

Swiss Comment to

CP Recognition and Measurement of Social Benefits

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1. Introduction

The Swiss Public Sector Financial Reporting Advisory Committee (SRS-CSPCP) was established in 2008 by the Swiss Federal Ministry of Finance together with the cantonal Ministers of Finance. One of its aims is to provide the IPSAS Board with a consolidated statement for all three Swiss levels of government (municipalities, cantons and Confederation).

The SRS-CSPCP has discussed the *Consultation Paper Recognition and Measurement of Social Benefits* and comments as follows.

2. General Remarks

The SRS-CSPCP regards this CP basically as positive. The issue of social benefits is complex. Therefore the text is also often difficult to figure out. But the paper is organized comprehensibly and clearly. This CP provides us with a consistent basis for a future standard on social benefits. Such a consistent basis is necessary since the amounts of liabilities with respect to social benefits can be extremely high. A future standard must offer feasible solutions, which best reflect the economic reality, even if one already knows that it may sometimes be very difficult.

With that in mind and in view of all the possible options, which still remain to be decided upon, at this point the view expressed by the SRS-CSPCP cannot be regarded as final. As a consequence, the SRS-CSPCP reserves the right to reconsider its position regarding the answer it gives to the following specific matters for comment. As a matter of fact, its position may be revised after the IPSASB launches the next step in the discussion for the drawing up of a standard about social benefits.

3. Preliminary View 1 – Scope and Definitions

Social Benefits are benefits provided to individuals and households, in cash or in kind, to mitigate the effect of social risks.

The other key definitions are as follows:

(a) **Social risks** are events or circumstances that may adversely affect the welfare of individuals and households either by imposing additional demands on their resources or by reducing their income.

Social benefits are provided to mitigate social risks in the following circumstances:

- Households could receive benefits when they meet certain eligibility criteria that originate from a social risk without making any contributions;
- Households could make contributions and receive benefits in the event of the occurrence of the specified social risks; and
- Households could make contributions to a scheme to accumulate entitlements to future benefits, with the benefits being provided following the occurrence of the specified social risk.

(b) **Social Benefits in Cash** are social benefits paid in cash, by or on behalf of a public sector entity, that allow individuals and households to use this cash indistinguishably from income from other sources. Social benefits in cash do not include reimbursements.

(c) **Social Benefits in Kind** are goods and services provided as social benefits to individuals and households by or on behalf of a public sector entity, and all reimbursements for the costs incurred by individuals and households in obtaining such goods and services.

(d) **Reimbursements** are cash payments made as a social benefit by or on behalf of a public sector entity to compensate a service provider or an individual or household for all or part of the expense incurred or to be incurred by that individual or household in accessing specific services.

(e) **Social Insurance** is the provision of social benefits where the benefits received are conditional on participation in a scheme, evidenced by way of actual or imputed contributions made by or on behalf of the recipient. Social insurance may form part of an employer-employee relationship (employment-related social insurance) or may arise outside an employer-employee relationship (social security).

(f) **Social Security** is social insurance that arises outside of an employer-employee relationship, and provides benefits to the community as a whole, or large sections of the community. Social security is imposed and controlled by a government entity.

(g) **Social Assistance** is the provision of social benefits to all persons who are in need without any formal requirement to participate as evidenced by the payment of contributions.

3.1. Specific Matter for Comment 1

In your view:

(a) Is the scope of this CP (i.e., excluding other transfers in kind, collective goods and services, and transactions covered in other IPSASs) appropriate?

(b) Do the definitions in Preliminary View 1 provide an appropriate basis for an IPSAS on social benefits?

Please explain the reasons for your views.

- (a) In its Comments on the *Consultation Paper IPSASs and Government Finance Statistics Reporting Guidelines* of December 2012 the SRS-CSPCP stated that convergence of IPSASs with the GFS is desirable. Therefore the SRS-CSPCP welcomes the idea that the scope of this CP should be consistent with the definition of social benefits in Government Finance Statistics (GFS). The scope of this CP is actually in line with the definition of social benefits under GFS. This is something the SRS-CSPCP strongly supports.

It would, however, like to point out that the content of the box "Employment related Social Insurance" in Diagram 2 (page 26) should be more specific. The wording should better reflect that this box concerns the case in which the public entity (e.g. a government) acts as employer. In other words, the considerations listed in the text (§ 2.34 or better § 2.18) should be better emphasised in the diagram.

- (b) The SRS-CSPCP is of the opinion that the proposed definitions provide an appropriate basis for a standard on social benefits.

