 Annual Report, United States General Accounting Office (GAO)
Notes to Principal Statements, page 72

Non-reciprocal Revenues

527. A non-reciprocal transfer is one in which the entity receives assets or services or has liabilities extinguished without directly giving approximately equal value in exchange to the other party or parties to the transfer. Taxation is the major source of such inflows of economic benefits. Some jurisdictions use the term "non-exchange" transfer to refer to non-reciprocal transfers.

528. In addition to taxes, governments may also receive grants, donations and payments from other parties. For example, national governments may receive aid or grants from other sovereign governments or from supranational authorities. Entities which form part of a national government may receive transfers from the parent government, which under some circumstances might be viewed as an exchange relationship with the parent government (refer to the discussion of Reciprocal (Exchange) Revenues later in this Chapter) but under other circumstances might be viewed as non-reciprocal transfers.

529. A concept of revenue used in some jurisdictions, including the United States, proceeds from the principle that the bottom line of the primary operating statement should be the net cost of government activities carried on by the responsible government entity, i.e., costs of the particular programs administered by the reporting entity less any exchange revenues derived from selling government goods and services for a price. Under this approach, non-exchange revenues derived primarily from accrued taxes are treated as a revenue of the whole of government except for taxes which are dedicated to finance specific programs. However, whatever form of presentation is adopted, the gross amount of revenues should be clearly disclosed.

Revenues Derived from the use of the Powers of Government

530. Governments may use their powers to collect a range of non-reciprocal revenues. These include a variety of direct and indirect taxes, duties, fees and fines such as;

- income tax;
- fringe benefit tax;
- sales tax;
- value-added tax;
- payroll tax;
- property tax;
- capital gains tax;
- stamp, check and credit duties;
- death/estate duties;
- license tax;
- road-user charges and motor vehicle fees;
- levies; and
- fines.

531. Collections of taxes are generally viewed as part of the operating revenues of a government.

532. Taxes frequently make up the majority of a government's revenues and are generally viewed as an important component in assessing both the government's financial performance during the period and, in conjunction with borrowing levels, in assessing intergenerational equity. Because IAS 18, *Revenue* focuses on exchange transactions, taxes and other non-reciprocal transactions are not covered in the IAS. Although taxes are often the main source of revenues at a whole of government level, this may or may not be so for other levels of government or for individual government entities. Some government entities tax in their own right and may use the revenues collected for their operating costs. Others merely collect such revenues on behalf of a higher level of government and have no right to these revenues. In this case the collecting agency would account for the revenues collected as custodial or agency receipts (refer to discussion later in this Chapter).

533. There are a number of possible recognition points for taxation revenue. In the case of income tax, the following recognition points are possible:

- when the taxpayer earns the taxable income;
- at the end of the income year;
- when the tax returns are filed;
- when tax is assessed;
- when a tax liability is recognized by the taxpayer; or
- when payment is made.

534. Using the recognition criteria of probability and measurability, it is possible to specify points at which taxation revenue, in any particular government under an accrual basis, is first able to be recognized. Because of the differences in legislation and administrative systems across countries, it is possible that different countries will have different recognition points for similar taxes.

535. Examples of recognition points for taxes used by various governments are shown below.

Revenue

Revenue levied through the Crown's sovereign power

The Crown provides many services and benefits that do not give rise to revenue. Further, payment of tax does not of itself entitle a taxpayer to an equivalent value of services or benefits, as there is no direct relationship between paying tax and receiving Crown services and transfers. Such revenue is received through the exercise of the Crown's sovereign power.

Where possible, revenue is recognised at the time the debt to the Crown arises.

Revenue Type	Revenue Recognition Point
Source deductions (PAYE)	When an individual earns income that is subject to PAYE
Residents' withholding tax[1]	When an individual is paid interest or dividends subject to deduction at source
Fringe benefit tax (FBT)	When benefits are provided that give rise to FBT
Provisional tax	Payment due date
Terminal tax	Assessment filed date
Goods and services tax	When the liability to the Crown is incurred
Excise duty	When goods are subject to duty
Road user charges and motor vehicle fees	When payment for the fee or charge is made
Stamp, cheque and credit card duties	When the liability to the Crown is incurred
Other indirect taxes	When the debt to the Crown arises

[1] Corresponds to withholding taxes on residents' interest and dividend income in Note 1 to the Financial Statements.

Example 14.3
Financial Statements of the New Zealand Government
for the year ended 30 June 1999
Statement of Accounting Policies, page 58

State Taxation, Fines and Fees

State taxation is recognised as follows:

- Government-assessed revenues (primarily land tax) are recognised at the time the assessments are issued.

- Taxpayer-assessed revenues (including payroll tax and stamp duty), are recognised when the funds are received by the revenue collecting agency. Additional revenues are recognised for assessments subsequently issued following review of returns lodged by taxpayers.

- Revenue from traffic penalties is accounted for on a cash basis according to the amount collected in a financial year. This may include penalties imposed in an earlier financial year. Recipients of penalty notices have a variety of options available to them to dispose of the penalty. The payment option is generally taken in about 70% of cases. All other fines and fees are also recognised when cash is received.

Example 14.4
Consolidated Financial Statements of the NSW Public Sector 1996–97
The NSW Public Sector, Notes to and forming part of the Financial Statements, page 27

Taxation revenue

1.21 Revenues are recognised when the Government gains control of the future economic benefits that flow from taxes and when those future economic benefits can be measured reliably. The bases of recognition for major types of taxation revenue are summarised in Table 1.

Table 1: Taxation Revenue

Major type of taxation revenue	**Basis of revenue recognition**
Income Tax from Individuals (PAYE, PPS, Provisional Tax)	recognised on earnings of taxpayers during the reporting period where such amounts can be reliably measured and are expected to be collected
Company Tax & Superannuation Fund tax	recognised on company income for the reporting period
Sales Tax & Withholding Tax	recognised on defined sales and other relevant activities occurring during the reporting period
Fringe Benefits Tax	recognised on fringe benefits provided to employees during the reporting period
Excise Duty	recognised when goods are distributed for home consumption
Customs Duty	recognised when imported goods are distributed for home consumption

Example 14.5
Financial Statements of the Commonwealth Government of Australia
for the year ended 30 June 1997
Notes to and forming part of the Financial Statements, pages 38 and 39

536. In many cases the amount of revenue and the timing of its recognition will be clear (e.g., where the amounts are assessed and paid in the same reporting period or periodic installments have been made and only the final installment and potential refunds have to be estimated). In cases where the amount and timing of recognition is less clear, revenues are recognized if the amount of revenue in the reporting period can be reliably determined.

537. Where information on future taxes is not complete or reliable, the point of recognition may be when payment is received. For example, U.S. federal standards recognize that present U.S. administrative processes for tax collection do not provide the information necessary for accrual at the point the underlying event or transaction occurs. Additional tax accruals could be determined if necessary systems were improved. As a result, U.S. standard setters characterize the recognition and measurement standard for taxes as closer to the receipt of cash than to the point at which the taxable income is earned.

538. Examples of taxes collected by national governments and a local government are shown below.

Statement of Financial Performance
for the year ended 30 June 1999

Forecast 1998 Budget $m	Estimated Actual $m		Note	*Actual* 30 June 1999 $m	30 June 1998 $m
		Revenue			
		Levied through the Crown's Sovereign Power			
21,603	20,490	Direct taxation	1	20,289	21,260
12,095	11,866	Indirect taxation	2	11,867	11,722
33,698	32,356	Total taxation revenue		32,156	32,982
263	270	Compulsory fees, fines, penalties and levies		300	258
33,961	**32,626**	**Total Revenue Levied through the Crown's Sovereign Power**		**32,456**	**33,240**

Example 14.6
Financial Statements of the Government of New Zealand
for the year ended 30 June 1999
Statement of Financial Performance, page 26 (NZD)

REVENUES AND EXPENSES BY ECONOMIC TYPE
for the year ended 30 June 1997

	Note	1997 $m	1996[1] $m
Revenues			
TAXATION			
Income tax	**4**	90,416	83,738
Sales tax		13,365	13,107
Excise duty		13,276	12,949
Customs duty		3,261	3,167
Other taxes, fees and fines	**5**	6,326	5,336
Total taxation revenues		**126,644**	**118,297**
: :		: :	: :

[1] Trial and unaudited

Example 14.7
Financial Statements of the Commonwealth Government of Australia
for the year ended 30 June 1997
Revenues and Expenses by Economic Type, page 23 (AUD)

	1997/98 Gross Expenditure £000	1997/98 Income £000	**1997/98 Net Expenditure £000**	1996/97 Net Expenditure £000
	: :	: :	: :	: :
This was financed by				
Council Tax income	0	224,540	-224,540	-211,680
Non-domestic rate income	0	203,107	-203,107	-213,553

Example 14.8
Surrey County Council
Statement of Accounts 1997/98
Consolidated Revenue Account, page 15 (GBP)

Other Non-Reciprocal Transfers

539. The various types of transfers made by governments are discussed in Chapter 15. When another government is the recipient of these transfers they may meet the definition and recognition criteria for revenues.

540. In addition to receiving non-reciprocal transfers from other governments or supranational authorities, governments may also receive grants, contributions or donations from the private sector.

541. Although government transfers meet the definition of revenues, the main difference between these revenues and other revenues is that there is no point of exchange which may be used as the point of recognition. In the absence of a point of exchange, another suitable recognition point must be found.

542. The CICA Public Sector Accounting Recommendations consider the recognition of government transfers.

> *Government transfers should be recognized in a government's financial statements as expenditures or revenues in the period that the events giving rise to the transfer occurred, as long as:*
> *(a) the transfer is authorized;*
> *(b) eligibility criteria, if any, have been met by the recipient; and*
> *(c) a reasonable estimate of the amount can be made.* (PSAR Section PS 3410, paragraph .07)

543. The PSAR recognizes that it might not always be possible to estimate the exact transfer to be paid or received and that estimates may need considerable judgment. Estimates also may need to be reappraised as more experience is acquired. However, "the basis for determining the amount recognized for any particular transfer should be applied consistently from year to year" (PSAR Section PS 3410, paragraph .07).

544. The general recognition criteria discussed in this section apply to all types of government transfers. In relation to grants, recipient governments would recognize grants as revenues once the eligibility criteria have been met, the donor government has confirmed that it will make the transfer, and the amount which will be received can be reliably measured.

545. Where transfers represent a loan from another government or a supranational authority they represent a liability to the recipient. However, if the transfer is a non-repayable loan, it would meet the definition of revenues. Grants include savings in outflows of future economic benefits. One example is the forgiveness of debt from another government or a supranational authority. Since the forgiveness of debt owed by a national government will not represent a capital contribution by the controlling entity, it should be recognized by the beneficiary as an item of revenue.

Restricted Transfers

546. Unrestricted grants meet recognition criteria as soon as they are received or receivable. Recognition of restricted grants, however, may be more problematic.

547. Governments receive restricted grants to assist them in carrying out their responsibilities for providing services. That benefit might not actually be obtained until a subsequent period because of the timing of performance of necessary conditions. Since there is an obligation to meet the restrictions imposed, the key issue is the timing of the recognition of the inflows as revenues.

548. Some possible alternatives for revenue recognition are:

- Matching revenues with expenses/expenditures to which they relate. Revenue recognition does not occur until conditions have been fulfilled. Consistent with the accounting basis adopted, this results in a deferral of revenues as liabilities if the conditions have not been met.
- Recognizing the inflows as revenues when received or receivable, but segregating them in the financial statements as restricted in use.
- Recognizing the inflows as revenues when received or receivable, with disclosure of the restrictions in the notes to the financial statements only. This approach ignores restrictions for revenue recognition purposes.

549. In assessing the alternatives, it is useful to consider them in the context of different types of restricted-use revenues. For example, some contributions are received under a specific agreement or program and the purpose for which they are received is outlined in the terms of the agreement or related legislation. There is a clear understanding that the funds are to be spent only for very specific purposes. In other cases, the restriction may be related to a broad class of expenses/expenditures such as "growth-related infrastructure", which still allows the government some discretion in when the resources are used and on which projects. It is restrictive only in the sense that the government does not have the discretion to use the resources for unrelated purposes.

550. Debate exists on the appropriate timing of the recognition of contributions that are restricted in use. For example, the Australian Public Sector Accounting Standards Board (PSASB) argues that revenue recognition for contributions should be related to when the government obtains control over the contributed assets (AAG 14). The PSASB considers that when the government can deploy the resources to earn interest revenues, the government controls the assets because it can benefit from them in pursuit of its objectives. The PSASB argues that restrictions on the use of an asset should only influence the timing of revenue recognition if the restrictions affect the government's capacity to use the asset in pursuing its objectives. Although a government may be expected to use resources to pursue service-delivery objectives, revenue recognition should not be deferred: a liability does not exist unless the government is obliged to sacrifice future economic benefits directly to an external party in return for their contributions. Fiduciary obligations to carry out certain activities and sacrifice economic benefits in the future are not considered to be liabilities because such an approach could arguably impose an unacceptably broad notion of liabilities and the responsibility is no different from the fiduciary responsibilities of a government to use assets efficiently and effectively. If an entity failed to meet the specific conditions attaching to a contribution of assets, and the amount of the contribution is required to be repaid, a liability and an expense would need to be recognized for the amount payable at that point. A similar approach has also been adopted in South Africa.

551. However, others believe that externally restricted inflows should be recognized as revenues only once the resources have been used for the purpose or purposes specified, or when the related expenses are recognized. It is argued that the government has an obligation to external parties until the resources are used as stipulated, and that this obligation is best reflected by recording the unspent portion as deferred revenue. It is also contended that this approach results in a more appropriate matching of the recognition of expenses/expenditures with the revenues related to them. Under this view, disclosure alone of the limitation on the government's discretion to use resources other than as specified by the external party is insufficient. This approach has been adopted in relation to both governments and accounting by charities or not-for-profit organizations in Canada, and in Sweden.

552. The PSC intends to engage in further work on the recognition of non-reciprocal revenues in the future. Whichever method is used, it is appropriate to disclose the accounting policy followed for externally restricted inflows, a general description of the nature and source of the restrictions, the amount of externally restricted inflows by major source, and the amount of contributions recognized as revenues during the reporting period in respect of which the conditions specified by the contributor have not yet been met as at the reporting date.

553. Examples of accounting policies for recognition of government grants and contributions are shown below.

Commonwealth Grants

These are funds provided by the Commonwealth to assist the States in meeting their expenditure responsibilities. These grants are for either general or specific purposes. They are recognised when received.

Example 14.9
Consolidated Financial Statements of the NSW Public Sector 1996–97
The NSW Public Sector, Notes to and forming part of the Financial Statements, page 27

Grants and contributions

Apart from Revenue Support Grant, all other revenue grants are matched against expenditure to which they relate. Capital grants and contributions are also matched to the cost of the relevant assets. This is achieved through a Government Grant Deferred Account and Contributions Deferred Account. These hold grants and contributions received and release them to revenue over the expected life of the asset to offset the depreciation element of capital charges levied for the use of the asset.

Example 14.10
Surrey County Council
Statement of Accounts 1997/98
Accounting Policies, page 12

Reciprocal (Exchange) Revenues

554. Exchange revenues include revenues from sales of goods or services, dividends, interest, and net gains arising from the sale of assets. They also include fees charged by the government for services provided under a monopoly power. They derive their name from the fact that they are the result of reciprocal transfers, or exchanges. Because they are derived from exchanges in a similar manner to the private sector, the discussion in IAS 18, *Revenue* is relevant.

555. Where goods and services are provided at a subsidy, both the revenue from the purchaser and the government subsidy are revenue of the sub-entity.

556. For the majority of exchange transactions undertaken by governments, the circumstances are similar to those found in the private sector and usual criteria of probability and measurability can therefore be applied. Recognition of transactions prior to time of payment or receipt may lead to the recognition of unrealized gains or losses.

557. An excerpt showing the types of exchange revenues earned by the Commonwealth Government of Australia is shown below.

REVENUES AND EXPENSES BY ECONOMIC TYPE
for the year ended 30 June 1997

	Note	**1997 $m**	**1996[1] $m**
: :		: :	: :
NON-TAXATION			
Sales of goods and services (incl user charges / fees)		28,535	25,207
Interest and dividends	**6**	4,140	3,489
Net foreign exchange gains	**7**	197	1,313
Net gains from sale of assets	**14**	-	15
Net gains from asset sales program	**8**	1,392	-
Other sources of non-taxation revenues	**9**	2,716	3,931
Total non-taxation revenues		**36,980**	**33,955**
: :		: :	: :

[1] Trial and unaudited

Example 14.11
Financial Statements of the Commonwealth Government of Australia
for the year ended 30 June 1997
Revenues and Expenses by Economic Type, page 23 (AUD)

Net Gains on Sale of Assets

558. Net gains arising from the sale of assets are also exchange revenues and are generally separately disclosed. The presentation of gains arising on sale of assets may vary across jurisdictions. Some jurisdictions refer to the gross sale proceeds as revenue and the carrying amount as the expense. Other jurisdictions refer to the net gain as the revenue item. However, in both cases it is common practice to disclose the net gain as a single item on the face of the financial statements with details of gross proceeds and book value being disclosed by way of note. The practice adopted by a particular jurisdiction should be explained in the Statement of Accounting Policies.

Investment Revenues

559. Investment revenues include interest and dividend income. Interest and dividend revenues collected by governments are accounted for in the same way as in the private sector. Interest is recognized when it is due, even if it has not been received. The interest on certain financial investments is received at the end of the contract. In these cases it is necessary to apportion the interest over the period of the contract.

560. Interest earned on the proceeds of issuing currency is treated in the same way as other interest revenues. Such interest is sometimes referred to as seigniorage. Dividends are often recognized when they are declared, although they may not be received immediately.

561. Examples of an accounting policy and note disclosure of investment income are shown below.

Investment Revenue

Interest and other investment income is recognised in the period in which it is earned.

Example 14.12
Consolidated Financial Statements of the NSW Public Sector 1996-97
The NSW Public Sector, Notes to and forming part of the Financial Statements, page 28

Forecast 1998 Budget $m	Forecast Estimated Actual $m		Actual 30 June 1999 $m	Actual 30 June 1998 $m
		NOTE 3: Investment Income		
		Interest Income		
		Marketable securities, deposits, mortgages and cash		
386	333	balances	343	390
		Advances		
245	222	Student loans	229	187
21	21	Contact Energy Limited	17	33
55	42	Other entities	41	36
707	**618**	**Total Interest Income**	**630**	**646**
		Dividend Income		
		Dividends from State-owned enterprises		
186	58	Electricity Corporation of New Zealand Limited	57	136
59	81	Trans Power New Zealand Limited	81	67
47	32	Television New Zealand Limited	102	21
18	13	New Zealand Post Limited	14	15
12	17	Government Property Services Limited	17	6
7	3	Land Corporation Limited	3	10
9	12	Other	8	18
46	65	Contact Energy Limited	65	48
116	122	Housing New Zealand	122	50
9	-	Housing Corporation of New Zealand	-	11
27	78	Other dividends	77	16
536	**481**	**Total Dividend Income**	**546**	**398**
		Other Investment Income		
-	54	Gains on marketable securities and deposits	13	110
-	-	Gain on incorporation of Public Trust Office reserves	86	-
	1,421	Gain on sale of Contact Energy Limited	1,421	-
	204	Gains on sale of Airport companies	204	-
-	-	Other	1	-
-	**1,679**	**Total Other Investment Income**	**1,725**	**110**
1,243	**2,778**	**Total Investment Income**	**2,901**	**1,154**

Example 14.13
Financial Statements of the Government of New Zealand
for the year ended 30 June 1999
Notes to the Financial Statements, page 66 (NZD)

Other Gains

562. Gains may arise from increases in the value of assets due to movements in market prices or currency movements and increases due to natural accretion (e.g., growth of forests, livestock). They may also include decreases in the value of liabilities due to currency movements. These gains may be realized or unrealized. The treatment of realized net gains on the sale of assets has been discussed earlier in this Chapter. The treatment of unrealized gains on assets due to changes in market value is discussed below.

Other Gains – Changes in Market Value

563. Because the accrual basis recognizes events in the period in which they occur, preparers of financial statements must decide whether to recognize unrealized gains as revenue. Practices regarding revaluation of assets vary between countries.

564. The treatment of unrealized gains depends on the measurement base adopted. Under historical cost accounting, the occurrence of a transaction (e.g., the sale of the asset) is normally required for an increase in an asset's value to be recognized. In contrast, under modified historical cost, increases in an asset's value may be recognized when the change in value occurs, if that class of assets is revalued regularly. Such gains are normally taken directly to net assets/equity although there may be some circumstances in which the gains are recognized as revenues.

565. IAS 16, *Property, Plant and Equipment* allows two different treatments for the valuation of assets. Where property, plant or equipment is recorded at the lower of depreciated historic cost or recoverable amount, increases in the value of assets are not normally recognized. However, a subsequent increase in the recoverable amount may be written back in certain circumstances (paragraph 59). Where assets are revalued regularly to fair value, revaluation increases should be taken directly to net assets/equity unless the revaluation represents a reversal of a previous decline in value, in which case the revaluation increase should be treated as income (paragraphs 39 and 40). Changes in the value of land (unless held as an investment) are usually treated in the same way. The treatment of revaluations varies between jurisdictions.

566. IAS 25, *Accounting for Investments*[7] discusses the treatment of gains and losses arising from revaluations of investment properties and some financial investments. Investment properties may be accounted for as if they were property, plant and equipment, or as long-term investments (paragraph 28). Under IAS 25 gains and losses on short-term investments may be accounted for as income and expense, or they may be accounted for as long-term investments. Gains and losses on long-term investments are taken to the revaluation reserve, subject to the proviso that the decrease does not exceed the amount held in the revaluation reserve in respect of that same asset (paragraphs 31 and 32). Where alternative treatments are available the entity should follow a consistent policy. An example of an accounting policy for gains resulting from the change in value of investments is shown below.

Unrealised gains on investments other than foreign exchange gains

1.22 Unrealised gains, other than foreign exchange gains, arising from the changes in the value of investments are treated as follows:

- the Reserve Bank of Australia takes such gains to reserves where market price is greater than cost; only realised gains are available for distribution as dividends;
- the Department of the Treasury except in relation to the quota in the International Monetary Fund, does not recognise such gains except in the case of a formal revaluation.

Example 14.14
Financial Statements of the Commonwealth Government of Australia
for the year ended 30 June 1997
Notes to and forming part of the Financial Statements, page 39

[7] The International Accounting Standards Committee has signaled its intention to withdraw IAS 25, *Accounting for Investments* following the approval of IAS 40, *Investment Property.*

Other Gains – Foreign Exchange Gains

567. Foreign exchange gains or losses arise on foreign currency monetary items. Monetary items include accounts receivable, accounts payable, and long-term liabilities or receivables. When there is a time delay between time of recognition of the transaction and time of payment, a foreign exchange gain or loss will occur. If the transaction is not completed by balance date the exchange difference resulting from translation of balances at the closing rate is an unrealized gain or loss. IAS 21, *The Effects of Changes in Foreign Exchange Rates* outlines the accounting treatment for both realized and unrealized gains or losses arising from movements in foreign currency exchange rates.

568. IAS 21 requires that exchange differences be recognized as income or expense in the period in which they arise (paragraph 15) with the exception of exchange differences arising on a monetary item that, in substance, forms part of an entity's net investment in a foreign entity, and exchange differences arising on a foreign currency liability accounted for as a hedge of an entity's net investment in a foreign entity. Exchange differences arising in these situations are classified as net assets/equity until the disposal of the net investment, at which time they should be recognized as income and expenses (paragraphs 15,17 and 19). Exchange differences are also discussed in Chapter 15 of this Study. The exchange differences on borrowings and monetary investments could be significant for many governments.

569. Under a historical cost model, declines in the value of liabilities due to foreign currency movements are recognized as revenue. However, declines in liabilities due to movements in interest rates are not recognized until the liability is settled. The reverse applies to increases in the value of liabilities.

570. The disclosure of recognized gains and losses may occur in the Statement of Financial Performance, or in the case of gains and losses which have been taken directly to reserves, in an additional statement. For example, in the United Kingdom, Financial Reporting Standard 3 requires a statement of total recognized gains and losses to show the extent to which shareholders' funds have increased or decreased from all the various gains and losses recognized in the period.

571. Examples of accounting policies for and disclosure of gains are shown below.

Gains

Realised gains arising from sales of assets or the early repurchase of liabilities are recognised in the Statement of Financial Performance in the period in which the transaction occurs.

Unrealised foreign-exchange gains on monetary assets and liabilities, and unrealised gains on marketable securities held for trading purposes, are recognised in the Statement of Financial Performance.

Unrealised and realised gains related to hedging activity are recognised in the Statement of Financial Performance in the same period in which gains on the underlying hedged position are recognised.

Unrealised gains arising from changes in the value of physical assets (including State highways) are recognised at balance date. To the extent that a gain reverses a loss previously charged to the Statement of Financial Performance, the gain is credited to the Statement of Financial Performance. Otherwise, gains are credited to an asset revaluation reserve for that class of asset.

Unrealised gains arising from changes in the value of commercial forests are credited to the Statement of Financial Performance.

Unrealised gains (excluding foreign-exchange gains) arising from changes in the value of investments and marketable securities held for investment are recognised at balance date only to the extent that they reverse a loss previously charged to the Statement of Financial Performance. Gains effecting such a reversal are credited to the Statement of Financial Performance.

Example 14.15
Financial Statements of the Government of New Zealand
for the year ended 30 June 1999
Statement of Accounting Policies, pages 59

NOTE 7. NET FOREIGN EXCHANGE GAINS/(LOSSES)

	1997 $m	1996[1] $m
FOREIGN EXCHANGE GAINS		
Non-speculative	633	3,197
Total foreign exchange gains	**633**	**3,197**
less **FOREIGN EXCHANGE LOSSES**		
Non speculative	436	1,884
Total foreign exchange losses	**436**	**1,884**
Net foreign exchange gains/(losses)	**197**	**1,313**

[1] Trial and unaudited.

Example 14.16
Financial Statements of the Commonwealth Government of Australia
for the year ended 30 June 1997
Notes to and forming part of the Financial Statements, page 49 (AUD)

Custodial/Agency Receipts

572. Custodial receipts include taxes collected as agent for another government, contributions towards pension and welfare funds and other receipts collected as agent for another entity.

573. The responsibilities of a government agency may include the levying and/or collection of taxes, fines or fees as agent of the government or another government organization, and employee contributions towards pension and welfare funds. These items may be referred to as custodial receipts, agency receipts or administered revenues. The definition of revenue refers to economic benefits in the form of inflows that result in equity. Custodial receipts are economic benefits in the form of inflows, but they normally do not belong to the collecting agency. If the collecting agency is unable to use for its own purposes the proceeds of user charges, taxes, fines and fees without further authorization, the revenues are not attributable to the collecting agency, and should be classified as custodial receipts and not recorded on the face of the financial statements contained in governmental financial reports.

574. Accountability for custodial receipts may be demonstrated by disclosing information on these receipts in a separate Statement or in the Notes to the Financial Statements. The only portion of custodial receipts which should be recorded as revenue is any commission received for the collection or handling of these flows. However, in practice some jurisdictions recognize custodial receipts in the Statement of Financial Performance. An example of a statement of custodial flows is shown below.

575. Refer also to Chapters 12,13 and 15 for discussion of administered assets, liabilities and expenses.

U.S. Department of the Interior
Consolidated Statement of Custodial Activity
for the years ended September 30, 1998 and 1997
(dollars in thousands)

	1998	1997
Collections on Behalf of the Federal Government		
Mineral Lease Collections		
Rents and Royalties	$ 4,479,181	$ 4,891,647
Offshore Lease Sales	1,464,798	1,338,559
Other	155	48,588
Total Mineral Lease Collections	5,944,134	6,278,794
Earnings on Escrow Investments		
Interest Earned - Federal Investments	52,356	40,181
Amortized Discount on Federal Investments (Note 3)	36,902	45,876
Total Earnings on Escrow Investments	89,258	86,057
Receivable Accrual Adjustment	32,731	-
Total Collections on Behalf of the Federal Government	$ 6,066,123	$ 6,364,851
Disposition of Collections		
Transferred to Others (Note 17)		
Department of the Treasury	$ 3,675,277	$ 3,820,661
National Park Service Conservation Funds	896,980	1,046,980
States	655,242	684,908
Bureau of Reclamation	422,871	442,985
Indian Tribes and Agencies	71,010	53,954
Minerals Management Service Offshore Program	71,675	41,000
Other Federal Agencies	27,304	29,553
Other Transfers	28,053	62,123
Total Transferred to Others	5,848,412	6,182,164
Increase in Collections Pending Transfer	217,711	182,687
Total Disposition of Collections	$ 6,066,123	$ 6,364,851

The accompanying notes are an integral part of these financial statements.

Example 14.17
U.S. Department of the Interior
Annual Report Fiscal Year 1998, page 62 (USD)

Classification

576. Classification depends on users' needs and on how they can best be met. The constraints identified in the discussion of classification of assets (Chapter 12) apply here also.

577. Classifying revenues into various types helps users to determine how dependent the government is on any particular source of revenues, and consequently, the sustainability of its fiscal position. For this reason it may be useful to distinguish taxes (fiscal revenues) from non-fiscal revenues. Some broad classifications which may be used are:

- Reciprocal (exchange) revenues and gains;
- Non-reciprocal revenues – revenues from the use of the powers of Government; and
- Non-reciprocal revenues – grants, contributions and donations.

578. The classification of user charges as reciprocal or non-reciprocal may vary between jurisdictions. Where the user charge represents a service provided by the government and the price is set at the cost of the service, or after allowing for a reasonable rate of return on costs, then the charge may be classified as reciprocal. However, where there is an element of taxation in that the price exceeds costs (and any allowance for a reasonable return) the charge, or part of the charge, may be regarded as non-reciprocal.

579. Existing systems for classification of revenue include the System of National Accounts (SNA) and the International Monetary Fund's Government Finance Statistics (GFS). These are shown in Chapter 19.

580. The particular types of revenue, and the names attached to them, will vary between jurisdictions. Different countries will also vary in the amount of detail they wish to provide and the extent to which governmental financial reports follow other classifications such as GFS and the SNA.

581. A possible classification system for revenues and examples of classification by function and economic type are shown below.

Non-reciprocal Revenues/Revenue from the use of the Powers of Government (depending on the particular jurisdiction)
Taxes on income, profits and capital gains
Sales taxes
Property taxes
Payroll taxes
Poll taxes
Social security contributions
Taxes on specific services
Excises
Customs and import duties
License, registration and permit fees
Fines
Revenue from the issue of currency

Reciprocal (Exchange) Revenue and Gains
Sales
Dividends
Interest
Royalties
Net gains on assets sold

Grants, Contributions and Donations
(with separate disclosure of any restrictions on use)
From other levels of government
From other governments
From supranational authorities
From the private sector

Other Gains (realized and unrealized)
Foreign exchange gains
Increases in market value of assets
Increases due to natural accretion (e.g., growth of forests or livestock)

REVENUES AND EXPENSES BY FUNCTION *for the year ended 30 June 1997*			
		1997[3]	**1996[1]**
	Note	**$m**	**$m**
Revenues by source			
Taxation		126,644	118,297
Non-taxation		36,980	33,955
Total revenues		**163,624**	**152,252**
Expenses by purpose[2]			
General public services			
Legislative and executive affairs		356	605
Financial and fiscal affairs		2,528	5,615
Foreign economic aid		1,956	1,748
General research		1,049	1,290
General services		1,191	2,409
Government superannuation benefit		4,132	3,985
Defence		11,758	9,004
Public order and safety		1,486	1,302
Education	**3(a)**	10,930	9,819
Health		**3(b)**	18,629
16,453			
Social security and welfare	**3(c)**	48,201	45,632
Housing and community amenities		1,800	531
Recreation and culture		1,691	1,669
Fuel and energy		282	310
Agriculture, forestry and fishing		4,420	2,895
Mining, manufacturing and construction		2,384	1,606
Transport and communications	**3(d)**	21,010	18,411
Other economic affairs		3,722	4,717
Central banking		887	1,381
Other purposes			
Public debt interest		8,499	9,917
General purpose inter-government transactions	**3(e)**	19,130	17,110
Natural disaster relief		29	n/a
Asset sales		81	9
Total expenses		**166,151**	**156,418**
Operating result		**(2,527)**	**(4,166)**

The above statement should be read in conjunction with the accompanying notes.

1 Trial and unaudited.

2 Refer to the glossary for an explanation of terms.

3 Allocation of total expenses by government function are classified using estimates, based upon cash related information.

