

**Sector-neutral Accounting Standards:
A Ten-year Experiment**

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Abstract

In 1992, New Zealand adopted a sector-neutral approach to standard setting – where the difference in accounting treatment is driven by differences in the nature of transactions and not by ownership or the objectives of the reporting entity. In the process of adopting International Financial Reporting Standards, New Zealand standard-setters are currently struggling to maintain sector-neutrality in financial reporting because international standards are primarily developed for profit-oriented entities. With the possible loss of sector-neutral financial reporting, it is appropriate to review the outcome of ten-year experiment. In particular, we focus on the impact that transactions that are common to a number of public benefit entities have on accounting standards that apply to profit-orientated entities. The results of this review may be useful to future standard setters and to the joint FASB/IASB convergence project.

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Key Words: financial reporting, standard setting, not-for-profit, sector-neutral

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INTRODUCTION

In 2004, the US Government produced a set of accrual based financial statements.¹ Over a decade earlier, New Zealand was the first sovereign entity to issue audited financial statements that fully complied with local accounting standards, for the six months ended 31 December 1991, based on full accrual accounting. The issuance of full accrual financial statements for a sovereign entity is a milestone in sector-neutral financial reporting. In 1992, the Financial Reporting Standards Board (FRSB) of New Zealand adopted a sector-neutral approach to standard setting. Under this approach, accounting standards are developed by a single standard setting Board and applied to both private (i.e., commercial or for-profit) sector entities and public benefit entities.² Under a sector-neutral approach, accounting principles or rules are driven by differences in the nature of the underlying transactions, events or conditions and not by ownership or the financial objectives of the reporting entity.

In December 2002, the New Zealand Accounting Standards Review Board (ASRB) announced its intention to recommend the adoption of International Financial Reporting Standards (IFRS). However, IFRS have been developed to apply to large, profit-oriented entities. In adopting international standards the FRSB is struggling to maintain sector-neutral standards within New Zealand equivalents to IFRS³. Indeed, it is possible that any advantages of sector neutral standard setting may be lost. It is therefore an opportune time to describe some of the benefits of New Zealand's ten-year experiment in setting sector-neutral accounting standards. We believe these results have implications for future international standard setting efforts.

A major debate in the accounting literature is whether profit-oriented accounting standards (including the conceptual framework) are appropriate for public benefit entities (e.g., see Anthony 1988, Mautz 1989, Falk 1992 and the exchanges between Barton 1999 and McGregor 1999 and between Newberry 2001, 2002, Barton 2002, and Carnegie and Wolnizer 2002). We do not enter this debate. Our contribution is

¹ <http://www.fms.treas.gov/fr/04frusg/04frusg.pdf> page 5 of the "2004 Financial Report of the United States Government"

² We use the term public benefit entities to refer to entities whose objective is to provide goods or services for a community or social benefit and where risk capital has been provided with a view to supporting that primary objective rather than for the financial return to equity owners. Most entities in the public sector and not-for profit sector are public benefit entities.

³ The roles and development of the FRSB and ASRB are briefly described in the next section.

that we focus on the impact of sector-neutral standards on private sector accounting and on the conceptual framework.⁴

We conclude that the decision to make a sector-neutral standard setting Board in New Zealand in 1992 had benefits for private sector accounting standards. In addition to covering public sector issues, the resulting standards are more robust to a wider range of transactions, events or conditions, thus benefiting private sector entities. While we observe delays in the development of standards that had high components of public benefit material, we cannot attribute this solely to sector-neutrality. It appears that due process is time-consuming activity, especially when new concepts are being developed.

This paper is structured as follows. We first discuss the development of sector-neutral accounting standards. This is followed by a review of the impact of sector-neutrality to the conceptual framework, language, due process times, and specific requirements within standards. We conclude with a discussion.

THE DEVELOPMENT OF SECTOR-NEUTRAL ACCOUNTING STANDARDS

United States

The Financial Accounting Standards Board (FASB) appears to favor the development of a single conceptual framework for all accounting entities. In December 1980, the FASB issued SFAS No. 4 *Objectives of Financial Reporting by Nonbusiness Organizations*, in which it concluded that it was not necessary to develop an independent conceptual framework for any particular category of entities. Although, the FASB indicated that there was no persuasive evidence that the new objectives were inappropriate for government units, the FASB deferred this decision. The reason for the FASB's action was that, at that time, a new structure, outside the FASB, was being proposed for setting financial accounting and reporting standards for state and local government units.⁵ In 1984 the Governmental Accounting Standards Board was established within the Financial Accounting Foundation.

