ED 160 *Social Benefits*

Disclaimer

The views and opinions expressed in this presentation are those of the individual. Official positions of the ASB on accounting matters are determined only after extensive due process and deliberation.

Overview

- Project history and overview.
- Purpose of today.
- Overview of Exposure Draft
  - Objective
  - Scope
  - Insurance approach
  - Obligating event approach

History and overview

Project history and overview

Consultation Paper on Revenue and Non-exchange Expenses

2004 — ITC Social Policies of Government

2008 — ED 34 Social Benefits: Disclosure

Project Brief: Long Term Fiscal Sustainability

2013 — RPG 1 Long Term Sustainability Of an Entity's Finances

2015 — Consultation Paper: Recognition and Measurement of Social Benefits

2017 — ED 63: Social Benefits

Purpose of today

Objective and scope

What is the objective?

- Improve relevance and faithful representation of social benefits in financial statements.
- Help users to assess:
  - Nature of social benefits & key features of their operation.
  - Impact on financial position, performance and cash flows.

What is the scope?

- Applies to social benefits as defined.

What is a social benefit?	
Definition	**What does this mean?**
Social benefits are provided to:	Benefits can be in cash or in-kind.
Specific individuals or households who meet eligibility criteria;	Benefits to entities do not meet definition and where no eligibility criteria do not meet definition → non-exchange expenses project.
Mitigate the effect of social risks: and	Social risks are events or circumstances that: • Relate to the characteristics of individuals or households (e.g. age, health, poverty, employment status); and • Adversely affect the welfare of individuals or households, either by imposing additional demands on their resources or by reducing their income.
Address the needs of society as a whole; but	Meet the needs of society rather than a specific individual → distinguishing social benefit from insurance.
Are not universally accessible services	Universally accessible services are those that are made available by a government entity for all individuals or households to access, and where eligibility criteria (if any) are not related to social risk.

What is the scope?

Proposed Standard does not apply to:

- Financial instruments (IPSAS 29), e.g. concessionary loans.
- Employee benefits (IPSAS 39), e.g. employee pensions.
- Insurance contracts (relevant national or international accounting standard).
- Universally accessible services (as defined).

What is the scope?

Non-exchange expenses	Grants, Contributions and Other Transfers	• Grants to other public sector entities; grants to charities; disaster relief	
	Collective Services	• Defense; street lighting	
	Universally Accessible Services	• Universal education • Universal healthcare	GFS
ED 63	Social Benefits	• State pensions; unemployment benefits; income support	
Other IPSAS or IFRS	Employee Benefits	• Salaries; employee healthcare schemes; employee pensions	
	Contracts for Insurance	• Vehicle insurance; private medical insurance	
	Contracts for Goods and Services	• Purchase of goods; payment for services	

Source: IPSASB

Application locally?

In cash

Unemployment benefits.

Compensation for injury on duty and loss of income.

Road accident fund claims.

Social benefits (social development & SASSA).

National Home Builders Registration Council.

National Housing Finance Corporation.

National Student Financial Aid Scheme.

Rural Housing Loan Fund.

Social Housing Regulatory Authority.

Application locally?

<u>In kind</u>

Goods and services provided by municipalities (water and electricity to indigents, other – housing?)

Health.

Education.

Housing.

Views?

Specific matter for comment 1

Do you agree with the scope of the ED, specifically the exclusion of universally accessible services (BC21(c))?

What is the scope?

Specific matter for comment 2

Do you agree with the definitions of social benefits, social risks and universally accessible services?

Insurance approach

When is the approach applied?

- If a scheme satisfies certain criteria, an entity is permitted to recognise and measure R, E, A, L of the scheme by applying, by analogy, the requirements of international/national standard on insurance → only IFRS 17.
- If do not apply insurance approach, apply obligating event approach.

When is the approach applied?

Criteria:

- The scheme is intended to be fully funded from contributions; <u>and</u>
- Evidence that the entity manages the scheme in the same way as an issuer of insurance contracts, including assessing the financial performance and financial position of the scheme on a regular basis.

When is the approach applied?

