

# PSAB Update

Source: Adapted from CICA PSAB Presentations

# Agenda

- New Handbook Sections
- Current Projects Underway

# New Handbook Sections

- Liabilities
- Contingent Liabilities
- Contractual Obligations
- Measurement uncertainty
- Reporting entity
- GAAP

# Liabilities PS 3200

- Focused on substance rather than form
- Permits recognition of constructive/equitable obligations
- Provides additional guidance for applying definition

# Liabilities PS 3200

- Liabilities are present obligations of a government to others arising from past transactions or events, the settlement of which is expected to result in the future sacrifice of economic benefits.

# Liabilities PS 3200

## Characteristics of Liabilities

- Duty leaving little or no discretion to avoid
- Sacrifice of economic benefits
- “obligating” transaction or event

# Liabilities PS 3200

Discretion to avoid

- Discretion is ability to make choices
- Little or no discretion = no realistic alternative
- Constructive/Equitable = decision and communication
- Evidence needed of decision & communication

# Liabilities PS 3200

Sacrifice of economic benefit

- Transfer OR use of assets, provision of goods, other means
- Entity must exist
- Timing of settlement specified



# Liabilities PS 3200

Past transaction or event

- Must be an “Obligating” transaction or event
- Can not define generally
- Arise from others actions
- Arise from your own actions
- Retroactive legislation cannot create a past transaction or event

# Liabilities PS 3200

## Unrecognized liabilities

- Disclose nature of those not recognized with reason why estimate cannot be made

# Contingent Liabilities PS 3300

Reasons for the project

- Does not permit accrual of liability
- No disclosure guidance
- No guidance related to measurement uncertainty

# Contingent Liabilities PS 3300

## Benefits of new approach

- Defines a contingent liability
- Requires accrual when “likely”
- Provides de-recognition criteria
- Gives specific disclosure requirements

# Contingent Liabilities PS 3300

- Contingent liabilities are possible obligations that may result in the future sacrifice of economic benefits arising from existing conditions or situations involving uncertainty. That uncertainty will ultimately be resolved when one or more future events not wholly within the government's control occurs or fails to occur.

# Contingent Liabilities PS 3300

Two characteristics

- Must be existing condition or situation
- Expected future confirming event (existence uncertainty)

# Contingent Liabilities PS 3300

Existing condition or situation

- Must be at the financial statement date
- Retroactive legislation did not exist at F/S date
- Government announcements after date not a contingency

# Contingent Liabilities PS 3300

Confirming future event

- Not wholly in government's control
- Legislation is not a future confirming event



# Contingent Liabilities PS 3300

## Existence uncertainty

- Probability of future event happening
- Likely = high
- Unlikely = slight
- Undeterminable = not known

# Contingent Liabilities PS 3300

## Recognition

- Existing condition + future event likely
- Amount can be reasonably estimated
- Derecognize when settled or become unlikely

# Contingent Liabilities PS 3300

## De-recognition

- Likelihood continually reviewed
- Derecognize when unlikely
- If undeterminable continue to accrue

# Contingent Liabilities PS 3300

## Measurement

- Carrying amount continually reviewed
- Liability mitigated by counter claim (insurance)
- Recovery of counter claim must be likely

# Contingent Liabilities PS 3300

## Disclosure

- Likely contingencies but cannot recognize
- Additional exposure not accrued
- If occurrence is not determinable
- Nature AND extent or reasons for non-disclosure of extent
- Do not disclose unlikely

# Contractual Obligations PS 3390

Reasons for the project

- Existing Handbook did not define which commitments
- No guidance on what to disclose

# Contractual Obligations PS 3390

## Benefits of new approach

- Commitments = contractual obligations
- Similar to CICA Handbook
- Guidance on types of contractual obligations
- Provides guidance on what to disclose

# Contractual Obligations PS 3390

## Disclosure

- Nature = type
- Extent = amount
- Timing = when likely to occur



# Measurement Uncertainty PS 2130

Reasons for the project

- No PSA Handbook guidance
- Project on liabilities identified need
- Recommended a separate Section

# Measurement Uncertainty PS 2130

## Benefits of new Section

- Establishes basic principles of disclosure
- Applies to BOTH recognized and disclosed items
- Disclosed items could include subsequent events, environmental liabilities, contingent liabilities, landfill and contractual obligations

# Measurement Uncertainty PS 2130

- Material change in the amount
- Nature of uncertainty is disclosed
- Extent of uncertainty is disclosed
- If disclosure of amount could have adverse effect, then do not disclose but provide reason(s) for non-disclosure

# Reporting Entity PS 1300

## New definition

- Problems with accountability and control
- Focuses solely on control
- Provides guidance related indicators

# Reporting Entity PS 1300

## Control

- The power to govern the financial and operating policies of another organization...