To address concerns over the lack of quality and uniformity in not-for-profit accounting the FASB has issued four accounting standards: (1) SFAS No 93

⁴ New Zealand has a similar conceptual framework to the FASB and, accordingly, was part of the G4+1 group of standard setters.

⁵ See Figlewicz et al. (1985) for a history of financial accounting standards for the nonbusiness sector.

Recognition of Depreciation by Not-for-Profit Organizations (August 1987), (2) SFAS No 116 *Accounting for Contributions Received and Made* (June 1993), (3) SFAS No 117 *Financial Statement of Not-for-Profit Organizations* (June 1993), and (4) SFAS No 124 *Accounting for Certain Investments Held by Not-for-Profit Organizations* (1995). In 1994 the AICPA released SOP 94-2 to remove the uncertainty over whether GAAP applies to not-for-profit organizations. SOP 92-2 concludes that not-for-profit organizations should follow the guidance in Accounting Research Bulletins, APB Opinions, and FASB Statements and Interpretations, unless the specific pronouncement explicitly exempts not-for-profit organizations, or their subject matter precludes such applicability.

International Accounting Standards

One objective of the International Accounting Standards Board (IASB) is to develop, in the public interest, a single set of high quality, understandable and enforceable global accounting standards that require high quality, transparent and comparable information in financial statements and other financial reporting to help participants in the various capital markets of the world and other users of the information to make economic decisions (*IFRS Preface*). The *Preface* states that IFRSs are designed to apply to the general purpose of financial statements and other financial reporting of all-profit-oriented entities. It also states that although "...IFRSs are not designed to apply to not-for-profit activities in the private sector, public sector or government, entities with such activities may find them appropriate" (*Preface* paragraph 9).

The Public Sector Committee of the International Federation of Accountants has issued a Guideline stating that IFRSs are applicable to government business units. Furthermore, it prepares accounting standards for governments and other public sector entities (other than business units) based on IFRS (paragraph 9 of the *Preface*). However, this approach precludes the possibility that consideration of accounting issues for government and other public sector entities can provide higher quality solutions for profit-oriented entities.

New Zealand

The move to sector-neutral accounting standards in New Zealand developed in conjunction with commercial reforms of the public sector. In 1984 the newly elected Labour Government faced an economy with slow economic growth and high debt.

Government expenditure was 39 percent of GDP. Starting in 1986, the major commercial operations of the government were corporatized and required to operate as successful businesses.⁶

Within this climate of economic and political reform the Minister of Justice initiated a comprehensive review of legislation. Commercial legislation, which promoted the corporate body form for organizing the aggregation and use of capital, was seen to be central to the goal of an efficient economy (see discussion in Boston *et al* 1991 and McCulloch and Ball 1992).

Reform of the public sector was operationalized in two pieces of legislation: the *State Sector Act 1988* and the *Public Finance Act 1989*. The *State Sector Act 1988* established accountability and service performance of Government Departments. The *Public Finance Act 1989* allowed departments to operate their own bank accounts and requires them to operate accrual-based accounting systems. Accrual accounting was only one of the elements in a comprehensive program of public sector financial management reform (see Miah 1991; Hay 1992; and McCulloch and Ball 1992).⁷ Similar requirements were imposed on municipal (local) governments via the *Local Government Amendment Act No. 2 1989*. These legislative reforms in the public sector superseded, but were largely influenced by, developments in public sector accounting by the New Zealand Society of Accountants (NZSA).⁸

Financial accounting reforms in the public sector began earlier than the commercial reforms, because the Audit Office and Treasury had been concerned about the quality of financial information provided by Government Departments. A report by the Controller and Auditor General in 1978, describing financial management in the public sector as “mediocre” and accountability as “inadequate”, was particularly influential (Hay 2001).