Criterion # 1 Fully funded by contributions:

- Legislation or equivalent indicates that scheme to be funded by contributions or levies paid by or on behalf of beneficiaries, together with investment returns arising from the contributions; <u>and</u>
- One or more or both of the following indicators apply:
  (a) Contribution rates are regularly reviewed, or when specified criteria are met → ensure revenue sufficient to fully fund social benefit scheme.
  (b) Benefit levels are regularly reviewed or when specific criteria met → ensure level of benefits provided will not exceed level of funding available from contributions.

When is the approach applied?

Criterion 2 # Managing the scheme in the same way as an insurer:

Scheme has commercial substance, and except legislative vs contractual origins, has the “look and feel” of an insurance contract. Consider the following indicators:

a) Is the entity bound by the scheme in a similar way as an insurer by an insurance contract? The same if the entity’s ability to amend the scheme is limited to:

- Circumstances prescribed in legislation that establish the scheme.
- When a government is setting new contribution rates.

When is the approach applied?

Criterion # 2 Managing the scheme in the same way as an insurer

b) Are assets held in a separate fund, or otherwise earmarked, or restricted to being used to provide social benefits?

c) Does the legislation give the participants enforceable rights if the social risk occurs?

d) Financial performance and position of scheme are assessed on a regular basis where it is required to report internally on the scheme, and where necessary, to take action to address under-performance.

e) Is there a separate entity? (Not a requirement of IFRS 17)

What is the insurance approach?

What is an insurance contract?

A contract under which one party accepts significant insurance risk from another party (the policyholder) by agreeing to compensate the policyholder if a specified uncertain future event adversely affects the policy holder.

What is the insurance approach?

Recognise a group of insurance contracts at earliest of:

- Beginning of coverage period.
- Date when first payment from policyholder due.
- When the group becomes onerous.

What is the insurance approach?

Two approaches:

- Building blocks.
- Premium allocation approach → simplified approach to use in specific circumstances, primarily contract is 1 year or less.

Building blocks approach

Initial measurement	
Fulfilment cash flows	PV of future cash outflows minus PV of future cash inflows.
Estimates of future cash flows	Amount, timing and uncertainty of cash flows on probability weighted basis, about current and future conditions at measurement date, from entity perspective except where market variables used, for CF within contract boundary.
Adjustment for TVM and financial risks (if not in cash flows)	Reflect characteristics of CF and liquidity of contract, consistent with observable market prices for FI with similar timing, currency and liquidity.
Adjustment for non-financial risk	Compensation required for uncertainty about amount and timing of CF for non-financial risk.
Contractual service margin	Unearned profit to be recognised as service provided = fulfilment cash flows, derecognition of insurance acquisition costs, cash flows arising from contracts.
Total	

Building blocks approach

Subsequent measurement	
Liability for the remaining coverage period	Entity's obligation to investigate and pay valid claims under existing contracts for insured events that have not yet occurred (obligation for unexpired portion of coverage period)
Fulfilment cash flows	PV of future cash outflows minus PV of future cash inflows (determined as for initial measurement)
Contractual service margin	Includes new contracts, interest on margin, changes in fulfilment cash flows, amount recognised for services provided.
Liability for incurred claims	Obligation to investigate and pay valid claims for insured events that have occurred, plus events occurred but no claim, plus other expenses
Total	

Premium allocation

Initial measurement	
Liability for remaining coverage period	
Premiums received	Only if received on recognition
Minus insurance acquisition costs, unless recognised as an expense	Costs of selling, underwriting and starting a group of insurance contracts and are directly attributable to the portfolio of contracts.
Plus/minus derecognition of asset or liability related to acquisition costs	
Total	

Premium allocation

Subsequent measurement	
Liability for remaining coverage period	
Opening balance	
Premiums received	Only if received on recognition
Minus insurance acquisition costs, unless recognised as an expense	Same as previous.
Plus/minus amortisation of asset or liability related to acquisition costs	
Plus adjustment for financing component	TVM and financial risk, but ignore if contract less than a year
Minus insurance revenue recognised	Based on coverage for the period
Minus investment component paid	
Liability for incurred claims	Same as previous.
Total	

What is disclosed?

Objective is to give users a basis to assess the effect that social benefits may have on financial position, performance and cash flows [para 10]:

(a) Basis for determining that insurance approach appropriate.

(b) Information required by IFRS 17.

(c) Any additional information.

[para 11]

What is disclosed?