# Reporting Entity PS 1300

- Try to avoid the checklist approach!!

Some evidence that the indicators of control (.18 & .19) are being used as a checklist to determine inclusion or exclusion but there is more to it

# Reporting Entity PS 1300

- Do not forget .09 -.16
- For example, 1300.14 notes you can govern by:
  1. Establishing purpose or eliminate or restrict ability to make decisions by predetermining those policies
  2. Directing policies on an ongoing basis
  3. Vetoing, overruling or modifying policies

# Reporting Entity PS 1300

- Para. .18 and .19 are provided to assist you in determining if in certain circumstances you meet .08 & .14
- May establish conduct but governed by publicly-elected or self-sustaining board or you may appoint board but not govern the policies



# Reporting Entity PS 1300

Government business enterprises

Definition remains the same four criteria

- Separate legal entity
- Authority to carry on a business
- Sells goods and services outside the entity
- Maintain operations from revenues

# Reporting Entity PS 1300

## Accounting for organizations

- Still full consolidated BUT with two exceptions
- Exceptions are GBEs and SUCH sector
- Accounted for with modified equity
- GBEs continue with modified equity
- SUCH modified equity until April 1, 2008 then consolidate (.47)

# Reporting Entity PS 1300

- Use of modified equity for SUCH is permitted for organizations that (.49):
  1. Separate legal entities
  2. Have a defined service area
  3. Appointed or elected board
  4. Significant restrictions on access to net assets

# Reporting Entity PS 1300

## Trusts

- Definition stays the same
- Required disclosure only

# GAAP PS 1150

- Reasons for project
  1. Acceptance of PSA Handbook as GAAP
  2. Needed to define GAAP
  3. Needed to provide additional guidance when silent

# GAAP PS 1150

- Replaces:
  - OBJECTIVES OF FINANCIAL STATEMENTS – LOCAL GOVERNMENTS, paragraph PS 1700.44
  - FINANCIAL STATEMENT PRESENTATION – FEDERAL, PROVINCIAL & TERRITORIAL GOVERNMENTS, paragraph PS 1200.014

# GAAP PS 1150

.03 defines GAAP as:

GAAP encompass broad principles and conventions of general application, as well as rules and procedures that determine accepted accounting practices at a particular time

# GAAP PS 1150

## PSA HANDBOOK

Primary sources of GAAP should be consulted first when determining the accounting and reporting for a particular accounting issue



# GAAP PS 1150

- Primary sources are:
  - PSA Handbook sections 1200-3800
  - Public sector guidelines (PSGs)
  - Appendices and illustrative material of PSA Handbook sections and PSGs
- Formalizes status of PSA Handbook

# GAAP PS 1150

When the primary sources of GAAP are silent, the government should adopt accounting principles that are:

- consistent with primary source of GAAP; and
- consistent with conceptual framework; and determined using professional judgment

# GAAP PS 1150

- No listing of “other sources of GAAP”
- Different approach to existing material
- Any perceived ranking/hierarchy of other sources (e.g. public sector practices) removed
- Any source of GAAP can be considered – must meet criteria.

# GAAP PS 1150

- Financial statements prepared in accordance with regulatory, legislative or contractual requirements – only GAAP if compliant with proposed Section

# GAAP – Italicized vs. Non

Non-italicized text is equal to italicized

- Currently: italics = recommendation, non-italics = guidance
- Users paying more attention to italicized
- ED elevates status of non-italics = italics
- Interpreting issues: select the treatment that is most consistent with the italicized paragraphs.

# Current Projects Underway

- Tangible Capital Assets
- Government Transfers
- Financial Instruments
- Segment Disclosures
- Performance Reporting

# Tangible Capital Assets

## Capital Assets for Local Governments

- The Public Sector Accounting (PSA) Handbook does not currently provide standards for accounting for capital assets for local governments
- Tangible capital assets represent a significant investment. Information on capital assets is vital for stewardship, accountability, costing and developing asset management plans including ongoing maintenance and replacement requirements.

# Tangible Capital Assets

- In June 2005, PSAB approved associate drafts of:
  - Section PS 3150, *Tangible Capital Assets*
    - ~ establishes standards on how to account for and report tangible capital assets; and
  - A Public Sector Guideline, *Tangible Capital Assets of Local Governments*
    - ~ provides guidance on presenting information in notes or schedules related to tangible capital assets.
- These drafts have been reviewed by the School Board Reporting Entity Group to ensure input from the school board perspective is received by PSAB.



# PS 3150 Tangible Capital Assets

Start by defining a TCA

TCAs are non-financial assets having physical substance that meet ALL of the following:

- held for use, for rental to others, for administrative or maintenance of other acquired, constructed or developed assets
- have been acquired for use on a continuing basis
- economic useful lives beyond an accounting period
- not intended for sale

# PS 3150 The Stock of TCAs

- **Tangible capital assets should be accounted for and reported as assets** in the statement of financial position
- Betterments included in the stock
- “Contributed” assets included in the stock
- Stock includes infrastructure such as roads, bridges, water and sewer systems etc.