Example 14.18
Financial Statements of the Commonwealth Government of Australia
for the year ended 30 June 1997
Revenues and Expenses by Function, page 22 (AUD)

REVENUES AND EXPENSES BY ECONOMIC TYPE
for the year ended 30 June 1997

	Note	1997 $m	1996[1] $m
Revenues			
TAXATION			
Income tax	**4**	90,416	83,738
Sales tax		13,365	13,107
Excise duty		13,276	12,949
Customs duty		3,261	3,167
Other taxes, fees and fines	**5**	6,326	5,336
Total taxation revenues		**126,644**	**118,297**
NON-TAXATION			
Sales of goods and services (incl user charges / fees)		28,535	25,207
Interest and dividends	**6**	4,140	3,489
Net foreign exchange gains	**7**	197	1,313
Net gains from sale of assets	**14**	-	15
Net gains from asset sales program	**8**	1,392	-
Other sources of non-taxation revenues	**9**	2,716	3,931
Total non-taxation revenues		**36,980**	**33,955**
Total revenues		**163,624**	**152,252**
Expenses			
GOODS AND SERVICES			
Employees	**10**	23,867	21,641
Suppliers	**11**	18,096	15,321
Depreciation and amortisation	**12**	5,305	5,726
Net write-down of assets	**13**	1,727	3,187
Net losses from sale of assets	**14**	119	-
Other goods and services expenses	**15**	1,092	397
Total cost of goods and services		**50,206**	**46,272**
SUBSIDIES, BENEFITS AND GRANTS			
Subsidies		4,372	4,620
Personal benefits		57,578	53,826
Grants	**16**	41,317	39,700
Total subsidies, benefits and grants		**103,267**	**98,146**
INTEREST AND OTHER			
Interest and other financing costs	**17**	12,678	11,755
Net losses from asset sales program	**8**	-	245
Total interest and other		**12,678**	**12,000**
Total expenses		**166,151**	**156,418**
Operating result	**33**	**(2,527)**	**(4,166)**

The above statement should be read in conjunction with the accompanying notes.

[1] Trial and unaudited.

Example 14.19
Financial Statements of the Commonwealth Government of Australia
for the year ended 30 June 1997
Revenues and Expenses by Economic Type, page 23 (AUD)

CHAPTER 15

ACCRUAL BASIS – EXPENSES

Introduction

582. The definition of expenses, and the application of this definition to expenses in the public sector have previously been discussed in PSC Study 2 *Elements of the Financial Statements of National Governments* and PSC Study 10 *Definition and Recognition of Expenses/Expenditures*.

583. Both studies considered the applicability of the IASC definition of expenses to government reporting entities. In addition, Study 10 examined the applicability of the IASC expense recognition criteria to government transactions and events.

584. This Chapter both summarizes and extends the work in the Studies 2 and 10. It describes various types of government outflows and considers whether they meet the definition of an expense. It then considers the application of recognition criteria to these transactions and events. It also provides examples of expense disclosure and expense accounting policies from the financial statements of government reporting entities.

Definition of Expenses

585. The IASC Framework for the Preparation and Presentation of Financial Statements defines the element of expenses as follows:

> *Expenses are decreases in economic benefits during the accounting period in the form of outflows or depletions of assets or incurrences of liabilities that result in decreases in equity, other than those relating to distributions to equity participants.* (paragraph 70)

586. PSC Study 2 concluded that the IASC definition of expenses is appropriate for government reporting entities which have adopted the accrual basis of accounting and which prepare an articulated set of financial statements. However, the Study notes that the references to the term “equity” in the definition may not be appropriate for government reporting entities as it is not commonly used in the public sector. Instead, terms such as “net assets” or “net worth” may be used. This Study uses the term “net assets/equity” to refer to this element. PSC Study 10 also acknowledged that the IASC definition of expenses substantially applies to the accrual basis.

587. The definition of an expense does not apply to payments for operating items which relate to preceding or subsequent accounting periods. Payments which relate to the preceding accounting period occur when goods or services have been provided to the entity in the preceding accounting period but where payment does not occur until the next period. Such transactions are recognized as both an expense and a liability (accounts payable or creditors) in the preceding period. The payment of the liability is not an expense, although a cash, or other, payment would be recorded. Payments which relate to subsequent accounting periods occur when a prepayment is made (e.g., the payment of a portion of employees’ salaries in advance). Such prepayments are recognized as an asset at the time of payment and as an expense when the employee has earned the salary.

588. The definition of an expense does not apply to financing flows such as the repayment of debt, or investment flows such as the purchase of financial or physical assets.

Recognition of Expenses

589. This section discusses the recognition criteria for an expense under accrual accounting. There is a range of possible recognition points. Under accrual accounting, recognition may occur prior to payment (as in the case of items which are purchased on credit), at the time of payment, or after payment. The focus is on trying to determine when resources have been consumed by the entity.

590. The IASC Framework for the Preparation and Presentation of Financial Statements requires that, in order to be recognized as an expense, a transaction or event must meet both the definition of an expense and the recognition criteria of probability and measurability.

591. The IASC Framework for the Preparation and Presentation of Financial Statements outlines the following recognition principles:

> *Expenses are recognized in the income statement when a decrease in future economic benefits related to a decrease in an asset or an increase of a liability has arisen that can be measured reliably. This means, in effect, that recognition of expenses occurs simultaneously with the recognition of an increase in liabilities or a decrease in assets (for example, the accrual of employee entitlements or the depreciation of equipment).* (paragraph 94)
>
> *Expenses are recognized in the income statement on the basis of a direct association between costs incurred and the earning of specific items of income. This process, commonly referred to as the matching of cost with revenues, involves the simultaneous or combined recognition of revenues and expenses that result directly and jointly from the same transactions or other events; for example, the various components of expense making up the cost of goods sold are recognized at the same time as the income derived from the sale of the goods. However, the application of the matching concept under this framework does not allow the recognition of items in the balance sheet which do not meet the definition of assets or liabilities.* (paragraph 95)

592. Expenses are recognized when they meet the definition of an expense and satisfy the recognition criteria of measurability and probability. The presentation and disclosure of the accounting policies adopted in relation to recognition of expenses is essential.

593. Many of the expenses incurred by governments and their sub-entities are similar to those recognized in the private sector by businesses. They do not pose particular accounting or reporting issues for government, and the IASC accounting standards provide useful guidance on recognition and measurement.

594. Study 10 concluded that the IASC recognition criteria are adequate for some government transactions or events. However, in the absence of a point of exchange, another suitable recognition point must be found. Study 10 considered various recognition points for transactions and events with no point of exchange.

EXPENSES

Expenses are recognised when incurred and are reported in the financial year to which they relate.

Example 15.1
Consolidated Financial Statements of the NSW Public Sector 1996–97
The NSW Public Sector, Notes to and forming part of the Financial Statements, page 28

Types of Expenses

595. Public sector entities usually have some political or social welfare objectives. They are responsible for providing health, safety, education, social and other services to their constituencies. In rendering these services, public sector entities incur a range of different expenses, some of which, for reasons of type or relative amount, are more significant than in the private sector. The types of expenses that governments may report include:

- personnel expenses;
- cost of goods sold;
- cost of services provided;
- physical asset use (depreciation and loss of service potential);
- rental and leasing costs;
- maintenance and working expenses;
- interest;
- expenses relating to financial assets;
- government transfers;
- other losses;

- changes in market value; and
- foreign exchange losses.

596. Most of these items are similar to expenses recognized by business enterprises, such as personnel expenses, or interest on debt, but may be more material in the government context. Exchange expenses that are similar to those identified in the private sector do not pose particular accounting or reporting issues for government and are not discussed fully in this Study. Given the prevalence of non-reciprocal transfers in the public sector, this Chapter focuses on the expenses associated with non-reciprocal transfers. The Chapter also considers issues associated with depreciation, the activity of transfer agencies and development expenses in the public sector.

597. The types of expenses incurred by particular government entities will depend on the type of activities conducted by the entity. Entities providing mainly policy advice will spend a high proportion of their budget on personnel. Entities providing operational services (e.g., operating penal institutions) will incur a wider range of expenses. The following sections describe each category of expenses and discuss recognition issues associated with these expenses.

Appropriations

598. Appropriations are an authorization to spend funds, often for a specified purpose. Although the nature of appropriations varies across jurisdictions, they may fall into the following general categories:

- authorizations for services performed;
- authorizations for permanent increases to the resource base of a government entity; and
- authorizations for transfers to third parties.

599. Appropriations received in return for, or in expectation of, services performed meet the definition of revenue under accrual accounting. Appropriations which result in permanent increases to the resource base of an entity may be in the nature of a capital or equity contribution, where the government entity is corporatized or where a purchaser-provider (or similar) model of government has been adopted. The third category covers custodial or agency receipts and as such is not an element of the reporting entity. Where the purpose of an appropriation is unclear, the appropriation may need to be allocated across these categories, or the total amount recognized as revenue.

600. Depending on the legislative framework of a particular jurisdiction, the expenses resulting from the transfer of funds under appropriation may be classified as exchange expenses or non-reciprocal transfers.

Personnel Expenses (including Superannuation/Pension Expenses)

601. Personnel expenses include wages and salaries, all types of paid leave, recruitment and training costs and superannuation/pension and other benefits paid to staff.

602. The current period's portion of long-term superannuation/pension obligations is recorded as an expense. To the extent that these expenses remain unpaid at the end of the reporting period, it is necessary to recognize a liability in the Statement of Financial Position. Refer to Chapter 13 for a discussion of superannuation/pension liabilities.

603. The recognition and measurement of personnel expenses is generally the same in both the public and private sectors. Differences may arise in the area of superannuation/pension expenses. Government superannuation/pension schemes are more likely to be defined benefit schemes than are private sector schemes. In some jurisdictions public sector schemes operate on a pay-as-you-go basis, which is not usually an option in the private sector.

604. Examples of accounting policies and disclosure of personnel expenses are shown below.

Employee Related Expenses

These expenses include all costs related to employment such as salaries and wages, superannuation, leave entitlements, fringe benefits tax, workers' compensation, redundancies and other on-costs associated with leave entitlements. Payroll tax (a State tax) is eliminated on consolidation. Some employee related expenses are included in maintenance costs or capitalised as part of the construction costs of certain non-current physical assets.

Example 15.2
Consolidated Financial Statements of the NSW Public Sector 1996-97
The NSW Public Sector, Notes to and forming part of the Financial Statements, page 28

NOTE 10. EMPLOYEES

	1997 $m	1996[1] $m
Remuneration (for services provided)		
Salaries and wages	15,257	14,503
Superannuation	5,448	5,095
Leave and other entitlements	673	1,190
Separations and redundancies	1,722	98
Workers compensation premiums	725	170
Other	42	585
Total employees	**23,867**	**21,641**
: :	: :	: :

1 Trial and unaudited

Example 15.3
Financial Statements of the Commonwealth Government of Australia
for the year ended 30 June 1997
Notes to and forming part of the Financial Statements, page 51 (AUD)

Cost of Goods Sold and Cost of Services Provided

605. The costs associated with inventory, both purchased or internally created, sold or used during the period are treated as an expense. However the costs associated with inventory still on hand at the end of the accounting period, including work in progress, are treated as an asset.

Physical Assets' Use (Depreciation and Loss of Service Potential)

606. Payments which relate to the acquisition of physical assets (e.g., land and buildings, vehicles, office equipment) are recognized in the Statement of Financial Position as assets. They are not expenses because they do not result in a decrease in the net assets/equity of the entity. However the depreciation of those assets, as their service potential is consumed, is an expense in the periods in which the asset is used. Long-term intangible assets are generally amortized.

607. The consumption of limited-life physical assets occurs in the public sector, and the requirements of IAS 16, *Property, Plant and Equipment* may be applied to public sector assets. Sometimes the view is taken that depreciation is not relevant for public sector assets such as infrastructure, heritage and community assets, because their economic benefits are realized over an extended period of time. However, if the asset has a finite life, the service potential or future economic benefits embodied in the asset will be consumed or will expire and will therefore give rise to expenses. This section

discusses loss of service potential under three categories:

- loss of service potential associated with physical assets, generally known as depreciation;
- loss of service potential of infrastructure assets; and
- loss of service potential of intangible assets.

Depreciation – Physical Assets

608. The costs associated with physical assets include the initial cost of purchase, the cost of repairs (or maintenance) and the restoration of service potential in the asset (capital expenditure).

609. Under accrual accounting, if the initial purchase cost and subsequent restoration of service potential in the asset meet the definition and recognition criteria for an asset, then they are recognized as an asset, not an expense. The loss of service potential in the asset as a result of time, use in production and obsolescence is recognized as depreciation expense. The cost of repairs and maintenance is also recognized as an expense at the time it occurs.

610. An asset can be said to be consumed if its service potential declines from its acquisition to its eventual disposal, for example a bridge's expected future life in use may decline with time, wear or for some other reason. When it occurs, the loss of service potential of major assets from wear and obsolescence is material to users of financial reports and the accurate reporting of such expense is one of the chief benefits from using the accrual accounting in the public sector.

611. The required accounting treatments for depreciation are set out in IAS 16, *Property, Plant and Equipment.* The standard applies only to those depreciable assets listed in the standard.

612. Depreciation is defined by IAS 16 as "the systematic allocation of the depreciable amount of the asset over its useful life" and the depreciable amount is "the cost of an asset, or other amount substituted for cost in the financial statements, less its residual value." (paragraph 7) That is, depreciation is an allocation of the cost of an asset to those accounting periods during which the asset is used. The cost of an asset may be regarded as a prepayment which is expensed over the relevant period. The "useful life" is measured in time, units of production or units of service.

613. The generally accepted accounting practice is to report the periodic loss of service potential as a period expense (depreciation expense) and as an addition to the cumulative depreciation provision deducted from the gross value of the asset.

614. The main purpose of depreciation is to allocate the cost of a fixed asset over a period so that accurate measurement of expenses (i.e., consumption of service potential) is achieved. Depreciation is then the allocation of that fixed asset cost to each of the particular years the asset is used. The written down (or book) value of the assets as shown in the financial statements therefore represents the cost of the asset yet to be allocated to future years.

615. The allocation of depreciation gives a more accurate assessment of the net surplus or deficit and thereby prevents net assets/equity from being overstated. This is particularly important for governments monitoring specific fiscal goals such as a specified target level of net assets/equity.

616. Examples of depreciation policies are shown below.

Depreciation

Depreciation of fixed assets other than freehold land, furniture and fittings and capital work in progress, is provided on a straight line basis so as to allocate the cost (or valuation) of assets, less any estimated residual value, over their estimated useful lives. Revalued fixed assets are depreciated on their revalued amount on a straight line basis over their remaining useful lives. The estimated economic useful lives are:

Buildings	50 years
Specialist Military Equipment	5 – 50 years
Plant and Equipment	5 – 50 years
Office and Computer Equipment	5 – 20 years

Example 15.4
Annual Report of the New Zealand Defence Force
for the year ended 30 June 1999
Statement of Accounting Policies, page 114

Capital Assets

14. Depreciation, on a straight line basis, has been provided for in the accounts for all short lived assets (vehicles, plant and equipment) over a period of five years, unless a significantly different life is anticipated. Depreciation for infrastructure assets has been provided over the estimated useful life of the infrastructure, ranging from seven years for minor highways works to 40 years for bridge reconstruction.

15. Property assets are not depreciated as the Authority can demonstrate that the remaining life of the existing assets is in general, in excess of 20 years, and that the level of repairs and maintenance undertaken extends the life of the properties sufficiently for any depreciation not to be material. The charging of repairs and maintenance to revenue thus replaces the provision of depreciation. Land, non-operational properties and community assets are not depreciated.

Example 15.5
Surrey County Council
Statement of Accounts 1997/98
Accounting Policies, page 9

Depreciation

Depreciation across the State Public Sector is generally calculated at rates determined on a straight line basis to allocate the cost or valuation of an asset, less any estimated residual value, over its estimated useful life to the entity.

School buildings are depreciated at a rate of 1% per annum based on an estimated life expectancy of one hundred years. However, over a 100 year cycle, school buildings would normally be subject to a number of major refurbishments in order to achieve their estimated service potential. This element has not been taken into account in assessing the depreciation charges and the carrying value of school buildings.

Depreciation of residential properties controlled by the NSW Land and Housing Corporation has been calculated using the straight line method with the economic useful life being estimated as 50 years, with nil salvage value. The depreciation method relies on representative sample historical costs by building type and year of completion and average costs of construction extrapolated to the total number of properties in stock.

Sydney Water Corporation's depreciation of infrastructure assets is currently based on the assumption of normal wear and tear rather than condition-based. However, the Corporation is undertaking a revaluation project which will involve revaluation of assets on a segmented basis and condition-based assessments of asset lives. When implemented, this may impact on asset values and depreciation charges for some classes of assets.

The Roads and Traffic Authority recognises depreciation of roads based on condition-based assessment. The annual depreciation charge reflects the changes in the road condition during the year from normal wear, tear and deterioration. It is calculated by comparing the written down replacement value of the roads at the end of the year (reflecting current condition) with the value at the beginning of the year. Depreciation is not based on the useful life of roads because the useful life cannot be reliably determined.

Example 15.6
Consolidated Financial Statements of the NSW Public Sector 1996-97
The NSW Public Sector, Notes to and forming part of the Financial Statements, page 28

Loss of Service Potential – Infrastructure Assets

617. The accepted practice of allocating the acquisition cost of a physical asset over its estimated life on an arithmetical basis (i.e., depreciation) may not be sufficiently accurate for financial reporting of complex, multi-component assets, such as infrastructure assets. The depreciation of infrastructure assets reflects their loss of service potential over time. Expenditures on renewal and expansion which extend the service potential of an asset beyond its originally estimated useful life may be capitalized if they meet the definition and recognition for an asset.

618. The determination of depreciation of infrastructure assets is complicated by the number of components which make up a network and the fact that the service potential of different components is consumed at different rates. Networks such as roads, water supply and drainage have very long lives and are composed of many separate components that contribute to the operation of the network. In practical administration, it is necessary to group the component assets for financial recording and management. As this is done, the concept of "useful life" becomes more difficult to apply to the groups of assets. If the lives are long, and the system extensive, then it is probable that any single predetermined "life" or depreciation rate will be inappropriate for the system as a whole, and possibly for some material groups of components.

619. Financial reporting practices for infrastructure assets have been diverse and there is currently no consensus on an accounting technique for infrastructure assets (Rowles 1992). Various jurisdictions have formed their own approach to accounting for accounting for and valuing infrastructure assets. Alternatives include full depreciation accounting, renewals accounting and condition-based depreciation.

620. Full depreciation accounting for infrastructure assets has been discussed above. Some preparers

consider that a condition-based method of depreciation is more appropriate for infrastructure assets due to the long or indeterminate life of such assets. The long life of such assets generally means that some factors have a greater impact upon the condition and therefore the value of infrastructure assets, than shorter-lived assets. For example, the following factors are likely to affect the condition of a road over time and therefore its remaining service potential:

- the quality of the original asset e.g., the materials, methods and skills used in the construction of the road;
- wear and tear e.g., changes in traffic density and the environment in which the road is operated or constructed can significantly affect its service potential;
- reactive soils, extremes of climate etc; and
- the maintenance provided to the asset — the regularity and consistency of asset maintenance to an optimum level will significantly affect the life of the road or the run-down of its service potential.

621. Renewals accounting takes many forms. One form of renewals accounting is described as follows:

- infrastructure assets of a similar nature are treated as a single asset;
- replacements are expensed and no depreciation is charged provided overall service potential is being maintained; and
- additions which enhance the service potential of the network or system are capitalized.

622. Renewals accounting is accepted in some, but not all, jurisdictions as being acceptable for external financial reporting. However, preparers should note that, even in these jurisdictions, renewals accounting will normally only be accepted for external financial reporting if the entity has a formal asset management plan that enables an assessment of any change in service potential to be assessed and the infrastructure asset network is demonstrably in a steady state. This requires detailed information on the condition of all components of the system.

623. For an example of an accounting policy for infrastructural assets, including roads, which refers to condition-based depreciation see Example 15.6 above.

Maintenance – Infrastructure Assets

624. Where the amount of maintenance performed is less than the amount required to maintain an infrastructure asset at its current level of activity and condition, then deferred maintenance may accumulate. Deferred maintenance may be recognized in a variety of ways. Although it may result in a future outflow of resources, it does not meet the definition of a liability as there is no obligation to a third party. In some jurisdictions deferred maintenance is recognized by acknowledging that the deferred maintenance has reduced the value of the asset and devaluing the asset accordingly. Regardless of how deferred maintenance is acknowledged in the financial statements, governments should have information on the collective amount of deferred maintenance, as it represents an internal claim on future resources.

625. There is a link between the method and rate of depreciation applied to infrastructure assets and the maintenance expense. Some entities may choose to perform less maintenance and anticipate a shorter working life for an asset.

Loss of Service Potential – Intangible Assets

626. The use or consumption of intangible assets is referred to as amortization. Intangible assets may be amortized over the expected useful life of the benefits accruing from those assets, or the loss of service potential may be assessed in relation to changes in market value of the intangible asset. IAS 9, *Research and Development Costs* (paragraphs 21–24) discusses the amortization of development costs recognized as an asset.

Interest

627. The principles used to determine interest and financing costs in the private sector are equally applicable to the public sector. An example of the types of interest and financing costs recognized by a government is shown below.

NOTE 17. INTEREST AND OTHER FINANCING COSTS		
	1997	**1996[1]**
	$m	**$m**
INTEREST ON DEBT		
Government securities	8,102	9,046
Loans	1,388	1,237
Swaps	1,079	702
Taxation overpayments	660	299
Exchange settlement funds	407	-
Deposits	144	110
Leases	18	24
Other	23	163
Total interest on debt	**11,821**	**11,581**
OTHER FINANCING COSTS	857	174
Total interest and other financing costs	12,678	11,755

[1] Trial and unaudited

Example 15.7
Financial Statements of the Commonwealth Government of Australia
for the year ended 30 June 1997
Notes to and forming part of the Financial Statements, page 55 (AUD)

Expenses Relating to Financial Assets

628. Expenses associated with financial assets are discussed under the following sub-headings:

- forgiveness or writing down of loans;
- discounting of future expected revenues; and
- expenses relating to equity investments.

Forgiveness or Writing Down of Loans

629. The making of a loan which is repayable (and collectable) does not meet the definition of an expense as it does not result in a reduction of net assets/equity. Such loans meet the definition of an asset and would be recognized as an investment in the Statement of Financial Position (refer to the discussion of investments in Chapter 12). However, concessionary or suspensory loans which may be written off over time may meet the definition of an expense as the amount expected to be repaid declines. A corresponding amount would be deducted from the investment balance. The forgiving of loans would also meet the definition of an expense. The amount forgiven is normally recognized as an expense by the forgiving entity at the time it is forgiven.

Discounting of Future Expected Revenues

630. As with private sector entities, government entities may sometimes discount future revenues by entering into agreements to obtain cash now in return for transferring the rights to future revenues to another party. The fee implicit in such arrangements represents a financing expense.

Expenses Relating to Equity Investments

631. Two types of expenses may arise in relation to equity investments (including investments in government-owned entities). When the value at which the investment is recorded in the financial statements is written down, this will normally result in a loss. Refer to Chapter 12 for a discussion of financial investments and to the discussion of other losses later in this Chapter.

632. In addition, expenses may be incurred when a government makes a capital contribution directly to another entity. Normally a capital contribution would result in an increase in the carrying value of the investment. However a capital contribution may give rise to an expense when the capital contribution is not recoverable (e.g., when an equity contribution is made to a government agency in financial distress to prevent its collapse or to ensure that creditors of that agency do not suffer a loss). Contributions required because of obligations under guarantees and indemnities would also fall into this category.

Government Transfers

633. One definition of government transfers comes from IAS 20, *Accounting for Government Grants and Disclosure of Government Assistance*. This definition focuses on transfers of resources from the government to enterprises.

> <u>Government grants</u> *are assistance by government in the form of transfers of resources to an enterprise in return for past or future compliance with certain conditions relating to the operating activities of the enterprise.* (paragraph 3)

634. An alternative definition, which also encompasses transfers to individuals and inter-governmental transfers, comes from Public Sector Accounting Recommendation (PSAR) Section PS 3410, *Government Transfers,* of the Canadian Institute of Chartered Accountants (CICA).

> ***…government transfers*** *are transfers of money from a government to an individual, an organization or another government for which the government making the transfer does not:*
> *(a) receive any goods or services directly in return, as would occur in a purchase/sale transaction;*
> *(b) expect to be repaid in the future, as would be expected in a loan; or*
> *(c) expect a financial return, as would be expected in an investment.* (paragraph .03)

635. The PSAR identifies three major types of transfers: entitlements, transfers under shared cost agreements and grants. These categories are based on a concept of a spectrum in the degree of discretion the government has in making a transfer. Further discussion of each of these transfers is given below. Not all countries make this distinction between types of transfers.

636. Transfers, as discussed in this section, specifically exclude capital contributions made by a government in its capacity as owner. Capital contributions are not expenses. They are recognized as an investment by the entity making the contribution, and as part of the net assets/equity section of the statement of financial position by the entity receiving the contribution.

637. Although government transfers meet the definition of an expense, the main difference between these expenses and other expenses is that there is no point of exchange which may be used as the point of recognition. In the absence of a point of exchange, another suitable recognition point must be found. The application of liability recognition criteria to government transfers is discussed in Chapter 13. This discussion is directly applicable to the recognition of expenses. Where a government department makes transfers on behalf of a higher level of government, the department also needs to decide whether to account for the transfer as an expense or a custodial payment. Custodial payments are discussed later in this Chapter.

638. PSAR Section 3410 considers the recognition of government transfers. It states that:

> *Government transfers should be recognized in a government's financial statements as expenditures or revenues in the period that the events giving rise to the transfer occurred, as long as:*
> *(a) the transfer is authorized;*
> *(b) eligibility criteria, if any, have been met by the recipient; and*
> *(c) a reasonable estimate of the amount can be made.* (paragraph .07)

In the context of the accrual basis, the term expenditure should be read as referring to expenses.

639. Government transfers may have characteristics of more than one type of transfer. In deciding when to recognize the specific type of transfer, the following criteria may be applied:

- Has the event giving rise to a transfer occurred? An event could be described as a "happening of consequence to an entity" and can be classified either as government related or government acknowledged.
- Has the transfer been authorized? In many countries, transfers cannot be made without the approval of government or the legislature. Therefore, even though the other criteria have been met, without the proper authorization the transfer might not be recognized by the governing legislation.
- Has the recipient met the eligibility criteria?
- Can the amount be reasonably estimated? In many cases, this seems to be a serious impediment to recognizing a transfer. Judgment is required in such cases.

640. In summary, government transfers would be recognized in the financial statements of the government making the transfer as an expense in the period that the events giving rise to the transfer occurred, as long as:

- the transfer is authorized;
- eligibility criteria, if any, have been met by the recipient; and
- a reasonable estimate of the amount can be made.

641. The PSAR recognizes that it might not always be possible to estimate the exact transfer to be paid or received and that estimates may need considerable judgment. Estimates also may need to be reappraised as more experience is acquired. However, "the basis for determining the amount recognized for any particular transfer should be applied consistently from year to year" (PSAR Section PS 3410, paragraph .07).

642. The presentation and disclosure of the adopted accounting policies is essential: "In addition, disclosing a description of the accounting policies regarding government transfers and information on the major kinds of transfers made or received is useful in understanding the sources and types of revenues a government receives and in understanding the programs and activities it undertakes" (PSAR Section PS 3410, paragraph .55).

Entitlements

643. Entitlements are defined as "transfers that a government must make if the recipient meets specified eligibility criteria. Such transfers are non-discretionary in the sense that both:

(i) "who" is eligible to receive the transfer; and
(ii) "how much" is transferred are prescribed in legislation and/or regulations. (PSAR Section PS 3410, paragraph .04)

644. This definition is consistent with the one used by the FASAB, which describes an entitlement program as "a program in which the government becomes automatically obligated to provide benefits to members of a specific group who meet the requirements established by the law." (FASAB, SFFAS No. 5, Appendix B, Glossary)

645. Government transfers which may be classified as entitlements include welfare benefits, old age benefits, family allowances and unemployment benefits. Entitlements are unique to government although they share some characteristics with donations made in the private sector. Entitlements are typically paid to individuals although they may also be paid to private enterprises or governmental institutions.

646. A number of significant inter-governmental transfers are entitlements. Entitlements received by one government from another include formula-based equalization transfers and per capita transfers from provincial governments to local governments. Some transfers to institutions are also entitlements.

647. The governing legislation or regulations for these transfers set out the bases for determining the amount of the entitlement. Some, such as federal/provincial equalization, are based on complex formulas. Others may be calculated on a per capita or other unit basis.

648. The general recognition criteria discussed above apply to these entitlements. Entitlements "should be recognized by the transferring government for estimated unpaid entitlements due at the end of the accounting period to those individuals who had met eligibility criteria." (PSAR Section PS 3410 paragraph 19). However, it is also necessary to determine "cut off points" both for the initial recognition of entitlements and the measurement of the amount to be incorporated in the current financial statements.

649. One option for the initial recognition of an entitlement is to use the acceptance of an application for the entitlement as the point of recognition. Where entitlements are paid to institutions or other governments, estimation of the expense and associated liability may be more complex. For example, the necessary data for the calculation of an entitlement might not be available for a considerable time period, or the accounting period of the two entities could be different. When determining the amount of the expense and any associated liability to be accrued in the current financial statements for those receiving entitlements in this period, only those amounts already owed, but not yet paid, should be recognized.

650. Another issue is whether potential obligations arising from an existing policy, but relying on a future event (e.g., a person becoming or remaining unemployed next year) constitute an expense (and thus, a liability of the current year). In some jurisdictions, the assessment underlying the treatment in the financial statements is that such potential future obligations are not present liabilities because Government policies do not create a legal claim. In Australia, for example, "the making of election promises or the formulation of a budget will not, under normal circumstances, mean that the commitments included therein would meet the definition of a liability. This is because governments normally have discretion to avoid the sacrifice of future economic benefits that may be associated with the election promises or budget. Similarly, a government does not have a present obligation to sacrifice future economic benefits for social welfare payments that might arise in future reporting periods." (AARF, AAS 31, paragraph 12.1.2)

651. In other jurisdictions, legal obligations to continue benefit programs may be such that they do represent liabilities, and increases in these liabilities would be recorded each year as an expense. The treatment in a particular country will depend on the institutional arrangements of that country. Even in those cases where an expense/liability should be recognized, the reliability of the measurement can prevent the recognition of that expense/liability. In the absence of a clear legal responsibility, the existence of an obligation for which the government may have a liability must be assessed on the basis of available evidence. In situations such as these, estimates may be necessary in determining not only the amount to be paid in settlement of an obligation, but also the expectation that payment will be made. This issue is also discussed in Chapter 13.

Transfers under Shared Cost Agreements

652. Transfers under shared cost agreements are defined as "reimbursement of eligible expenditures pursuant to an agreement between the transferring government and the recipient." (PSAR Section PS 3410, paragraph 04)

653. These transfers are similar to entitlements in that the recipient has the right to a transfer after incurring eligible expenditures. They are different from other entitlements, however, because the recipient must spend money to be entitled to any reimbursement. In addition, the terms of specific shared cost agreements are usually negotiated and agreed upon in a signed contract.

> *Transfers under shared cost agreements should be recognized as revenue when the recipient incurs eligible expenditures because, under the agreement, the government must reimburse the recipient for the specified percentage of those eligible expenditures. Liabilities should be recognized by the transferring government at the end of the accounting period for the estimated, unpaid portion of incurred eligible expenditures owed to recipients pursuant to a shared cost agreement.* (PSAR Section PS 3410, paragraphs .31, .32)

Grants, Contributions and Donations

654. Grants, contributions and donations are transfers made by a government, other than entitlements and transfers under shared cost agreements. The transfer may take the form of cash, services, transfer of an asset, or reduction of a liability. "The government making the transfer has discretion as to whether or not to make a transfer, the conditions to be complied with, if any, how much will be transferred and to whom." (PSAR Section PS 3410, paragraph .04)

655. Conditions may or may not attach to the grant. In most cases, recipients have to apply for the money or meet some eligibility criteria; however, in contrast to entitlements, applying or meeting eligibility criteria does not guarantee that the recipient will receive the money. The government still has discretion to decide whether or not to make the transfer. There is usually a ceiling on the total amount that may be transferred under a particular grant program and some grant recipients are subject to performance or reporting requirements. As long as the grant is discretionary, the expense is incurred in the financial statements at the time of authorization, rather than at the time the application is made. (PSAR Section PS 3410, paragraph .38)

656. The accounting policy in the Financial Statements of the New Zealand Government for the recognition of grants and subsidies includes a requirement to give notice to the Crown.

> *Where grants and subsidies are discretionary until payment, the expense is recognised when the payment is made. Otherwise, the expense is recognised when the specified criteria have been fulfilled and notice has been given to the Crown.* (Financial Statements of the Government of New Zealand for the year ended 30 June 1999, page 60)

657. In addition to the transfer of grants to individuals or private sector enterprises, governments commonly use the term grants to refer to a wide range of transfers to government departments and government organizations. As these transfers are often made under appropriation, refer also to the discussion of appropriations earlier in this Chapter.

658. Grants include such transfers as: cultural grants, scholarships, research grants and regional development grants. Examples of accounting policies for and disclosure of government transfers are shown below.

Grants

1.24 In these consolidated financial statements grants which fall under Commonwealth/State funding arrangements are recognised as an expense in the reporting period in which goods and services are delivered by the grantee to intended beneficiaries.

1.25 Legislative obligations for education include amounts specified in the States Grants (Schools Assistance) Act and State Grants (Primary and Secondary Assistance) Act, Higher Education Funding Act and Vocational Education and Training Act.

1.26 Legislative obligations for health are similar in principle to the above obligations and include State Grants in relation to the Medicare arrangements and capital payments in relation to nursing homes and child care facilities.