"Any additional information" [para 12]:

(a) Characteristics of the scheme, including:

- (i) Nature of benefits provided (e.g. retirement, unemployment);
- (ii) Key features of the scheme (description of legislation, summary of main eligibility criteria).

(b) Description of significant amendments to the social benefit scheme made during the reporting period:

- (i) Changes to social benefits provided.
- (ii) Changes to eligibility criteria, or the individuals or households covered.

Views?

Specific matter for comment 3

Do you agree that, with respect to the insurance approach:

(a) It should be optional;

(b) The criteria for determining when the insurance approach may be applied;

(c) Directing preparers to apply IFRS 17 is appropriate; and

(d) The additional disclosures in paragraph 12 are appropriate?

Transitional provisions

Apply IFRS 17.

Obligating event approach

How is the approach applied?

Recognition of liability for social benefit scheme

Overarching principle:

- Present obligation for an outflow of resources that results from a past event; and
- Presentation obligation can be measured in a way that achieves the QCs and takes account of constraints in GPFRs.

How is the approach applied?

Recognition of liability for social benefit scheme

- Liability must involve an outflow of resources.
- Past event is the satisfaction by the beneficiary of all eligibility criteria for the next benefit, which includes being alive (whether an explicit or implicit criterion of the scheme).

How is the approach applied?

Recognition of an expense

- An entity shall recognise an expense for a social benefit scheme at the same point that is recognises a liability.
- Do not recognise an expense for a social benefit scheme where a social benefit is provided prior to all the eligibility criteria being satisfied → recognise as a payment in advance unless the amount is irrecoverable.

How is the approach applied?

Initial measurement of liability

- An entity shall measure the social benefit scheme at the best estimate of the costs that the entity will incur in fulfilling the present obligations represented by the liability.

How is the approach applied?

Initial measurement of liability

- The best estimate is:
  - The maximum amount = costs to fulfil the present obligations until the next point at which the eligibility criteria is required to be satisfied → the satisfaction of eligibility criteria affects recognition and not measurement [19,20]
  - Takes into account the possible effect of subsequent events on the level of benefits to be provided [21]
  - If not settled wholly before 12 months after end of reporting date, discount [22].

How is the approach applied?

Initial measurement of liability

- The best estimate is:
  - Discount rate reflects the time value of money. The currency and term of the financial instrument selected shall be consistent wit the social benefit liability [27].

How is the approach applied?

Subsequent measurement of liability

- Liability to be reviewed at each reporting date, and adjusted to reflect the current best estimate [26].
- Liability for social benefit scheme reduced as social benefits are provided [24].
- Any difference between the cost of providing social benefit and the carrying amount of the liability is recognised in surplus or deficit i.a.w. IPSAS 3 [24].
- Where discounted, liability is increased and interest expense recognised in each reporting period until the liability is settled, to reflect unwinding of the discount [25].

How is the approach applied?

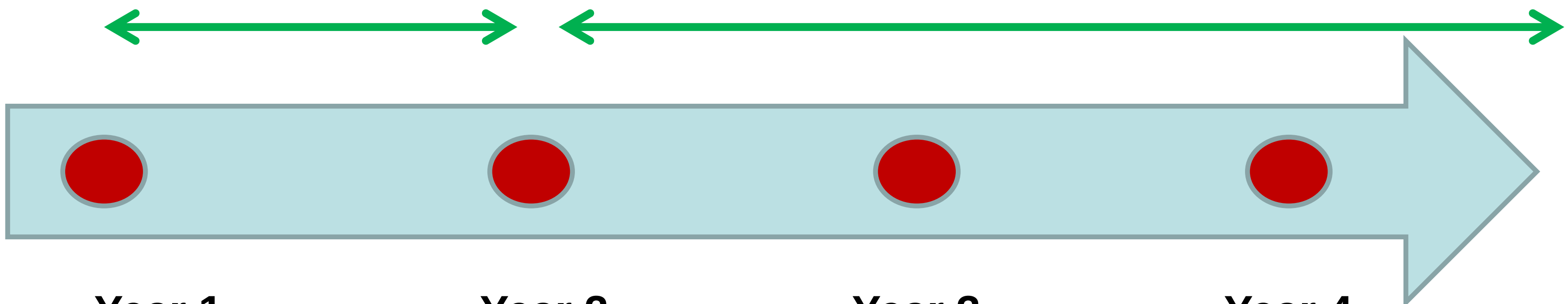
Measurement of an expense for a social benefit scheme

- Expense is equivalent to the amount of the liability measured.