In August 1981 the NZSA created a public sector working group reporting to the Accounting Research and Standards Board (the standard setting committee of the NZSA). The initial output of the working group was an informal pre-exposure draft *Public Sector Accounting Standard (PSAC) 1, General Accounting Principles for*

⁶ For background to these economic reforms see Scott *et al* (1997) and Boston *et al* (1991).

⁷ Other features include the distinction between outputs and outcomes; control over input resources, and the distinction between purchase and ownership interests (see McCulloch and Ball 1992).

⁸ The NZSA has been issuing accounting standards since 1946. The early history has been described in Zeff (1979). Bradbury (1998) discusses the move towards international convergence. The emergence of sector-neutral standards is described in Baskerville and Newby (2002).

Service Entities. In March 1985, the pre-exposure draft was replaced with a formal exposure draft, *ED-1: General Accounting Principles for Use in the Public Sector*.

In March 1986 the public sector working group was accorded full committee status as the Public Sector Accounting Standards Board, and given the task of researching and preparing exposure drafts of public sector accounting standards. In June 1986, ED-1 was withdrawn and 3 new EDs were released. In July 1987, the NZSA introduced a *Statement of Public Sector Accounting Concepts*. This exposure draft required public sector entities to establish performance measures and publish comparisons of their performance with stated objectives.

In December 1991 the Accounting Research and Standards Board released seven exposure drafts, collectively entitled “*A Proposed Framework for Financial Reporting in New Zealand*”.⁹ This *Framework* proposed a set of concepts to underlie the preparation of general-purpose external financial reports of all sectors: private, public, and not-for-profit.

The *Financial Reporting Act 1993* created the Accounting Standards Review Board (ASRB) as a statutory body, independent of the accounting profession, to review and approve Financial Reporting Standards.¹⁰ Although the standards continued to be developed by the accounting profession, the effect of the ASRB’s approval is to give legal backing to the standards. By the time the *Framework* was issued in its final form, the Financial Reporting Standards, approved by the ASRB, were to be sector-neutral and apply to all entities.¹¹

On 19 December 2002, the ASRB announced that New Zealand reporting entities would be required to apply IFRSs for periods commencing on or after 1 January 2007, with the option to early adopt from 1 January 2005. This decision to follow Australia and adopt international standards, which are for large profit-oriented entities, immediately caused significant issues with respect to public benefit entities. The current approach for adoption of IFRS is to allow additional recognition, measurement and guidance for public benefit entities in shaded boxes within the

⁹ The seven statements included an Explanatory Forward, Statement of Concepts, Public Sector Guide to the Statement of Concepts, Disclosure of Accounting Policies, Presentation of Financial Reports and two statements relating to Differential Reporting.

¹⁰ The introduction of the ASRB coincided with several name changes. The Accounting Research and Standards Board became the Financial Reporting Standards Board. The NZSA became the Institute of Chartered Accountants of New Zealand (ICANZ), and then the New Zealand Institute of Chartered Accountants (NZICA).

¹¹ The Public Sector Accounting Concepts and Technical Guidance Bulletins were withdrawn.

international standards, rather than maintain a separate series of public sector standards.¹² However, public benefit material in the standard must not be used by profit-oriented entities because there is a risk they cannot then claim to follow international accounting standards.

Table 1 offers a summary of the key changes to each standard in the process of adaptation of the IFRSs for public benefit entities. In some cases additional recognition, measurement and disclosure requirements applicable only to public-benefit entities were included in NZ equivalents to IFRS (e.g., NZ IAS 16 and NZ IAS 36). In other cases public benefit entities are exempt from the whole standards (e.g., NZ IAS 14 and NZ IAS 20).

The adoption of IFRS is seen by the Chief Accounting Advisor for the Secretary to the Treasury to place sector-neutral standards “at the crossroads” (Warren 2004); by the General Manager of Standards and Quality Assurance of ICANZ to “put sector-neutral standards at risk” (Lee and Teixeira 2004), by the government Controller and Auditor General as not resulting “in any immediate net benefits to users of financial reports of public sector entities” (Controller and Auditor General 2004, 5.25), and by the immediate past chairman of the FRSB as “...the end of sector-neutral standards in New Zealand” (Bradbury and van Zijl 2004). Such views reflect the widespread commitment to, and appreciation of the benefits of, sector neutral standards.