4. Preliminary View 2 – Identification of approaches

The IPSASB considers that a combination of option 1 (obligating event approach) and (for some or all contributory schemes) option 3 (insurance approach) may be required to reflect the different economic circumstances arising in respect of social benefits. The IPSASB does not consider that option 2 (social contract approach) is consistent with the Conceptual Framework. For this reason, the IPSASB has taken the preliminary view that the social contract approach is unlikely to meet the objectives of financial reporting.

4.1. Specific Matter for Comment 2

(a) Based on your review of Chapters 4 to 6, which approach or approaches do you support?

(i) The obligating event approach;

(ii) The social contract approach; and

(iii) The insurance approach.

Please provide reasons for your views, including the conceptual merits and weaknesses of each option; the extent to which each option addresses the objectives of financial reporting; and how the different options might provide useful information about the different types of social benefit.

(b) Are you aware of any additional approaches to accounting for social benefits that the IPSASB should consider in developing an IPSAS? If yes, please describe such approach(es) and explain the strengths and weaknesses of each.

(a) The SRS-CSPCP would not like to commit itself to one single approach. Indeed, the choice of approach over another very much depends on the nature of the considered social benefit. On the whole the SRS-CSPCP, like the IPSAS Board, believes that Approaches 1 and 3 should be used. To name the advantages and disadvantages of the individual approaches is a difficult task. To a great extent they depend on the system which actually provides social assistance and social security. Consequently, the comments below are to be considered with care, when it is a question of determining which option should be applied for which system. It is common to all approaches that their use is relatively complicated; but this is a result of the complexity of the issue. As mentioned the SRS-CSPCP, like the IPSAS Board, is of the opinion that the second approach (social contract approach) should not be used. Therefore, the question arises how future social benefits under the pay-as-you-go system can be recognised. This issue arises above all at the level of the central government (Confederation), where the old age and survivors' pension scheme (AHV) together with the disability insurance scheme (IV) are substantial financial issues.

(i) *The obligation event approach*

This approach has the advantage that the resulting liability can be recognized at various times. However, this gives rise to a very wide range in the estimate of the amount of the liability, which in turn is a disadvantage. In addition, no particular attention is given to the financing aspects, because only liabilities are recognized.

(ii) *The social contract approach*

This approach sounds really appealing, but is difficult to implement. In addition, it is really justified only for social benefits, for which the pay-as-you-go system applies.

(iii) *The insurance approach*

This approach could be used for various social insurances in Switzerland, because they are only financed by contributions (schemes primarily financed by contributions).

(b) The SRS-CSPCP does not wish any further approaches to accounting for social benefits.

4.2. Specific Matter of Comment 3

Having reviewed the three options in Chapters 4 to 6, are you aware of any social benefits transactions that have not been discussed in the CP, and which could not be addressed by one or more of the options set out in the CP?

If so, please provide details of the social benefit transactions you have identified and explain why the options set out in the CP do not adequately cover these transactions.

The SRS-CSPCP is not aware of any additional social benefits, which should be discussed in the CP.

5. Obligating Event Approach

5.1. Specific Matter for Comment 4

In your view, at what point should a future IPSAS specify that an obligating event arises under the obligating event approach? Is this when:

(a) Key participatory events have occurred;

(b) Threshold eligibility criteria have been satisfied;

(c) The eligibility criteria to receive the next benefit have been satisfied;

(d) A claim has been approved;

(e) A claim is enforceable; or

(f) At some other point.

In coming to this conclusion, please explain what you consider to be the relative strengths and weaknesses of each view discussed in this chapter.

If, in your view, a future IPSAS should consider that an obligating event can arise at different points depending on the nature of the social benefit or the legal framework under which the benefit arises, please provide details.

Please explain the reasons for your views.

The SRS-CSPCP is of the opinion that the *obligating event* determines at which point in time a liability should be recognised in the financial statements. None of the options should be discarded. However the chosen option should fulfil the *qualitative characteristics of the Conceptual Framework*. Thus none of the options should be selected arbitrarily. The SRS-CSPCP proposes that a liability should, where possible, be estimated at point (a). If this is not possible (because the *qualitative characteristics* are not fulfilled), point (b) can be considered and so on until point (e). Following such a procedure, while arbitrariness in the choice of the point of recognition cannot completely be excluded, it is at least reduced. The SRS-CSPCP does not see further points in time where a liability could be recognized, and therefore option (f) drops out.

5.2. Specific Matter for Comment 5

In your view, does an obligating event occur earlier for contributory benefits than non-contributory benefits under the obligating event approach?

Please explain the reasons for your views.