Practical application

Extent of obligation recognised

Disclosure of year 2-6



Year 1
First meet all eligibility criteria
Age
SA citizen
Means test

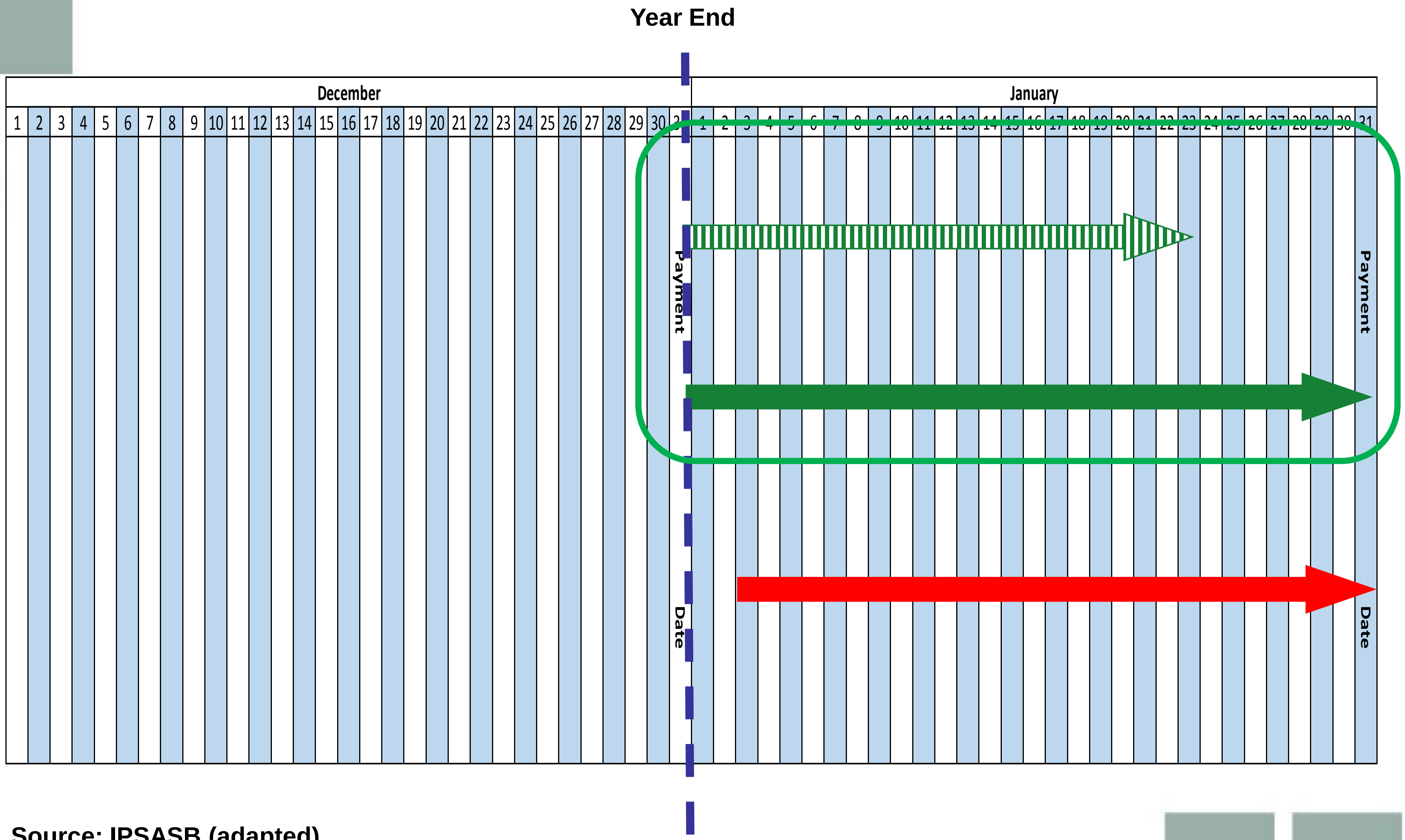
Year 2
Revalidate eligibility criteria
Still alive
SA citizen
Means test