Example 15.8
Financial Statements of the Commonwealth Government of Australia
for the year ended 30 June 1997
Notes to and forming part of the Financial Statements, page 39

Forecast 1998 Budget $m	Forecast Estimated Actual $m		Actual 30 June 1999 $m	Actual 30 June 1998 $m
		NOTE 5: Expenses by Input Type		
: :	: :	: : : :	: :	: :
		Analysis of Subsidies and Transfer Payments		
		Social Assistance Grants		
5,173	5,071	New Zealand superannuation	5,064	5,106
1,529	1,451	Domestic purposes benefit	1,451	1,501
1,470	1,486	Community wage	1,487	-
358	369	Unemployment benefit	369	1,436
947	921	Family support	915	881
844	843	Accommodation supplement	843	793
656	630	Invalids benefit	631	599
107	97	Sickness benefit	97	400
393	392	Student allowances	378	344
224	204	Disability allowance	204	198
90	126	Accident compensation for non-earners	126	129
22	22	Training benefit	22	98
951	982	Other social assistance grants	978	848
149	133	Subsidies	110	164
		Other Transfer Payments		
204	204	Official development assistance	204	195
13	13	Other	13	12
13,130	**12,944**	**Total Subsidies and Transfer Payments**	**12,892**	**12,704**

Example 15.9
Financial Statements of the New Zealand Government
for the year ended 30 June 1999
Notes to the Financial Statements, page 67 (NZD)

Other Losses

659. Other losses may arise from declines in the value of assets, or increases in the value of liabilities due to movements in market prices or currency movements.

Other Losses – Changes in Carrying Amount

660. IAS 16, *Property, Plant and Equipment* allows two different treatments for the valuation of assets. Property, plant or equipment may be recorded at the lower of depreciated historic cost or recoverable amount. Decreases in the recoverable amount are recognized as an expense (paragraph 56).

661. Alternatively, assets may be revalued regularly to fair value. IAS 16, *Property, Plant and Equipment* requires that a revaluation decrease be charged directly against any revaluation surplus to the extent that the decrease does not exceed the amount held in the revaluation reserve in respect of that same asset (paragraph 40). Changes in the value of land (unless held as an investment) are usually treated in the same way.

662. An example of an accounting policy for the valuation of forests, which may result in other gains or losses being recognized is shown below.

Commercial forests

Commercial forests are recorded at estimated net current value. This takes into account age, quality of timber and the forest management plan.

Example 15.10
Financial Statements of the Government of New Zealand
for the year ended 30 June 1999
Statement of Accounting Policies, page 62

663. IAS 25[8], *Accounting for Investments* discusses the treatment of gains and losses arising from revaluations of investment properties and some financial investments. Investment properties may be accounted for as if they were property, plant and equipment, or as long-term investments (paragraph 28). Gains and losses on short-term investments may be accounted for as income and expense, or they may be accounted for as long-term investments. IAS 25 requires that gains and losses on long-term investments be taken to the revaluation reserve, subject to the proviso that any decrease does not exceed the amount held in the revaluation reserve in respect of that class of assets (paragraphs 31 and 32).

664. Where alternative treatments are available the entity should follow a consistent policy.

Other Losses – Foreign Exchange Losses

665. Gains or losses arising from movements in foreign currency are discussed in IAS 21, *The Effects of Changes in Foreign Exchange Rates.* IAS 21 requires that exchange differences be recognized as income or expense in the period in which they arise (paragraph 15) with the exception of exchange differences arising on a monetary item that, in substance, forms part of an entity's net investment in a foreign entity; or exchange differences arising on a foreign currency liability accounted for as a hedge of an entity's net investment in a foreign entity. Exchange differences arising in these situations are classified as net assets/equity until the disposal of the net investment, at which time they are recognized as income and expenses (paragraphs 15, 17 and 19).

666. Increases in the value of liabilities due to foreign currency movements are recognized as expenses. However, where investments are recorded at face value, increases in liabilities due to movements in interest rates are not recognized until the liability is settled.

Custodial Payments – Administered Transactions

667. Custodial payments (also referred to as administered transactions) are payments made by a government reporting entity on behalf of another organization. They may include payments of grants or benefits made by a government department or agency to other organizations or individuals on behalf of a national or state government.

668. It may sometimes be difficult to distinguish whether a payment made by a government entity is a custodial payment or an expense of the administering entity. If the entity handling the payment also has discretion to distribute those funds within broad parameters established by the entity providing the funding, then the entity may be said to have control over the distribution of the funds.

669. The classification of such payments as custodial payments or as an expense depends on whether it is the principal or the agent who has ownership rights to the resources involved and makes key decisions such as:

- the identity of (class of) recipients, or criteria for their selection;
- the conditions of entitlement of third party recipients;
- refund of unexpended funds by the agent;
- any right of recovery of unfunded expenditure by that agent; and
- separate reimbursement of the agent's expenses.

[8] The International Accounting Standards Committee has signalled its intention to withdraw IAS 25, *Accounting for Investments* following the approval of IAS 40, *Investment Property.*

670. If an item meets the definition of an expense it is recognized within the financial statements of the administering entity. Both the receipt of funds for the payment, and the subsequent payment would be recorded in the financial statements of the administering entity.

671. Where an item does not meet the definition of an expense, it is usually because the administering entity does not have control over the cash flows. In that case, the items are not recognized as an expense in the financial statements. Instead accountability for the management of custodial payments may be demonstrated by disclosing details of such payments in a separate Statement or in the Notes to the Financial Statements. Any expenses associated with the handling of these payments would normally be recognized as an expense by the reporting entity making the payment. Because the administrative arrangements relating to custodial payments may differ between jurisdictions, the manner in which these transactions are displayed in the financial report may also vary. Items which are classified as custodial payments in one jurisdiction may be treated as expenses within another jurisdiction. In some cases it is appropriate for the entity making the payments to recognize both an asset and revenue when control of the funds to be transferred is obtained, and to recognize a liability and an expense when decisions on the transfer or the identification of a clear entitlement to those funds occurs.

672. Refer also to Chapters 12, 13 and 14 for a discussion of assets and liabilities administered on behalf of others, and revenues collected on behalf of others.

Classification

673. Classification depends on users' needs and on how they can best be met. The constraints identified in relation to the classification of assets (refer to Chapter 12) apply here also.

674. The major classification systems for expenses are:

- by function or program;
- by outputs;
- by organization; and
- by object of expense (input).

675. In a well designed system, multiple classifications can be incorporated within the system. The sections below describe each of these classification systems.

Classification by Function or Program

676. A classification by function or program provides useful information on the purposes or objectives of the activities giving rise to the expenses. It helps broad allocative decision making and the review by the legislative and executive branches of government. This information provides data which could be used to calculate expenditures per unit of activity. Most government outlays can be assigned to a specific function or broad sector of the government. Some, however, require judgment. For example, military colleges are usually classified as "defense" rather than "education".

677. Existing functional classification systems include the United Nations' System of National Accounts (SNA) and the International Monetary Fund's Government Finance Statistics (GFS). These are discussed in Chapter 19. For examples of functional classifications refer to Example 14.18 in Chapter 14 and the financial statements of the New Zealand Government (Appendix 2).

Classification by Output

678. Classification of expenses by outputs is essential for efficiency evaluation. Such a system of classification requires both a clear specification of the outputs produced by government and robust cost allocation systems.

679. Reporting which relates expenses to outputs provides a basis for the assessment of performance. It enables a comparison of actual efficiency against expectations, changes in efficiency between periods, and in some cases, a comparison with non-government suppliers. Such reporting is particularly useful for accountability purposes.

680. Output groupings are more useful at the sub-entity than at the whole of government level. Examples of groupings of outputs used by the New Zealand Treasury are shown below.

Expenses by Output Grouping

Customer oriented:	*Outputs with identifiable individual customers who voluntarily consume a service for their benefit.*
Transactions:	*Large scale processing of identical transactions (e.g., assessment of claims for income support payments).*
Professional/Managerial:	*Outputs characterised by a mixture of ongoing service and projects (e.g., policy advice).*
Investigations:	*Public good outputs where considerations of risk, due process, legal compliance and quality of judgement are most important.*
Behavioural:	*Involve outputs which try to change individual attitudes and behaviours such as counselling.*
Control:	*These outputs involve the use of coercive powers either to keep individuals within a controlled environment or preventing entry to an area.*
Emergency Services:	*These outputs involve the purchase of a planned level of response to emergencies.*
Contingent Military Capabilities:	*These outputs involve the purchase of specified levels of military capability.*

(The Treasury, April 1995)

681. An example of a cost accounting model using Activity Based Costing is provided below. Activity Based Costing is only one method of cost allocation. Other methods, including allocations based on the number of staff in an area, or the amount of floor space used, although simple, may provide similar measurement results at a much lower cost.

Cost Attribution

The NZDF uses the Costing, Budgeting, Management and Reporting Systems (MARS) to derive the costs of outputs in the statements in this report. This system attributes costs in a two-stage process. The first stage assigns support unit costs to a force element cost centre. The second stage allocates force element costs to outputs.

The costing model:

- traces the direct costs of a force element (for example, a squadron, a frigate, a battalion) directly to a force element cost centre;
- attributes support units costs to force elements and other support "customer" cost centres using drivers reflecting the resources required to support the "customer's" level of expected activity in the medium term, e.g. five year activity cycle;
- attributes overhead costs to force elements' cost centres using as a default the percentage of that force element's consolidated (i.e., including its direct support units) gross operating budget (exclusive of capital charge) to the total gross consolidated budget (exclusive of capital charge) for all force elements, unless a more meaningful driver is identified that will produce a material difference in output cost;
- attributes force element fully absorbed costs to outputs on a direct or "many to one" basis; and
- attributes costs for specific services, e.g. hydrography, on an agreed basis that best represents the manner in which the costs are incurred.

The basis for allocation of support units' and headquarters' costs to force elements and of fully absorbed cost of force elements to outputs are set for the year. The allocation rules will be reviewed if there is significant infrastructural change that is likely to alter the continued appropriateness of these rules.

Example 15.11
Annual Report of the New Zealand Defence Force
for the year ended 30 June 1999
Statement of Accounting Policies, page 113

Classification by Organization

682. Expenses can also be divided into separate sections for each ministry, department or agency. These organizations can then be held responsible for their expenses (e.g., Ministry of Agriculture, Ministry of Health). Such a classification is tailored to the particular structure of the government. Within each spending organization, the expenses can be further classified by object of expense.

Classification by Object of Expense (Input)

683. Expenses may be classified by the object of the expense, also referred to as input types. The object classification enables an entity to exercise control at various levels of management. Possible object classifications are shown below:

- personnel expenses;
- cost of goods sold;
- cost of services provided;
- physical asset use (depreciation and loss of service potential);
- rental and leasing costs;
- maintenance and working expenses;
- interest;
- expenses relating to financial assets;
- government transfers;
- other losses
  - changes in market value; and
  - foreign exchange losses.

684. In addition to disclosing functional classifications, the Notes to the Financial Statements of the Government of New Zealand display expenses by input type. They also disclose an analysis of subsidies and transfer payments, and operating expenses.

Forecast			***Actual***	
1998 Budget $m	**Estimated Actual $m**		**30 June 1999 $m**	**30 June 1998 $m**
		NOTE 5: Expenses by Input Type		
15,421	15,718	Operating expenses (see analysis below)	15,681	14,654
13,130	12,944	Subsidies and transfer payments (see analysis below)	12,892	12,704
2,564	2,520	Finance costs (see analysis below)	2,516	2,804
		Personnel		
2,483	2,564	Personnel expenses[1] (excluding pension expenses)	2,541	2,500
690	690	GSF Pension expenses	703	727
48	(217)	Movement in GSF unfunded pension liability	429	(233)
35	50	Other pension expenses	50	43
		Depreciation		
749	698	Physical assets	684	657
71	81	State highways	81	80
251	261	Rental and leasing costs	269	261
-	205	Net foreign-exchange losses/(gains) on liabilities	(22)	1,621
-	(256)	Net foreign-exchange (gains)/losses on assets	(25)	(1,608)
-	(2)	Loss/(gain) on sale of assets	26	1
290	-	Provision for future initiatives	-	-
100	-	Contingency expense provision	-	-
35,832	**35,256**	**Total Expenses**	**35,825**	**34,211**

Example 15.12
Financial Statements of the Government of New Zealand
for the year ended 30 June 1999
Notes to the Financial Statements, page 67 (NZD)

CHAPTER 16

ACCRUAL BASIS – EXTERNAL REPORTING

Introduction

685. This Chapter considers the types of governmental financial reports commonly prepared by government financial reporting entities using the accrual basis of accounting. Government financial reporting entities may be governments, departments or ministries of government, or other public sector entities that carry out the functions of government.

Financial Statements

686. Under accrual accounting the following financial statements are usually prepared:

- Statement of Financial Position;
- Statement of Financial Performance; and
- Statement of Cash Flows[9].

687. These Statements provide users with information about the resources controlled by the entity, and the net results of its operations (or the cost of providing its services). They also provide information useful in assessing financial position and changes in it, and in assessing whether the reporting entity is operating economically and efficiently. An additional statement, the Statement of Movements in Net Assets/Equity is also prepared in some jurisdictions.

688. Other notes to the Financial Statements are also prepared including:

- Accounting Policies;
- Commitments; and
- Contingencies.

689. Commitments and contingencies may be presented either as notes or as additional statements. Notes to the Financial Statements or supplementary schedules may also report summary information about such matters as compliance with spending mandates and relevant performance indicators.

Statement of Financial Position

690. The Statement of Financial Position includes details of all recognized assets and liabilities. In the public sector, the balance of assets less liabilities is referred to by a variety of terms including net assets, taxpayers' funds, owners' equity, public equity, or net financial position. This Study refers to this balance as "net assets/equity". For a discussion of the benefits of information on assets, liabilities and net assets/equity refer to Chapter 11.

691. Examples of Statements of Financial Position are included in Appendix 2.

Statement of Financial Performance

692. The Statement of Financial Performance includes details of all recognized revenues and expenses. The Statement shows the surplus (or deficit) of revenue over expenses. This is a useful measure of whether a government has managed to meet current expenses from current revenue, and whether its net resource position has increased or decreased. For a discussion of the benefits of information on revenue and expenses refer to Chapter 11.

693. Examples of Statements of Financial Performance are included in Appendix 2.

Statements of Movements in Net Assets/Equity

694. Some jurisdictions prepare a statement which links the Statement of Financial Performance to the

[9] These statements may be referred to by a variety of names both within and across jurisdictions. The Statement of Financial Position may also be referred to as a balance sheet or statement of assets and liabilities. The Statement of Financial Performance may also be referred to as a statement of revenues and expenses, an income statement, an operating statement, or a statement of net costs.

Statement of Financial Position and explains movements in opening and closing balances. Such Statements include Statements of Net Assets/Equity or Movements in Net Assets/Equity, Statements of Total Recognized Gains and Losses, and Statements of Activities (as required by FASB 117).

695. IAS 1, *Presentation of Financial Statements* requires that entities prepare a statement showing changes in equity. (paragraph 86) However, different jurisdictions have varying national requirements regarding the production of such statements. Where such statements are not prepared, it is usual to disclose movements in components of equity by way of note disclosure.

696. Financial Reporting Standard 3 (FRS 3) of the Accounting Standards Board in the United Kingdom requires the preparation of a Statement of Total Recognised Gains and Losses to show the extent to which shareholders' funds have increased or decreased from all various gains and losses recognized in the period. FRS 3 also requires a separate Reconciliation of Movements in Shareholders' Funds to highlight other changes in shareholders' funds.

697. FASB 117 *Financial Statements of Not for Profit Organizations* requires a Statement of Activities which must show the change in unrestricted net assets/equity, temporarily restricted net assets, permanently restricted net assets/equity and total net assets/equity. The standard makes the distinctions between these classes of net assets/equity to highlight the impact of donor imposed conditions or restrictions on the availability of net assets/equity for various purposes.

698. Examples of statements showing movements in net assets/equity are included in Appendix 2.

Statement of Cash Flows

699. Accrual accounting systems record both the elements recognized under accrual accounting (assets, liabilities, revenue, expenses and net assets/equity) and details of cash flows. Accrual accounting provides additional information — it does not supplant any of the information which would be available under a cash-based system. A Statement of Cash Flows is produced under accrual accounting. The Statement of Cash Flows provides a summary of cash receipts and cash payments during the year, classified under various sub-headings (operating, investing and financing) and reconciles opening and closing cash balances. The Statement may include a reconciliation between operating cash flows and the accrued deficit or surplus shown in the Statement of Financial Performance.

700. The purpose of the Statement is to help users to assess the entity's ability to generate cash flows and to assess the entity's financial performance and financial position. It can inform users, such as creditors and investors, of the effects of operating, financing and investing activities on the cash resources of the entity. In combination with other financial information, the Statement of Cash Flows may help users to:

(a) estimate the entity's future net cash flows and especially to assess the entity's ability to generate positive cash flows from operating activities;
(b) assess the entity's ability to meet its obligations and to assess its need for external financing;
(c) assess the entity's ability to meet fiscal targets;
(d) compare the entity's surplus (deficit) on an accruals basis with the cash flows from operating activities;
(e) assess possible liquidity problems;
(f) assess financial flexibility, that is, the entity's ability to optimize cash resources and to respond to unexpected adversity or opportunities; and
(g) project future cash flows by providing a better understanding of the cash flow effects of the variables described in the entity's Statement of Financial Position and Statement of Financial Performance.

701. The Statement of Cash Flows, in conjunction with the Statement of Financial Position, can provide a comprehensive set of information in relation to net debt. Taken together these statements show the total amount of net debt, movements during the year, and how the current year's cash requirements have been financed.

702. Examples of Statements of Cash Flows are included in Appendix 2.

Notes to the Financial Statements and Statement of Accounting Policies

703. The Notes to the Financial Statements are regarded as an integral part of the financial statements. They provide more detailed disclosure (e.g., of the amounts of specific taxes raised), than is possible or desirable in the face of the main statements.

704. The Notes to the Financial Statements include a Statement of Accounting Policies. It is fundamental to the understanding and interpretation of governmental financial reports that those who use them are aware of the accounting policies on which they are based. IAS 1, *Presentation of Financial Statements* discusses the selection and disclosure of accounting policies.

> *Accounting policies are the specific principles, bases, conventions, rules and practices adopted by an enterprise in preparing and presenting financial statements.* (paragraph 21)

705. IAS 1 requires disclosure of all significant accounting policies, which is normally made by way of a Statement of Accounting Policies. Accounting policies typically contain a description of the reporting entity, any legislative requirements under which the financial statements are prepared, the basis of accounting, the measurement base and the detailed accounting policies used. The detailed accounting policies include a description of recognition and measurement decisions applied in respect of various types of revenue, expenses, assets and liabilities. Where consolidated financial statements are prepared, all reporting entities being consolidated must generally have the same accounting policies. Where different entities within the reporting entity have different policies or operate on different bases of accounting (e.g., GBEs may use accrual accounting and the remainder of the entity may use a modified form of accrual accounting), then various options are available to the reporting entity. These options include making adjustments to bring the financial statements onto the same basis, or disclosure of the effect that use of different bases has on the statements. The use of different bases makes it difficult to interpret the financial statements. Examples of Statements of Accounting Policies are included in Appendix 2.

706. Under the accrual basis of accounting, disclosure of contingencies and commitments is required. The distinction between contingencies and commitments is discussed in Chapter 13.

Additional Disclosures

707. A range of additional information may be disclosed in the Notes to the Financial Statements. Its purpose may be to provide further information to readers in respect of financial elements recognized in the statements, (e.g., a physical description of particular assets) or to provide information on the nature and possible value of items not recognized as financial elements in the financial statements (e.g., assets not recognized because they did not meet the recognition criteria). This section briefly outlines some of the additional disclosures which may be found in financial statements.

708. Additional statements or note disclosures under accrual accounting could include:

- resources (lists of physical assets and investments);
- borrowings;
- related party transactions;
- unappropriated items;
- tax expenditures; and
- forecast information.

709. Although all assets and liabilities which meet definition and recognition criteria are recognized in the accrual financial statements, some assets and liabilities may not meet these criteria, or additional information concerning the composition of assets and liabilities may be useful to readers. Such statements may be particularly useful during the transition to accrual accounting when the recognition of classes of assets and liabilities may occur over time. For example, a government which has not yet recognized physical assets within its financial statements may collect and report such information by way of note. For further discussion of additional disclosures made in these circumstances refer to Chapter 17.

710. A Statement of Resources may be used to disclose further details of physical assets, including heritage assets. Where the historical cost measurement base is used in the financial statements, additional note disclosure of market values of assets and liabilities may be appropriate.

711. Examples of Statements of Borrowings are shown in Appendix 2. Such Statements may include an analysis of borrowings by book value, nominal value and market value. They may also include a maturity profile for borrowings, movements during the year, and an analysis of domestic and foreign currency debt.

712. "Stewardship Information" is a term used by the U.S. federal government to describe a range of specified additional disclosures in the financial statements. The views of the U.S. federal government on the type of information which should be included in stewardship information are discussed below.

713. In some situations the government contributes significantly to the national wealth, the benefits of which do not reside with the federal government. The U.S. requires the reporting of costs incurred to aid research and development, to provide education and other enhancements to the human capital of the nation, or to assist state and local governments to build infrastructure, as stewardship information. The stewardship information shows the costs incurred under these investment programs for the most recent five years and the related outputs and outcomes.

714. An alternative approach is to provide forward-looking information on the expected effects of spending under current policy settings in the Budget documents. Detailed information on specific programs may also be presented in special purpose financial reports such as the Estimates.

715. Like other countries, the U.S. has benefit and social insurance programs which citizens expect will be continued. The strengths of the various obligations differ from program to program. For contributory social insurance programs, many citizens believe that long-term benefits are "owed" to those who have made contributions; but only amounts due and currently payable are required to be recognized as liabilities. However, extensive future-oriented stewardship information is required to facilitate an understanding of the financial health of those programs and to assist users in assessing their potential effects on the future deficit, and on related taxes and program benefits.

716. Similarly, in New Zealand the financial statements include extensive disclosure of the government's obligations under the accident compensation scheme and the superannuation/pension scheme for government employees.

717. Disclosure of related party transactions provides further information on transactions between the entity and parties such as controlled entities, senior management and Ministers (or equivalents). These transactions have already been recorded within the financial statements. Further information on such transactions is provided because parties that are related to the reporting entity are in a position to influence the terms and conditions on which transactions with the entity take place. Separate disclosure allows readers to gauge the nature and extent of these transactions and their possible impact upon the financial position and financial performance of the entity. IAS 24, *Related Parties* provides a description of related parties and requires certain disclosures to be made in relation to these parties and transactions. Examples of transactions which are typically disclosed include loans from the entity to related parties, remuneration of senior management, and sales of goods and services or the transfer of assets between the parties. Various jurisdictions have national or federal standards which address these issues. An example of disclosure of related party transactions within the United States context follows.

Note 1.L. Related Party Transactions

Federal Reserve Banks (FRBs), which are not part of the reporting entity, serve as the Federal Government's depositary and fiscal agent. They process Federal payments and deposits to Treasury's account and service Federal debt securities. FRBs owned $477.9 billion of Federal debt securities held by the public as of September 30, 1998. FRB earnings that exceed statutory amounts of surplus established for the Federal banks are paid to the Government and are recognized as non-exchange revenue. Those earnings totaled $24.6 billion for the year ended September 30, 1998. The primary source of these earnings is from interest earned on Federal debt securities held by the FRBs.

FRBs issue Federal Reserve Notes, the circulating currency of the United States. These notes are collateralized by specific assets owned by the FRBs, typically Government securities. Federal Reserve notes are backed by the full faith and credit of the U.S. Government.

The Government does not guarantee payment of the liabilities of Government-sponsored enterprises such as the Federal National Mortgage Association or the Federal Home Loan Mortgage Corporation. These enterprises also are excluded from the reporting entity.

Example 16.1
Financial Report of the United States Government – 1998
Notes to the Financial Statements, pages 64 and 65 (USD)

Compliance with Appropriations

718. As discussed in Chapter 2, compliance reporting may form part of the end of year governmental financial reports, or the budget statements for the following year. An extract from a Statement highlighting use of resources in excess of appropriations (on the accrual basis) subject to later validation is shown below. An example of compliance reporting is also found in Chapter 2.

Statement of Unappropriated Expenditure, Expenses or Liabilities
as at 30 June 1999

An appropriation is a statutory authorisation by Parliament for the expenditure of public money or the incurring of expenses or liabilities. This statement reports expenditure, expenses or liabilities spent or incurred in excess of or without appropriation by Parliament.

Section 12(1) of the Public Finance Act 1989 authorises the Minister of Finance to approve limited amounts of expenditure, expenses or liabilities in excess of, or without appropriation. Unappropriated amounts spent or incurred in terms of such an approval are shown separately in this statement.

Unappropriated expenditure, expenses or liabilities in excess of the limits which the Minister of Finance can approve require validating legislation.

Amounts in this statement are expressed in thousands of dollars, reflecting the level at which appropriations are made.

Department Vote - Appropriation	Unappropriated expenditure, expenses or liabilities approved by the Minister of Finance under section 12 ($000)	Unappropriated expenditure, expenses or liabilities amount requiring validating legislation ($000)	Amount Appropriated ($000)
Ministry of Agriculture and Forestry			
Agriculture and Forestry –			
Outputs supplied by the Department			
Verification services	977	-	30,193
Outputs supplied by the Department			
Contestable quality management services	74	-	-
Biosecurity –			
Outputs supplied by the Department			
Border inspection	594	-	29,924
: :	: :	: :	: :

Example 16.2
Financial Statements of the New Zealand Government
for the year ended 30 June 1999
Statement of Unappropriated Expenditure, Expenses and Liabilities, page 49 (NZD)

Tax Expenditures

Tax expenditures are estimates of the revenue foregone because of preferential provisions of the tax structure. They are due to special exclusions, exemptions, deductions, credits, deferrals, and tax rates that depart from a 'baseline'. These exceptions are generally intended to achieve public policy objectives by providing benefits to qualifying individuals or entities or by encouraging particular activities. They also may be intended to improve tax equity or offset imperfections in other parts of the tax structure. Tax expenditures are not revenue. They are not inflows of resources to the reporting entity. (SFFAS No. 7, page 75)

719. The U.S. standards allow entities to disclose tax expenditure information that is relevant to the performance of the entity's programs but caution that this information should be appropriately qualified and explained to help the reader assess the possible impact of the specific tax expenditures on the success of the related programs. In addition, with similar cautionary language, they permit the disclosure of the cost to state and local governments and to citizens of federal laws which mandate them to make expenditures or incur other types of costs, such as costs related to federal regulations that establish the characteristics of a product or the methods of production (also referred to as directed flows of resources or unfunded mandates). (SFFAS No. 7, page 28)

720. Tax expenditures represent taxation revenue foregone by the government (and may also be referred to as taxes foregone). Although tax expenditures result in less taxation revenue being collected than would otherwise be the case, no government currently recognizes tax expenditures as an expense. It is not accepted practice to recognize opportunity costs. However, governments may wish to disclose estimates of tax expenditures as supplementary information.

Forecast Information

721. Governments which collect taxes (including property taxes) usually prepare statements outlining forecasts of taxes or rates and if appropriate, details of the appropriations or legislative authorities for which approval is sought. This information may be presented in conjunction with external financial reports, but it is more commonly published as a separate document. The type of information presented in budget documents is determined by the nature of appropriations. A full discussion of forecast information is outside the scope of this Study.

CHAPTER 17

MODIFICATIONS TO THE ACCRUAL BASIS

Introduction

722. This Chapter describes some of the common modifications to the accrual basis, with particular emphasis upon the rationale underlying an approach currently used by the Government of Canada referred to by them as “modified accrual accounting”.

723. Examples of the variations on accrual accounting which may be found in practice include:

- recognition of all assets apart from infrastructure, defense and cultural/heritage assets which are expensed at time of acquisition or construction;
- recognition of most assets and liabilities in accordance with the accrual basis, but with the recognition of revenues being on a cash basis or some modification to the cash basis;
- recognition of short-term financial assets and liabilities only; and
- recognition of all liabilities with the exception of certain liabilities such as pension liabilities.

724. The non-recognition of certain classes of assets or liabilities is one of the most common variations to accrual accounting. One variation which has been adopted by most governments within Canada, and by some governments within the United States, involves the expensing of all non-financial assets at the time of purchase. This variation has been referred to in previous PSC publications as the modified accrual basis of accounting. It may also be referred to in some jurisdictions as the expenditure method. The rationale underlying the method adopted in Canada is discussed further below under the heading Focus on Net Debt/Net Financial Assets.

725. Another government which currently uses a modification of the accrual basis for central state entities and for local authorities is Spain. It recognizes some non-financial assets in accordance with the accrual basis but recognizes expenditures on defense, infrastructure and cultural assets at the time of acquisition or construction.

Assets

726. In relation to assets, the main modification to the accrual basis of accounting is that certain classes of assets are not recognized in the statement of financial position. Instead the class of assets is expensed at the time of acquisition. Sometimes this treatment is adopted because of the practical difficulties of, and cost associated with, identifying or valuing such assets. Heritage assets and infrastructure assets may not be recognized for this reason. In other cases, a jurisdiction may argue that there is a theoretical basis for adopting this treatment for certain classes of assets e.g., Canada has chosen to expense all non-financial assets as part of its focus upon the net debt position of a government.

727. Where a jurisdiction recognizes only non-financial assets, its definition of financial assets may be broader than the definition given in IAS 32, *Financial Instruments: Disclosure and Presentation*. IAS 32 defines financial assets as follows:

> *A financial asset is any asset that is:*
> *(i) cash;*
> *(ii) a contractual right to receive cash or another financial asset from another enterprise;*
> *(iii) a contractual right to exchange financial instruments with another enterprise under conditions that are potentially favorable; or*
> *(iv) an equity instrument of another enterprise.* (paragraph 5)

728. Some jurisdictions recognize all assets which can be considered to be available for financing payments of existing liabilities and operations in the immediate future, other than readily saleable physical assets. The IAS 32 definition may therefore be broadened to include any asset which is convertible into cash and not intended for consumption in the ordinary course of operations. Financial assets could therefore include inventories held for sale in the ordinary course of operations and land held for resale, both of which are not normally classified as financial assets under accrual accounting.

729. This definition of financial assets also differs from the definition of financial assets under the SNA and the GFS. The definition of financial assets under these two systems is similar to the IAS 32 definition, although the IAS definition may exclude gold held by governments and the SNA definition specifically includes it. Land held for resale is not recognized as a financial asset under the IAS 32 definition.

Liabilities

730. Some jurisdictions choose not to recognize certain liabilities, such as pension liabilities, which meet the definition and recognition criteria under accrual accounting. This may be for pragmatic reasons such as the time and expense involved in measuring the liability, or it may be the result of a policy decision to specifically exclude this liability from the published financial statements. It should be noted that where a class of liability has not been recognized because it is not able to be reliably measured, this is not a departure from accrual accounting — it is only where a liability could be reliably measured, but the jurisdiction has chosen not to, that a departure occurs.

731. An interesting liability recognition issue may arise when a liability exists and where a government has agreed to settle the liability by the transfer of an asset rather than by cash e.g., land transfers arising from indigenous land claims. If that asset itself has not been recognized in the financial statements, e.g., heritage land, the question is whether the liability can be recognized. Some jurisdictions recognize such liabilities by first recognizing the asset in question. Other jurisdictions do not recognize these liabilities or the settlement of them.

Revenues

732. The recognition of revenues will depend on the modification which has been adopted by the jurisdiction. The most common difference arises when a class of assets has been expensed at the time of acquisition or construction. In that case revenues will include the total proceeds from sale of physical assets. Such revenues are usually separately disclosed to highlight their non-recurring nature. Another difference is that where a class of assets or liabilities is not recognized, receipts of donated assets or payment by a third party of a liability would not be recognized as revenue.

733. An example illustrating the recognition of proceeds from the disposal of assets as revenue by the Government of Canada is shown below.

TABLE 3.3

REVENUES FROM ALL SOURCES
(in millions of dollars)

	Gross revenues	Less revenues of consolidated Crown corporations	Less revenues netted against expenditures: External revenues	Less revenues netted against expenditures: Internal revenues	Less deferred revenues netted against expenditures	Less tax credits and repayments	Net revenues
External transactions	167,543	1,498	2,302		3	8,069	155,671
Internal transactions by main classification—							
Excise taxes and duties							
Return on investments	27						27
Privileges, licences and permits	5						5
Refunds of previous years' expenditures	59						59
Service fees	3,113			3,103			10
Proceeds from sales	277			277			
Proceeds from the disposal of surplus Crown assets	11						11
Miscellaneous non-tax revenues	1,482			1,444			38
Total internal transactions	4,974			4,824			150
Total revenues	172,517	1,498	2,302	4,824	3	8,069	155,821

Example 17.1
Public Accounts of Canada 1999, Volume 1
Section 3 (CAD)

Expenses

734. Under the accrual method, the cost of all non-current physical assets is capitalized in the Statement of Financial Position, and recognized in the Statement of Financial Performance as depreciation or amortization over the life of the assets. Under certain modifications to accrual accounting, expenses would include the cost of acquisition or construction of any asset which has not been recognized in the statement of financial position. Expenses under such modified forms of accrual accounting are sometimes referred to as expenditures, and the cost of assets which have been expensed may be referred to as capital expenditures.

735. If certain classes of physical or intangible assets are expensed, depreciation and amortization of those assets no longer occurs. In addition, losses may only be recognized in relation to assets and liabilities which have been recognized on the Statement of Financial Position.

736. The following example from Canada illustrates the reporting of expenditures on the construction and purchases of assets.