IMPACT OF SETTING SECTOR-NEUTRAL ACCOUNTING STANDARDS

The setting of sector-neutral accounting standards has been a key element in the financial reform of the New Zealand government over the past 10 years. The impact of sector-neutral approach to setting accounting standards can be illustrated by examining the additional guidance for public benefit entities included in New Zealand adaptations of IFRS.¹³ Using Table 1 as the basis for discussion minimizes any personal bias in the discussion. In particular, we describe the public-benefit amendments to IFRS under three headings: (1) amendments that modify profit-oriented recognition, measurement and disclosure, (2) amendments that provide additional guidance to public benefit entities, and (3) amendments that provide public benefit entities with exemptions from the standard. We also examine accounting

¹² The adoptions also allow additional disclosures and removal of allowed alternatives under IFRS for all entities.

¹³ This process captures the main public benefit entity accounting requirements that are preserved in IFRS. However, much of the detailed public benefit entity guidance (including illustrative examples) has not been carried forward or modified the NZ adaptation of IFRS and therefore may disappear as authoritative support.

standards in current NZ GAAP where there is no equivalent IFRS. The latter two headings are items that indicate deficiencies in IFRS from a public-benefit perspective. We also provide observations of the impact of considering sector-neutral standards on the conceptual framework, the use sector neutral terminology and the timeliness of due process

Amendments That Modify Profit-Oriented Recognition, Measurement and Disclosure Requirements

Non-cash Generating Assets

A major area where public benefit considerations have impacted measurement principles applied to both sectors is the impairment of assets where the service potential is not primarily dependent on the assets ability to generate cash flows. The “value in use” concept, as defined in IAS 36 *Impairment of Assets*, assumes that assets are held to generate cash flows (at a commercial return) or that assets can be grouped into a “cash generating unit”. This basis for assessing impairment creates difficulties for public benefit entities that hold assets for the purpose of service delivery rather than to generate net cash inflows (e.g., national parks, school grounds, municipal sport fields). For public benefit entities, it is difficult to apply IAS 36 to assess impairment without additional guidance.¹⁴ A similar issue arises in the lower of cost or market rule in inventory. IAS 2 *Inventories* is silent about treatment of inventory that is not for sale in the ordinary course of business. The issue is assessing the recoverability of an item of inventory without a direct cash flow, because it is freely dispensed by public benefit entity.

Control

A second major issue where profit-oriented recognition and measurement principles have been modified is the assessment of “control” in IAS 27 *Consolidated and Separate Financial Statements*, where there is an absence of legal instruments of ownership (that are typical in public-benefit entities). For example, an entity that is established by statute but where the government has the right to appoint the governing body. The New Zealand adaptation of IAS 27 amendment requires the determination of control to undertaken by reference to IPSAS 6 *Consolidated Financial Statements*

¹⁴ The standard FRS-3 *Accounting for Property, Plant and Equipment* stated that non-cash generating assets should not be recorded at an amount greater than net market value (or depreciated replacement cost where net market value cannot be determined).

and Accounting for Investments in Subsidiaries (paragraphs 26-36) and the existing standard FRS-37 *Consolidating Investments in Subsidiaries* (paragraphs 4.13-4.37 and 5.9-5.11). The FRSB are considering amendments to the concept of control in the public sector and currently developing a discussion paper to solicit comments.

Assets Acquired At No Cost and Revaluations

Within the public sector there are several instances where assets are transferred to another entity at no cost. This can occur when the government establishes commercial organizations from government departments, as part of a privatisation programme. Under existing NZ standards such transfers are recorded at “fair value” by the receiving entity. Guidance for assets acquired at no cost was inserted into NZ equivalents relating to inventory (NZ IAS 20), property, plant and equipment (NZ IAS 16) and investment properties (NZ IAS 40).

A number of “practical” amendments were included to ease the transition of public benefit entities towards full accrual accounting and were included in IFRS. These include the use of class of assets for revaluations (NZ IAS 16 and NZ IFRIC 1). The disclosure of cost is not required (NZ IAS 16).