Need not be explicit requirement of scheme

Year 3
Revalidate eligibility criteria
Still alive
SA citizen
Means test

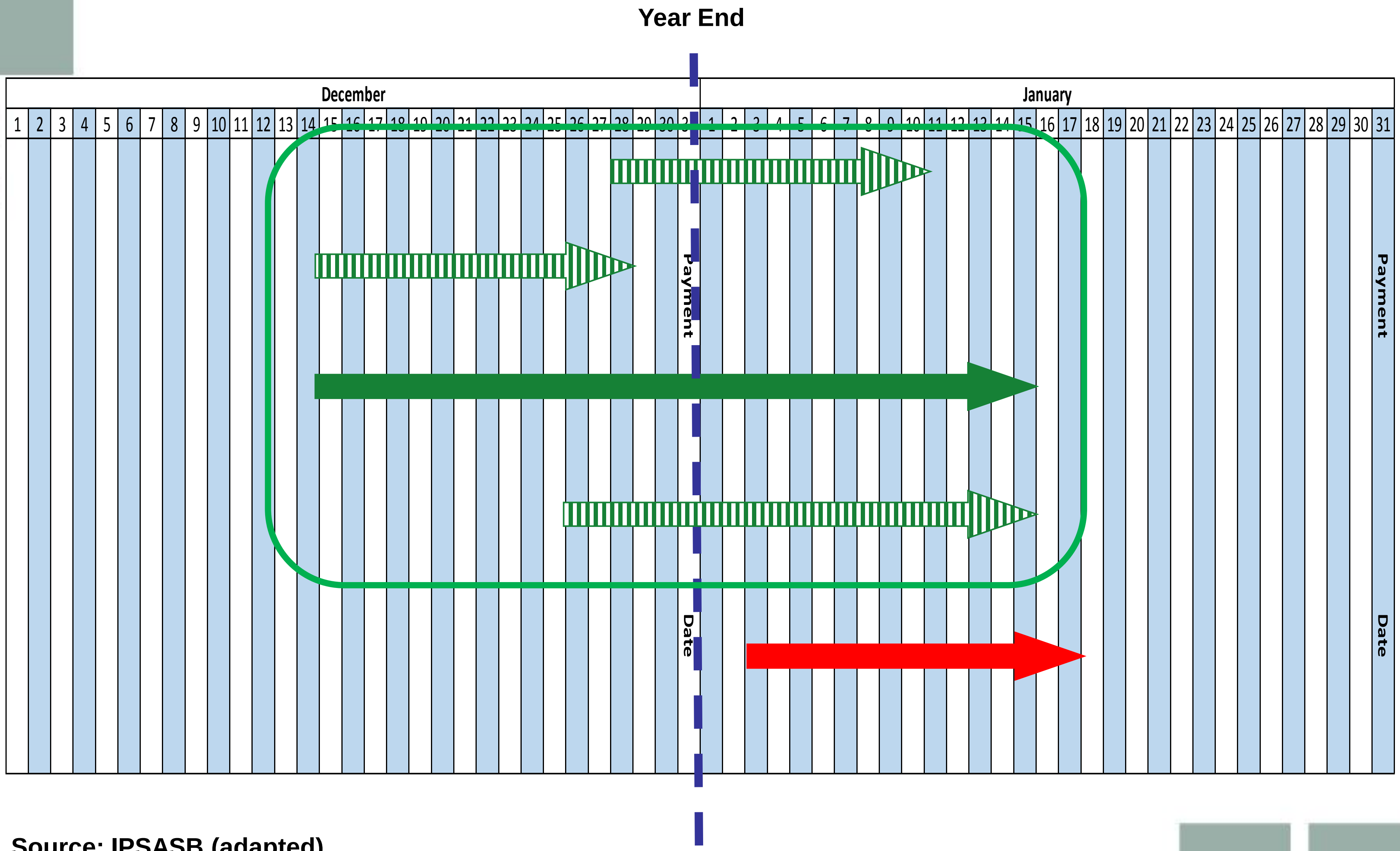
Year 4
Revalidate eligibility criteria
Still alive
SA citizen
Means test

Practical application



Source: IPSASB (adapted)