TABLE 3.10

TOTAL EXPENDITURES BY STANDARD OBJECT
(in millions of dollars)

	Total expenditures	Less: Internal expenditures	Less: Internal revenues netted against expenditures	Total external expenditures
:	: :	: :	: :	: :
Purchased repair and maintenance	1,780	11	267	1,502
Utilities, materials and supplies	2,791	4	87	2,700
Construction or acquisition of land, buildings and works	1,191	18	430	743
Construction or acquisition of machinery and equipment	2,335	1	22	2,312
:	: :	: :	: :	: :
:				

Example 17.2
Public Accounts of Canada 1999, Volume 1
Section 3 (CAD)

External Reporting

737. Generally the same types of statements are prepared under the various modifications to the accrual basis as under the accrual basis itself. The main difference is that where significant classes of assets are treated as expenditures, the Statement of Financial Performance may be referred to as a Statement of Revenues and Expenditures.

Additional Disclosures

738. Governments which do not recognize certain classes of assets or liabilities may nevertheless choose to provide supplementary information on these assets. Where additional disclosure of such items is made, additional record keeping costs will be incurred. These costs will be largely the same as the costs normally borne by entities maintaining details of such items as part of an accrual accounting system. The prior collection of information on these assets and/or liabilities would be helpful if the entity subsequently decides to recognize these items, and would reduce implementation costs at that point. Where additional information on items is collected, care must be taken to ensure that such information is reliable and complete. For example, it may be sensible to concentrate on collating information on one class of assets at a time. Incomplete or inaccurate records are of little value and may be misleading.

Focus on Net Debt/Net Financial Assets

739. The federal and all the provincial governments in Canada presently report in accordance with the expenditure basis of modified accrual accounting as set out in standards issued by the Public Sector Accounting and Auditing Board of the Canadian Institute of Chartered Accountants. However, the Government of Canada has announced its intention to adopt full accrual accounting and to move towards full recognition of physical assets (Canada, 1995 Official Budget Papers, The Budget Plan, Chapter 4).

740. In Canada, the method of accounting which has been adopted has been heavily influenced by the stated objective of evaluating the government's financial position and changes therein during the reporting period. This focus on financial position has led public sector standard setters in Canada to the conclusion that the financial statements should report cash and other resources which are on hand and which are available to finance the government's activities and meet its liabilities and commitments. Thus "future economic benefits" or "service potential" of assets is defined as being related to the financing of activities or the repayment of liabilities.

741. Under the Canadian model all liabilities and financial assets are recognized on the Statement of Financial Position. Financial assets constitute those assets that are available to a government as at the reporting date for conversion into cash (or other exchangeable resources) to finance future activities, or to settle liabilities and commitments. Information about the nature and terms of a government's financial assets and the method of valuation is necessary to understand and assess the financial resources available to discharge existing liabilities or finance future operations. Non-financial assets are expensed immediately on acquisition regardless of the length of their economic lives.

742. The financial statements under this model provide information that will describe the government's financial position in terms of its liabilities and financial assets at the end of the accounting period. This information includes indicators that can be used to determine whether the government's financial position has improved or deteriorated. One important indicator of financial position is the difference between a government's liabilities and financial assets — often referred to as net debt or net financial assets. When liabilities are greater than financial assets, the residual amount is negative and represents a measure of the future revenues required to meet the effects of past events. When liabilities are smaller than financial assets, the residual amount represents the financial assets available to finance future operations. Net debt is a key indicator because it is a measure of either the future revenue required to pay for past transactions or the financial assets on hand which can provide resources for future operations. The annual surplus or deficit under this method represents the change in net debt.

743. The exclusion of capital asset costs and consumption information from this model is considered appropriate as proponents of this model consider that such information has most relevance for internal management purposes. For external accountability purposes, net debt is a key performance indicator of how well a government is managing its finances. The focus of this model is on providing information on whether a government has been able to finance its activities and meet its liabilities and commitments. It uses net debt and changes therein as a prime measurement indicator of financial position and performance.

744. Under this model the Statement of Financial Performance accounts for the difference between a government's revenues and expenditures of the accounting period, adjusted for changes in valuation allowances in the accounting period. That difference provides a measure of the extent to which revenues raised in the period were sufficient to meet expenditures of that period. It is an important measure because it shows whether a government has met its expenditures by raising revenues or by incurring liabilities and, therefore, helps users understand and assess the results of a government's financial activities and the demands on future revenues.

PART IV – MEASUREMENT BASES

CHAPTER 18

MEASUREMENT BASES

Introduction

745. A number of different measurement bases may be used in recording transactions and events. The measurement base is influenced by the basis of accounting.

746. Choosing a measurement system for use in preparing financial reports has two aspects:

- selecting the measurement base, that is, the dimension(s) or attribute(s) of elements that are to be measured; and
- selecting the monetary unit in which the measurements are to be expressed.

747. Initial recognition of a financial element most commonly occurs as a result of a transaction (e.g., the purchase of an asset). The measurement method for the first recognition, therefore, will often be a cost-based method. Elements related to the purchase of an asset are normally recorded initially at the transaction cost (assuming that cost records have been kept). There may be a further recognition stage which is referred to as remeasurement. Remeasurement involves changing the monetary amount at which an asset or liability is recorded when the recognition criteria for a change are met. Such a change will usually be attributable to events other than transactions, for example, the passing of time giving rise to the need for depreciation, the diminution in value of an amount owed by a debtor to allow for the possibility of a bad debt, or a change in value of a marketable security from that used in the initial transaction. Remeasurement is generally only applied to assets and liabilities, although under conditions of hyperinflation it may also be applied to other elements.

748. The issues concerning choice of measurement base, acceptability of remeasurement and accounting for changes in the purchasing power of the monetary unit are not unique to the public sector. These issues are also relevant for the private sector, and generally accepted accounting principles have evolved to deal with them.

Cash Basis and Modifications to the Cash Basis

749. The elements that are recognized under the cash basis of accounting are cash receipts, cash payments and cash balances. These elements are normally recognized at historical cost. Historical cost is the amount of cash paid or the amount of cash received at the time the payment or receipt occurred.

750. This usually provides an accurate view of the significance of items recognized. Only under hyperinflationary conditions will the historical cost basis of measurement affect users' understanding of the reported transactions and balances.

751. Historical cost is also the measurement system used in conjunction with modifications to the cash basis of accounting.

Accrual Basis and Modifications to the Accrual Basis

752. The IASC Framework for the Preparation and Presentation of Financial Statements (paragraph 99 onwards), which assumes the use of accrual accounting, states:

> *Measurement is the process of determining the monetary amounts at which elements of the financial statements are to be recognized and carried in the balance sheet and income statement. This involves the selection of the particular basis of measurement.*
>
> *A number of different measurement bases are employed to different degrees and in varying combinations in financial statements. They include the following:*
>
> *(a) Historical cost. Assets are recorded at the amount of cash or cash equivalents paid or the fair value of the consideration given to acquire them at the time of their acquisition. Liabilities are*

recorded at the amount of proceeds received in exchange for the obligation, or in some circumstances (for example, income taxes), at the amounts of cash or cash equivalents expected to be paid to satisfy the liability in the normal course of business.

(b) Current cost. Assets are carried at the amount of cash or cash equivalents that would have to be paid if the same or an equivalent asset was acquired currently. Liabilities are carried at the undiscounted amount of cash or cash equivalents that would be required to settle the obligation currently.

(c) Realizable (settlement) value. Assets are carried at the amount of cash or cash equivalents that could currently be obtained by selling the asset in an orderly disposal. Liabilities are carried at their settlement values; that is, the undiscounted amounts of cash or cash equivalents expected to be paid to satisfy the liabilities in the normal course of business.

(d) Present value. Assets are carried at the present discounted value of the future net cash inflows that the item is expected to generate in the normal course of business. Liabilities are carried at the present discounted value of the future net cash outflows that are expected to be required to settle the liabilities in the normal course of business.

753. In addition to these measurement bases, the concept of deprival value is sometimes used to justify the selection of a particular measurement base when an entity is deprived of an asset. Different measurement bases may be selected depending upon whether the assets can be replaced and/or would be replaced. By way of illustration, the current market (buying) price of a similar asset may be used where a similar asset can be purchased but present value may be used where the asset would not be replaced.

754. The IASC Framework for the Preparation and Presentation of Financial Statements has been prepared specifically for business undertakings. As with business enterprises, the historical cost basis, together with the remeasurement of certain assets, is commonly used by public sector entities. The remeasurement of certain elements, particularly non-current assets, is a response to the criticism that the historical cost basis of measurement is not relevant to various users. An IASC review of the recognition and measurement of financial assets and financial liabilities has resulted in the publication of both a Discussion Paper on Financial Assets and Financial Liabilities (March 1997) and IAS 39, *Financial Instruments: Recognition and Measurement*.

755. It has become accepted measurement practice to modify historical cost records where:

- inventories' realizable value is considered to be less than the cost of acquisition or manufacture;
- revenue receivable and other receivables are estimated to realize less than the amount invoiced;
- repayment of a loan or part of a loan is doubtful;
- plant, buildings or other fixed assets do not meet the "recoverable amount test";
- the recognized cost of work in progress where the forecast completion cost of work in progress is estimated to be in excess of its future completed "net current value"; and
- any asset has a permanent diminution in value below the cost of acquisition.

756. Such reductions of historical cost amounts can appropriately be applied in the public sector where such assets are recognized; the only exception may be the "recoverable amount test" for fixed assets where these assets do not generate economic benefits in the form of cash flows.

757. Valuation practices for financial reporting in general have developed with an emphasis on market prices as a basis for valuation. However there are significant assets for which there are no active markets; such assets (e.g., road systems) are usually important in size, scope and value. An alternative valuation practice is to value such assets on the basis of replacement cost depreciated for loss of the asset's service potential since acquisition and adjusted for any technical obsolescence or redundant capacity, that is, the so-called "optimized depreciated replacement cost" basis. Examples of the measurement bases used by particular jurisdictions for various assets are illustrated in Chapter 12.

758. The existing private sector practice of modifying recognized historical cost values downward is widely accepted internationally. There is more disagreement on whether modification of historical cost asset values should encompass an increase in recognized asset values. A compromise position called modified historical cost reporting accepts periodic revaluation of some or all non-current physical (fixed) assets.

759. This debate is relevant to the public sector. The periodic expense reported for loss of service potential of a long-lived asset will usually be materially different depending on whether the asset is recognized at acquisition cost or at a current value. Users of financial reports are likely to be better informed if they have access to information on the current values of long-lived assets.

760. The SNA requires that all assets and liabilities be valued at market value. When actual market prices are unavailable, an attempt should be made to estimate what the price would be if the asset were acquired in the market on the date to which the Balance Sheet relates. Where assets have delayed returns or returns spread over lengthy periods, present value may be appropriate. Financial assets and liabilities are also required to be valued at market value, but, where these are not traded, the amount of principal outstanding, or the face value, may be used as a default. (IMF 1996, page 80)

761. Where financial statements are prepared using one measurement system e.g. historical cost, preparers may choose to disclose additional information on asset values under another measurement system e.g., revalued amounts, or inflation adjusted amounts. Although such information is often prepared for internal management purposes it may also be of interest to external users of the financial statements.

Monetary Unit

762. The elements in financial statements are usually expressed in the domestic currency of the reporting entity.

Historical Cost and Changing Prices

763. Financial statements prepared under the historical cost basis of accounting do not take account of changes in the general level of prices or of changes in the specific prices of assets held, except to the extent that property, plant and equipment may have been revalued, or inventories or other current assets reduced to net realizable value. Entities wishing to show the impact of changing prices on their operations may adopt either a general purchasing power approach, a current cost approach or a mixture of these two approaches. IAS 15, *Information Reflecting the Effects of Changing Prices*, outlines the ways in which these approaches may be used to prepare supplementary financial statements for enterprises using accrual accounting. Where hyperinflation is present, IAS 29, *Financial Reporting in Hyperinflationary Economies* requires the restatement of the primary financial statements in terms of the measuring unit current at period end.

764. An example of the application of inflation accounting to government entities is the pilot study within the United Kingdom where some central government departments are implementing “real terms accounting” i.e., financial capital maintenance (FCM) accounting which recognizes holding losses arising from general price inflation.

Conclusion

765. It is unlikely that any single measurement basis can cater for every need or would be sufficiently reliable for financial reporting in all circumstances. Hence it is desirable to choose the measurement base most appropriate to the circumstances.

766. This Study does not attempt to give definitive advice on the measurement of financial elements. The measurement bases adopted by a government will depend in part on generally accepted accounting principles in that jurisdiction.

PART V – SYSTEM OF NATIONAL ACCOUNTS AND GOVERNMENT FINANCE STATISTICS

CHAPTER 19

SYSTEM OF NATIONAL ACCOUNTS AND GOVERNMENT FINANCE STATISTICS

Introduction

767. In addition to governmental financial reports, most governments produce financial information in accordance with two other accounting frameworks: the System of National Accounts (SNA) and the International Monetary Fund's (IMF) Government Finance Statistics (GFS). An overall understanding of the objectives of these frameworks is essential for preparers of this information.

768. This Chapter outlines the objectives of the SNA and GFS and shows some of the classifications used within each framework. It also discusses the ability of government reporting entities using different bases of accounting for financial reporting purposes to collect the information required by the SNA and GFS. The GFS system is currently under revision. The discussion of GFS in this Chapter is based on the draft material for IMF, A Manual on Government Finance Statistics (forthcoming), as appearing on the IMF website (http://www.imf.org) as of December 1999.

Objectives of the System of National Accounts and Government Finance Statistics

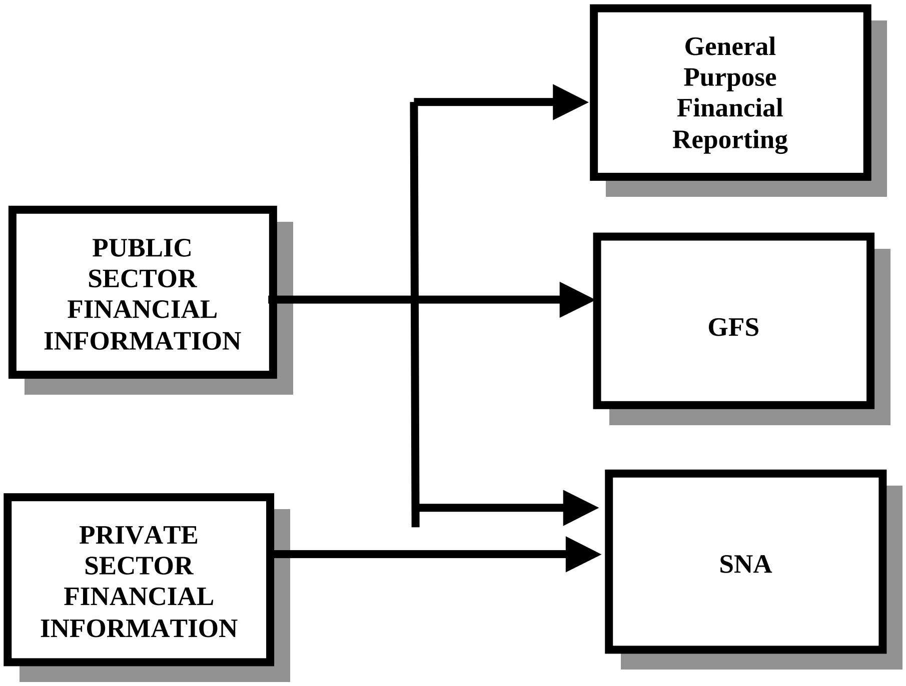
769. Although the SNA and GFS are largely based on the same principles, they have quite different objectives and focus on different reporting entities. The two systems have been designed for different purposes and have evolved over time to meet the needs of particular groups of users.

770. The SNA compiles aggregate statistics, particularly measures of national income and net worth[10], for the whole economy — of which general government is just one sector. The reporting entity for the purposes of the SNA is a nation. GFS is a specialized system designed for fiscal analysis of the general government sector rather than a whole nation. It uses the same underlying framework as the SNA, but the reporting entity for the purposes of GFS is the general government sector within a country, or levels of government within that country.

771. Governmental financial reports prepared in respect of a particular government reporting entity will usually have an even narrower focus than GFS statements prepared for the general government sector. Reporting entities could be individual government departments, state or federal governments, or local governments and national governments. However, consolidated governmental financial reports will include all GBEs and other trading entities controlled by that government. GFS statistics for the general government sector do not include corporations and quasi-corporations. However, these are included in GFS statistics compiled for the public sector.

772. The following diagram provides a stylized illustration of the relationship between the three reporting systems. Governmental financial reporting occurs within each government entity. The general government sector for GFS reporting may include a number of government reporting entities. In turn, the general government sector forms part of the national economy.

[10] Elsewhere in this document, the term "net assets/equity" has been used to describe the balance of assets less liabilities. This Chapter uses "net worth" because this is the term used in the SNA, ESA and GFS.



773. The GFS system is closely linked with the SNA so that analysts may assess general government sector developments within a broad economic framework. Ideally, government reporting entities would be able to establish financial information systems which can be used to compile all three sets of information and minimize duplication of information and time spent making adjustments to data. However, the extent to which this is possible may be constrained by the basis of accounting used for financial reporting purposes. Governments may use the cash or accrual bases of accounting, or various modifications to those bases when preparing financial reports. The SNA is an accrual-based system. GFS is currently cash-based but the revised GFS will be on an accrual basis.

774. The different measurement objectives of the SNA and GFS require separate classification categories for standard presentational purposes. The GFS classification system, however, will provide additional detail to enable compilers to generate SNA data for the general government sector.

775. Their asset classifications are almost identical, although the GFS classifications also distinguish between financial assets acquired for policy purposes and those acquired for liquidity management purposes and they separate financial assets and liabilities into "domestic" and "abroad".

776. The SNA is concerned with measuring production, accumulation, and net worth of the economy. A standard set of accounts is compiled for each of the five institutional sectors of the economy, including the general government sector. The revised GFS will not focus on production. Its main purpose is to identify the resource flows that are useful in analyzing the fiscal performance of governments. Harmonization of GFS with SNA and the adoption of the accrual method of recording will allow GFS to produce several balancing items that coincide with those in SNA, net worth being one.

777. The GFS statement of government operations will present the current and capital components of flows that generate a financing requirement, and show the components of net lending or borrowing that are used to finance government operations of the period. The GFS integrated statements of stocks and flows will correspond to the SNA accumulation accounts and Balance Sheets. In addition, the GFS system will provide a cash flow statement of government operations that has no equivalent in SNA.

778. For example, the Consolidated Financial Statements of the Commonwealth Government of Australia is a governmental financial report which also includes information using GFS classifications and by GFS sub-sectors.

System of National Accounts

779. The international standard for national accounts is the System of National Accounts. National accounts differ from governmental accounts in that the reporting entity for the purposes of national accounts is typically a nation or a region within a nation. The reporting entity for governmental accounts may be any level of government within a nation, or any entity within a particular level of government. The SNA is a comprehensive accounting framework which uses consistent accounting definitions and concepts to summarize economic transactions occurring within the economy into a coherent picture of aggregate economic activity. It is an accounting system which allows nations to monitor their financial position, track trends in national development and to compare one nation's development with that of another. However, national income is primarily an economic measure.

780. Most countries prepare national accounts based on the SNA. However, there are still differences between countries in technologies, institutions and statistical methods. The range of national accounts produced by each country also varies, with some countries producing a more comprehensive set than others. The reliability of national accounts varies from country to country depending on the availability of data. A variety of sources of data is used to compile national accounts. Where data are unavailable, estimates may be used.

781. When the SNA was first introduced in 1953, its emphasis was mainly on quantifying the production of goods and services in the economy, the sources and distribution of income, and capital accumulation. The most recent developments place more emphasis on the analysis of financial flows and balances, and their links to the production process.

782. National accounts based on the SNA attempt to allow international comparisons to be made and provide users with information which is useful for:

- current economic analysis;
- short- and medium-term forecasting;
- model building;
- structural analysis of the economy; and
- the analysis of social and demographic information.

783. Gross domestic product and gross national income are two of the balancing items derived from the national accounts. These concepts provide a means of appraising the performance of the economy as a whole. They make it possible to compare one year's level of output with another year's level or to measure changes in the distribution of income and product among different groups or sectors. The best known use of those statistics is for public policy purposes (e.g., to estimate the effect of an increase in government spending on national income).

784. Statistics of national output can be presented in a number of different ways. These include:

- by final expenditure (consumption, investment and export);
- by industry (manufacturing, construction, wholesale and retail trade, etc);
- by type of income (wages and salaries, interest, rents, profits, etc.); and
- by economic sector (general government, corporations, households).

785. The national accounts framework is used by economic analysts for measuring activity in all sectors of the economy. It also allows data to be aggregated by economic sector. For each sector of the economy, including the general government sector, it is possible to prepare:

- a Production Account showing the sources and disposal of income;
- Income Accounts showing the nature and financing of consumption and saving;
- a Capital Account showing the use of saving;
- a Financial Account showing the direction and method of lending between sectors; and
- a Balance Sheet giving details of assets, liabilities, and net worth.

786. Although none of the national accounts' tables are directly comparable to the statements within governmental financial reports, an analysis of such statements under the national accounts framework is possible. For example, the Crown Accounts published by Statistics New Zealand (1996) are a

restatement of the Financial Statements of the Government of New Zealand. Production, Income and Outlay, and Capital Finance accounts are produced in this analysis. The government's financial transactions with other sectors of the economy, such as private enterprises, households, local government and GBEs, can also be identified and recorded.

787. The classifications shown below have been taken from the System of National Accounts (1993). Only the main categories are shown.

SNA Asset Classifications

Non-financial assets
- Produced assets
  - Fixed Assets (Tangible and Intangible)
  - Inventories
  - Valuables
- Non-produced assets
  - Tangible non-produced assets
  - Intangible non-produced assets

Financial assets
- Monetary gold and SDRs
- Currency and deposits
- Securities other than shares
- Loans
- Shares and other equity
- Insurance technical reserves
- Other accounts receivable (SNA 1993, pages 588-589)

SNA Liability Classifications

Currency and deposits
Securities other than shares
Loans
Shares and other equity[11]
Insurance technical reserves
Other accounts payable (SNA 1993, page 589)

788. Because the SNA is designed to record transactions across the entire economy it does not contain revenue classifications as such. Instead it classifies transactions and flows as follows:

- transactions in goods and services;
- distributive transactions;
- transactions in financial instruments; and
- other accumulation entries.

789. Other accumulation entries include consumption of fixed capital and acquisitions and disposals of assets.

European System of Accounts (ESA 1995)

790. Some jurisdictions are required to comply with regional forms of statistical reporting. The European System of National and Regional Accounts (ESA 95)[12] is one such system. It is a statistical system developed within the European Union which is intended to provide member countries with a set of harmonized and reliable statistics. These statistics are required for a number of purposes, including achieving the objectives of the Treaty on European Union and the Economic and Monetary Union. The ESA 95 has statutory backing in the form of a Regulation issued by the Council of the European Union.

[11] Equities are considered liabilities in the SNA to avoid overstating national wealth.

[12] The material in this section has been drawn from the "European System of Accounts ESA 1995, Luxembourg: Office for Official Publications of the European Communities, 1996". Readers are referred to this publication for a comprehensive description of ESA 95.

791. The concepts within the ESA 95 are harmonized with other international systems such as the SNA, the IMF Balance of Payments Manual, the GFS and the OECD Revenue Statistics.

792. The ESA 95 is consistent with the SNA with respect to definitions, accounting rules and classifications used. However there are some differences between the two systems to take account of its use within the European Union, both in relation to presentation of information and also the use of more precise definitions and accounting rules.

793. The differences in presentation include:

- a different structure to the discussion of transactions. The ESA organizes the discussion by transactions in products, distributive transactions and financial transactions. The SNA organizes the comparable discussion by type of account;
- the ESA provides a definition of a concept and examples of items which are included or excluded from that concept. In contrast the SNA provides more general discussion of concepts and the rationale underlying concepts;
- the ESA contains additional discussion of regional accounts and quarterly accounts which is not found in the SNA; and
- the SNA contains a chapter on satellite accounts which is not provided in the ESA.

794. The differences which result from more precise defintions of concepts and terms include:

- the ESA has introduced further clarification on the classification of output by sector;
- the ESA specifies concrete recording thresholds;
- the ESA does not require the recording of certain categories of household production goods which are not relevant to member countries;
- the ESA makes explicit reference to specific institutional arrangements in the European Union such as the INTRASTAT system;
- the ESA contains European Union specific classifications; and
- the ESA contains an additional classification for all external transactions: they are required to be divided into transactions between residents of the European Union and those with residents outside the European Union.

795. Within the ESA accounts are grouped in three categories:

- current accounts (including both production accounts and distribution and use of income accounts);
- accumulation accounts; and
- balance sheets.

796. Current accounts concern the generation, distribution and redistribution of income and its use in the form of final consumption. They also permit the calculation of saving within the economy. Accumulation accounts analyze the various components of changes in the assets and liabilities of various units and enable changes in net worth to be recorded. Balance sheets show the total assets and liabilities of the various units at the beginning and the end of the accounting period, together with their net worth.

797. The accounts are prepared in three forms:

- integrated economic accounts showing the accounts for all institutional sectors, the total economy and the rest of the world in a single table;
- a sequence of accounts giving more detailed information; and
- matrices in which the account is represented by a row/column pair.

798. General government is one of the sectors within the ESA. General government is divided into the following sub-sectors:

- Central government;
- State government;
- Local government; and
- Social security funds.

799. The sub-sector central government includes all administrative departments of the State and other central agencies whose competence extends normally over the whole economic territory, except for the administration of social security funds.

800. The sub-sector state government consists of state governments, which are separate institutional units exercising some of the functions of government at a level below that of central government and above that of the governmental institutional units existing at a lower level, except for the administration of social security funds.

801. The sub-sector local government includes those types of public administration whose competence extends to only a local part of the economic territory, apart from local agencies of social security funds.

802. The sub-sector social security funds includes all central, state and local institutional units whose principal activity is to provide social benefits and which fulfil each of the following two criteria:

- by law or by regulation certain groups of the population are obliged to participate in the scheme or to pay contributions; and
- general government is responsible for the management of the institution in respect of the settlement or approval of the contributions and benefits independently from its role as a supervisory body or employer.

Government Finance Statistics

803. "The government finance statistics system (GFS system) is a set of economic and statistical concepts, accounting rules, and classification guidelines for organizing data on general government sector operations in a systematic manner." (IMF 1996, page 3)

804. The GFS system is a specialized system designed to meet the needs of fiscal analysis. It provides information relating to the operations of the central, state, and local government subsectors of the general government sector. It was designed by the International Monetary Fund with the intention of encouraging governments to produce comparable financial information.

805. To the extent possible, the revised GFS will be harmonized with the following systems:

- system of national accounts;
- balance of payments; and
- monetary and financial statistics.

806. It is expected that harmonization with the SNA will make the compilation of GFS an intermediate stage in the compilation of national accounts statistics.

807. The revised GFS system will have a sequence of financial statements which link the opening and closing Balance Sheets with the transactions and other flows of the general government sector. Data from the system can be used to:

- develop a series of summary measures;
- analyze the operations of a specific level of government;
- analyze transactions between levels of government;
- analyze specific government operations (e.g., expenditure on social services); and
- analyze the net wealth of the general government sector.

808. The revised system would require the preparation of comprehensive Balance Sheets which include all financial and non-financial assets and liabilities. As with the SNA, changes in assets and liabilities resulting from factors other than transactions (e.g., changes in prices or exchange rates) will be included to permit reconciliation of opening and closing balances. However, the analytical framework of the revised GFS will distinguish between changes in net worth that result from transactions and those that arise from valuation changes or other changes in the volume of assets. Transactions in kind would also be accounted for. While the 1986 GFS manual focused on the overall deficit or surplus measured on a cash basis, the revised manual proposes several balancing items measured on an accrual basis.

809. The classifications shown below have been taken from the revised GFS manual (IMF 1999). Only the main categories are shown.

GFS Asset Classification

Non-financial assets
- Fixed assets
- Inventories
- Valuables
- Land
- Subsoil assets
- Noncultivated biological resources
- Water resources
- Intangible non-produced assets (IMF 1999, page 10.4)

Financial assets
- Acquired for policy purposes (classified as either Domestic or Abroad)
  - Securities other than shares
  - Loans
  - Shares and other equity
  - Financial derivatives
  - Other financial assets
- Acquired for liquidity management purposes (classified as either Domestic or Abroad)
  - Monetary gold and SDRs
  - Currency and deposits
  - Securities other than shares
  - Loans
  - Shares and other equity
  - Financial derivatives
  - Other financial assets (IMF 1999, page 8.7)

GFS Liability Classification

Classified as Domestic or Abroad
- Currency and deposits
- Securities other than shares
- Loans
- Financial derivatives
- Other liabilities (IMF 1999, page 8.7)

810. Examples of the proposed classification of expenses under the revised GFS are shown below.

01.	**General public services**	**06.**	**Housing and community amenities**
01.1	Executive and legislative organs, financial and fiscal affairs, external affairs	06.1	Housing development
		06.2	Community development
01.2	Foreign economic aid	06.3	Water supply
01.3	General services	06.4	Street lighting
01.4	Basic research	06.5	R&D Housing and community amenities
01.5	R&D General public services	06.6	Housing and community amenities n.e.c.
01.6	General public services n.e.c.	**07.**	**Health**
01.7	Public debt transactions	07.1	Medical products, appliances and equipment
01.8	Transfers of a general character between levels of government	07.2	Out-patient services
		07.3	Hospital services
02.	**Defence**	07.4	Public health services
02.1	Military defence	07.5	R&D Health
02.2	Civil defence	07.6	Health n.e.c.
02.3	Foreign military aid	**08.**	**Recreation, culture and religion**
02.4	R&D Defence	08.1	Recreational and sporting services
02.5	Defence n.e.c.	08.2	Cultural services
03.	**Public order and safety**	08.3	Broadcasting and publishing services
03.1	Police services	08.4	Religious and other community services
03.2	Fire-protection services	08.5	R&D Recreation, culture and religion
03.3	Law courts	**09.**	**Education**
03.4	Prisons	09.1	Pre-primary and primary education
03.5	R&D Public order and safety Recreation, culture and religion n.e.c.	09.2	Secondary education
		09.3	Post-secondary non-tertiary education
03.6	Public order and safety n.e.c.	09.4	Tertiary education
04	**Economic affairs**	09.5	Education not definable by level
04.1	General economic, commercial and labour affairs	09.6	Subsidiary services to education
		09.7	R&D Education
04.2	Agriculture, forestry, fishing and hunting	09.8	Education n.e.c.
04.3	Fuel and energy	**10.**	**Social protection**
04.4	Mining, manufacturing and construction	10.1	Sickness and disability
04.5	Transport	10.2	Old age
04.6	Communication	10.3	Survivors
04.7	Other industries	10.4	Family and children
04.8	R&D Economic affairs	10.5	Unemployment
04.9	Economic affairs n.e.c.	10.6	Housing
05.	**Environmental protection**	10.7	Social exclusion n.e.c.
05.1	Waste management	10.8	R&D Social protection
05.2	Waste water management	10.9	Social protection n.e.c.
05.3	Pollution abatement		
05.4	Protection of biodiversity and landscape		
05.5	Environmental protection n.e.c.		
05.6	R&D Environmental protection		

(IMF 1999, *Draft Manual of Government Finance Statistics* Table 6.1: Classification of Expense by Function of Government)

10000	**Expense**
11000	**Compensation of employees**
11100	Wages and salaries
11110	Wages and salaries in cash
11120	Wages and salaries in kind
11200	Social contributions
11210	Actual social contributions
11220	Imputed social contributions
12000	**Use of goods and services**
13000	**Consumption of fixed capital**
14000	**Property expense**
14100	Interest
14110	To other levels of national government
14120	To other residents
14130	To nonresidents
14200	Rent
15000	**Subsidies**
15100	To public nonfinancial corporations
15200	To private financial corporations
15300	To public financial corporations
15400	To other enterprises
16000	**Grants**
16100	To foreign governments
16110	Current
16120	Capital
16200	To international organizations
16210	Current
16220	Capital
16300	To other units of the general government sector
16310	Current
16320	Capital
17000	**Social benefits**
17100	Social security benefits
17200	Social assistance benefits
17300	Government employee social benefits
18000	**Other expense**
18100	Current expense
18200	Capital transfers

(IMF 1999, *Draft Manual of Government Finance Statistics*
Table 6.2: Economic Classification of Expense)

Issues facing Compilers using the Cash Basis or Modifications to the Cash Basis of Accounting

811. The main issue facing compilers of GFS, SNA and ESA statistics who use the cash or modifications to the cash basis of accounting is the need to make adjustments to their cash-based information to prepare the GFS, SNA and ESA reports. SNA is an accrual-based system and it is proposed that the GFS system also move to the accrual basis. However, many governments using the cash basis of accounting prepare national accounts by estimating adjustment entries to the extent possible.

812. Although it is proposed that the GFS system move to an accrual basis of accounting, countries are not expected to introduce an accrual system of accounting immediately, but to move progressively towards implementation of the GFS recommendations by either operating an accrual-based system or estimating a number of items. As stated in the draft GFS manual:

> *It is recognized that the implementation of the fully integrated GFS system presented in this manual will take some time and will need to progress at a pace determine by the differing needs and circumstances of the country involved. In particular, many countries will need to revise their underlying accounting systmes to reflect the accrual accounting principles and revised classifications of the GFS system.* (IMF 1999, page 1.4)

813. Compilers using modifications to the cash basis of accounting would face similar issues to compilers using cash accounting. However, they would have slightly more information available regarding short-term financial assets and liabilities.