Depreciation

A third major adaptation of IFRS for public benefit entities relates to the accounting for property plant and equipment (IAS 16). The existing NZ requirements include a components approach for the depreciation (rather than the long-run average renewals approach) of infrastructure assets. It also required the use of depreciated replacement cost when assessing “fair value” in a monopoly context (i.e., NZ IAS 16).

In each of the above cases, while the transactions are more significant or material to public benefit entities, they are also of relevance to profit orientated entities. For example, profit oriented entities increasingly own and commercially operate infrastructure networks. Service departments within large organizations will have to assess the lower of cost or market of inventory held for supply rather than resale and will have to assess recovery of assets that do not have direct cash flows. Hence, under a principles-based accounting regime, the consideration of a wider range of transactions is likely to develop more robust accounting principles.

Amendments That Provide Additional Guidance to Public Benefit Entities

In many cases the move to accrual accounting in the public benefit sector utilized existing profit-oriented accounting concepts, but resulted in more guidance being given in the accounting standards than might have been given to solely for profit-oriented entities. For example, the discussion and guidance in the New Zealand standard FRS-3 *Property Plant and Equipment* contained reference to public benefit issues such as accounting for infrastructure assets (paragraphs 4.6, 4.17, 4.37, 4.53, 6.2, 8.12), heritage assets (paragraphs 4.38, 4.53). Reference was also found to establishing fair value in a monopoly context (paragraph 4.26), fair valuing assets in airports, port companies, local and government bodies (paragraph 4.26A), police stations and post offices (paragraph 4.27). This guidance may be lost when NZ moves to full IFRS in 2007.

The following IFRSs have been modified to include examples that would assist public benefit entities: inventories (NZ IAS 2), cash flow statements (NZ IAS 7), events after balance date (NZ IAS 10), and property, plant and equipment (NZ IAS 16).

Amendments that provide Public Benefit Entities with Exemptions

These amendments to IFRS are major issues where IFRS are not deemed to be useful or relevant to public benefit entities. The major exemptions relate to segment reporting (IAS 14), accounting for government grants (IAS 20) and provisions, contingent liabilities and contingent assets (IAS 37).

Segment Reports

Several submissions on the exposure draft, noted that NZ IAS 14 was inappropriate for public benefit entities because the requirements for cost allocations for segments was in conflict with current practice of service performance reporting. Additional guidance was also needed in the reporting of actual results against planning documents and forecasts. The FRSB decided to exempt public benefit entities from NZ IAS 14 and amended the scope of IAS 14 in May 2005.

Government Grants

In 1993 a revision of SSAP-16 *Accounting for Grants and Donations* was proposed in ED-70, to extend the public sector principles to the not-for-profit sector. ED-70 was withdrawn in 1995, due to unresolved debates and variances in recommended practice

in other jurisdictions, and SSAP-16 was withdrawn shortly after (Baskerville, 1995). This withdrawal encapsulated unresolved debates on revenue recognition, and the likely constituency rejection of the proposed strong conceptual basis that was to apply to revenue recognition by all entities, especially large government entities which would have been subject to this new standard.

In 1999 the IASB issued a discussion paper on "Accounting by Recipients for Non-Reciprocal Transfers" (Westwood and Mackenzie 1999). This Discussion Paper sought to establish principles that would lead to consistent accounting treatments by recipients of non-reciprocal transfers, often referred to as 'contributions'. This project has not been further developed. The IASB website notes that "evidence and experience from IASC projects on Investment Property and Agriculture, demonstrates that IAS 20 does not clearly address the accounting for government grants in a fair value model. Nor does it address the receipt of similar assistance from non-governmental sources (such as the World Bank and the United Nations)".¹⁵

For the NZ adoption of IAS 20 *Government Grants and Disclosure of Government Assistance*, public benefit entities are required to apply the disclosure requirements of this standard but are not allowed to apply the recognition, measurement and presentation requirements. IAS 20 allows government grants to reduce the carrying amount of the asset. For public sector organizations government grants are likely to have a material impact on the financial statements and following IAS 20 would result in assets and equity of public benefit entities being materially understated. The NZ IFRS require donated or subsidised assets to be initially recorded at fair value (i.e., NZ IAS 2, NZ IAS 16 and NZ IAS 38).