Practical application

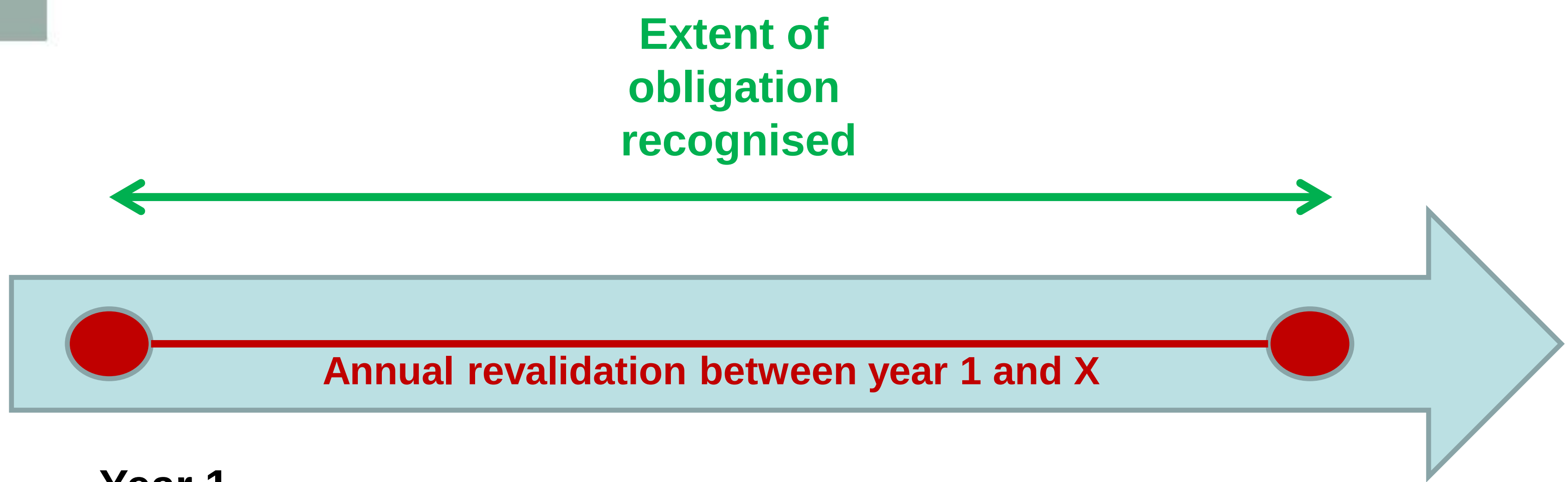


Source: IPSASB (adapted)

Alternative views?

- The obligating event is dependent on the economic substance of the scheme.
- The approach to treating all schemes the same is inconsistent with the Framework.
- “Being alive” is a measurement and not a recognition criterion.

Alternative views?



Year 1

First meet all eligibility criteria
Age 60
SA citizen
Means test

Year X

No more benefits due
Death
No longer satisfy means test

What is disclosed?

- Objective is to give users a basis to assess the effect that social benefits may have on financial position, performance and cash flows [para 29]
- An entity discloses information that:
  - Explains the characteristics of its social benefit schemes
  - Identifies and explains amounts in the financial statements
  - Quantifies and explains future cash flows [para 30]

What is disclosed?

#1 Information about characteristics of the scheme:

(a) Nature of benefits provided (retirement, unemployment).

(b) Key features of the scheme (legislative framework, e.g. eligibility criteria).

(c) Description of how scheme is funded (budget appropriation, transfer from another entity). If funded by contributions:

(i) a cross reference to where information can be found on those social contributions in the entity's FS.

(ii) statement on the availability of information on the contributions and dedicated assets in another entity's FS. [para 30]

What is disclosed?

#1 Information about characteristics of the scheme:

(d) Description of significant amendments to scheme, along with expected effect of amendments on future obligations. Amendments include:

- Changes to the level of social benefits provided.
- Changes to the eligibility criteria, or to the individuals or households covered. [para 31]

What is disclosed?

#2 Explanation of amounts in the financial statements:

- Where liability not expected to be settled by the end of the next reporting period, disclose significant assumptions used to determine the present value, including the basis on which discount rate determined. [32]
- Total expense recognised in the statement of financial performance, and reconciliation of the opening and closing balances of the liability for each scheme:… [33]

What is disclosed

#2 Explanation of amounts in the financial statements:

- Liabilities and expenses recognised in the period, comprising:
  - Amounts recognised in the reporting period
  - Changes in accounting estimates
  - Interest expense
- Prepayments.
- Liabilities settled during the reporting period. [33]

What is disclosed?