The SRS-CSPCP is of the opinion that the *obligating event* does not depend on the way social benefits are financed. Consequently it is irrelevant to identify the obligating event whether the social benefit concerned is financed with or without contributions.

5.3. Specific Matter for Comment 6

In your view, should a social benefit provided through an exchange transaction be accounted for:

(a) In accordance with a future IPSAS on social benefits; or

(b) In accordance with other IPSASs?

Please provide any examples you may have of social benefits arising from exchange transactions.

Please explain the reasons for your views.

The SRS-CSPCP prefers Solution (a), i.e. social benefits with a specific exchange transaction should also be dealt with in a future new standard on social benefits. There are some instances for that in Switzerland : the obligatory accident insurance and (very specific to Switzerland) the military insurance, in which everyone is insured, who performs military, civil defence or community service or takes part in assignments of the Swiss Corp for Humanitarian Aid and the Confederation's peace keeping missions and good services.

Preliminary View 3 – obligation event approach (cost of fulfillment)

Under the obligating event approach, liabilities in respect of social benefits should be measured using the cost of fulfillment. The cost of fulfillment should reflect the estimated value of the required benefits.

5.4. Specific Matter for Comment 7

In your view, under the obligating event approach, when should scheme assets be included in the presentation of a social benefit scheme:

(a) In all cases;

(b) For contributory schemes;

(c) Never; or

(d) Another approach (please specify)?

Please explain the reasons for your views.

The SRS-CSPCP believes that assets associated with social benefits, whatever the insurance system, must be recognized in the financial statements. It therefore supports Option (a). However, depending on the approach used (obligation event approach, social contract approach, insurance approach), this option is expected to be difficult to implement.

6. Social Contract Approach

6.1. Specific Matter for Comment 8

In your view, under the social contract approach, should a public sector entity:

(a) Recognize an obligation in respect of social benefits at the point at which:

(i) A claim becomes enforceable; or

(ii) A claim is approved?

(b) Measure this liability at the cost of fulfillment?

Please explain the reasons for your views.

The SRS-CSPCP is unable to find a meaningful answer to this question. But as this approach is not approved, the answer is otiose.

7. Insurance Approach

7.1. Specific Matter for Comment 9

Do you agree with the IPSASB's conclusions about the applicability of the insurance approach?

Please explain the reasons for your views.

The SRS-CSPCP is of the opinion that the measurements in the *insurance approach* are complicated. Social benefits are not contracts. Instead, in many cases, there is personal right grounded on a legal basis, e.g. obligatory non-occupational accident insurance.

Therefore SRS-CSPCP agrees with the IPSAS Board, which in paragraph 6.24 states that this approach is not appropriate for all social benefits, but can be used only in conjunction with another approach.

7.2. Specific Matter for Comment 10

Under the insurance approach, do you agree that where a social security benefit is designed to be fully funded from contributions:

(a) Any expected surplus should be recognized over the coverage period of the benefit; and

(b) Any expected deficit should be recognized as an expense on initial recognition?

Please explain the reasons for your views.

In the opinion of the SRS-CSPCP over a long period surpluses and deficits should balance out and therefore the same method must be used in recognising them. The SRS-CSPCP is of the opinion that the insurance approach should be designed in accordance with the standards for private insurance contracts applicable in the future (successor standard to IFRS 4).

7.3. Specific Matter for Comment 11

In your view, under the insurance approach, what is the appropriate accounting treatment for the expected deficit of a social security benefit that is not designed to be fully funded from contributions:

- (a) Recognize an expense on initial recognition;*
- (b) Recognize the deficit as an expense over the coverage period of the benefit;*
- (c) Offset the planned subsidy and the liability only where this is to be received as a transfer from another public sector entity;*
- (d) Offset the planned subsidy and the liability irrespective of whether this is to be received as a transfer from another public sector entity or as an earmarked portion of general taxation; or*
- (e) Another approach?*

Please explain the reasons for your views.

The SRS-CSPCP is of the opinion that (a) is the correct way. This is consistent with the position adopted by the SRS-CSPCP that future tax revenues may not be recognized and therefore also not set off; on the other hand benefit obligations should be accrued. Alternative (b) drops out, because the SRS-CSPCP does not believe that the accrual is dependent on the way of financing (cf. also response to Question 5). Alternatives (c) and (d) drop out, because future tax revenues may not be recognized.

The SRS-CSPCP wishes that the IPSAS Board explains in a future ED with the aid of an example how these alternatives are to be applied.