Social Policy Obligations

NZ IAS 37 exempts the Crown from applying the standard to social policy obligations (i.e. the obligations expressed in legislation that have characteristics similar to an executory contract). Such obligations arise where the Crown is obligated to provide goods, services or transfers to a community in the future using funding to be obtained from the community in future periods. This exemption continues the exemption of accounting for social policies of the Crown under existing New Zealand accounting standards. In 2004 IPSAS issued an invitation to comment, *Accounting for Social*

¹⁵ See http://www.iasb.org/current/iasb.asp?showPageContent=no&xml=16_67_67_02012000.htm viewed June 29 2005.

Policies of Government. Based on the responses to this document the IPSASB is working to develop an exposure draft.

Current NZ GAAP where there is no equivalent IAS

Prospective financial information is of particular importance for local government sector, because every three years they are required to prepare long term council community plans covering a period of not less than 10 consecutive financial years. Forecast information in this plan is required to be prepared in accordance with generally accepted accounting principles.

The FRSB had issued for comment ED-103 *Prospective Financial Information*, which addressed a number of issues affecting the application of the existing FRS-39 *Prospective Financial Information*. In December 2005 the FRSB issued a new FRS 42 *Prospective Financial Statements* to accommodate these concerns.

Impact of Sector-Neutral Standards Setting on the Conceptual Framework

A major impact of sector-neutral standards was a change in the objectives of reporting. The “stewardship” role for financial reporting was replaced with a more generic notion of “accountability” and given, at least, equal status with the decision usefulness role.¹⁶ The NZ *Framework* uses the following description: “Accountability is the requirement for one party to account to another party for its performance over a given period: for example, directors are accountable to shareholders, and Parliament holds minister to account (*Statement of Concepts for General Purpose Financial Reporting* para 3.3)”.

The notion of “accountability” is more fully explained, together with the notion of “governing body”, in the *Framework for Differential Reporting*.¹⁷ This *Framework* states that general purpose financial reports are essential for entities with public accountability or where there is separation of the owners and the governing body. However, the *Framework* does not allow differential reporting where there is lack of separation of between the owners and governing body, if the parent entity or ultimate controlling entity has the coercive power to tax, rate or levy to obtain public funds (*Framework for Differential Reporting* paragraph. 4.22). This *Framework* was revised

¹⁶ Support for the accountability approach, over the decision approach, in private sector accounting can be found in Ijiri (1983) and Roberts and Scapens (1985).

¹⁷ “Differential reporting” is the partial or complete exemption from complying with a particular accounting standard by qualifying (typically small) entities. Also referred to as “little GAAP”.

in August 2005 to accommodate the differential adoption of IFRS standards for small and medium entities (including clubs, incorporated societies, public sector bodies as well as companies) on their adoption of IFRSs.

A second significant feature of sector-neutral reporting is the increase in content of the annual report. Under current NZ GAAP a statement of service performance providing non-financial measures (in addition to financial performance) is recommended (but not required) to meet financial reporting objectives.¹⁸ In meeting the objectives of general purpose reporting, interpretive comments and prospective information (e.g., financial budgets and comparison with actual results) are suggested to supplement “traditional” historical information reporting. Also the users of financial statements, acknowledged in the *Framework*, were increased to include taxpayers, donors and representative groups (e.g. voters).

No changes were made to the qualitative characteristics and the assumptions underlying the preparation of general purpose financial reports. However, the phrase “service potential” (in addition to “future economic benefit”) was included in the definitions of financial elements (assets, liabilities, revenues and expenses).

The Impact of Sector-Neutral Standard Setting on Terminology

Sector-neutral accounting standards altered and expanded the language for both sectors. For example, sector-neutral terms were employed for financial statements (e.g., “financial performance” replaced “income statement”; “financial position” replaced “balance sheet”), financial statement items (e.g., “financial surplus” replacing “profit”), and other terms used in accounting standards (e.g., “fairly present” and “fairly reflect” replaced “true and fair view”, and “governing body” replaced “directors”).