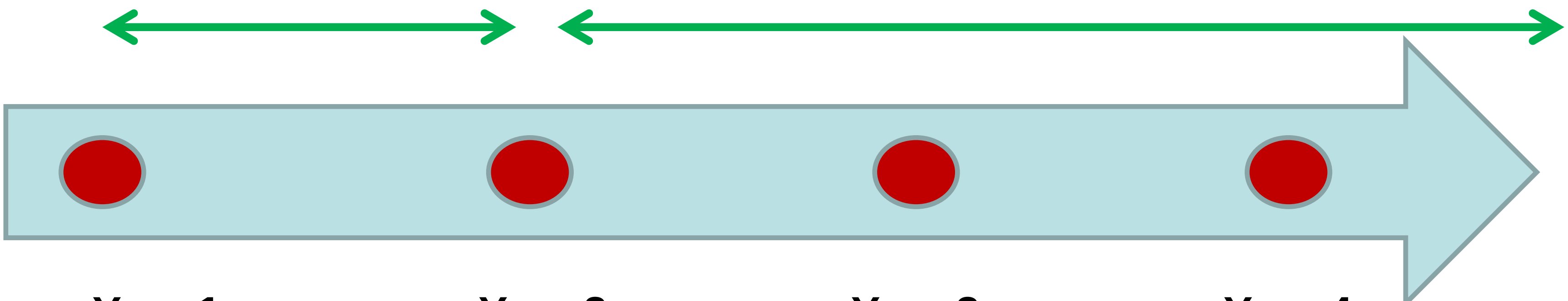
#3 Explanation of future cash flows that may arise from social benefit schemes :

- For each social benefit scheme:
  - Best estimate of the undiscounted projected cash outflows that will arise in each of the 5 reporting periods immediately following the reporting date. Not limited to current beneficiaries.
  - Key assumptions that an entity has relied on in making its best estimate of the projected cash outflows. [para 34]

Practical application

Extent of obligation recognised

Disclosure of year 2-6
Undiscounted cash flows
Existing and new participants



Year 1
First meet all eligibility criteria
Age
SA citizen
Means test

Year 2
Revalidate eligibility criteria
Still alive
SA citizen
Means test

Year 3
Revalidate eligibility criteria
Still alive
SA citizen
Means test

Year 4
Revalidate eligibility criteria
Still alive
SA citizen
Means test

Discounted (if material)
Only current participants

Transitional provisions

Retrospectively, applying IPSAS 3.

Other reporting?

Long terms sustainability of an entity’s finances:

Entities are encouraged, but not required, to prepare GPFRs that provide guidance on the long term sustainability of an entity’s finances.

Views?

Specific matter for comment 4

Do you agree that, under the obligating event approach, the past event that gives rise to a liability for a social benefit scheme is the satisfaction by the beneficiary of all eligibility criteria for the next benefit, which includes being alive (whether this is explicitly stated or implicit in the scheme provisions)?

If not, what past event should give rise to a liability for a social benefit?

Views?

Specific matter for comment 5

Regarding the disclosure requirements for the obligating event approach, do you agree that:

(a) The disclosures about the characteristics of an entity’s social benefit schemes (para 31) are appropriate?

(b) The disclosures of the amounts in the financial statements (para 32-33) are appropriate?

Contd…

Views?

Specific matter for comment 5

Regarding the disclosure requirements for the obligating event approach, do you agree that:

(c) For the future cash flows related to an entity's social benefit schemes (para 34):

(i) It is appropriate to disclose the projected future cash flows; and

(ii) Five years is the appropriate period over which to disclose those future cash flows?

Views?

Specific matter for comment 6

RPG 1 on *Reporting on the Long Term Sustainability of an Entity's Finances,* developed to provide information on social benefits that cannot be addressed in GPFSs.

The IPSASB discussed whether this type of reporting should be mandatory.

Should the IPSASB undertake further work on LTFS, and if yes, how?

Any new developments of perspectives that would be relevant to the IPSASB's work?

Submitting comments

Due date 2 March 2018

Visit our website for more information on these Exposure Drafts

www.asb.co.za

Submit your comments to info@asb.co.za

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