7.4. Specific Matter for Comment 12

In your view, under the insurance approach, should an entity use the cost of fulfillment measurement basis or the assumption price measurement basis for measuring liabilities?

Please explain the reasons for your views.

The SRS-CSPCP is of the opinion that the liabilities should be measured on the basis of *fulfillment costs*, because there is no active market.

7.5. Specific Matter for Comment 13

Do you agree that, in those cases where the link between contributions and benefits is not straightforward, the criteria for determining whether the insurance approach is appropriate is:

- The substance of the scheme is that of a social insurance scheme; and*
- There is a clear link between the benefits paid by a social security scheme and the revenue that finances the scheme.*

If you disagree, please specify the criteria that you consider should be used.

Please explain the reasons for your views.

The SRS-CSPCP agrees with this statement.

7.6. Specific Matter for Comment 14

Do you support the proposal that, under the insurance approach, the discount rate used to reflect the time value of money should be determined in the same way as for IPSAS 25?

Please explain the reasons for your views.

The SRS-CSPCP supports this proposal. In IPSAS 25 a method has already been proposed. Therefore there is no reason to determine the discount rate in a different way.

7.7. Specific Matter for Comment 15

Under the insurance approach, do you support the proposals for subsequent measurement set out in paragraphs 6.73–6.76?

Please explain the reasons for your views.

The SRS-CSPCP agrees in principle with most proposals in paragraphs 6.73 to 6.76, apart from the last *bullet point* in paragraph 6.73: changes to the discount rate should not be recognized in the statement of financial performance, but, similarly to IPSAS 25, over equity (or OCI).

8. Additional Comments

Complements for appendix A Examples of Social Benefits: paragraphs A.29 to A.35 (retirement benefits) and A.51 to A.59 (unemployment insurance)

A.29 : *Employers are legally bound to deduct the employees' contributions from all salaries or salary-like benefits and to pay these, along with their own contributions, to the compensation fund to which they are affiliated. The contributions are a fixed percentage of the insured person's income, equally divided between employees and employers. **It is a state-run scheme. Non-working and self-employed people must also compulsorily contribute to it. The Swiss central government finances 19.5% of the outgoing annual payments***

A.30 : *The pensions paid are mainly based on an individual's contribution record. **However other factors are also taken into account to set the amount of the benefits.** A full, continuous contribution record is required for a full pension, with a reduced pension being payable for shorter contribution periods. Errors in the contribution record can be corrected within 5 years, however errors further back and years with less than minimal contribution cannot be rectified.*

A.31 : *Men are entitled to old-age pensions from the age of 65. Since 1 January 2005 the age limit for entitlement for women is 64. **Early withdrawal is possible from 62 (women) resp. 63 (men). Withdrawal can be postponed until the age of 70. In such cases the retirement pension are actuarially reduced or increased.***

A.34 : *Since the Swiss old-age and survivors' insurance is funded on a "pay-as-you-go" basis by the contributions of the working population, the balance between the two is increasingly out of kilter. To face up such difficulties, **a smoothing fund (buffer fund) has been established. Presently it amounts to the equivalent of more than 100% of the annual outgoing payments.** The Swiss Confederation also contributes 19.55 % of the outgoing payments. ~~It acquires this sum through direct federal and value-added taxes (VAT) as well as the taxes on tobacco products, alcohol and gambling casinos.~~ **This contribution amount** is specified in legislation, as are the contributions from employees/employers, as well as the benefits. In*

addition, a fixed proportion of VAT is directly allocated to the scheme **and an amount of gambling casinos.**

A.35 : Therefore, in case of a deficit of the scheme, there is no automatic adjustment of any funding source and parliament needs to determine which sources are adjusted or whether they change benefits. No guarantee is provided, and there is no default option. **However a smoothing fund has been established that currently amounts to more than 100% of the annual outgoing payments. In case the financial situation would get worse, the Executive should submit to the Parliament the necessary amendment to the existing act in order to balance the budget of the scheme.**

A.53: The unemployment insurance is financed through mandatory contributions from employers and employees. It is funded on a « pay-as-you-go » basis, analogous to Swiss old-age and survivors' insurance (A.34)

A57: ...which ~~collect~~ receive contributions and pay benefits. Some offices are operated by state ~~or local~~ government, trade unions and employer's organisations.

A58: ~~There are no contributions financed through tax revenues.~~ Federal and state governments contribute to the cost of employment services and labour market measures. However, federal ~~and state~~ governments have provided loans to the compensation ~~bodies~~ body during...

A59. ...is responsible for the employment insurance and acts as compensation body.

Lausanne, November 9, 2015