814. The IMF envisages that a handbook which addresses practical compilation issues for different groups of compilers will be prepared.

Issues facing Compilers using the Accrual Basis or Modifications to the Accrual Basis

815. Those governments using the accrual basis of accounting to prepare their financial reports will have most of the information required for the preparation of national accounts and GFS statistics readily available. The main differences between accrual governmental financial reports prepared for external financial reporting purposes and national accounts or the proposed GFS reports are discussed in this section.

816. Differences include the concept of capital and the use of imputed figures for some items. The SNA differs from accrual-based external financial reporting in that it includes some items which are not transactions or events normally recognized in the governmental financial reports.

817. The proposed GFS reports also have a different focus from the governmental financial reports. As well as showing what would normally be termed operating revenue and expenses, the GFS also includes a full reconciliation of opening and closing net worth. Current, capital and financing flows are all included. Non-financial asset sales and purchases are classified as capital flows, and increases and decreases in financial assets and liabilities as financing flows.

818. Although GFS statements and the governmental financial reports may differ in their treatment of some assets, the coverage of assets is similar. GFS coverage includes only those assets which can be used in economic activity, are subject to ownership rights, and which can be expressed in monetary terms. One difference between GFS and governmental financial reports is that, in common with the SNA, GFS does not recognize certain military assets. The SNA distinguishes between defense assets which are used in combat and other defense assets. Under the SNA, expenditures by the military on weapons of destruction and the equipment needed to deliver them (rockets, missiles, warheads) are treated as intermediate consumption (i.e., they are expensed) rather than as fixed assets. However, assets with a dual military/civil use (e.g., some aircraft and hospitals) are recorded as capital expenditure in the national accounts.

819. Another difference between the various systems is the classification of monetary gold. Although the SNA/GFS and IAS definitions of assets are functionally equivalent, the IAS definition of a financial asset excludes monetary gold held by governments, which is specifically included in the SNA definition of financial assets. However, monetary gold is still recognized as an asset under the IAS definition of an asset — it is merely the classification which is different.

820. A major difference between GFS and governmental financial reports relates to the valuation of assets and liabilities. In governmental financial reports, depending on the country, assets are valued either at historical cost, less accumulated depreciation or in the case of certain assets (e.g., land and buildings) they may be revalued periodically. When an asset is sold or transferred there is usually some difference between the transaction price and the recorded book value. This difference is shown as a gain or loss on sale. In governmental financial reports liabilities are recorded at the amount of the proceeds received in exchange for the obligation or at the amount of cash or cash equivalent required to satisfy the liability. Gains and losses on settlement of liabilities are not common but may occur occasionally. In contrast, GFS requires that all assets and liabilities be revalued to current prices every year. As a result, in GFS statements, changes in value from one period to the next are treated as other economic flows and no gain or loss is recognized when an asset is disposed of or a liability is liquidated in a transaction. In order to facilitate the preparation of GFS statistics, it is helpful if all gains and losses recorded on the disposal of assets and liabilities are separately identified.

821. Under the accrual basis or modifications to that basis, a bad debt expense for actual or expected bad debts may be recorded. In general, GFS does not write down the asset until the claim is formally canceled. Under GFS if the cancellation is by mutual agreement, it is a transaction; if the government unilaterally writes off the asset, it is an other economic flow. In order to facilitate preparation of GFS statistics, bad debt expense and any associated bad debt provision should be separately identified.

822. This Chapter has identified some of the differences which may occur in the treatment of items between GFS and governmental financial reports. In order to assist users who wish to use both types of information, it is helpful if governments prepare a reconciliation between the reported surplus under

governmental financial reports and GFS. This allows readers to understand the differences between the reported figures.

All Compilers

823. GFS requires that expenses be classified using both the economic and functional classifications. Compilers should therefore ensure that information for governmental financial reports is recorded using both these categories, in addition to any other classifications which the entity may use. This would allow individual entities to prepare GFS statistics more easily and would reduce the need for adjustments when combining the reports of different entities for GFS purposes.

APPENDIX 1

GLOSSARY OF TERMS

This glossary contains definitions of some terms used in this Study. While these terms may be used interchangeably in other publications, the intended definitions in this publication are as given below.

Accrual basis: means a basis of accounting under which transactions and other events are recognized when they occur (and not as cash or its equivalent is received or paid) and are recorded in the accounting records and reported in the financial statements of the periods to which they relate.

Appropriation: refers to an authorization by the legislature to expend or commit funds. The nature of appropriations varies between jurisdictions.

Basis of accounting: refers to the body of accounting principles that determine when the effects of transactions or events should be recognized for financial reporting purposes. It relates to the timing of the measurements made, regardless of the nature of the measurement. Common bases of accounting are the cash basis of accounting (i.e., effects of transactions or events are recognized when cash is paid or received) and the (full) accrual basis of accounting (i.e., effects of transactions or events are recognized when they take place). There are many variations of both bases.

Capital contributions: refers to future economic benefits that have been contributed to the entity by parties external to the entity, other than those which result in liabilities of the entity, that establish a financial interest in the net assets/equity of the entity which:

- conveys entitlement both to distributions of future economic benefits by the entity during its life, such distributions being at the discretion of the ownership group or its representatives, and to distributions of any excess of assets over liabilities in the event of the entity being wound up; and/or
- can be sold, transferred or redeemed.

Carrying amount: is the amount at which an asset is included in the financial statements after deducting any accumulated depreciation thereon.

Cash basis: means a basis of accounting under which transactions and other events are recognized when cash is received or paid. It measures financial results for a period as the difference between cash receipts and cash payments.

Closing rate: is the spot exchange rate at the reporting date.

Commitment: refers to a government's responsibility for a future liability, based on an existing contractual agreement. Under the accrual basis of accounting the term commitment usually refers to amounts committed under leases or, under contract, for capital expenditure. Under the cash basis of accounting, the term may refer to amounts within an operating or capital budget where a contractual obligation has been entered into, but a cash payment has not yet been made.

Consolidated financial statements: the financial statements of a group presented as those of a single reporting entity.

Custodial activities: means the making of transactions or the management of assets or liabilities by a government reporting entity on behalf of another organization.

Distributions to the controlling entity or owners: refers to future economic benefits distributed by the entity to all or part of its ownership group, either as a return on investment or as a return of investment.

Elements of financial statements: the types or classes of items that are reported in the financial statements, including notes thereto and related schedules.

Exchange difference: is the difference resulting from reporting the same number of units of a foreign currency in the reporting currency at different exchange rates.

Exchange rate: is the ratio for exchange of two currencies.

Fair value: is the amount for which an asset could be exchanged between knowledgeable, willing parties, in an arm's length transaction.

Financial condition: refers to a government's health as measured by sustainability, vulnerability and flexibility, looked at in the context of the overall economic and financial environment.

Financial instrument: refers to any contract that gives rise to both a financial asset of one entity and a financial liability or equity instrument of another entity.

Financial position: refers to the financial status of a government at a given point in time, as shown in the financial statements.

Financial reporting: refers to the communication of financial information by an entity to interested parties. It encompasses all reports that contain financial information based on data generally found in the financial accounting and reporting system. It includes financial statements as well as financial information presented in budgets, fiscal plans and estimates of expenditure or reports on the performance of individual programs or activities.

Financial reports: the general purpose financial reports (referred to in this Study as governmental financial reports), that are designed to meet the common information needs of users outside the reporting entity. Those external users rely on the reports as an important source of financial information because they have limited authority, ability, or resources to obtain additional information. While financial statements comprise the core of the financial reports, other financial information, such as performance measures or budget information, might also be included.

Financial statements: the accounting statements prepared by a reporting entity to communicate information about its financial performance and position. They include those notes and schedules that are needed to clarify or further explain items in the statements. For business-oriented enterprises, financial statements normally include a Balance Sheet, Income Statement, Statement of Retained Earnings, and Statement of Cash Flows. Governments and governmental units may have a similar set of statements or may have lists of assets and liabilities, revenue and expenses. The statements similar to the Balance Sheet and Income Statement are commonly referred to as Statement of Financial Position and Statement of Financial Performance in the public sector.

Flexibility: the degree to which a government can increase its financial resources to respond to rising commitments, by either expanding its revenues or increasing its debt burden.

Foreign currency: is a currency other than the reporting currency of the entity.

Foreign entity: is a foreign operation, the activities of which are not an integral part of those of the reporting entity.

Fund accounting: is an accounting system structured to treat restricted assets as a separate accounting, and in many cases a separate financial reporting, entity. On this basis, funds represent a pool of resources set aside for the carrying on of specific activities or attaining certain objectives in accordance with legislative or other regulatory restrictions placed on the use of those resources.

Government: refers to government, government agencies and similar bodies whether local, national or international.

Government Business Enterprises: refers to businesses which operate within the public sector ordinarily to meet a political or social interest objective. They are ordinarily required to operate commercially, that is, to make profits or to recoup, through user charges, a substantial proportion of their operating costs.

Governmental financial reports: refers to financial reports which are intended to meet the needs of external users who are unable to require, or contract for, the preparation of special reports to meet their specific information needs.

Heritage asset: assets earmarked by the government for preservation because of their unique historical, geographical, cultural or environmental attributes.

Intergenerational (or interperiod) equity: refers to the concept that current generations should pay for services received and that these costs should not be passed on to future generations.

Investment property: refers to an investment in land or buildings that are not occupied substantially for use by, or in the operations of, the investing entity, or another entity in the same group as the investing entity.

Measurement focus: refers to the messages and information portrayed in the financial statements. A particular measurement focus is accomplished by considering not only when the effects of transactions and events involving those resources are recognized (i.e., the basis of accounting), but also what resources are measured. For example, the financial statements of business enterprises are designed to measure profit or loss and changes in shareholders' funds. Government financial statements could be designed to express, for example, the flow of economic resources, the flow of total financial resources or the flow of current financial resources.

Modifications to the accrual basis: common modifications to the accrual basis of accounting include the recognition of some, but not all assets, particularly physical assets, and the recognition of some, but not all liabilities, particularly pension liabilities.

Modifications to the cash basis: a common modification to the cash basis of accounting involves holding the books open for around a month after year end (the specified period). Receipts and payments which occur during the specified period but originate in the previous reporting period are recognized as receipts and payments of the previous reporting period. Cash flows at the beginning of the reporting period which have already been accounted for in the previous reporting period are deducted from the current period. The primary financial statement is the Cash Flow Statement.

Monetary financial assets and liabilities: refers to financial assets and liabilities to be received or paid in fixed or determinable amounts of money.

Non-reciprocal transactions: are transactions in which an entity receives assets (including cash) or has liabilities extinguished without directly giving approximately equal value in exchange to the other party or parties to the transfer. Taxation is a common form of a non-reciprocal transaction.

Outcomes: refers to benefits sought by a Government.

Outputs: refers to goods and services produced by departments.

Parent: refers to an entity that has one or more subsidiaries.

Programs: refers to a group of outputs, services or activities intended to contribute to some government policy outcome.

Reciprocal transactions: refers to a transaction in which an entity receives assets (including cash) or has liabilities extinguished and gives approximately equal value in exchange to the other party or parties to the transfer.

Recognition: refers to the process of incorporating in the financial statements an item that meets the definition of an element and satisfies the criteria for recognition. It involves the depiction of that item in words and by a monetary amount and the inclusion of that amount in the financial statement totals.

Recoverable amount: is the amount which the entity expects to recover from the future use of an asset, including its residual value on disposal.

Reporting date: refers to the end of the reporting period to which the financial report relates.

Reporting entity: those entities in respect of which it is reasonable to expect the existence of users dependent upon financial reports for information which will be useful to them for accountability and decision making purposes. The term may refer to departments or ministries of government, or other entities that are part of government.

Reporting model: refers to the configuration and presentation of financial statements; in particular, what statements are included in the set of financial statements, how they interrelate, and how key measures are displayed in them.

Resource accounting: covers a set of accruals accounting techniques for reporting on the expenditure of the United Kingdom central government, comprising departments and their executive agencies including Trading Funds, and a framework for analyzing expenditure by departmental objective, relating this to outputs where-ever possible.

Sub-entity: refers to a reporting entity such as a government department.

Sustainability: the degree to which a government can maintain existing programs and meet existing creditor requirements without increasing the debt burden on the economy.

Vulnerability: the degree to which a government becomes dependent on, and therefore vulnerable to, sources of funding outside its control or influence, both domestic and international.

APPENDIX 2

EXAMPLES OF FINANCIAL STATEMENTS

CASH BASIS
Report of the Director of Audit on the Accounts of the Government of the Hong Kong Special Administrative Region for the year ended 31 March 1999
Report on the Accounts and Finance for the year 1997, Parliament of Fiji

MODIFICATIONS TO THE CASH BASIS
Public Accounts of Ontario, 1992–93 (Canada)

ACCRUAL BASIS
Agencia Estatal De La Administración Tributaria (the Spanish Tax Agency) for the year ended December 31, 1997
Financial Statements of the Government of New Zealand for the year ended 30 June 1999
Annual Report and Financial Accounts 1997–98, West Sussex County Council (United Kingdom)

MODIFICATIONS TO THE ACCRUAL BASIS
Public Accounts of Canada 1999
Compte Général de L'Administration Des Finances (CGAF) for 1996 (France)

The examples in this Appendix illustrate current practice. The examples are intended to facilitate understanding and to put the examples used throughout the Study into context. They have also been selected to illustrate the variety of accounting treatments and forms of presentation used by different jurisdictions.

For reasons of space, only the main financial statements, or in some cases selected financial statements, are reproduced in this Appendix. Although the notes to the financial statements have not been included they are an integral part of the financial statements and are treated as such by an auditor when forming an opinion on the financial statements. Readers are therefore encouraged to refer to the complete financial statements (including the notes and the auditor's report). Website references for downloading or ordering documents of the selected governments are provided in Appendix 3.

Report of the Director of Audit

on the Accounts of the

Hong Kong Government

for the year ended

31 March 1999

October 1999

GENERAL REVENUE ACCOUNT
STATEMENT OF RECEIPTS AND PAYMENTS
FOR THE YEAR ENDED 31 MARCH 1999

		Note	1999 $'000	1998 $'000
Cash and bank balances at 1 April 1998			**2,330,994**	2,680,644
Revenue	(Schedule 1)		**179,143,145**	228,676,125
Expenditure	(Schedule 2)		**(194,693,918)**	(165,180,619)
(Deficit)/Surplus for the year			**(15,550,773)**	63,495,506
Other cash movements		**1**	**15,586,716**	(63,845,156)
Cash and bank balances at 31 March 1999			**2,366,937**	2,330,994

Note :

1. These transactions arise from increases and decreases in assets (other than cash and bank balances) and liabilities.

THE TREASURY,
Hong Kong, 16 June 1999

SHUM Man-to
Director of Accounting

政府一般收入帳目
1998年4月1日至1999年3月31日收支表

	註釋	1999 $'000	1998 $'000
1998年4月1日現金及銀行結餘		**2,330,994**	2,680,644
收入（附表1）		**179,143,145**	228,676,125
開支（附表2）		**(194,693,918)**	(165,180,619)
年內(虧絀)/盈餘		**(15,550,773)**	63,495,506
其他現金轉動	**1**	**15,586,716**	(63,845,156)
1999年3月31日現金及銀行結餘		2,366,937	2,330,994

註釋:
1.這些項目是因資產（不包括現金及銀行結餘）及負債有所增減而引致。

香港庫務署　　1999年6月16日　　庫務署署長　**沈文燕**

政府一般收入帳目

General Revenue Account

審計署署長向立法會主席提交的報告書

REPORT OF THE DIRECTOR OF AUDIT TO THE PRESIDFNT OF THE LEGISLATIVE COUNCIL

我已審核及審計刊於第9頁至第25頁的財務報表，該等財務報表根據第12頁載列的會計政策所擬備。

I have examined and audited the financial statements on pages 9 to 25 which have been prepared under the accounting policies set out on page 12.

庫務署署長及審計署署長的責任

Respective responsibilities of the Director of Accounting Services and the Director of Audit

按照《公共財政條例》(第2章)第16(1)條的規定，庫務署署長負責編製及監管香港特別行政區政府的帳目。

The Director of Accounting Services is responsible for the compilation and supervision of the accounts of the Government of the Hong Kong Special Administrative Region in accordance with section 16(1) of the Public Finance Ordinance (Cap. 2).

我的責任是根據我的審計工作的結果，對財務報表作出獨立意見，並向立法會主席報告。

It is my responsibility to form an independent opinion, based on my audit, on the financial statements and to report my opinion to you.

意見的基礎

Basis of opinion

茲證明我已按照《核數條例》(第122章)第12(1)條的規定及審計署的審計準則，審核及審計上述的財務報表。審計範圍包括以抽查方式查核與財務報表所載數額及披露事項有關的憑證，亦包括評估庫務署署長於擬備該等財務報表時所作的判斷、所釐定的會計政策

I certify that I have examined and audited the financial statements referred to above in accordance with section 12(1) of the Audit Ordinance (Cap. 122) and the Audit Commission auditing standards. An audit includes examination, on a test

是否適合政府一般收入帳目的具體情況、及有否貫徹運用並足夠披露該等會計政策。

我在策劃和進行審計工作時，均以取得一切我認為必需的資料及解釋為目標，使我能獲得充分的憑證，就該等財務報表是否存有重要錯誤陳述，作合理的確定。在作出意見時，我亦已衡量該等財務報表所載資料在整體上是否足夠。我相信，我的審計工作已為下列意見建立合理的基礎。

意見

我認為上述的財務報表恰當顯示政府一般收入帳目在一九九九年三月三十一日的資產負債情況及結算至該日止全年度的收支帳目，並已按照《公共財政條例》及《核數條例》第11(1)條適當擬備。

審計署署長　　陳彥達

香港審計署

一九九九年十月十一日

basis, of evidence relevant to the, amounts and disclosures in the financial statements. It also includes an assessment of the judgements made by the Director of Accounting Services in the preparation of the financial statements, and of whether the accounting policies are appropriate to the circumstances of the General Revenue Account, consistently applied and adequately disclosed.

I planned and performed my audit so as to obtain all the information and explanations which I considered necessary in order to provide me with sufficient evidence, to give reasonable assurance as to whether the financial statements are free from material rnisstatement. In forming my opinion 1 also evaluated the overall adequacy of the presentation of information in the financial statements. I believe, that my audit provides a reasonable basis for my opinion.

Opinion

In my opinion the financial statements properly present the assets avid liabilities of the General Revenue Account as at 31 March 1999 and the receipts and payments for the year then ended and have been properly prepared in accordance with the Public Finance Ordinance and section 11(1) of the Audit Ordinance.

Dominic Y T Chan
Director of Audit

Audit Commission
Hong Kong
11 October 1999

CAPITAL WORKS RESERVE FUND
STATEMENT OF RECEIPTS AND PAYMENTS
FOR THE YEAR ENDED 31 MARCH 1999

		Note	1999 $'000	1998 $'000
Cash and bank balances at 1 April 1998			**23,047**	484,675
Revenue	(Schedule 1)		**25,685,731**	57,184,335
Expenditure	(Schedule 2)		**(40,016,774)**	(77,915,410)
Deficit for the year			**(14,331,043)**	(20,731,075)
Other cash movements		**1**	**14,340,753**	20,269,447
Cash and bank balances at 31 March 1999			**32,757**	23,047

Note :

1: These transactions arise from increases and decreases in assets (other than cash and bank balances) and liabilities.

THE TREASURY,
Hong Kong, 16 June 1999

SHUM Man-to
Director of Accounting

基本工程儲備基金
1998年4月1日至1999年3月31日收支表

	註釋	1999 $'000	1998 $'000
1998年4月1日現金及銀行結餘		**23,047**	484,675
收入（附表1）		**25,685,731**	57,184,335
開支（附表2）		**(40,016,774)**	(77,915,410)
年內虧絀		**(14,331,043)**	(20,731,075)
其他現金轉動	**1**	**14,340,753**	20,269,447
1999年3月31日現金及銀行結餘		**32,757**	23,047

註釋：
1. 這些項目是因資產（不包括現金及銀行結餘）及負債有所增減而引致。

香港庫務署 1999年6月16日 庫務署署長 **沈文燾**

基本工程儲備基金

審計署署長向立法會主席提交的報告書

我已審核及審計刊於第29頁至第37頁的財務報表，該等財務報表根據第31頁載列的會計政策所擬備。

庫務署署長及審計署署長的責任

按照《公共財政條例》(第2章)第16(1)條的規定，庫務署署長負責編製及監管香港特別行政區政府的帳目。

我的責任是根據我的審計工作的結果，對財務報表作出獨立意見，並向立法會主席報告。

意見的基礎

茲證明我已按照《核數條例》(第122章)第12(1)條的規定及審計署的審計準則，審核及審計上述的財務報表。審計範圍包括以抽查方式查核與財務報表所載數額及披露事項有關的憑證，亦包括評估庫務署署長於擬備該等財務報表時所作的判斷、所釐定的會計政策

Capital Works Reserve Fund

REPORT OF THF, DIRECTOR OF AUDIT TO THE PRESIDENT OF THE LEGISLATIVE COUNCIL

I have examined and audited the financial statements on pages 29 to 37 which have been prepared under the accounting policv set out on page 31.

Respective responsibilities of the Director of Accounting Services and the Director of Audit

The Director of Accounting Services is responsible for the compilation and supervision of the accounts of the Government of the Hong Kong Special Administrative Region in accordance with section 16(1) of the Public Finance Ordinance (Cap. 2).

It is my responsibility to form an independent opinion. based on my audit, on the financial statements and to report my opinion to you.

Basis of opinion

I certify that I have examined and audited the financial statements referred to above in accordance with section 12(1) of the Audit Ordinance (Cap. 122) and the Audit Commission auditing standards. An audit includes examination, on a test basis of evidence relevant to

是否適合基本工程儲備基金的具體情況、及有否貫徹運用並足夠披露該等會計政策。

the amounts and disclosures in the financial statement. It also includes an assessment of the judgements made by the Director of Accounting Services in the Preparation of the financial statements, and of whether the accounting policy is appropriate to the circumstances of the Capital Works Reserve Fund, consistently applied and adequately disclosed.

我在策劃和進行審計工作時，均以取得一切我認為必需的資料及解釋為目標，使我能獲得充分的憑證，就該等財務報表是否存有重要錯誤陳述，作合理的確定。在作出意見時，我亦已衡量該等財務報表所載資料在整體上是否足夠。我相信，我的審計工作已為下列意見建立合理的基礎。

I planned and performed my audit so as to obtain all the information and explanations which I considered necessary in order to provide me with sufficient evidence to give reasonable assurance as to whether the financial statements are free from material misstatement. In forming my opinion I also evaluated the overall adequacy of the presentation of information in the financial statements. I believe that my audit provides a reasonable basis for my opinion.

意見

我認為上述的財務報表適當顯示基本工程儲備基金在一九九九年三月三十一日的資產負債情況及結算至該日止全年度的收支帳目，並已按照《公共財政條例》及《核數條例》第11(1)條適當擬備。

Opinion

In my opinion the financial statements properly present the assets and liabilities of the Capital Works Reserve Fund as at 31 March 1999 and the receipts and payments for the year then ended and have been properly prepared in accordance with the Public Finance Ordinance and section 11(1) of the Audit Ordinance.

審計署署長　　陳　彥　達

香港審計署

一九九九年十月十一日

Dominic Y T Chan
Director of Audit

Audit Commission
Hong Kong
11 October 1999

Report on
THE ACCOUNTS AND FINANCE
For the Year 1997

PARLIAMENT OF FIJI
PARLIAMENTARY PAPER NO. 39 OF 1998

APPENDIX 2

Consolidated Fund

STATEMENT OF BALANCES FOR THE YEAR ENDED 31 DECEMBER 1997

Previous Year		*Current Year*
$		$
139,761,120	Operating Fund Account ……………………………………..	141,715,132
20,232,908	Borrowing Fund Account …………………………………….	40,527,802
(283,291)	Lending Fund Account ……………………………………….	1,279,210
(11,223,353)	Revolving Fund Account ……………………………………..	(15,508,484)
.....	Special Fund Account ………………………………………...	.....
2,000,000	Contingencies Fund Account …………………………………	1,500,000
150,487,384	Total Consolidated Fund ……………………………………..	169,513,660
	Represented By :	
5,932,605	Cash at Bank ...……………………………………………	12,372,957
155,752,425	Investment in Shares and Equities ...……………………...	170,415,528
161,685,030		182,788,485
11,197,646	*Less:* Amount Held for Consolidated Trust Fund …...…….	13,274,825
150,487,384		169,513,660

Ministry of Finance
Suva, Fiji
30 June 1998

S Narube
Permanent Secretary of Finance

Operating Fund Account

STATEMENT OF RECEIPTS AND EXPENDITURE FOR THE YEAR ENDED 31 DECEMBER 1997

Previous Year			*Current Year*	
$	$		$	$
		RECEIPTS		
545,177,522		Operating Revenue …………………………	588,686,798	
8,679,620		Capital Revenue …………………………….	6,584,394	
182,186,863	736,044,005	Value Added Tax …………………………..	204,208,997	799,480,189
	210,538,306	Transferred from Borrowing Fund Account..		270,965,421
	7,509,141	Transferred from Lending Fund Account …..		3,979,857
	20,000	Investment in Shares ………………………..		14,663,103
	954,111,452			1,089,088,570
		EXPENDITURE		
558,676,041		Operating Expenditure………………………	590,143,681	
203,771,757		Capital Expenditure…………………………	262,314,207	
34,891,311	797,339,109	Value Added Tax …………………………...	49,395,453	901,853,341
	151,253,076	Transferred to Borrowing Fund Account……		180,157,337
	13,100,000	Transferred to Lending Fund Account…..…		5,123,880
	961,692,185			1,087,134,558
	(7,580,733)	(Deficit)/Surplus for the year ……………….		1,954,012
	147,341,853	*Add:* The Balance at 1 January of ……..…		139,761,120
	139,761,120	Leaving A Balance at 31 December of ……..		141,715,132

Ministry of Finance
Suva, Fiji
30 June 1998

S Narube
Permanent Secretary for Finance

Operating Fund Account

ABSTRACT OF GENERAL AND CAPITAL REVENUE FOR THE YEAR 1997

Heads of Revenue	Estimate	Actual Revenue	Increase	Decrease
	$	$	$	$
GENERAL REVENUE				
1. Customs……………………………………	208,398,000	219,561,599.47	11,163,599.47	....
2. Port and Harbour Dues, etc. ………………	336,500	520,103.10	183,603.10	....
3. Licences …………………………………	13,638,500	12,935,501.10	....	702,998.90
4. Inland Revenue …………………………	423,575,000	445,202,163.76	21,627,163.76	....
5. Internal Revenue not Otherwise Classified ………………………………..	6,800,000	6,396,820.17	....	403,179.83
6. Fees, Royalties, Sales and Reimbursements…………………………	43,758,900	50,898,246.90	7,139,346.90	....
7. Posts and Telecommunications…………	5,494,700	117,379.91	....	5,377,320.09
8. Rent of Government Property…………..	5,622,000	6,843,586.17	1,221,586.17	....
9. Interest				
Public Account……………………	350,000	263,189.99	....	86,810.01
Transferred from Lending Fund Account …………………………..	550,300	243,719.51	....	306,580.49
10. Miscellaneous……………………………	28,208,200	51,107,856.43	22,899,656.43	....
11. New Revenue Measures…………………	6,059,200	....	....	6,059,200.00
General Revenue Total…………..	742,791,300	794,090,166.51	64,234,955.83	12,936,089.32
CAPITAL REVENUE				
12. Grant Aid ………………………………..	8,135,700	4,945,111.96	....	3,190,588.04
13. Contributions for Capital Projects ………	20,000	345,556.22	325,556.22	....
14. Transferred from Lending Fund Account.	2,600,000	2,785,485.97	185,485.97	....
Miscellaneous……………………………	650,000	1,293,725.57	643,725.57	....
Capital Revenue Total	11,405,700	9,369,879.72	1,154,767.76	3,190,588.04
TRANSFERRED FROM BORROWING FUND ACCOUNT				
15. Overseas Loans …………………………	18,300,000	8,653,769.41	....	9,646,230.59
16. Domestic Loans…………………………	263,852,200	262,311,651.40	....	1,540,548.60
Total………………………………	282,152,200	270,965,420.81	....	11,186,779.19
Capital Revenue Total…………..	293,557,900	280,335,300.53	1,154,767.76	14,377,367.23
Grand Total ………………………	1,036,349,200	1,074,425,467.04	65,389,723.59	27,313,456.55

Operating Fund Account

ABSTRACT OF OPERATING AND CAPITAL EXPENDITURE FOR THE YEAR 1997

Heads of Expenditure	Revised Estimate	Expenditure	Increase	Decrease
	$	$	$	$
GENERAL ADMINISTRATION				
OFFICE OF THE PRESIDENT				
Operating…………………………..	774,000	852,724.78	78,724.78	....
VAT………………………………..	77,400	26,726.16	....	50,673.84
CABINET OFFICE				
Operating…………………………..	3,150,658	3,105,567.49	....	45,090.51
VAT………………………………..	294,300	310,928.76	16,628.76	....
PUBLIC SERVICE COMMISSION				
Operating………………………….	4,962,750	4,555,764.87	....	406,985.13
Capital……………………………..	1,878,450	1,269,010.03	....	609,439.97
VAT………………………………..	375,800	384,643.95	8,843.95	....
DISCIPLINARY APPEAL BOARD				
Operating…………………………..	600	....	....	600.00
VAT...	100	....	....	100.00
NATIONAL ARCHIVES OF FIJI				
Operating...	253,442	254,687.83	1,245.83	....
VAT…...	22,400	32,380.81	9,980.81	....
OFFICE OF THE ATTORNEY-GENERAL & MINISTER FOR JUSTICE				
Operating...	2,967,100	2,918,111.51	....	48,988.49
VAT...	274,800	272,874.37	....	1,925.63
MINISTRY OF FINANCE AND ECONOMIC DEVELOPMENT				
Operating...	8,664,469	7,997,144.58	....	667,324.42
Capital..	2,117,800	887,458.15	....	1,230,341.85
VAT………………………………..	403,100	340,348.22	....	62,751.78
INLAND REVENUE				
Operating…………………………..	4,729,368	4,657,860.37	....	71,507.63
VAT………………………………..	432,400	425,000.51	....	7,399.49
CUSTOMS AND EXCISE				
Operating…………………………..	4,286,400	4,629,982.87	343,582.87	....
VAT………………………………..	428,600	427,384.49	....	1,215.51
PRINTING AND STATIONERY				
Operating…………………………..	1,608,050	1,592,706.73	....	15,343.27
Capital..	366,150	363,474.12	....	2,675.88
VAT………………………………..	176,400	156,021.11	....	20,378.89

Operating Fund Account

ABSTRACT OF OPERATING AND CAPITAL EXPENDITURE FOR THE YEAR 1997

Heads of Expenditure	Revised Estimate	Expenditure	Increase	Decrease
	$	$	$	$
SUPPLIES				
Operating…………………………..	4,361,807	4,687,721.79	325,914.79	....
Capital……………………………..	559,493	559,492.43	....	0.57
VAT………………………………..	506,500	505,836.61	....	663.39
INFORMATION, TECHNOLOGY AND COMPUTING SERVICES				
Operating…………………………..	2,185,342	2,098,724.92		86,617.08
Capital……………………………..	378,000	367,389.44	....	10,610.56
VAT………………………………..	253,300	253,075.04	....	224.96
BUREAU OF STATISTICS				
Operating…………………………..	1,616,021	1,609,860.79	....	6,160.21
VAT………………………………..	177,000	174,612.40	....	2,387.60
CENTRAL PLANNING OFFICE				
Operating…………………………..	999,200	679,173.40	....	320,026.60
VAT………………………………..	96,500	59,132.47	....	37,367.53
MINISTRY OF FIJIAN AFFAIRS, REGIONAL DEVELOPMENT AND MULTI-ETHNIC AFFAIRS				
Operating…………………………..	12,746,200	12,360,462.75	....	385,737.25
Capital……………………………..	150,000	103,464.73	....	46,535.27
VAT………………………………..	106,600	(2,839.52)	....	109,439.52
MINISTRY OF HOME AFFAIRS AND IMMIGRATION				
Operating.......................................	1,945,265	1,942,662.81	....	2,602.19
Capital……………………………..	15,108	15,030.12	....	77.88
VAT………………………………..	196,365	195,864.15	....	500.85
FIJI MILITARY FORCES				
Operating…………………………..	43,997,185	44,696,549.95	699,364.95	....
Capital……………………………..	300,000	238,545.52	....	61,454.48
VAT………………………………..	4,210,700	3,682,305.85	....	528,394.15
PRISONS				
Operating…………………………..	5,843,177	6,738,733.90	895,556.90	....
VAT………………………………..	587,200	612,737.84	25,537.84	....
FIJI POLICE				
Operating…………………………..	28,044,800	29,918,598.17	1,873,798.17	....
Capital……………………………..	1,585,000	1,566,356.84	....	18,643.16
VAT………………………………..	2,786,000	2,899,458.71	113,458.71	....
MINISTRY OF LABOUR AND INDUSTRIAL RELATIONS				
Operating…………………………..	2,058,900	2,155,815.78	96,915.78	....
VAT………………………………..	179,500	201,761.41	22,261.41	....