IAS 1 *Presentation of Financial Statements* notes that the terminology used in the standard is suitable for profit-oriented entities, including public sector business. It notes public benefit entities seeking to apply the Standard “...may need to amend the descriptions used for particular line items in the financial statements and for the financial statements” (IAS 1.5). The New Zealand experience indicates that

¹⁸ The voluntary reporting of non-financial measures is also supported by AAA (2002) and Hertz (2003).

amendments to terminology to encompass public benefit entities is not significant and does not cause confusion to the users of profit-oriented financial statements.¹⁹

Impact of Sector-Neutral Standard Setting on the Timeliness of Due Process

A potential concern with setting sector-neutral standards is that dealing with additional public sector issue increases the time taken to develop exposure drafts, to review responses, and to ensure that the approved Financial Reporting Standards meet with constituency compliance. Hertz (2003) also notes that improving the speed of standard setting is an important challenge for the FASB. To provide evidence on this issue we compare the number of months taken between the issue of an exposure draft and the approval of the Financial Reporting Standards.²⁰ Table 2, provides a comparison of the time for due process before and after sector-neutral standard setting (i.e., pre and post 1992). We also analyse those standards that have high public sector relevance (Panel A) to a (“control”) set of standards least affected by public sector issues (Panel B).

From Table 2, it is apparent that some accounting issues take a considerable period for due process, whether or not standard has a high level of public sector relevance. For example, accounting for property, plant and equipment (FRS-3) required three exposure drafts prior to sector-neutral standard setting. Accounting for associated or controlled entities (FRS-36, 37 and 38) has taken considerable time for completion of due process, irrespective of sector-neutrality.

Refining accounting concepts such as control; the measurement and recognition of infrastructure assets, valuation and depreciation; and similar treatment for donated or subsidised assets, has strengthened the relevance of accounting standards to both profit-oriented and public sectors, while the length of due process has not been extensive.

On the other hand, the adaptation of IFRS has slowed the development of public sector issues. The Controller and Auditor-General (2004) complains that “...important issues of relevance to the users of reports of public sector entities – such as how to

¹⁹ Indeed, anecdotal evidence indicates that students, particularly those where English is their second language, prefer sector-neutral terms such as “statement of financial position” to “balance sheet” and “statement of financial performance” to “profit and loss account” or “income statement”.

²⁰ Baskerville and Newby (2002) provide data on public sector participation in due process from 1977-1998. They document a failure in the due process resulting from public sector opposition to directors’ remuneration disclosures.

properly account for non-exchange transactions and how to report broader (non-financial) measures of performance – have received no attention in the past few years”.

DISCUSSION AND CONCLUSION

This review of the ten-year experiment in New Zealand draws attention to how consideration of accounting issues in the public sector can strengthen accounting standards for private sector entities. For example, sector-neutral standards in New Zealand have impacted financial reporting objectives by increasing the weighting of “accountability” relative to “decision usefulness” and emphasizing the voluntary reporting of non-financial measures.

Consideration of public sector issues has extended the accounting requirements for recognition and measurement principles applied to all sectors. For example, in terms of specific accounting standards it has impacted the definition of “control”, the measurement of “donated assets” and the “impairment” of assets that are held for distribution rather than the generation of cash flows. By considering public-benefit entity issues, the resulting standard should be more robust to a wider set of transactions, events and conditions. Thus, public sector issues can be seen as a useful test of the “external validity” of existing accounting principles developed for private sector financial reporting.

This study has provides an historic outline of the ten-year experiment in New Zealand, and the impact on financial reporting by private sector or publicly-listed entities. We hope the possible demise of sector-neutral standards in the face of adopting International Financial Reporting Standards should not reduce the value and insights, for standard-setters and accounting historians, of sector-neutral accounting standards for private sector entities.

