Senate Economics Legislation Committee

ANSWERS TO QUESTIONS ON NOTICE

Treasury Portfolio

Additional Estimates, 16 February 2006

Question: AT 45

Topic: *Accounting Standards and the Public Sector*

Hansard Page: Written

Senator WATSON asked:

1. Why does the Australian Accounting Standards Board (AASB) wish to withdraw Australian Accounting Standards (AAS) AAS27 Financial Reporting by Local Governments, AAS 29 Financial Reporting by Government Departments and AAS31 Financial Reporting by Governments?

2. Does the AASB acknowledge that there are significant differences between the public sector and the private sector?

3. What would the AASB say in response to this statement from Ian McPhee FCPA, at a recent CPA Australia meeting:
"It is appropriate, in my view, to have a presumption in favour of sector-neutral standards, but where a case can be made, departures from this approach should be allowed. On this basis, in light of the marked differences between the for-profit and public sectors, and the scale of public sector activities, I am strongly in favour of the AASB continuing to develop public sector standards".

4. How does the AASB propose that government departments value such assets as heritage buildings, natural assets, and museum collections?

5. What benefit would valuing such assets provide?

6. How does the AASB propose that Government Departments account for the value of land under roads? Is it worth billions of dollars or nothing?

7. Removing the proposed standards would greatly increase the accounting costs for the public sector. What benefit would it provide and does it outweigh the costs?

Answer:

General comment

These general comments are made to provide a context to the responses to Questions 1 to 7.

AAS 27, AAS 29 and AAS 31 presently operate in conjunction with the other AASB Standards. They contain some specific requirements and guidance for local governments, government departments and governments in preparing their financial reports, however, most of the requirements that these entities must apply are contained in other AASB Standards. In a number of cases, AAS 27, AAS 29 and AAS 31 simply cross-reference to the requirements in those other Standards. Because of the introduction of IFRSs, AAS 27, AAS 29 and AAS 31 are in urgent need of revision.

Australia has gained a good reputation for public sector financial reporting through the application by the Commonwealth, States, Territories and local governments of all applicable AASB Standards, including AAS 27, AAS 29 and AAS 31. The AASB is keen to maintain and enhance this reputation by promoting further improvements to public sector financial reporting.

The current review of AAS 27, AAS 29 and AAS 31 is not intended to diminish the profile of public sector reporting in Australia, but is intended to streamline the reporting requirements applied in the Australian public sector and to ensure that public sector accountants and private sector accountants are familiar with the one core set of requirements.

With the benefit of hindsight, the AASB could probably have better communicated its intention to review of AAS 27, AAS 29 and AAS 31 because it appears to have given rise to a misapprehension that the AASB lacks interest in public sector issues. The AASB is pursuing a wide range of issues of specific interest to the public sector, either at a domestic level, or in conjunction with other national and international standard setters. These issues include projects on convergence of GAAP and Government Finance Statistics, Heritage Assets, Administered Items, Budget Reporting, Non-Exchange Revenue Recognition and Social Policy Obligations.

The AASB is conscious of the need to be open and transparent in its activities. In relation to public sector standards specifically, the AASB has a comprehensive Policy Paper on its web site (www.aasb.com.au), which is updated periodically to reflect recent developments (most recently updated as at 14 July 2006 – a copy is attached). The AASB also uses the following processes:

(a) all technical matters are discussed and decided in meetings that are open to the public;

(b) the AASB meets periodically with its Consultative Group and other interested parties, which include various public sector representatives, to discuss the AASB's projects; and

(c) new and changed requirements are made only after a public consultation process, which involves Exposure Drafts or Invitations to Comment.

AASB staff are available to provide further information about the questions on notice and any related matters should this be necessary.

Answers to specific questions

Question 1.

The AASB has been reviewing AAS 27, AAS 29 and AAS 31 and intends issuing an Exposure Draft for public comment that will propose relocating much of the material currently in those Standards to other topic-based Standards to place the requirements in a better context. This may ultimately lead to the withdrawal of AAS 27, AAS 29 and AAS 31. The AASB has adopted a principle to avoid leaving a vacuum in the requirements as a result of the review process.

The AASB does not necessarily "wish to withdraw" AAS 27, AAS 29 and AAS 31. Whether or not they are withdrawn will depend on what the best outcome is considered to be based on comments received.

Question 2.