# PS 3150 Works of Art etc.

- Works of art and historical treasures (statues) are excluded from the stock of TCAs
- Argue that they cannot be recognized because a reasonable estimate of the benefits cannot be made
- Existence required to be disclosed

# PS 3150 The Value of TCAs

- **Measurement at historical cost**
- Recognized that we may need estimates of historical costs to get started

# PS 3150 What is Cost?

- Need to define what is included in the cost to be reported

Cost is the amount of consideration given up to acquire, construct or better and **includes costs directly attributable to the asset** including carrying costs such as installation

Cost of contributed assets = fair value

# PS 3150 Components

- Assets acquired in a single purchase the cost is allocated to each component based on fair values
- Complex systems comprised of many components the level of detail you choose to keep is up to you
- More detail equates to better cost information i.e., useful lives and costs

# PS 3150 Capitalization of Interest

- Permits capitalization of interest during construction when you have a policy to do so
- Consider the directly attributable aspect of the definition of cost i.e., borrow generally or specifically
- Capitalize interest on all TCAs financed

# PS 3150 Betterments

- It is the cost incurred to enhance service potential represented by increased capacity, operating costs are lowered, useful life is extended or quality of output is improved



# PS 3150 Accounting for Use

- Amortization should be accounted for as expense in the statement of financial activities
- Amortized in a rationale and systematic manner
- Amortize the cost less any residual value

# PS 3150 Useful life

- Depends on expected use
- Just because the physical attributes of an asset may last a long period is NOT justification for establishing a useful life beyond the EXPECTED useful life
- Factors to consider include wear and tear from use, maintenance program, past experience
- Regular reviews of useful life

# PS 3150 Write-down

- **Determine when** to write down i.e., how the asset is used, technological developments, physical damage, removal decline in service
- **Determine the amount** is an issue the private sector uses cash flows but public sector reflects service potential
- **Adjusts the original cost** not NBV
- Permanent decline in value no reversal of write-down

# PS3150 Disposals

- Revenue from disposal will no longer equal proceeds
- Difference between proceeds and carrying value can be revenue (gain) or expense (loss)
- Any revenue or expense recorded in the statement of financial activities

# Government Transfers

Amendments to Section PS 3410, *Government Transfers*, needed to address application and interpretation issues raised by the government community.

# Government Transfers

## Issues:

- resolving the debate over the appropriate accounting for multi-year funding provided by governments;
- clarifying the degree to which stipulations imposed by a transferring government should impact the timing of recognition of the transfer by both the transferor and recipient governments; and
- addressing the appropriate accounting for capital transfers received under an expense-based accounting regime

# Financial Instruments

- Purpose of the project - develop accounting standards for the recognition, de-recognition, measurement, presentation and disclosure of financial instruments in government financial statements

# Financial Instruments – Issues

- Recognition – establish criteria
- Measurement cost or fair value
- Adjustments for fair value – where
- Hedge accounting
- Disclosure requirements



# Financial Instruments - Approach

- Develop a survey to determine nature and extent of FI in the public sector in Canada
- Assess the applicability of the AcSB's work – in particular *Financial Instruments – Recognition and Measurement*
- Do NOT re-invent the wheel

# Segment Disclosures

- Reason for project - to help users of financial statements better understand the different types of activities that governments engage in.

# Segment Disclosures

Why have the project?

- Concerns re burying the financial statements of certain government organizations when fully consolidated
- New reporting entity definition – new organizations consolidated. Providing guidance about the relevant disclosures is important
- Consistency and comparability in disclosures

# Segment Disclosures

- The major issues are:
  - Defining segments for governments
  - Identifying the nature of additional information to be disclosed
  - Identifying the thresholds or quantitative levels for additional disclosures
  - Assessing current disclosure requirements for GBEs and other government organizations and determining how these relate to segment disclosures

# Performance Reporting

- Project objective - develop a core set of underlying economic performance measurement and reporting principles to be used as a guide in the development of more specific indicators of performance measurement – SORP
- Reason for project -
  - Initiatives are diverse and fragmented
  - Limitations of F/S information
  - Strengthening decision-making and accountability
- Second project – follows FSD&A

# Performance Reporting

Using 9 principles of Canadian Comprehensive Auditing Foundation (CCAF - 2002) as a starting point:

1. Focus on the few critical aspects of performance.
2. Look forward as well as back.
3. Explain key risk considerations.
4. Explain key capacity considerations.
5. Explain other factors critical to performance.
6. Integrate financial and non-financial information.
7. Provide comparative information.
8. Present credible information, fairly interpreted.
9. Disclose the basis for reporting.