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Table 1**New Zealand Adaptations of the International Financial Reporting Standards**

This table summarises key amendments to IFRS to accommodate public benefit entities (PBE)

Topic	Standard	Paragraph	Summary of adaptation
Presentation of Financial Statements	NZ IAS 1	11.2	Definition of materiality considers stewardship function
	NZ IAS 1	14.1	Not required to state compliance with all IFRS
	NZ IAS 1	24.1 - 24.2	Assessment of going concern
	NZ IAS 1	92.1	No disclosure of cost of sales
Inventories	NZ IAS 2	8.1-8.2	PBE examples
	NZ IAS 2	9.1-9.3	Inventories held for distribution
	NZ IAS 2	10.1	Acquired at no cost
	NZ IAS 2	34.1	Expense of write-downs
	NZ IAS 2	36.1	Disclosures
Cash Flow Statements	NZ IAS 7	14.1	PBE examples
	NZ IAS 7	49.1	Restrictions on use of cash must be disclosed
Events after Balance Date	NZ IAS 10	6.1	PBE examples
	NZ IAS 10	15.1	Going concern assumption discussed
Segment Reporting	NZ IAS 14	4.1	Exclusion of PBE from scope
Property Plant and Equipment	NZ IAS 16	5.1	PBE examples
	NZ IAS 16	15.1-15.2	Acquired at no cost
	NZ IAS 16	33.1-33.14	Depreciated replacement cost valuations permitted
	NZ IAS 16	39.1-39.2, 40.1 - 40.2	Class of assets basis permitted for revaluations
	NZ IAS 16	61.1-61.2	Depreciation requirement. No long-run-average renewals approach as previously used by some public benefit entities
	NZ IAS 16	77.1	Disclosure of cost not required for revalued classes of assets
Accounting for Government Grants and Disclosures of Government Assistance	NZ IAS 20	1.1	Exclusion of PBE from recognition, measurement and presentation
Related Party Disclosures	NZ IAS 24	17.1	Exclusion of normal supply relationship by Crown
Consolidated and Separate Financial Statements	NZ IAS 27	12.1	Reference to IPSAS 6, and NZ FRS-37 on additional guidance for control
	NZ IAS 27	27.1	Difference in reporting dates extended beyond 3 months
Impairment of Assets	NZ IAS 36	2.1	Exclusion of assets where benefits are not directly related to ability to generate cash flows
Provisions, Contingent Liabilities and Contingent Assets	NZ IAS 37	1.1,3.1-3.3	Exclusion of Crown from scope of social policy obligation
Intangible Assets	NZ IAS 38	44.1	Application of government grants
	NZ IAS 38	124.1	Use of class of assets basis
Investment Properties	NZ IAS 40	9.1	Clarification of scope
	NZ IAS 40	20.1	Acquired at no cost
Changes in Existing Decommissioning, Restoration, and Similar Liabilities	NZ IFRIC 1	6.1	Use of class of assets basis

TABLE 2**Time for Due Process**

Number of months between issue of exposure draft and issue of final standard

	Pre-1992	Months	Post 1992	Months
Panel A: Standards with higher levels of public sector adaptation				
FRS-2: Presentation of Financial Reports	SSAP 1	23	ED 65	29
FRS-3: Property, Plant and Equipment (Including Depreciation)	SSAP 4 and 6	89	ED 82	36
	ED 28	15		
	ED50 and 50A	26		
FRS-36: Accounting for Acquisitions Resulting in Combinations of Entities or Operations	SSAP 7	17	ED 83	40
FRS-37: Consolidating Investments in Subsidiaries	ED 16	17	ED 84	40
FRS-38: Accounting for Investments in Associates	ED 38	12	ED 81	40
	ED 49 and 49A	8		
FRS 9: Information To Be Disclosed In Financial Statements	ED 17	18	ED 67	16
FRS-15: Provisions, Contingent Liabilities and Contingent Assets	ED 24	21	ED 78 and 86	66
Panel B: Standards with lower levels of public sector adaptation				
FRS-4: Accounting for Inventories	SSAP 3	27	No post-1992 ED	
	SSAP 9	12		
	ED 33	14		
FRS-5: Events After Balance Date	ED 31	11	ED 88	7
FRS-7: Extraordinary Items and Fundamental Errors	ED 12	12	No post-1992 ED	
	ED 34	12		
	ED 57 and 57A	20		
FRS-10: Statement of Cash Flows	ED 18	27	No post-1992 ED	
	ED 39	8		
	ED 55	13		
FRS-13: Accounting for Research and Development Activities	ED 21	26	ED 69 and 69A	24
	ED 54	9		
FRS-14: Accounting for Construction Contracts	ED 22	18	No post-1992 ED	