Operating Fund Account

ABSTRACT OF OPERATING AND CAPITAL EXPENDITURE FOR THE YEAR 1997

Heads of Expenditure	Revised Estimate	Expenditure	Increase	Decrease
	$	$	$	$
MINISTRY OF FOREIGN AFFAIRS				
Operating…………………………..	9,248,600	8,986,230.14	....	262,369.86
Capital...	98,000	215,404.50	117,404.50	....
VAT………………………………..	990,800	664,557.65	....	326,242.35
OFFICE OF THE AUDITOR-GENERAL				
Operating…………………………..	1,097,500	998,425.74	....	99,074.26
VAT………………………………..	109,400	85,740.93	....	23,659.07
ELECTIONS OFFICE				
Operating…………………………..	385,600	362,242.00	....	23,358.00
Capital...	52,600	52,580	....	20.00
VAT………………………………..	43,800	33,006.55	....	10,793.45
JUDICIAL				
Operating…………………………..	4,629,900	4,484,084.58	....	145,815.42
VAT………………………………..	462,700	449,332.61	....	13,367.39
LEGISLATURE				
Operating…………………………..	5,923,600	5,435,325.14	....	488,274.86
VAT………………………………..	591,400	635,674.76	44,274.76	....
OFFICE OF THE OMBUDSMAN				
Operating…………………………..	229,000	230,485.44	1,485.44	....
VAT………………………………..	22,800	17,044.10	....	5,755.90
OFFICE OF THE DIRECTOR OF PUBLIC PROSECUTIONS				
Operating…………………………..	656,300	655,805.26	....	494.74
VAT………………………………..	65,600	62,820.68	....	2,779.32
DEPARTMENT OF REGIONAL DEVELOPMENT				
Operating………………………….	8,781,900	8,323,745.53	....	458,154.47
Capital……………………………..	5,110,000	5,557,087.70	447,087.70	....
VAT………………………………..	1,003,400	969,449.46	....	33,950.54
MINISTRY OF INFORMATION, BROADCASTING, TELEVISION AND TELECOMMUNICATIONS				
Operating…………………………..	1,674,000	1,539,914.08	....	134,085.92
VAT………………………………..	153,700	126,520.10	....	27,179.90
DEPARTMENT OF WOMEN AND CULTURE				
Operating…………………………..	797,400	794,303.52	....	3,096.48
Capital……………………………..	225,100	48,467.93	....	176,632.07
VAT………………………………..	59,000	48,036.22	....	10,963.78

Operating Fund Account

ABSTRACT OF OPERATING AND CAPITAL EXPENDITURE FOR THE YEAR 1997

Heads of Expenditure	Revised Estimate	Expenditure	Increase	Decrease
	$	$	$	$
DEPARTMENT OF MULTI-ETHNIC AFFAIRS				
Operating..…………………………	1,006,600	974,264.90	....	32,335.10
Capital...	1,000,000	998,544.95	....	1,455.05
VAT..	27,200	23,997.09	....	3,202.91
Operating-Total…………………	169,625,134	170,237,681.62	4,316,589.51	3,704,041.89
Capital-Total……………………	13,835,701	12,242,306.46	564,492.20	2,157,886.74
VAT-Total………………………	15,114,765	14,074,433.49	240,986.24	1,281,317.75
General Administration-Total…..	198,575,600	196,554,421.57	5,122,067.95	7,143,246.38
Net Decrease…………	....	....	....	2,021,178.43
SOCIAL SERVICES MINISTRY OF EDUCATION, WOMEN AND CULTURE				
Operating…………………………..	133,069,869	132,709,952.66	....	359,916.34
Capital……………………………..	2,562,000	2,536,567.08	....	25,432.92
VAT………………………………..	11,422,931	11,330,569.50	....	92,361.50
UNIVERSITY OF THE SOUTH PACIFIC				
Operating………………………….	21,104,900	21,097,245.78	....	7,654.22
MINISTRY OF HEALTH AND SOCIAL WELFARE				
Operating…………………………..	70,524,763	71,801,136.55	1,276,373.55	....
Capital……………………….………..	8,340,500	6,227,514.68	....	2,112,985.32
VAT………………………………..	7,927,237	6,567,031.50	....	1,360,205.50
MINISTRY OF URBAN DEVELOPMENT HOUSING AND ENVIRONMENT				
Operating…………………………..	2,888,200	2,828,646.39	....	59,553.61
Capital……………………………..	948,200	845,907.02	....	102,292.98
VAT………………………………..	173,400	162,153.01	....	11,246.99
DEPARTMENT OF SOCIAL WELFARE				
Operating…………………………..	6,265,550	6,196,902.18	....	68,647.82
Capital……………………………...	1,125,650	586,646.00	....	539,004.00
VAT………………………………..	152,800	151,392.46	....	1,407.54
FIJI INSTITUTE OF TECHNOLOGY				
Operating…………………………..	4,487,800	4,840,300.00	352,500.00	....
Capital……………………………...	1,410,000	1,057,500.00	....	352,500.00
VAT………………………………..	418,700	418,700.00	....	....

Operating Fund Account

ABSTRACT OF OPERATING AND CAPITAL EXPENDITURE FOR THE YEAR 1997

Heads of Expenditure	Revised Estimate	Expenditure	Increase	Decrease
	$	$	$	$
MINISTRY OF YOUTH, EMPLOYMENT OPPORTUNITIES AND SPORTS				
Operating…………………………..	4,179,300	4,110,853.07	....	68,446.93
Capital...	88,800	88,400.00	....	400.00
VAT………………………………..	330,100	296,635.27	....	33,464.73
Operating-Total ………………	242,520,382	243,585,036.63	1,628,873.55	564,218.92
Capital -Total ………………..	14,475,150	11,342,534.78	....	3,132,615.22
VAT-Total ……………………	20,425,168	18,926,481.74	....	1,498,686.26
Social Services-Total… ……..	277,420,700	273,854,053.15	1,628,873.55	5,195,520.40
Net Decrease…..........…..	....	....	....	3,566,646.85
ECONOMIC SERVICES				
MINISTRY OF AGRICULTURE, FISHERIES AND FORESTS				
Operating…………………………..	18,509,100	19,448,678.55	939,578.55	....
Capital……………………………..	20,887,600	18,144,286.24	....	2,743,313.76
VAT………………………………..	3,169,700	2,844,031.88	....	325,668.12
AGRICULTURAL TRIBUNAL				
Operating…………………………..	149,200	143,420.87	....	5,779.13
VAT………………………………..	14,900	10,523.09	....	4,376.91
DEPARTMENT OF FORESTS				
Operating…………………………..	5,166,100	5,044,410.28	....	121,689.72
Capital……………………………..	2,039,000	2,038,998.78	....	1.22
VAT………………………………..	589,500	410,435.32	....	179,064.68
MINISTRY OF LANDS, MINING AND ENERGY				
Operating…………………………..	20,678,900	18,683,227.75	....	1,995,672.25
Capital……………………………..	2,415,500	1,860,938.75	....	554,561.25
VAT………………………………..	2,225,700	1,912,648.91	....	313,051.09
MINISTRY OF COMMERCE, TRADE, INDUSTRY AND PUBLIC ENTERPRISES				
Operating…………………………..	4,439,000	4,119,150.60	....	319,849.40
Capital……………………………..	1,300,000	497,007.69	....	802,992.31
VAT………………………………..	510,400	181,584.09	....	328,815.91
DEPARTMENT OF CO-OPERATIVES				
Operating………………………….	1,595,500	1,595,384.40	....	115.60
VAT……………………………….	159,700	158,300.00	....	1,400.00
MINISTRY OF TOURISM AND CIVIL AVIATION				
Operating…………………………..	3,028,700	2,960,075.62	....	68,624.38

APPENDIX 7 (*continued*)

Operating Fund Account

ABSTRACT OF OPERATING AND CAPITAL EXPENDITURE
FOR THE YEAR 1997

Heads of Expenditure	Revised Estimate	Expenditure	Increase	Decrease
	$	$	$	$
Capital……………………………..	4,500,000	4,500,000.00	....	....
VAT………………………………..	137,100	111,794.10	....	25,305.90
DEPARTMENT OF ENERGY				
Operating..	422,200	359,674.67	....	62,525.33
Capital...	1,514,200	1,446,752.85	....	67,447.15
VAT...	93,600	93,600.00	....	....
Operating-Total.......................	53,988,700	52,354,022.74	939,578.55	2,574,255.81
Capital-Total...........................	32,656,300	28,487,984.31	....	4,168,315.69
VAT-Total..............................	6,900,600	5,722,917.39	....	1,177,682.61
Economic Services-Total..........	93,545,600	86,564,924.44	939,578.55	7,920,254.11
Net Decrease................	....	....	....	6,980,675.56
INFRASTRUCTURE DEPARTMENT OF CIVIL AVIATION				
Operating...	3,894,700	3,504,755.67	....	389,944.33
Capital...	985,400	800,000.00	....	185,400.00
VAT...	71,500	2,750.90	....	68,749.10
DEPARTMENT OF METEOROLOGICAL SERVICES				
Operating...	1,978,800	1,943,374.30	....	35,425.70
Capital...	98,400	96,712.82	....	1,687.18
VAT...	380,500	335,802.48	....	44,697.52
MINISTRY OF PUBLIC WORKS, INFRASTRUCTURE AND TRANSPORT				
Operating...	46,727,500	49,098,452.45	2,370,952.45	....
Capital...	56,708,000	58,592,698.00	1,884,698.00	....
VAT...	10,376,900	8,616,863.89	....	1,760,036.11
DEPARTMENT OF MARINE				
Operating...	7,138,000	6,859,740.22	....	278,259.78
Capital...	200,000	171,004.15	....	28,995.85
VAT...	726,200	606,834.77	....	119,365.23

Operating Fund Account

ABSTRACT OF OPERATING AND CAPITAL EXPENDITURE FOR THE YEAR 1997

Heads of Expenditure	Revised Estimate	Expenditure	Increase	Decrease
	$	$	$	$
DEPARTMENT OF ROAD TRANSPORT				
Operating..	2,263,000	2,248,501.30	....	14,498.70
Capital...	555,000	552,182.81	....	2,817.19
VAT...	313,000	311,975.38	....	1,024.62
Operating-Total........................	62,002,000	63,654,823.94	2,370,952.45	718,128.51
Capital-Total............................	58,546,800	60,212,597.78	1,884,698.00	218,900.22
VAT-Total................................	11,868,100	9,874,227.42	....	1,993,872.58
Infrastructure-Total................	132,416,900	133,741,649.14	4,255,650.45	2,930,901.31
Net Decrease..........................	....	....	1,324,749.14	....
UNALLOCABLE				
MISCELLANEOUS SERVICES				
Operating..	40,487,802	37,949,092.85	....	2,538,709.15
Capital...	153,864,118	150,028,783.73	....	3,835,334.28
VAT...	2,546,300	797,392.70	....	1,748,907.30
PENSIONS, GRATUITIES AND COMPASSIONATE ALLOWANCES				
Operating..	22,561,000	22,363,023.50	....	197,976.50
TRANSFERRED TO BORROWING FUND ACCOUNT				
CHARGES ON ACCOUNT OF PUBLIC DEBT				
Operating..	167,239,300	180,157,336.87	12,918,036.87	....
Operating-Total..................	230,288,102	240,469,453.22	12,918,036.87	2,736,685.65
Capital-Total.......................	153,864,118	150,028,783.73	....	3,835,334.27
VAT-Total..........................	2,546,300	797,392.70	....	1,748,907.30
Unallocable-Total...............	386,698,520	391,295,629.65	12,918,036.87	8,320,927.22
Net Increase	....	....	4,597,109.65	....
Operating-Total..................	758,424,318	770,301,018.15	22,174,030.93	10,297,330.78
Capital-Total.......................	273,378,069	262,314,207.06	2,449,190.20	13,513,052.14
VAT-Total..........................	56,854,933	49,395,452.74	240,986.24	7,700,466.50
Grand-Total	1,088,657,320	1,082,010,677.95	24,864,207.37	31,510,849.42
Net Decrease....................	....	....	....	6,646,642.05

Operating Fund Account

ABSTRACT OF OPERATING AND CAPITAL EXPENDITURE FOR THE YEAR 1997

Heads of Expenditure	Revised Estimate	Expenditure	Increase	Decrease
1. Established Staff..........................	310,404,326	312,770,025.52	2,365,699.52	....
2. Unestablished Staff.......................	41,867,907	42,121,657.61	253,750.61	....
3. Travel and Communications	13,331,465	14,455,054.71	1,123,589.71	....
4. Maintenance and Operations........	23,764,777	24,947,381.57	1,182,604.57	....
5. Purchase of Goods and Services...	60,592,793	60,157,179.51	....	435,613.49
6. Operating Grants and Transfers....	94,777,331	92,732,852.21	....	2,044,478.79
7. Special Expenditures	23,885,419	20,596,506.65	....	3,288,912.35
8. Capital Construction.....................	79,230,040	77,975,043.70	....	1,254,996.30
9. Capital Purchase	11,992,203	9,467,641.87	....	2,524,561.13
10. Capital Grants and Transfers	182,155,826	174,871,521.49	....	7,284,304.51
11. Pensions, Gratuities and Compassionate Allowances	22,561,000	22,363,023.50	....	197,976.50
12. Charges on Account of Public Debt..	167,239,300	180,157,336.87	12,918,036.87	....
13. Value Added Tax.........................	56,854,933	49,395,452.74	....	7,459,480.26
Total	1,088,657,320	1,082,010,677.95	17,843,681.28	24,490,323.33
Net Decrease............................	....	....	....	6,646,642.05

Ministry of
Finance

Ontario

1992-1993

Public Accounts of Ontario

Financial Statements

Statement of Revenue

Province of Ontario

For the year ended March 31, 1993 ($millions)	Budget 1993	**Actual 1993**	Actual 1992
Taxation			
Personal Income Tax	13,880	**13,543**	13,712
Retail Sales Tax	7,865	**7,316**	7,487
Corporations Tax	3,270	**2,713**	3,184
Employer Health Tax	2,745	**2,592**	2,648
Gasoline Tax	1,850	**1,834**	1,618
Tobacco Tax	985	**969**	1,028
Fuel Tax	450	**439**	379
Land Transfer Tax	445	**356**	415
Commercial Concentration Tax	113	**111**	111
Race Tracks Tax	98	**82**	82
Other Taxation	65	**86**	74
	31,766	**30,041**	30,738
Other			
Vehicle Registration Fees	675	**665**	652
Liquor Control Board Of Ontario Profits	685	**615**	675
Other Fees And Licenses	630	**584**	513
Ontario Lottery Corporation Revenues	470	**538**	455
Sales And Rentals (note 2)	1,202	**512**	94
Liquor Licensing Board Of Ontario Revenues	650	**511**	483
Royalties	210	**191**	191
Utility Service Charges	160	**167**	160
Fines And Penalties	155	**152**	142
Miscellaneous	212	**277**	326
	5,049	**4,212**	3,691
Government of Canada			
Established Programs Financing	3,692	**4,316**	3,542
Canada Assistance Plan	2,250	**2,283**	2,159
Fiscal Stabilization	1,190	**300**	-
National Training Act	105	**104**	113
Vocational Rehabilitation	63	**75**	50
Bilungualism Development	72	**70**	72
Young Offenders Act	60	**60**	63
Other	361	**346**	343
	7,730	**7,554**	6,324
Total Revenue	44,545	**41,807**	40,753

See accompanying Notes to the Financial Statements.

Statement of Expenditure

Province of Ontario

For the year ended March 31, 1993 ($millions)	Budget 1993	**Actual** **1993**	Actual 1992
Ministry			
Agriculture and Food	573	**573**	612
Attorney General	745	**752**	693
Board of Internal Economy	148	**133**	140
Citizenship	64	**67**	62
Colleges and Universities	3,277	**3,396**	3,296
Community and Social Services	9,548	**9,413**	8,314
Consumer and Commercial Relations	179	**173**	175
Correctional Services	579	**583**	591
Culture and Communications	311	**335**	328
Education	6,124	**6,197**	6,414
Energy	54	**48**	57
Environment	629	**620**	659
Executive Offices	16	**14**	14
Financial Institutions	63	**56**	63
Government Services	728	**681**	779
Health	17,186	**16,973**	16,834
Housing	1,005	**999**	848
Industry, Trade and Technology	352	**282**	199
Technology Fund	81	**80**	82
Intergovernmental Affairs	8	**9**	7
Labour	274	**262**	236
Management Board	100	**72**	65
Municipal Affairs	1,082	**1,077**	1,077
Ontario Native Affairs Secretariat	42	**33**	31
Natural Resources	651	**658**	710
Northern Development And Mines	308	**341**	357
Office for Disability Issues	11	**9**	7
Office for The Greater Toronto Area	3	**2**	2
Office of Francophone Affairs	4	**4**	4
Office for Seniors' Issues	7	**6**	8
Office Responsible for Women's Issues	25	**24**	23
Revenue	749	**774**	894
Skills Development	394	**350**	252
Solicitor General	581	**593**	613
Tourism and Recreation	191	**192**	211
Transportation	2,564	**2,575**	2,738
Treasury and Economics	45	**46**	45
Economic Development Projects	26	**12**	47
Interest on Debt Issued for Provincial Purposes (note 3)	5,275	**5,293**	4,196
Jobs Ontario Capital Fund (note 4)	500	**-**	-
Expenditure Savings and Constraints (note 4)	(400)	**-**	-
Contingency Fund (note 4)	365	**-**	-
Total Expenditure (note 3)	54,467	**53,707**	51,683

See accompanying Notes to the Financial Statements.

Statement of Changes in Financial Position

Province of Ontario

For the year ended March 31, 1993 ($millions)	Budget 1993	**Actual 1993**	Actual 1992
Deficit for the year	9,922	**11,900**	10,930
Loans Receivable and Investments Activities			
Loans Receivable	23	**328**	(12)
Water Treatment and Waste Control Facilities	75	**(20)**	17
Cash used in loans and investments activities	98	**308**	5
Total Financing Requirements	10,020	**12,208**	10,935
Financing Activities, net			
Debt issued for Provincial Purposes			
Non-Public			
Canada Pension Plan	(536)	**164**	489
Teachers' Pensions	(506)	**(506)**	(44)
Public Service Pensions	(124)	**(62)**	(87)
Public			
Debentures and Notes	9,992	**14,866**	8,887
Treasury Bills	600	**1,031**	1,381
Other	(10)	**(10)**	(10)
	9,416	**15,483**	10,616
Province of Ontario Savings Office	210	**28**	145
Other Liabilities	44	**13**	65
Cash Provided by financing activities	9,670	**15,524**	10,826
Change in cash and temporary investments			
(Decreases) Increases	(350)	**3,316**	(109)
Cash and temporary investments at beginning of period		**2,498**	2,607
Cash and temporary investments at end of period		**5,814**	2,498

See accompanying Notes to the Financial Statements.

Statement of Financial Position

Province of Ontario

For the year ended March 31, 1993 ($millions)	**1993**	1992
Financial Assets		
Cash and Temporary Investments (note 5)	**5,814**	2,498
Loans receivable (note 6)	**1,015**	687
Investments in Water Treatment and Waste Control Facilities (at cost less recoveries) (note 7)	**510**	530
	7,339	3,715
Advances to Ontario Hydro, secured by Bonds (note 8)	**6,717**	6,933
Total Financial Assets	**14,056**	10,648
Accumulated Deficit	**61,268**	49,368
	75,324	60,016
Liabilities		
Debt Issued for Provincial Purposes (note 9)	**66,101**	50,618
Deposits with the Province of Ontario Savings Office (note 10)	**2,068**	2,040
Other Liabilities (note 11)	**438**	425
Total Liabilities for Provincial Purposes	**68,607**	53,083
Debt Incurred for Ontario Hydro (note 9)	**6,717**	6,933
	75,324	60,016
Contingent Liabilities (note 12)	**—**	—

See accompanying Notes to the Financial Statements.

The accompanying March 31, 1993 financial statements of the Province of Ontario's Consolidated Revenue Fund, including the notes are the responsibility of the Office of the Controller and have been prepared in accordance with the accounting policies as described in the Summary of Significant Accounting policies. In the opinion of the Office of the Controller, these financial statements have been properly prepared, include all material items, and contain all information available up to July 23, 1993.

ELEANOR CLITHEROE, Deputy Minister of Finance

JIM EVANS, Controller

Notes to the Financial Statements (all tables in millions of dollars)

1. Statement of Significant Accounting Policies

Reporting entity
The financial statements, prepared using the concept of a Consolidated Revenue Fund, are designed to provide an accounting of the financial resources appropriated by the Ontario Legislature. The accounting policies and practices followed by the Province are designed to report the financial transactions of Government ministries as Consolidated Revenue Fund cash inflows and outflows. Activities of agencies of Government of Ontario are reported only to the extent to which their operations have been financed from, or have contributed to, the Consolidated Revenue Fund.

Basis of accounting[5]
The cash basis of accounting used by the province is modified to allow for an additional thirty days to pay for goods and services received during the fiscal year just ended and for certain non-cash transactions. Cash inflows, however, are closed at March 31 for cash received.

Capital costs are charged to expenditure when paid.

(Other Accounting Policies not reproduced here)

[13] This Province has since changed its basis of accounting. The latest financial statements of the Province may be viewed at http://www.gov.on.ca/fin/

Auditor's Report

To the Legislative Assembly of the
Province of Ontario

I have audited the statement of financial position of the Province of Ontario's Consolidated Revenue Fund as at March 31, 1993 and the statements of revenue, expenditure, accumulated deficit and changes in financial position for the year then ended. These financial statements are the responsibility of the Government. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with generally accepted accounting standards. Those standards require that I plan and perform an audit in order to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the Government, as well as evaluating the overall financial statement presentation.

As outlined in note 1 to the financial statements, the modified cash basis of accounting is used in the preparation of these financial statements. This basis of accounting permits the flow of expenditures to be managed in such a way that expenditure is not necessarily reflected in the period in which it has been incurred. Specifically, Government matching contributions of $584 million to the Teachers' Pension Plan and the Public service plan which pertained to and would normally be charged to expenditure in the March 31,1993 fiscal year, were deferred until April 1993. This was partially offset by employer special payments of $56 million to the Teachers' Pension Plan which, although due in the March 31, 1994 fiscal year, were charged to expenditure in the March 31,1993 fiscal year. If these transactions had been recorded in the year in which they were incurred, total expenditure and the deficit for the year ended March 31, 1993 would be increased by $528 million and the accumulated deficit would be increased by $528 million.

In my opinion, except for the failure to record expenditure in the year in which it has been incurred as described in the preceding paragraph, these financial statements present fairly, in all material respects, the financial position of the Province's Consolidated Revenue Fund as at March 31, 1993 and the results of its operations and changes in its financial position for the year then ended in accordance with the accounting policies stated in note 1 to the financial statements.

According to note 1, these financial statements have been designed to provide an accounting of the financial resources appropriated by the Ontario Legislature by reporting the financial transactions of Government ministries as Consolidated Revenue Fund cash inflows and outflows. However, the financial statements are not summary financial statements that would more fully report on the nature and extent of the financial affairs and operations of the Government of Ontario.

Therefore, during the 1993/94 fiscal year, I will strongly urge the Government to base these financial statements on the recommendations of the Public Sector Accounting and Auditing Board of the Canadian Institute of Chartered Accountants, since my audit of and opinion on the March 31, 1994 statements will be based on those recommendations. This Board has issued statements that recommend standards for good practice in financial reporting and accounting by Canadian governments. The recommendations that would have the most significant impact to provide a clearer and fuller understanding of the financial position and the results of operations of the Government are:

- reflecting revenues and expenditures on an accrual basis of accounting, including the value of pension benefits earned by employees, in order to reflect revenues and expenditures in the determination of the surplus or deficit for the period in which they are considered to have been earned and incurred, respectively, whether or not such transactions have been settled by the receipt or payment of cash or its equivalent; and
- the inclusion of all organizations owned or controlled by the Government, in order to provide an accounting for the full nature and extent of the financial affairs and resources for which the Government is responsible.

Toronto, Ontario	Erik Peters, C.A.
July 23, 1993	Provincial Auditor

FINANCIAL STATEMENTS OF THE SPANISH TAX AGENCY

For the year ended December 31, 1997

Content

- Administration Proceedings
- Balance Sheet
- Statement of Financial Performance
- Budget Settlement:
  – Settlement of the expenditure budget (Parts 1 & 2)
  – Settlement of the revenues budget (Parts 1 & 2)
  – Budgetary Result

ADMINISTRATION PROCEEDINGS:

All the transactions registered all through 1997 in the accounting system of the ***AGENCIA ESTATAL DE LA ADMINISTRACIÓN TRIBUTARIA*** (the Spanish Tax Agency) have been fairly reflected in the accounts for the year ended December 31, 1997.

Madrid, April 29, 1998

Financial Management Deputy   Personnel and Administration Director

D. Juan Costa Climent, Chairman of the ***AGENCIA ESTATAL DE ADMINISTRACIÓN TRIBUTARIA***, approves the annual accounts (a 217-page report) for the year ended December 31, 1997, in compliance with the corresponding legislation (*Instrucción de Contabilidad de la Administración Institucional del Estado aprobada por Orden del Ministerio de Economía y Hacienda de 1 de Febrero de 1996).*

Madrid, April 29, 1998

Chairman of the ***AGENCIA ESTATAL DE ADMINISTRACIÓN TRIBUTARIA***

AGENCIA ESTATAL DE ADMINISTRACIÓN TRIBUTARIA

BALANCE SHEET

for the year ended December 31, 1997

ASSETS				LIABILITIES			
Account No		**1997**	**1996**	**Account No**		**1997**	**1996**
	A) FIXED ASSETS	**99,738,624,000**	**96,361,671,777**		**A) EQUITY**	**106,321,754,157**	**102,932,868,283**
	II. Intangible Fixed Assets	***354,143,578***	***439,752,488***		***I. Net worth***	***98,363,113,398***	***98,367,669,898***
215	3. Software	1,562,506,455	1,185,544,665	100	1. Net worth	21,749,525,297	21,749,525,297
217	5. Rights on leased goods	0	248,286,350	101	2. Assigned property	76,559,993,101	21,749,525,297
(281)	7. Depreciation	-1,208,362,877	-994,078,527	103	3. Granted property	53,595,000	76,564,549,601
	III. Tangible Fixed Assets	***99,384,480,422***	***95,921,919,289***		***III. Results of previous years***	***4,565,198,385***	***53,595,000***
220, 221	1. Land and buildings	91,641,073,573	89,336,252,338	120	1. Profit from previous years	4,565,198,385	0
222, 223	2. Machinery and equipment	1,734,852,981	1,541,478,002	129	***IV. Results for the year***	***3,393,442,374***	
224, 226	3. Furniture and tools	5,659,687,230	4,491,825,051		**C) LONG-TERM LIABILITIES**	**0**	**4,565,198,385**
227, 228, 229	5. Other tangible fixed assets	23,236,366,347	19,366,719,840		***II. Other long-term debt***	***0***	***152,076,661***
(282)	6. Depreciation	-22,887,499,709	-18,814,355,942	173	2. Other long-term debt	0	152,076,661
27	**B) DEFERRED EXPENSES**	**0**	**21,809,440**		**D) SHORT-TERM LIABILITIES**	**14,261,556,942**	**13,140,136,865**
	C) CURRENT ASSETS	**20,844,687,099**	**19,841,600,592**		***III. Current liabilities***	***14,261,556,942***	***13,140,136,865***
	II. Debtors	***15,632,874,750***	***17,826,271,989***	40	1. On-budget debt	10,608,355,625	9,466,541,992
43	1. On-budget receivables	15,575,023,326	17,676,619,394	41	2. Off-budget debt	501,209,892	529,223,119
44	2. Off-budget receivables	69,452,353	82,394,279	475, 476, 477	4. Public Institutions	3,151,054,314	3,127,634,170
470, 472	4. Public Institutions	153,927,969	227,642,701	523, 554	5. Other liabilities	937,111	16,737,584
(555)	5. Other receivables	-165,528,898	-160,384,385				
	III. Short -term Investments	***33,026,376***	***51,579,523***				
544	2. Other investments and temporary lending	25,016,548	25,530,529				
565	3. Short-term garantee deposits received	8,009,828	26,048,994				
57	***IV. Cash and banks***	***5,178,785,973***	***1,963,749,080***				
	TOTAL ASSETS (A+B+C)	**120,583,311,099**	**116,225,081,809**		**TOTAL NET WORTH AND LIABILITIES (A+C+D)**	**120,583,311,099**	**116,225,081,809**

AGENCIA ESTATAL DE ADMINISTRACIÓN TRIBUTARIA

STATEMENT OF FINANCIAL PERFORMANCE

for the year ended December 31, 1997

EXPENSES				REVENUES			
Account No.		**1997**	**1996**	**Account No.**		**1997**	**1996**
	A) TOTAL EXPENDITURE	**122,761,575,980**	**119,088,444,272**		B) TOTAL REVENUE	**126,155,018,354**	**123,653,642,657**
	1. Operating expenses	***122,638,292,620***	***118,685,907,701***		***1. Ordinary revenues***	***19,461,967***	***4,042,100***
	a) Personnel expenses	89,545,348,003	87,250,104,715		*a) Taxes*	19,461,967	4,042,100
640,641	a.1) Wages and salaries	84,556,146,197	82,177,741,066	740	a.15) Tax on services provided	19,461,967	4,042,100
642,644	a.2) Social Security expenses	4,989,201,806	5,072,363,649		***2. Other ordinary revenues***	***4,500,682,292***	***4,247,240,379***
645	*b)Other welfare expenses*	95,936,039	101,241,846	773	*a) Reimbursements*	29,499,230	10,172,209
68	*c) Fixed assets depreciation*	4,286,367,991	3,964,387,055		*c) Other ordinary revenues*	4,212,867,249	3,952,825,609
	e) Other operating expenses	28,709,527,433	27,355,578,349	775,776,777	c.1) Other ordinary revenues	4,212,867,249	3,952,825,609
62	e.1) Outside services	28,442,591,511	26,957,497,184	761	*e) Revenues from marketable securities and loans*	0	29,659,615
63	e.2) Tax	266,869,942	385,810,288		*f) Interests and similar revenues*	258,315,813	254,582,946
676	e.3) Other operating expenses	65,980	12,270,877	769	f.1) Other interests	258,315,813	254,582,946
	f) Financial expenses	1,113,154	14,595,736		***3. Grants and transfers***	***121,478,653,113***	***119,350,183,706***
662,669	f.1) Financial expenses from debt	1,113,154	14,595,736	750	*a) Current transfers*	117,155,883,113	118,306,241,070
	2. Grants and transfers	***49,705,851***	***68,331,251***	*755*	*c) Capital transfers*	*4,322,770,000*	*1,043,942,636*
650	*a) Current transfers*	49,705,851	68,331,251		***4. Extraordinary gains and revenues***	***156,220,982***	***52,176,472***
	3. Extraordinary losses and expenses	***73,577,509***	***334,205,320***	*771*	*a) Gains from fixed assets*	*2,729,921*	*20,537,524*
671	*a) Losses from fixed assets*	2,092,789	67,718,579	778	*c) Extraordinary revenues*	108,571,607	9,958,778
678	*b) Extraordinary expenses*	316,087	225,032	779	*d) Gains and revenues of previous years*	44,919,454	21,680,170
679	*c) Losses and expenses of previous years*	71,168,633	266,261,709				
	SURPLUS FOR THE YEAR (B-A)	**3,393,442,374**	**4,565,198,385**				

AGENCIA ESTATAL DE ADMINISTRACIÓN TRIBUTARIA

1997 Budget Settlement

C.1.1). Settlement of the expenditure budget (Part 1)
ORGANIC CLASSIFICATION : 15.302
FUNCTIONAL CLASSIFICATION, PROGRAM EXPENDITURE: 613-G NATIONAL TAX SYSTEM APLICATION
800-X TRANSFERS AMONG SUBSECTORS

ECONOMIC CLASSIFIC.		BUDGETARY APPROPIATION			ENGAGED EXPENDITURE	NET OBLIGATIONS RECOGNISED	NON-DISPOSED APPROPIATION
		INITIAL	CHANGES	FINAL			
1	Personnel expenses	85,602,000,000	6,068,133,204	91,670,133,204	89,607,956,869	89,603,002,702	2,067,130,502
2	Operating expenditure on goods and services	19,998,650,000	10,672,317,792	30,670,967,792	29,105,981,184	28,772,329,350	1,898,638,442
3	Financial expenses	18,394,000	3,500,000	21,894,000	1,227,981	1,227,981	20,666,019
4	Current transfers	53,178,000	1,650,000	54,828,000	49,705,851	49,705,851	5,122,149
	CURRENT TRANSACTIONS TOTAL	**105,672,222,000**	**16,745,600,996**	**122,417,822,996**	**118,764,871,885**	**118,426,265,884**	**3,991,557,112**
6	Fixed assets	4,324,620,000	7,488,346,645	11,812,966,645	9,452,683,680	7,844,497,499	3,968,469,146
	CAPITAL TRANSACTIONS TOTAL	**4,324,620,000**	**7,488,346,645**	**11,812,966,645**	**9,452,683,680**	**7,844,497,499**	**3,968,469,146**
	NON-FINANCIAL OPERATIONS TOTAL	**109,996,842,000**	**24,233,947,641**	**134,230,789,641**	**128,217,555,565**	**126,270,763,383**	**7,960,026,258**
8	Variation in financial assets	43,000,000		43,000,000	41,987,717	41,987,717	1,012,283
	FINANCIAL OPERATIONS TOTAL	**43,000,000**		**43,000,000**	**41,987,717**	**41,987,717**	**1,012,283**
	TOTAL	**110,039,842,000**	**24,233,947,641**	**134,273,789,641**	**128,259,543,282**	**126,312,751,100**	**7,961,038,541**