The AASB appreciates that the business models employed in public not-for-profit sector entities government and for-profit entities are different, but this does not necessarily mean that transactions conducted in each sector should be treated differently. The AASB acknowledges that there are cases where different treatments are appropriate as between public not-for-profit sector entities and for profit entities. This is evidenced by the considerable amount of work being conducted by the AASB on the Harmonisation of Generally-Accepted Accounting Principles and Government Finance Statistics project and the AASB's extensive commitment to supporting and using the work of the International Public Sector Accounting Standards Board (IPSASB) of the International Federation of Accountants. Examples of not-for-profit specific treatments include those for non-exchange revenues; property, plant and equipment acquired for no or nominal cost; and revaluation of property, plant and equipment by class.

Question 3.

The AASB fully concurs with Ian McPhee's statement, which is consistent with current AASB policy. The proposed review of AAS 27, AAS 29 and AAS 31 in the manner contemplated does not conflict with either the AASB's policy or Ian McPhee's statement.

Question 4.

At present, heritage assets are required to be treated under AASB 116 *Property, Plant and Equipment*. There is also commentary in AAS 29 that provides guidance on measuring infrastructure, heritage and community assets, which acknowledges the special characteristics of these assets.

The AASB is aware of concerns about applying the generic requirements in AASB 116 to heritage assets, particularly in respect of measurement, and is participating in the work of the IPSASB on developing requirements/guidance dealing specifically with heritage assets. There is currently an IPSASB Consultation Paper on issue for public comment, which incorporates a Discussion Paper authored by the UK Accounting Standards Board. It should also be noted that some for-profit entities control heritage assets and face similar issues. The Board intends to incorporate into AASB 116 a statement that clarifies that infrastructure, cultural and heritage assets fall within the scope of that Standard and additional guidance that clarifies the application of AASB 116 to such assets. In particular, the guidance will note that the application of AASB 116 would result in the recognition of only those heritage assets that can be reliably measured. It depends on the circumstances as to whether the reliable measurement recognition criterion can be satisfied in relation to a particular heritage asset. Of those heritage assets that satisfy the reliable measurement criterion for initial recognition purposes, AASB 116 permits but does not require recognised heritage assets to be revalued. Furthermore, given the nature of many heritage assets that meet the recognition criteria and the manner in which they are preserved or maintained, those assets may have indefinite useful lives and therefore may not be subject to depreciation, however, they would be subject to impairment testing.

Question 5.

In conducting its work the AASB applies an underlying presumption that it is relevant for assets and liabilities that meet the recognition criteria to be recognised in the balance sheet on the basis that entities should be accountable for their assets and liabilities. The Heritage Assets project is aimed at helping to determine the circumstances in which the recognition criteria are met and the relevance of information about heritage assets in financial reports and the types of disclosures that would be useful.

Question 6.

The Board notes that the current transitional provisions for land under roads are due to lapse at the end of the reporting period ending after 31 December 2006. The Board decided at its September 2006 meeting to extend the provisions for one year so that they do not lapse prior to the issue of amended or new Standards arising out of the short-term review of AAS 27, AAS 29 and AAS 31. A Standard giving effect to this decision by amending AASB 1045 *Land Under Roads: Amendments to AAS 27A, AAS 29A and AAS 31A* will be issued after the October 2006 Board meeting.

As part of the short-term review of AAS 27, AAS 29 and AAS 31, the Board intends in due course proposing that the transitional provisions lapse at the end of the reporting period ending after 31 December 2007. Requirements relating to the transition into AASB 116 on or before that date would also be proposed, providing the equivalent kind of relief, limited to land under roads, available in AASB 1 *First-time Adoption of Australian Equivalents to International Financial Reporting Standards* for first-time adoption of Australian equivalents to IFRSs.

The current position of the AASB is that land under roads should be treated in the same manner as other property, plant and equipment (including land under other infrastructure such as railway lines and schools) – that is, it should be recognised under AASB 116 when it meets the asset definition and recognition criteria. Arguments in favour of this position include the following:

(a) land under roads is an asset for which the controlling entity is accountable. In other words, it is useful to know how much value (which is significantly more than zero) is tied up in land under roads that can be reliably measured since this will encourage the controlling entity to actively consider its strategies for managing the asset – for example, selling off land under roads that is no longer needed; and

(b) when land is acquired and paid for, the acquisition cost should not be recognised as an expense.

The AASB appreciates that there are also arguments against recognising land under roads, and that views differ about whether the benefits outweigh the costs of recognition. The AASB will consider these in light of comments on the Exposure Draft.

Question 7.

The AASB does not believe that if AAS 27, AAS 29 and AAS 31 were to be removed that accounting costs in the public sector would increase. This is because the same issues are being dealt with, whether the requirements are in AAS 27, AAS 29 and AAS 31 or other, largely topic-based, standards. In fact the AASB considers that a more logical arrangement of the requirements by topic will in the longer term assist those in the public sector who use the standards because the relevant requirements, guidance and discussion for each particular transaction type will be located in one place.