AGENCIA ESTAL DE ADMNISTRACIÓN TRIBUTARIA

1997 Budget Settlement

C.1.2). Settlement of the expenditure budget (Part 2)

ORGANIC CLASSIFICATIONS: 15.302

FUNCTIONAL CLASSIFICATION PROGRAM EXPENDITURE: 613-G NATIONAL TAX SYSTEM APLICATION
800-X TRANSFERS AMONG SUBSECTORS

ECONOMIC CLASSIF.		NET OBLIGATIONS RECOGNISED AS OF DECEMBER,31	NET OBLIGATIONS RECOGNISED DURING THE FOLLOWING JANUARY	TOTAL OF NET OBLIGATIONS RECOGNISED	PAID (all through the year)	OBLIGATIONS DUE FOR PAYMENT AT YEAR END
1	Personnel expenses	89,603,002,702		89,603,002,702	89,584,952,172	18,050,530
2	Operating expenditure on goods and services	28,772,329,350		28,772,329,350	23,145,492,297	5,626,837,053
3	Financial expenses	1,227,981		1,227,981	1,227,981	
4	Current transfers	49,705,851		49,705,851	48,308,719	1,397,132
	CURRENT TRANSACTIONS TOTAL	**118,426,265,884**		**118,426,265,884**	**112,779,981,169**	**5,646,284,715**
6	Fixed assets	7,844,497,499		7,844,497,499	3,085,409,727	4,759,087,772
	CAPITAL TRANSACTIONS TOTAL	**7,844,497,499**		**7,844,497,499**	**3,085,409,727**	**4,759,087,772**
	NON-FINANCIAL OPERATIONS TOTAL	**126,270,763,383**		**126,270,763,383**	**115,865,390,896**	**10,405,372,487**
8	Variation in financial assets	41,987,717		41,987,717	41,987,717	
	FINANCIAL OPERATIONS TOTAL	**41,987,717**		**41,987,717**	**41,987,717**	
	TOTAL	**126,312,751,100**		**126,312,751,100**	**115,907,378,613**	**10,405,372,487**

AGENCIA ESTATAL DE ADMINISTRACIÓN TRIBUTARIA

1997 Budget Settlement

C.2).Settlement of the revenues budget (Part 1)

ECONOMIC CLASSIFICATION		BUDGETARY REVENUE ESTIMATION		
		INITIAL	CHANGES	FINAL
3	Rates and other income	6,587,805,000	0	6,587,805,000
4	Current transfers	92,860,767,000	24,233,947,641	117,094,714,641
5	Property revenue	225,000,000	0	225,000,000
	CURRENT TRANSACTIONS TOTAL	**99,673,572,000**	**24,233,947,641**	**123,907,519,641**
6	Sale of physical assets	0	0	0
7	Capital transfers	4,324,620,000	0	4,324,620,000
	CAPITAL TRANSACTIONS TOTAL	**4,324,620,000**	**0**	4,324,620,000
	NON-FINANCIAL OPERATIONS TOTAL	**103,998,192,000**	**24,233,947,641**	**128,232,139,641**
8	Variation in financial assets	6,041,650,000	0	6,041,650,000
	FINANCIAL OPERATIONS TOTAL	**6,041,650,000**	**0**	**6,041,650,000**
	TOTAL	**110,039,842,000**	**24,233,947,641**	**134,273,789,641**

AGENCIA ESTATAL DE ADMINISTRACIÓN TRIBUTARIA

1997 Budget Settlement

C.2).Settlement of the revenues budget (Part 2)

ECONOMIC CLASSIFICATION		NET RECEIVABLES RECOGNISED	NET COLLECTION	CANCELLED RECEIVABLES	RECEIVABLES DUE FOR COLLECTION AT YEAR END
3	Rates and other income	4,260,136,636	4,252,455,482	0	7,681,154
4	Current transfers	117,155,883,113	102,711,701,273	0	14,444,181,840
5	Property revenue	260007623	221654115	0	38,353,508
	CURRENT TRANSACTIONS TOTAL	**121,676,027,372**	**107,185,810,870**	**0**	**14,490,216,502**
6	Sale of physical assets	2,712,365	2,712,365	0	0
7	Capital transfers	4,322,770,000	3,241,615,000	0	1,081,155,000
	CAPITAL TRANSACTIONS TOTAL	**4,325,482,365**	**3,244,327,365**	**0**	**1,081,155,000**
	NON-FINANCIAL OPERATIONS TOTAL	**126,001,509,737**	**110,430,138,235**	**0**	**15,571,371,502**
8	Variation in financial assets	60,887,698	60,887,698	0	0
	FINANCIAL OPERATIONS TOTAL	**60,887,698**	**60,887,698**	**0**	**0**
	TOTAL	**126,062,397,435**	**110,491,025,933**	**0**	**15,571,371,502**

AGENCIA ESTATAL DE ADMINISTRACIÓN TRIBUTARIA

for the year ended December 31,1997

BUDGET SETTLEMENT

C.4). BUDGETARY RESULT

	NET RECEIVABLES RECOGNISED	NET OBLIGATIONS RECOGNISED	BALANCES
1. (+) Non-financial operations	126,001,509,737	126,270,763,383	-269,253,646
2. (+) Financial operations	60,887,698	41,987,717	18,899,981
3. (+) Commercial operations (*)			
I. BUDGETARY RESULT OF THE YEAR (1+2+3)	**126,062,397,435**	**126,312,751,100**	**-250,353,665**
II. NET VARIATION OF FINANCIAL LIABILITIES			
III. BUDGET BALANCE OF THE YEAR (I+II)			**-250,353,665**

*** Applicable only to industrial and commercial entities**

FINANCIAL STATEMENTS

OF THE GOVERNMENT OF NEW ZEALAND

For the year ended 30 June 1999

REPORT OF THE AUDIT OFFICE

To the Readers of the Financial Statements of the Government of New Zealand for the Year Ended 30 June 1999

We have audited the financial statements on pages 26 to 100. The financial statements provide information about the past financial performance of the Government of New Zealand (the Government) and its financial position as at 30 June 1999. This information is stated in accordance with the accounting policies as set out on pages 57 to 64.

Responsibilities of the Government

Section 29 of the Public Finance Act 1989 places a responsibility on the Treasurer and the Minister of Finance to ensure that the financial statements fairly reflect the performance and position of the Government. Section 27 of the Public Finance Act 1989 requires the Treasury to prepare, in accordance with generally accepted accounting practice, annual financial statements which fairly reflect the financial position of the Government as at 30 June 1999 and the results of its operations and cash flows for the year ended 30 June 1999.

Auditor's responsibilities

Section 30 of the Public Finance Act 1989 requires the Audit Office to audit the annual financial statements presented by the Government. It is the responsibility of the Audit Office to express an independent opinion on the financial statements.

Basis of opinion

An audit includes examining, on a test basis, evidence relevant to the amounts and disclosures in the financial statements. It also includes assessing:

- the significant estimates and judgements made in the preparation of the financial statements; and
- whether the accounting policies are appropriate to the circumstances of the Government, consistently applied and adequately disclosed.

We conducted our audit in accordance with generally accepted auditing standards, including the Auditing Standards issued by the Institute of Chartered Accountants of New Zealand. We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material mis-statements, whether caused by fraud or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Unqualified opinion

We have obtained all the information and explanations we have required.

In our opinion the financial statements of the Government of New Zealand on pages 26 to 100:

- comply with generally accepted accounting practice; and
- fairly reflect:
  - the results of its operations and cash flows for the year ended 30 June 1999; and
  - the financial position as at 30 June 1999.

Our audit was completed on 10 September 1999 and our unqualified opinion is expressed as at that date.

D J D Macdonald
Controller and Auditor-General
Wellington
New Zealand

Statement of Responsibility

These Financial Statements have been prepared by the Treasury in accordance with the provisions of the Public Finance Act 1989. The Financial Statements comply with generally accepted accounting practice.

The Treasury is responsible for establishing and maintaining a system of internal control designed to provide reasonable assurance that the transactions recorded are within statutory authority and properly record the use of all public financial resources by the Crown. To the best of my knowledge, this system of internal control has operated adequately throughout the reporting period.

Dr A E Bollard
Secretary to the Treasury
10 September 1999

We accept responsibility for the integrity of these Financial Statements, the information they contain and their compliance with the Public Finance Act 1989.
In our opinion, these Financial Statements fairly reflect the financial position of the Crown as at 30 June 1999 and its operations for the year ended on that date.

Hon Bill English
Treasurer
10 September 1999

Rt Hon Sir William Birch
Minister of Finance
10 September 1999

Ministerial Statement

These financial statements show a strong result in a year marked internationally by a weak economic environment and domestically affected by two quarters of recession. A $1.8 billion surplus was posted, and net debt fell by $2.4 billion.

The 1998/99 fiscal surplus contains a number of one-offs, most significantly the gains on the sale of Contact Energy Limited, and the negative impact of the Government Superannuation Fund unfunded liability revaluation. At one level the small underlying surplus of around $150 million is evidence that the Asian crisis put the Crown finances to the test but it also reiterates two key lessons.

- New Zealand's fortunes are inextricably linked to the world market place. The Asian downturn in 1998/99 cost us exports and a large amount of tax revenue.

  It is a reminder that the Government must continually focus on policies that allow New Zealand enterprises to compete internationally.

- The importance of a transparent and disciplined medium term fiscal strategy of running surpluses and reducing debt. While investing significantly in health and education, we have budgeted prudently for over 8 years now through carefully targeted spending. It was this discipline that has laid the platform for tax cuts, the latest round putting around $1.2 billion back in taxpayers pockets in 1998/99.

Last December, a year-end deficit of $52 million was forecast, reflecting an underlying deficit of around $250 million. Instead, we have emerged from the worst shock in 20 years with a robust fiscal position. More importantly, we were able to achieve this without compromising the level of service New Zealanders expect of their Government.

Hon Bill English
Treasurer

10 September 1999

Rt Hon Sir William Birch
Minister of Finance

10 September 1999

Statement of Financial Performance
for the year ended 30 June 1999

Forecast 1998 Budget $m	Forecast Estimated Actual $m		Note	Actual 30 June 1999 $m	Actual 30 June 1998 $m
		Revenue			
		Levied through the Crown's Sovereign Power			
21,603	20,490	Direct taxation	1	20,289	21,260
12,095	11,866	Indirect taxation	2	11,867	11,722
33,698	32,356	Total taxation revenue		32,156	32,982
263	270	Compulsory fees, fines, penalties and levies		300	258
33,961	**32,626**	**Total Revenue Levied through the Crown's Sovereign Power**		**32,456**	**33,240**
		Earned through the Crown's Operations			
1,243	2,778	Investment income	3	2,901	1,154
673	657	Sales of goods and services		683	689
380	413	Other operational revenue	4	401	420
-	(12)	Unrealised gains/ (losses) arising from revaluations of commercial forests		(84)	78
2,296	**3,836**	**Total Revenue Earned through the Crown's Operations**		**3,901**	**2,341**
36,257	**36,462**	**Total Revenue**		**36,357**	**35,581**
		Expenses	5		
		By functional classification			
12,939	12,894	Social security and welfare		12,906	12,509
738	473	GSF pension expenses		1,132	494
6,444	6,577	Health		6,573	6,001
5,953	5,910	Education		5,899	5,714
1,624	1,714	Core government services		1,705	1,562
1,395	1,527	Law and order		1,499	1,345
1,115	1,031	Defence		1,030	1,065
933	1,018	Transport and communications		1,029	948
876	898	Economic and industrial services		858	840
329	342	Primary services		334	423
327	328	Heritage, culture and recreation		316	297
51	45	Housing and community development		41	29
154	30	Other		34	167
2,564	2,520	Finance costs	5	2,516	2,804
-	(51)	Net foreign-exchange (gains)/ losses		(47)	13
290	-	Provision for future initiatives		-	-
100	-	Contingency expense provision		-	-
35,832	**35,256**	**Total Expenses**		**35,825**	**34,211**
425	**1,206**	**Revenue less Expenses**		**532**	**1,370**
880	958	Net surplus, less distributions, attributable to State-owned enterprises and Crown entities	9	1,245	1,164
1,305	**2,164**	**Operating Balance**		**1,777**	**2,534**

The accompanying Notes are an integral part of these Statements.

Statement of Financial Position
as at 30 June 1999

Forecast 1998 Budget $m	Estimated Actual $m		Note	*Actual* 30 June 1999 $m	30 June 1998 $m
		Assets			
53	135	Cash and bank balances		230	171
8,193	9,773	Marketable securities and deposits	6	11,153	10,285
4,042	3,779	Advances	7	3,628	3,367
5,135	5,045	Receivables	8	5,250	5,040
306	314	Inventories		321	302
20,540	12,049	State-owned enterprises and Crown entities	9	12,917	19,022
256	187	Other investments	10	270	261
15,478	15,453	Physical assets	11	15,258	14,962
481	500	Commercial forests	12	422	573
8,490	8,436	State highways	13	8,770	8,359
2	3	Intangible assets		4	14
62,976	**55,674**	**Total Assets**		**58,223**	**62,356**
		Liabilities			
4,426	4,261	Payables and provisions	14	5,005	4,639
1,826	2,023	Currency issued		1,960	1,809
36,860	36,056	Borrowings		36,712	37,892
8,144	7,878	Pension liabilities	15	8,524	8,095
51,256	**50,218**	**Total Liabilities**		**52,201**	**52,435**
11,720	**5,456**	**Total Assets less Total Liabilities**		**6,022**	**9,921**
		Crown Balance	16		
4,650	(1,595)	Accumulated operating balance		(1,197)	3,132
7,070	7,051	Revaluation reserve		7,219	6,789
11,720	**5,456**	**Crown Balance**		**6,022**	**9,921**

The accompanying Notes are an integral part of these Statements.

Statement of Movements in Equity[6]

for the year ended 30 June 1999

Forecast 1998 Budget $m	Forecast Estimated Actual $m		Note	Actual 30 June 1999 $m	Actual 30 June 1998 $m
10,415	**9,921**	**Opening Crown Balance**		**9,921**	**7,470**
1,305	2,164	Operating balance for the period		1,777	2,534
-	270	Net revaluations		466	(83)
1,305	**2,434**	**Total Recognised Revenues and Expenses**		**2,243**	**2,451**
-	(6,899)	Accident Rehabilitation and Compensation Insurance Corporation recognition policy change	9	(6,142)	-
11,720	**5,456**	**Closing Crown Balance**	**16**	**6,022**	**9,921**

The accompanying Notes are an integral part of these Statements.

[6] For further discussion of the accounting policy change illustrated in this statement, readers are referred to Chapter 13 Accrual Basis – Liabilities, or a full copy of the financial statements at http:/www.gov.nz.

Forecast 1998 Budget $m	Estimated Actual $m		*Actual* 30 June 1999 $m	30 June 1998 $m
		Cash Flows from Operations		
		Cash was Provided From		
		Direct Taxation		
		Individuals		
12,571	12,325	Source deductions	12,328	12,739
3,639	3,548	Other persons	3,566	3,721
(1,025)	(1,104)	Refunds	(1,189)	(1,078)
344	334	Fringe benefit tax	329	341
15,529	**15,103**	**Total Individuals**	**15,034**	**15,723**
		Companies		
4,805	4,500	Gross companies	4,467	4,386
(485)	(592)	Refunds	(646)	(603)
4,320	**3,908**	**Total Companies**	**3,821**	**3,783**
1,688	1,627	Withholding taxes	1,654	1,863
1	2	Other direct taxation	2	2
21,538	**20,640**	**Total Direct Taxation**	**20,511**	**21,371**
		Indirect Taxation		
		Goods and Services Tax		
12,818	12,425	Gross goods and services tax	12,628	12,068
(4,497)	(4,250)	Refunds	(4,194)	(4,144)
8,321	**8,175**	**Total Goods and Services Tax**	**8,434**	**7,924**
1,980	1,930	Excise duties	1,864	1,919
1,766	1,614	Other indirect taxation	1,575	1,845
12,067	**11,719**	**Total Indirect Taxation**	**11,873**	**11,688**
33,605	**32,359**	**Total Taxation Receipts**	**32,384**	**33,059**
250	**245**	**Compulsory Fees, Fines, Penalties and Levies**	**251**	**242**
		Other Receipts		
1,091	954	Interest, profits and dividends	1,034	731
661	628	Sales of goods and services	642	676
374	416	Other operating receipts	372	383
2,126	**1,998**	**Total Other Receipts**	**2,048**	**1,790**
35,981	**34,602**	**Total Cash Provided from Operations**	**34,683**	**35,091**
		Cash was Disbursed To		
4,366	4,643	Departmental outputs	4,536	4,193
14,239	14,635	Other outputs	14,402	13,965
2,635	2,418	Finance costs	2,398	2,378
151	154	Subsidies	134	156
		Current transfers		
12,773	12,678	Social assistance grants	12,601	12,387
219	220	Other transfers	220	209
290	-	Provision for future initiatives	-	-
100	-	Contingency expenditure provision	-	-
34,773	**34,748**	**Total Cash Disbursed to Operations**	**34,291**	**33,288**
1,208	**(146)**	**Net Cash Flows from Operations**	**392**	**1,803**

The accompanying Notes are an integral part of these Statements.

Statement of Cash Flows *(continued)*
for the year ended 30 June 1999

Forecast 1998 Budget $m	Forecast Estimated Actual $m		Actual 30 June 1999 $m	Actual 30 June 1998 $m
1,208	**(146)**	**Subtotal (brought forward)**	**392**	**1,803**
		Cash Flows from Investing Activities		
		Cash was Provided From		
588	3,403	Net sale/ (purchase) of investments	1,554	(942)
171	219	Sale of physical assets	239	123
759	**3,622**	**Total Cash Provided**	**1,793**	**(819)**
		Cash was Disbursed To		
518	332	Net increase in advances	179	434
1,439	1,283	Purchase of physical assets	1,142	1,104
1,957	**1,615**	**Total Cash Disbursed**	**1,321**	**1,538**
(1,198)	**2,007**	**Net Cash Flows from Investing Activities**	**472**	**(2,357)**
10	**1,861**	**Net Cash Flows from Operating and Investing Activities**	**864**	**(554)**
		Cash Flows from Financing Activities		
		Cash was Provided From		
-	214	Issue of circulating currency	151	68
573	2,903	Issues of Government stock	4,756	2,332
-	-	Other New Zealand-dollar borrowing[1]	1,124	1,470
-	-	Borrowing in foreign currencies[1]	2,703	3,939
573	**3,117**	**Total Cash Provided**	**8,734**	**7,809**
		Cash was Disbursed To		
		Repayment of Government stock	1,882	2,541
333	3,280	Repayment of other New Zealand-dollar borrowing[1]	3,915	975
240	1,755	Repayment of foreign-currency borrowing[1]	3,763	3,812
573	**5,035**	**Total cash disbursed**	**9,560**	**7,328**
-	**(1,918)**	**Net Cash Flows from Financing Activities**	**(826)**	**481**
10	**(57)**	**Net Movement in Cash**	**38**	**(73)**
43	171	**Opening Cash Balance**	171	196
-	21	Foreign-exchange gains on opening cash	21	48
53	**135**	**Closing Cash Balance**	**230**	**171**

[1] Issues and repayments of other New Zealand-dollar borrowing and foreign-currency borrowing are forecast on a net basis. Actual issues and repayments are reported on a gross basis.

The accompanying Notes are an integral part of these Statements.

Forecast 1998 Budget $m	Estimated Actual $m		*Actual* 30 June 1999 $m	30 June 1998 $m
		Reconciliation Between the Operating Balance and Net Cash Flows from Operations		
1,305	**2,164**	**Operating Balance**	**1,777**	**2,534**
		Items included in the operating balance but not in net cash flows from operations		
		Valuation Changes		
-	12	Revaluation of commercial forests	84	(78)
-	(73)	Unrealised net foreign-exchange gains	(44)	(155)
-	**(61)**	**Total Valuation Changes**	**40**	**(233)**
		Physical Asset Movements		
820	779	Depreciation	765	737
-	(2)	Loss/(gain) on sale of physical assets	26	1
820	**777**	**Total Physical Asset Movements**	**791**	**738**
		Other Non-cash Items		
(880)	(958)	Net surplus, less distributions, attributable to State-owned enterprises and Crown entities	(1,245)	(1,164)
-	(1,625)	Gain on sale of Contact Energy Limited and Airport companies	(1,625)	-
48	(217)	Movement in pension liabilities	429	(233)
(36)	9	Other	5	56
(868)	**(2,791)**	**Total Other Non-cash Items**	**(2,436)**	**(1,341)**
-	**(50)**	**Total Other investing and financing items**	**69**	**(128)**
		Movements in Working Capital[1]		
(88)	(6)	Increase in taxes receivable	(135)	(10)
76	(58)	(Increase)/decrease in other receivables	(75)	14
(8)	(12)	Increase in inventories	(19)	(7)
(29)	(109)	Increase/(decrease) in payables	380	236
(49)	**(185)**	**Total Movements in Working Capital**	**151**	**233**
1,208	**(146)**	**Net Cash Flows from Operations**	**392**	**1,803**

[1] Only movements in working capital resulting from operations are included.

The accompanying Notes are an integral part of these Statements.

Statement of Cash Flows *(continued)*
for the year ended 30 June 1999

Forecast 1998 Budget $m	*Forecast* Estimated Actual $m		*Actual* 30 June 1999 $m	*Actual* 30 June 1998 $m
		Reconcilation of Net Cash Flows from Operations with Net Cash Proceeds from Domestic Bonds		
1,208	**(146)**	**Net Cash Flows from Operations**	**392**	**1,803**
		Investing Flows		
		Net advances		
2	210	Housing Corporation of New Zealand	212	(75)
11	11	Contact Energy Limited	11	177
(507)	(534)	Student loans	(470)	(534)
(43)	(42)	Residual Health Management Unit	43	(23)
19	23	Other	25	21
(518)	**(332)**	**Total Net Advances**	**(179)**	**(434)**
		Net investments		
-	2,331	Contact Energy Limited	2,331	-
-	487	Auckland and Wellington Airport companies	487	-
-	-	Housing New Zealand Limited	-	300
819	759	Net (purchase)/sale of marketable securities and deposits	(1,184)	(1,038)
(210)	(75)	Hospital and health services	(45)	(163)
(21)	(99)	Other	(35)	(41)
588	**3,403**	**Total Net Investments**	**1,554**	**(942)**
		Physical assets		
(1,268)	(1,064)	Net purchase of physical assets	(903)	(981)
10	**1,861**	**Available to Repay Debt**	**864**	**(554)**
		Used in:		
(333)	(3,280)	Net (repayment)/issue of other New Zealand-dollar borrowing	(2,791)	495
(240)	(1,755)	Net (repayment)/issue of foreign-currency borrowing	(1,060)	127
(10)	57	(Increase)/decrease in cash	(38)	73
-	214	Issue of circulating currency	151	68
(583)	**(4,764)**		**(3,738)**	**763**
(573)	**(2,903)**	**Net (Cash Proceeds from)/Repayments of Domestic Bonds**	**(2,874)**	**209**

The accompanying Notes are an integral part of these Statements.

Forecast 1998 Budget $m	Forecast Estimated Actual $m		Actual 30 June 1999 $m	Actual 30 June 1998 $m
(573)	**(2,903)**	**Net (Cash Proceeds from)/Repayments of Domestic Bonds (brought forward)**	**(2,874)**	**209**
		Gross Cash Proceeds from Domestic Bonds		
2,392	3,463	Domestic bonds (market)	3,450	2,034
-	1,002	Domestic Bonds (non market)	977	-
289	320	Inflation bonds	329	298
2,681	**4,785**	**Total Gross Cash Proceeds from Domestic Bonds**	**4,756**	**2,332**
(2,108)	(1,782)	Repayment of domestic bonds (market)	(1,782)	(2,541)
-	(100)	Repayment of domestic bonds (non market)	(100)	-
573	**2,903**	**Net Cash Proceeds from/(Repayments of) Domestic Bonds**	**2,874**	**(209)**

The accompanying Notes are an integral part of these Statements.

Statement of Borrowings
Analysis at 30 June 1999 — Book Values

Forecast 1998 Budget $m	*Forecast* Estimated Actual $m		*Actual* 30 June 1999 $m	*Actual* 30 June 1998 $m
		Outstanding Debt		
		New Zealand-Dollar Debt		
20,736	22,743	Government stock	22,701	19,859
6,635	5,850	Treasury bills	5,881	8,008
277	275	Loans and foreign-exchange contracts	299	289
1,241	-	Reserve Bank bills	-	1,204
935	-	Earthquake Commission deposits	-	-
327	685	Retail stock	729	491
30,151	**29,553**	**Total New Zealand-Dollar Debt**	**29,610**	**29,851**
		Foreign-Currency Debt		
3,256	2,857	United States dollars	3,565	4,088
1,621	1,770	Japanese yen	1,706	1,852
1,832	1,876	European and other currencies	1,831	2,101
6,709	**6,503**	**Total Foreign-Currency Debt**	**7,102**	**8,041**
36,860	**36,056**	**Total Outstanding Debt**	**36,712**	**37,892**
		Less		
		Financial Assets		
		Marketable Securities and Deposits[1]		
376	2,403	New Zealand dollars	3,601	1,219
3,738	3,161	United States dollars	3,857	4,367
1,998	2,356	Japanese yen	1,827	2,238
2,081	1,853	European and other currencies	1,868	2,461
8,193	**9,773**	**Total Marketable Securities and Deposits**	**11,153**	**10,285**
		Advances and Cash		
885	385	Advances to State-owned enterprises and Crown entities	299	783
3,040	3,061	Student loans	3,002	2,470
117	333	Other advances	327	114
53	135	Cash	230	171
4,095	**3,914**	**Total Advances and Cash**	**3,858**	**3,538**
12,288	**13,687**	**Total Financial Assets**	**15,011**	**13,823**
24,572	**22,369**	**Net Crown Debt**	**21,701**	**24,069**
25,680	23,236	Net New Zealand-dollar debt	22,309	25,152
(1,108)	(867)	Net foreign-currency debt	(608)	(1,083)
24,572	**22,369**	**Net Crown Debt**	**21,701**	**24,069**

[1] As at 30 June 1999 foreign currency securities with a face value of $1,945 million (30 June 1998: $1,214 million) had been transferred to counterparties as security for borrowings.

The accompanying Notes are an integral part of these Statements.

	30 June 1999		30 June 1998	
	Nominal value $m	Current market value $m	Nominal value $m	Current market value $m
Outstanding Debt				
New Zealand-Dollar Debt				
Government stock	22,460	23,445	19,799	20,522
Treasury bills	5,980	5,879	8,184	7,807
Loans and foreign-exchange contracts	301	316	292	305
Reserve Bank bills	-	-	1,213	1,204
Retail stock	729	737	491	493
Total New Zealand-Dollar Debt	**29,470**	**30,377**	**29,979**	**30,331**
Foreign-Currency Debt				
United States dollars	3,706	3,739	4,244	4,345
Japanese yen	1,796	1,915	1,942	2,069
European and other currencies	1,852	1,865	2,111	2,130
Total Foreign-Currency Debt	**7,354**	**7,519**	**8,297**	**8,544**
Total Outstanding Debt	**36,824**	**37,896**	**38,276**	**38,875**
Marketable Securities and Deposits				
New Zealand dollars	3,601	3,601	1,220	1,218
United States dollars	3,787	3,851	4,106	4,361
Japanese yen	1,675	1,834	2,150	2,247
European and other currencies	1,814	1,870	2,252	2,461
Total Marketable Securities and Deposits	**10,877**	**11,156**	**9,728**	**10,287**

The current market value has been determined using the present value of cash flows discounted at a rate derived from a market yield curve.

The accompanying Notes are an integral part of these Statements.

Statement of Borrowings *(continued)*

Maturity Profiles as at 30 June 1999 — Book Values

	1999/00 $m	2000/01 $m	2001/02 $m	2002/03 $m	2003/04 $m	2004/05-2008/09 $m	2009/10 and after $m	Total book value $m
Outstanding Debt								
New Zealand-Dollar Debt								
Government stock	3,285	3,184	2,909	1,426	3,642	3,154	5,101	22,701
Treasury bills	5,881	-	-	-	-	-	-	5,881
Loans and foreign-exchange contracts	147	2	70	50	5	24	1	299
Reserve Bank bills	-	-	-	-	-	-	-	-
Retail stock	577	69	47	36	-	-	-	729
Total New Zealand-Dollar Debt	**9,890**	**3,255**	**3,026**	**1,512**	**3,647**	**3,178**	**5,102**	**29,610**
Foreign-Currency Debt								
United States dollars	1,849	188	-	78	565	558	327	3,565
Japanese yen	230	-	622	301	1	457	95	1,706
European and other currencies	973	621	-	-	-	228	9	1,831
Total Foreign-Currency Debt	**3,052**	**809**	**622**	**379**	**566**	**1,243**	**431**	**7,102**
Total Outstanding Debt	**12,942**	**4,064**	**3,648**	**1,891**	**4,213**	**4,421**	**5,533**	**36,712**
Marketable Securities and Deposits								
New Zealand dollars	3,601	-	-	-	-	-	-	3,601
United States dollars	2,744	100	151	67	(26)	777	44	3,857
Japanese yen	572	87	349	307	82	420	10	1,827
European and other currencies	1,109	505	95	20	(2)	36	105	1,868
Total Marketable Securities and Deposits	**8,026**	**692**	**595**	**394**	**54**	**1,233**	**159**	**11,153**

The maturities of marketable securities and deposits in this Statement are based on the contractual maturity dates.

The accompanying Notes are an integral part of these Statements.

	As at 1 July 1998 $m	Increases/ Additions $m	Decreases/ Disposals/ Repayments $m	Foreign Exchange Contracts $m	Currency Realignment $m	Unamortised premiums/ discounts $m	As at 30 June 1999 $m
Outstanding Debt							
By Type							
New Zealand-Dollar Debt							
Government stock	19,859	4,536	(1,882)	-	-	188	22,701
Treasury bills	8,008	-	(2,204)	-	-	77	5,881
Loans and foreign-exchange contracts	289	21	(11)	-	-	-	299
Reserve Bank bills	1,204	-	(1,204)	-	-	-	-
Retail stock	491	1,038	(800)	-	-	-	729
Total New Zealand-Dollar Debt	**29,851**	**5,595**	**(6,101)**	**-**	**-**	**265**	**29,610**
Foreign Currency-Debt							
United States dollars	4,088	118	(605)	(33)	(16)	13	3,565
Japanese yen	1,852	54	(441)	-	240	1	1,706
European and other currencies	2,101	228	(602)	43	56	5	1,831
Total Foreign-Currency Debt	**8,041**	**400**	**(1,648)**	**10**	**280**	**19**	**7,102**
Total Outstanding Debt	**37,892**	**5,995**	**(7,749)**	**10**	**280**	**284**	**36,712**
Less							
Financial Assets							
Marketable Securities and Deposits							
New Zealand dollars	1,219	2,006	(3)	379	-	-	3,601
United States dollars	4,367	64,483	(64,748)	(294)	109	(60)	3,857
Japanese yen	2,238	6,260	(7,143)	314	182	(24)	1,827
European and other currencies	2,461	2,474	(2,429)	(451)	(201)	14	1,868
Total Marketable Securities and Deposits	**10,285**	**75,223**	**(74,323)**	**(52)**	**90**	**(70)**	**11,153**
Advances and Cash	**3,538**	**1,605**	**(1,306)**	**-**	**21**	**-**	**3,858**
Total Financial Assets	**13,823**	**76,828**	**(75,629)**	**(52)**	**111**	**(70)**	**15,011**
Net Crown Debt	**24,069**	**(70,833)**	**67,880**	**62**	**169**	**354**	**21,701**

The accompanying Notes are an integral part of these Statements.

Statement of Commitments
as at 30 June 1999

	As at 30 June 1999 $m	As at 30 June 1998 $m
By Type		
Capital Commitments		
Specialist military equipment	361	554
Land and buildings	125	73
Other plant and equipment	32	68
Investments	232	211
State-owned enterprises and Crown entities	1,207	1,280
Total Capital Commitments	**1,957**	**2,186**
Operating Commitments		
Non-cancellable accommodation leases	638	710
Other non-cancellable leases	2,443	3,525
Non-cancellable contracts for the supply of goods and services	454	365
Other operating commitments	909	879
State-owned enterprises and Crown entities	2,516	3,872
Total Operating Commitments	**6,960**	**9,351**
Total Commitments	**8,917**	**11,537**
By Term		
Capital Commitments		
One year or less	1,511	1,567
From one year to two years	246	377
From two to five years	186	196
Over five years	14	46
Total Capital Commitments	**1,957**	**2,186**
Operating Commitments		
One year or less	2,136	2,414
From one year to two years	966	1,180
From two to five years	1,293	1,911
Over five years	2,565	3,846
Total Operating Commitments	**6,960**	**9,351**
Total Commitments	**8,917**	**11,537**

Commitments of the Reserve Bank of New Zealand, State-owned enterprises and Crown entities are included in the Statement of Commitments. Commitments to State-owned enterprises and Crown entities are excluded.

The accompanying Notes are an integral part of these Statements.

ANNUAL REPORT *& Financial Accounts*

west
sussex
county
council

annual report

97-98

Statement of Responsibilities for the Statement of Accounts

The County Council's responsibilities

The County Council is required:

- to make arrangements for the proper administration of its financial affairs and to secure that one of its officers has the responsibility for the administration of those affairs. In this authority, that officer is the County Treasurer;
- to manage its affairs to secure economic, efficient and effective use of resources and safeguard its assets.

The County Treasurer's responsibilities

The County Treasurer is responsible for the preparation of the authority's statement of accounts which, in terms of the CIPFA/LASAAC Code of Practice on Local Authority Accounting in Great Britain ("the Code"), is required to present fairly the financial position of the authority at the accounting date and its income and expenditure for the year ended 31st March 1998.

In preparing this statement of accounts, the County Treasurer has:

- selected suitable accounting policies and then applied them consistently;
- made judgements and estimates that were reasonable and prudent;
- complied with the Code.

The County Treasurer has also:

- kept proper accounting records which were up to date;
- taken reasonable steps for the prevention and detection of fraud and other irregularities.

The Audit Report

To: West Sussex County Council
We have carried out the audit of the statement of accounts on pages 38 to 52 which have been prepared in accordance with the accounting policies applicable to local authorities as set out on pages 33 to 36.

Respective Responsibilities of County Treasurer and Auditors
As described above the County Treasurer is responsible for the preparation of the statement of accounts. It is our responsibility to form an independent opinion, based on our audit, on the statement and to report our opinion thereon.

Basis of Opinion
We carried out our audit in accordance with the Audit Commission Act 1998 and the Code of Audit Practice issued by the Audit Commission, which requires compliance with relevant auditing standards.

Our audit included examination, on a test basis, of evidence relevant to the amounts and disclosures in the statement of accounts. It also included an assessment of the significant estimates and judgements made by the authority in the preparation of the statement of accounts and of whether the accounting policies are appropriate to the authority's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the statement of accounts is free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the statement of accounts.

Opinion
In our opinion the statement of accounts presents fairly the financial position of West Sussex County Council at 31st March 1998 and its income and expenditure for the year then ended.

PETER ARKELL
District Audit **30th September 1998**

Consolidated Revenue Account for the year ended 31st March 1998

Net Expend -iture 1996-97	Service	Gross Expend -iture 1997-98	Income From Fees & Charges	Income From Specific Grants	Net Expend -iture 1997-98
£000		**£000**	**£000**	**£000**	**£000**
On its services the County Council spent:					
	Coast and Countryside				
1,381	Countryside Facilities	1,558	107	74	1,377
456	Public Rights of Way	504	18	10	476
128	Coast Protection	165			165
1,965		**2,227**	**125**	**84**	**2,018**
	Education				
261,798	Schools	290,300	22,852	2,604	264,844
4,201	Continuing Education	33,019	29,637	0	3,382
19,719	Other Education	23,150	3,204	1,008	18,938
1,076	Service Strategy and Regulation	1,622			1,622
286,794		**348,091**	**55,693**	**3,612**	**288,786**
	Fire, Police Liaison and Public Protection				
18,867	Fire Brigade	21,008	1,099		19,909
2,011	Trading Standards	1,967			1,967
45	Home Defence	256		214	42
20,923		**23,231**	**1,099**	**214**	**21,918**
	General Purposes				
8,436	Wastes Management	11,411	1,387		10,024
772	Other Services	1,607	455	372	780
9,208		**13,018**	**1,842**	**372**	**10,804**
	Highways and Transport				
37,070	Highways	41,853	4,967	34	36,852
1,095	Public Transport	1,205			1,205
38,165		**43,058**	**4,967**	**34**	**38,057**
	Library and Archives				
8,573	Library	9,311	942		8,369
711	Archives	750	12		738
9,284		**10,061**	**954**	**0**	**9,107**
1,345	**Magistrates' Courts**	**4,474**	**116**	**3,001**	**1,357**
	Personnel and Finance				
751	Central Support Services	2,148	1,517		631
-22	Corporate Business Units	1,617	1,809		-192
1,345	Other Services	2,120	839		1,281
2,074		**5,885**	**4,165**		**1,720**
748	**Probation**	**847**			**847**
1,838	**Property**	**3,790**	**2,130**		**1,660**
	Social Services				
90,617	Service	147,598	39,950	6,352	101,116
3,448	Service Strategy and Regulation	3,447			3,447
94,065		**151,045**	**39,950**	**6,352**	**104,563**
2,384	**Strategic Planning**	**2,752**	**229**		**2,523**
2,959	**Corporate and Democratic Core**	**3,387**			**3,387**
471,752	**Net Cost of Services**	**611,866**	**111,270**	**13,849**	**486,747**

Consolidated Revenue Account for the year ended 31st March 1998

Net Expend -iture 1996-97 £000	Service	Gross Expend -iture 1997-98 £000	Income From Fees & Charges £000	Income From Specific Grants £000	Net Expend -iture 1997-98 £000
	Financing Items and Other Operating Costs				
4,106	Flood Defence Levy	4,331			4,331
-1,283	Investment Income	83	1,837		-1,754
-281	Contributions from Commercial Activities		90		-90
11,923	Capital - Revenue Financing of Expenditure	10,256			10,256
-66,356	- Asset Management Revenue Account	-67,173			-67,173
-51,891		**-52,503**	**1,927**	**0**	**-54,430**
419,861	**Net Operating Expenditure**	**559,363**	**113,197**	**13,849**	**432,317**
	Transfer to or from Reserves				
122	Local Management of Schools	1,041			1,041
122		**1,041**	**0**	**0**	**1,041**
419,983	**Amount to be met from Government Grants and Local Taxpayers**	**560,404**	**113,197**	**13,849**	**433,358**
	This was financed by -				
-1,257	Collection				
	Fund surpluses and deficits		1,244		-1,244
-134,553	Precept on the Collection Funds-council tax		143,524		-143,524
-148,375	Non - domestic rate income		142,258		-142,258
-136,302	Revenue Support Grant		145,974		-145,974
40	Former rates adjustments		-81		81
-420,447	**Total**	**0**	**432,919**	**0**	**- 432,919**
-464	**Surplus or deficit for the year**	**560,404**	**546,116**	**13,849**	**439**

The Consolidated Balance Sheet

At 31 March 1997 £000	£000	BALANCE SHEET	Notes	At 31 March 1998 £000	£000
			:		
		Fixed Assets	1		
		Operational assets			
906,192		Land and buildings		909,920	
2,280		Vehicles, furniture & equipment		2,022	
80,230		Infrastructure		81,287	
5,023		Non-operational assets		5,391	
	993,725				998,620
	22	Deferred charges	4		2
	9	Long-term investments	5		9
	4,978	Long-term debtors			4,477
	998,734	**Net long-term assets**			**1,003,108**
		Current Assets			
1,360		Stocks and work in progress	6	1,039	
19,525		Debtors	7	19,683	
7,330		Payments in advance		6,342	
56,372		Short-term investments	5	52,275	
732		Cash in hand		906	
	85,319				80,245
		Current Liabilities			
824		Temporary borrowing		4,476	
27,960		Creditors	8	28,454	
6,219		Provisions	10	6,532	
1,099		Receipts in advance		5,202	
29,119		Cash overdrawn		9,927	
	65,221				54,591
	20,098	**Net Current Assets**			**25,654**
	28,183	**Government Grants Deferred Account**			**31,075**
	990,649	**Total Net Assets**			**997,687**
		Financed by:			
	893,202	Fixed asset reinstatement reserve	12		878,930
	70,466	Capital financing reserve	12		86,647
	47	Capital receipts	9		5
	22,177	Specific reserves	12		27,787
	4,757	County fund balance	12		4,318
	990,649				**997,687**

Cash Flow Statement

1996-97			1997-98	
£000	£000		£000	£000
		Revenue Activities		
		Expenditure		
299,924		Cash paid to or on behalf of employees	308,853	
234,473	534,397	Other operating costs	236,336	545,189
		Income		
-135,903		Precept – Council income tax	-144,687	
-148,375		Business Rates income	-142,258	
-136,302		Revenue Support Grant	-145,974	
-15,222		Other Government Grants	-13,849	
-56,933		Cash received for goods and services	-73,037	
-47,587	-540,322	Other cash income	-44,001	-536,806
	-5,925	**Net cash flow**		-18,617
		Servicing of Finance		
		Expenditure		
127		Interest paid	63	
		Income		
-1,410	-1,283	Interest received	-1,837	-1,774
		Capital Activities		
		Expenditure		
28,692		Purchase of fixed assets	20,244	
		Income		
-11,715		Sale of fixed assets	-7,287	
-3,645		Capital grants and contributions received	-3,731	
-151		Other capital cash income		
-15,711	12,981		-11,018	9,226
	5,773	**Net cash inflow/outflow before financing**		-11,165
		Financing		
		Expenditure		
		Income		
-82	-82	Long-term debtors and creditors	-452	-452
	5,691	**Increase/decrease in cash and cash equivalents**		**-11,617**

Government of Canada Gouvernement du Canada

Prepared by the
Receiver General for Canada

Public Accounts of Canada

1999

Volume I

Summary Report
and Financial
Statements

Canada

STATEMENT OF RESPONSIBILITY

The financial statements in this section are prepared by the Government of Canada in accordance with the accounting policies set out in Note 1 to the statements on a basis consistent with that of the preceding year.

Responsibility for the integrity and objectivity of the financial statements rests with the Government. The financial statements are prepared under the joint direction of the President of the Treasury Board, the Minister of Finance, and the Receiver General for Canada in compliance with governing legislation. The financial statements are generally prepared on an accrual basis of accounting; two notable exceptions are that capital assets are charged to budgetary expenditures at the time of acquisition or construction and tax revenues are generally reported on a cash basis. The information included in these financial statements is based on the Government's best estimates and judgement, with due consideration given to materiality.

To fulfill its accounting and reporting responsibilities, the Government maintains systems of financial management and internal control which give due consideration to costs, benefits and risks. These systems are designed to provide reasonable assurance that transactions are properly authorized by Parliament, are executed in accordance with prescribed regulations, and are properly recorded so as to maintain accountability of public money and safeguard the assets and properties of Canada under Government administration. The Receiver General for Canada maintains the accounts of Canada, a centralized record of the Government's financial transactions, and obtains additional information as required, from departments, agencies and Crown corporations, to meet accounting and reporting requirements.

The Government presents the financial statements to the Auditor General of Canada who audits them and provides an independent opinion to the House of Commons. The duties of the Auditor General in that respect are contained in section 6 of the *Auditor General Act* and section 9 of the *Debt Servicing and Reduction Account Act.* Additional information is provided in the observations of the Auditor General at the end of this section.

Annually, the financial statements are tabled in Parliament as part of the *Public Accounts of Canada*, and are referred to the Standing Committee on Public Accounts, which reports to Parliament on the results of its examination together with any recommendations it may have with respect to the financial statements and accompanying audit opinion.

On behalf of the Government of Canada.

V. PETER HARDER *Secretary of the Treasury Board and Comptroller General of Canada*	C. SCOTT CLARK *Deputy Minister of Finance*	RANALD A. QUAIL *Deputy Receiver General for Canada*

OPINION OF THE AUDITOR GENERAL
ON THE
FINANCIAL STATEMENTS OF THE GOVERNMENT OF CANADA

To the House of Commons:

My responsibility: I have audited the statement of assets and liabilities of the Government of Canada as at March 31, 1999 and the statements of revenues, expenditures and accumulated deficit, changes in financial position and transactions for the year then ended. These financial statements are the responsibility of the Government. My responsibility, as required by section 6 of the *Auditor General Act*, is to express an opinion on these financial statements based on my audit as to whether:

1. the financial statements present information fairly (fairness);
2. the financial statements were prepared in accordance with the Government's stated accounting policies (compliance); and
3. the Government's stated accounting policies were applied on the same basis as in the preceding year (consistency).

The scope of my audit: I conducted my audit in accordance with generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting policies used and significant estimates made by the Government, as well as evaluating the overall financial statement presentation.

In my opinion:

1. ***Fairness:*** These financial statements present fairly, in all material respects, the financial position of the Government of Canada as at March 31, 1999 and the results of its operations, the changes in its financial position and its financial requirements for the year then ended.

2. ***Compliance:*** These financial statements were prepared in accordance with the stated accounting policies of the Government of Canada set out in Note 1 to the financial statements.

3. ***Consistency:*** The Government's stated accounting policies have been applied on a basis consistent with that of the preceding year.

My opinion on the March 31, 1998 financial statements:

In my report dated July 27, 1998, I expressed a qualified opinion on the March 31, 1998 financial statements of the Government of Canada, for the recording of a transaction related to the Canada Millennium Scholarship Foundation as if it were a liability and an expenditure. In my opinion, this understated the 1997-98 surplus by $2.5 billion and overstated accounts payable and accrued liabilities as well as the accumulated deficit by the same amount.

Additional information: Additional information and comments on the financial statements and this opinion are included in my observations at the end of Section 1, Volume 1 of the *Public Accounts of Canada*.

L. Denis Desautels, FCA
Auditor General of Canada

Ottawa, Canada
July 26, 1999

GOVERNMENT OF CANADA
Statement of Transactions
for the Year Ended March 31, 1999
(in millions of dollars)

	1999	1998
BUDGETARY TRANSACTIONS		
Revenues ...	155,671	153,162
Expenditures ...	-152,787	-149,684
Surplus for the year ...	2,884	3,478
NON-BUDGETARY TRANSACTIONS		
Net source from loans, investments and advances ...	500	2,031
Net source from pension and other accounts ...	7,024	3,829
Net source from other transactions ...	1,083	3,391
Net source ...	8,607	9,251
Source of funds (excluding foreign exchange transactions) ...	11,491	12,729
NET REQUIREMENT FOR FOREIGN EXCHANGE TRANSACTIONS ...	***-5,700***	***-2,155***
Total source of funds ...	5,791	10,574
NET REQUIREMENT FOR UNMATURED DEBT TRANSACTIONS ...	***-6,864***	***-9,561***
Decrease (-) or increase in cash ...	-1,073	1,013
CASH IN BANK AT BEGINNING OF YEAR [1] ...	***10,379***	***9,366***
CASH IN BANK AT END OF YEAR [1] ...	***9,306***	***10,379***

The accompanying notes are an integral part of these statements.
Details (unaudited) can be found in other sections of this volume.
In this statement, a positive amount indicates a source of funds and a negative amount indicates a requirement for funds.
[1] Cash in bank excludes outstanding cheques, warrants and deposits.

GOVERNMENT OF CANADA

Statement of Revenues, Expenditures and Accumulated Deficit for the Year Ended March 31, 1999

(in millions of dollars)

	1999		1998	
	Gross [1]	Net [1]	Gross [1]	Net [1]
REVENUES (Note 4)				
TAX REVENUES—				
Income tax—				
Personal	77,707	72,488	75,672	70,787
Corporation	21,575	21,575	22,496	22,496
Other income tax revenues	2,901	2,901	2,974	2,974
	102,183	***96,964***	***101,142***	***96,257***
Excise taxes and duties—				
Goods and services tax	23,534	20,684	22,353	19,461
Energy taxes	4,716	4,716	4,638	4,638
Customs import duties	2.359	2,359	2,766	2,766
Other excise taxes and duties	3,640	3,640	3,995	3,995
	34,249	***31,399***	***33,752***	***30,860***
Employment insurance premiums	***19,363***	***19,363***	***18,802***	***18,802***
TOTAL TAX REVENUES	***155,795***	***147,726***	***153,696***	***145,919***
NON-TAX REVENUES—				
Return on investments	5,072	4,991	4,511	4,427
Other non-tax revenues	6,676	2,954	6,155	2,816
TOTAL NON-TAX REVENUES	***11,748***	***7,945***	***10,666***	***7,243***
TOTAL REVENUES	**167,543**	**155,671**	**164,362**	**153,162**
EXPENDITURES (Note 5)				
TRANSFER PAYMENTS—				
Old age security benefits, guaranteed income supplement and spouse's allowance	22,285	22,781	21,758	22,225
Other levels of government	25,523	25,523	20,504	20,504
Employment insurance benefits [2]	11,884	11,884	11,842	11,842
Canada child tax benefits	5,715		5,352	
Other transfer payments	21,585	18,735	23,557	20,664
TOTAL TRANSFER PAYMENTS	***86,992***	***78,923***	***83,013***	***75,235***
CROWN CORPORATION EXPENDITURES	***4,995***	***3,497***	***3,775***	***2,548***
OTHER PROGRAM EXPENDITURES—				
National Defence	9,125	8,781	9,240	8,879
All other departments and agencies	22,153	20,192	22,113	20,279
TOTAL OTHER PROGRAM EXPENDITURES	***31,278***	***28,973***	***31,353***	***29,158***
TOTAL PROGRAM EXPENDITURES	***123,265***	***111,393***	***118,141***	***106,941***
PUBLIC DEBT CHARGES	***41,394***	***41,394***	***40,931***	***40,931***
TOTAL EXPENDITURES	**164,659**	**152,787**	**159,072**	**147,872**
SURPLUS BEFORE CHANGE IN ACCOUNTING POLICY	**2,884**	**2,884**	**5,290**	**5,290**
Change in accounting policy (Note 2)			-1,812	-1,812
SURPLUS FOR THE YEAR	**2,884**	**2,884**	**3,478**	**3,478**
ACCUMULATED DEFICIT, BEGINNING OF YEAR	**579,708**	**579,708**	**583,186**	**583,186**
ACCUMULATED DEFICIT, END OF YEAR (Note 6)	**576,824**	**576,824**	**579,708**	**579,708**

The accompanying notes are an integral part of these statements.

Details (unaudited) can be found in other sections of this volume.

(1) The difference between Gross and Net is revenues netted against expenditures, revenues of consolidated Crown corporations credited to expenditures and tax credits and expenditures related to the tax system included in revenues.

(2) Employment insurance benefits exclude administration costs of $1,360 million ($1,322 million in 1998) related to the operation of the Employment Insurance Account. These costs have been allocated to other program expenditures.

GOVERNMENT OF CANADA
Statement of Assets and Liabilities
at March 31, 1999
(in millions of dollars)

	1999	1998
LIABILITIES		
ACCOUNTS PAYABLE, ACCRUALS AND ALLOWANCES—		
Accounts payable and accrued liabilities	24,509	22,364
Interest and matured debt	9,791	10,419
Allowance for employee benefits	6,926	6,729
Allowance for loan guarantees and borrowings of Crown corporations	4,090	4,188
TOTAL ACCOUNTS PAYABLE, ACCRUALS AND ALLOWANCES	***45,316***	***43,700***
INTEREST-BEARING DEBT—		
Unmatured debt—		
Payable in Canadian currency—		
Marketable bonds	295,752	294,583
Treasury bills	96,950	112,300
Canada savings bonds	27,662	29,769
Bonds for Canada Pension Plan	4,063	3,456
	424,427	*440,108*
Payable in foreign currencies	36,000	27,183
Total unmatured debt (Note 7)	*460,427*	*467,291*
Pension and other accounts—		
Public sector pensions (Note 8)	122,407	117,457
Canada Pension Plan (net of securities) (Note 9)	5,427	4,205
Other pension and other accounts	6,724	5,872
Total pension and other accounts	*134,558*	*127,534*
TOTAL INTEREST-BEARING DEBT	***594,985***	***594,825***
TOTAL LIABILITIES	**640,301**	**638,525**
ASSETS		
CASH AND ACCOUNTS RECEIVABLE—		
Cash in bank	9,306	10,379
Cash in transit	5,432	4,530
	14,738	*14,909*
Less outstanding cheques and warrants	4,045	3,218
Total cash	*10,693*	*11,691*
Accounts receivable (net of allowance for doubtful accounts of $2,432 million ($2,261 million in 1998))	4,580	4,122
TOTAL CASH AND ACCOUNTS RECEIVABLE	***15,273***	***15,813***
FOREIGN EXCHANGE ACCOUNTS (Note 10)	***34,668***	***28,968***
LOANS, INVESTMENTS AND ADVANCES—		
Enterprise Crown corporations (Notes 11 and 14)	11,052	12,601
National governments, including developing countries and international organizations (Note 12)	7,555	6,869
Provincial and territorial governments and other loans, investments and advances	3,100	2,591
Portfolio investments	1,241	1,241
	22,948	*23,302*
Less allowance for valuation	9,412	9,266
TOTAL LOANS, INVESTMENTS AND ADVANCES	***13,536***	***14,036***
TOTAL ASSETS	**63,477**	**58,817**
ACCUMULATED DEFICIT (Note 6)	**576,824**	**579,708**

The accompanying notes are an integral part of these statements.
Details (unaudited) can be found in other sections of this volume.

GOVERNMENT OF CANADA
Statement of Changes in Financial Position
for the Year Ended March 31, 1999 (1)

(in millions of dollars)

	1999	1998
OPERATING ACTIVITIES —		
Surplus for the year	2,884	3,478
Expenditures not requiring cash :		
Interest on pension and other accounts	10,048	9,474
Government contribution for employee benefits	2,116	1,773
Provision for valuation of assets and liabilities	-698	2,620
	14,350	***17,345***
Net payments from pension and other accounts	-3,531	-5,110
Net change in accounts receivable, accounts payable and accruals	181	-470
CASH PROVIDED BY OPERATING ACTIVITIES	***11,000***	***11,765***
INVESTING ACTIVITIES —		
Net decrease in loans, investments and advances	566	1,467
CASH PROVIDED BY INVESTING ACTIVITIES	***566***	***1,467***
FOREIGN EXCHANGE ACTIVITIES —		
Net increase in foreign currencies borrowings	8,817	4,167
Net increase in foreign exchange accounts	-5,700	-2,155
CASH PROVIDED BY FOREIGN EXCHANGE ACTIVITIES	***3,117***	***2,012***
TOTAL CASH GENERATED BEFORE FINANCING ACTIVITIES	***14,683***	***15,244***
FINANCING ACTIVITIES —		
Net decrease in Canadian currency borrowings	15,681	13,728
CASH USED FOR FINANCING ACTIVITIES	***15,681***	***13,728***
Net decrease (-) or increase in cash	**-998**	**1,516**
CASH AT BEGINNING OF YEAR	*11,691*	*10,175*
CASH AT END OF YEAR	***10,693***	***11,691***

The accompanying notes are an integral part of these statements.
Details (unaudited) can be found in other sections of this volume.

(1) The figures in this statement differ from those shown in the Statement of Transactions because the non-cash transactions have been reclassified and shown separately.

FRANCE

REPORT PRESENTING THE *COMPTE GÉNÉRAL DE L'ADMINISTRATION DES FINANCES (CGAF)* FOR 1996

The **CGAF** or **General Financial Administration Account** is a document summarizing government accounts for a given year, and is therefore a fundamentally important step in the drafting of the Budget Review Law.

Pursuant to Article 131 of the Decree of December 29, 1962, it includes the following:

- a general balance of government accounts which results from the summarized accounts of government accountants;
- a breakdown of budget revenue;
- a breakdown of budget expenditure showing expenditure totals by budget chapters for each ministerial department; the breakdown must be certified by the minister concerned;
- a breakdown of transactions posted to special Treasury accounts; and
- a breakdown of the income statements.

1996 General Financial Administration Account Report

INCOME STATEMENT

The income statement shows the year's expenditure and revenue items and distinguishes between those arising from current government operations, financial transactions and extraordinary transactions.

FRF billion

	1996	1995	%
Operating revenue	1 643,80	1 528,40	7,60
Operating expenditure	1 706,70	1 616,10	5,60
OPERATING INCOME	**- 62,90**	**- 87,70**	**28,30**
Financial revenue	53,20	56,20	- 5,40
Financial expenditure	252,40	262,80	- 4,00
FINANCIAL INCOME	**- 199,20**	**- 206,60**	**3,60**
Extraordinary revenue	18,40	29,10	- 36,70
Extraordinary expenditure	32,90	57,10	- 42,80
EXTRAORDINARY INCOME	**- 14,50**	**- 28,00**	**48,20**
Total revenue	**1 715,30**	**1 613,70**	**6,30**
Total expenditure	**1 992,00**	**1 936,00**	**2,90**
CHANGE IN NET WORTH	**- 276,70**	**- 322,30**	**16,50**

The change in net worth is carried to the liabilities side of the balance sheet under account 117.

The change in net worth for 1996 was - 276.7 billion FRF versus - 322.3 billion FRF in 1995. This 16.5% improvement stems from a substantial 6.3% increase in revenue and containment of expenditure growth at 2.9%.

FROM THE BUDGET OUTTURN BALANCE TO THE INCOME ACCOUNT

The compilation of the income account from the budget outturn balance proceeds as follows:

- exclusion of budget transactions carried to the balance sheet (acquisitions, fixed assets, loans and advances);
- incorporation of revenue and expenditure arising from outright treasury transactions (e.g., profits and losses on loans and loan guarantees);
- incorporation of depreciation at conventional values equal to the fixed assets acquired during the year; and
- restatement of budget receipts on an accrued basis: all of the revenue paid in between 1 January and 31 December is reported in the budget outturn, but it is revenue falling due between these two dates that is the revenue for the year.

BALANCE SHEET AT 31 DECEMBER 1996

AGGREGATED BALANCE SHEET AT 31.12.96

ASSETS	1996			1995
	Gross	Depreciation	Net	Net
FIXED ASSETS (1)				
20 - Intangible fixed assets	1,226,955,394.36	1,226,955,394.36		
21 - Tangible fixed assets	1,155,974,845,009.73	1,144,201,310,878.15	11,773,534,131.58	10,634,344,937.91
25 - Loans	134,272,758,186.01		134,272,758,186.01	133,195,048,533.45
26 - Endowments, interests and connected claims	493,671,462,401.28		493,671,462,401.28	619,259,528,402.80
27 - Advances and other financial assets	100,488,903,767.15		100,488,903,767.15	68,514,044,869.53
369.31 - Claims corresponding to government securities issued for the government debt management fund	20,985,750,000.00		20,985,750,000.00	18,207,650,000.00
TOTAL FIXED ASSETS	**1,906,620,674,758.53**	**1,145,428,266,272.51**	**761,192,408,486.02**	**849,810,616,743.69**
CURRENT ASSETS (II)				
41 - Taxpayers	346,821,036,487.40		346,821,036,487.40	335,682,680,617.79
46 - Misc. Receivables	7,731,336,186.04		7,731,336,186.04	7,734,328,054.68
47 - Nominal and suspense accounts receivable	48,300,836,881.92		48,300,836,881.92	50,158,851,651.69
51 - Banks and financial institutions	64,261,598,755.27		64,261,598,755.27	117,078,093,760.90
53 - Cash	347,904,422.94		347,904,422.94	346,932,533.49
58 - Transfers between financial accounts	7,175,200.00		7,175,200.00	4,051,850.00
TOTAL II - CURRENT ASSETS	**467,469,887,933.57**		**467,469,887,933.57**	**511,004,938,468.55**
ACCRUALS				
482 - Deferred costs and commitments	37,943,847,742.22		37,943,847,742.22	49,889,191,966.99
483 - Expenditure carried to the next year's budget	23,258,308,090.95		23,258,308,090.95	22,968,434,371.83
484-491 - Other accrued receivables	18,123,230,039.89		18,123,230,039.89	38,748,236,249.36
TOTAL IV	**79,325,385,873.06**		**79,325,385,873.06**	**111,605,862,588.18**
129 - Issue premia and index-linking gains	25,538,953,276.89	1,706,736,351.21	23,832,216,925.68	25,025,275,253.51
TOTAL IV	**25,538,953,276.89**	**1,706,736,351.21**	**23,832,216,925.68**	**25,025,275,253.51**
GRAND TOTAL (I+II+III+IV)	**2,478,954,901,842.05**	**1,147,135,002,623.72**	**1,331,819,899,218.33**	**1,497,446,693,053.93**

(1) Accounts 269 and 36 (except 369.31) are posted as liabilities because they show a credit balance.

BALANCE SHEET 31 DECEMBER 1996
AGGREGATED BALANCE SHEET 31.12.96

LIABILITIES	FRF 1996	FRF 1995
NET POSITION (1)	**-2,503,817,442,382.99**	**-2,095,993,626,581.65**
112 - Carried forward from previous year	-2,249,012,304,214.94	-1,928,267,509,108.23
115 - Appraisal increase credit	21,859,929,649.19	154,583,565,685.13
117 - Result for the year	-276,665,067,817.24	-322,309,683,158.55
FINANCIAL LIABILITIES (2)	**3,285,655,913,687.20**	**3,018,257,545,767.93**
Negotiable financial debt	3,132,715,339,626.35	2,847,120,571,927.11
12 - Long-term borrowing on the capital market	2,041,508,019,626.35	1,786,100,709,927.11
145 - Holders of negotiable Treasury notes and bills	1,091,207,320,000.00	1,061,019,862,000.00
Non-negotiable financial debt	136,140,574,060.85	151,936,973,840.82
14 except 145 - Treasury notes and bills and short-term borrowing	66,705,562,499.27	69,144,021,520.17
16 - Misc. government liabilities	54,508,471,920.51	68,230,134,366.01
17 - Debts arising from coin in circulation	13,728,528,536.17	13,312,983,050.63
18 - Short-term debt	1,198,011,104.90	1,249,834,904.01
Assistance from the Banque de France (account 519)	16,800,000,000.00	19,200,000,000.00
TOTAL I (= 1+2)	**781,838,471,304.21**	**922,263,919,186.28**
OTHER LIABILITIES (II)		
269 - Payments to be made on non-fully paid shares	29,257,029.00	29,257,029.00
36 except 369.31 - Unincorporated government agencies	2,152,762,917.86	1,949,416,866.55
38-39 - Transactions with specific government budgets	3,608,514,101.26	3,832,135,448.66
40 - Payees of cheques drawn on the Treasury	1,640,926,722.09	1,825,600,088.44
42-513 - Correspondents, financial organisations	169,624,594,906.10	178,273,847,521.02
43 - Correspondents, local communities and public establishments	101,074,164,003.30	94,002,116,460.32
44 - Other Treasury correspondents	82,554,507,978.83	66,545,882,661.96
45 - Depositors	24,952,086,820.90	26,721,385,679.10
46 - Misc. creditors	14,749,739,304.29	13,430,485,875.41
47 - Nominal and suspense accounts payable (475 to 478)	73,343,577,956.04	76,916,384,448.48
TOTAL II	**473,730,131,739.67**	**463,526,512,078.94**

BALANCE SHEET 31 DECEMBER 1996
AGGREGATED BALANCE SHEET 31.12.96
(continued)

LIABILITIES	FRF 1996	FRF 1995
ACCRUALS		
486 - Expenditure deferred to next budget	63,599,753,093.18	91,925,224,192.80
487-488 - Other accrual accounts payable (except 488.8)	8,695,393,959.25	10,316,739,567.83
495 - Repayments of funds for cancelled expenditure by ministries	49,536.42	45,561,381.99
TOTAL III	**72,295,196,588.85**	**102,287,525,142.62**
488.8 - Exchange adjustment - liability	3,956,099,585.60	9,368,736,646.09
TOTAL IV	**3,956,099,585.60**	**9,368,736,646.09**
GRAND TOTAL (I+II+III+IV)	**1,331,819,899,218.33**	1,497,446,693,053.93

(1) Only financial items are reported up until 31 December 1987.
(2) Not including the debt guaranteed or managed by the government and posted to account 80. The amount was 431,114,395,039.91 FRF at 31 December 1996 and 562,747,091,384.96 FRF at 31 December 1995.

APPENDIX 3

WEB SITE REFERENCES

832.Readers may wish to access electronic copies of financial statements or other documents referred to in this Study. These web sites were current at the time of printing.

Australia
http://www.dofa.gov.au – Financial Statements of the Commonwealth Government of Australia
http://www.treasury.nsw.gov.au – Consolidated Financial Statements of the NSW Public Sector and NSW Budget Sector

Canada
http://www.pwgsc.gc.ca – Public Accounts of Canada
http://www.gov.on.ca/fin/ – Public Accounts of Ontario

Hong Kong
http://www.info.gov.hk/tsy – Accounts of the Government of the HKSAR

International
http://www.imf.org – Manual on Government Finance Statistics

India
http://cga.nic.in – Annual Financial Statement

Mauritius
http://ncb.intnet.mu – Annual Report

New Zealand
http://www.govt.nz – Financial Statements of the Government of New Zealand

United Kingdom
http://www.westsussex.gov.uk/tr/factfig.htm –West Sussex financial facts and figures

United States
http://www.doi.gov – U.S. Department of the Interior Annual Report
http://www.financenet.gov/financenet/fed/docs/docsstmt.htm – Consolidated Financial Statements of the United States Government
http://www.gao.gov/reports.htm – Comptroller General's Annual Report, United States General Accounting Office (GAO)

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Public Accounts of Ontario, 1992–93

Cayman Islands

Cayman Islands Government, Accounts for the year ended 31st December 1997

Fiji

Report on the Accounts and Finance, Parliament of Fiji, For the Year 1997

Hong Kong

Report of the Director of Audit on the Accounts of the Government of the Hong Kong Special Administrative Region for the year ended 31 March 1999

India

Annual Financial Statement of the Government of India for the financial year 1997–98

International

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