**IPSASB**

**Exposure Draft (ED) 47**

March 2012

*Comments due: July 31, 2012*

*Proposed International Public Sector Accounting Standard*

# Financial Statement Discussion and Analysis

International Public Sector Accounting Standards Board

The International Public Sector Accounting Standards Board (IPSASB) sets International Public Sector Accounting Standards (IPSASs) for use by public sector entities, including national, regional, and local governments, and related governmental agencies. A key part of the IPSASB's strategy is to converge the IPSASs, to the extent appropriate, with the IFRSs issued by the IASB.

The objective of the IPSASB is to serve the public interest by setting high-quality public sector accounting standards and by facilitating the adoption and implementation of these, thereby enhancing the quality and consistency of practice throughout the world and strengthening transparency and accountability of public sector finances.

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The structures and processes that support the operations of the IPSASB are facilitated by the International Federation of Accountants (IFAC).

The mission of the International Federation of Accountants (IFAC) is to serve the public interest by: contributing to the development, adoption and implementation of high-quality international standards and guidance; contributing to the development of strong professional accountancy organizations and accounting firms, and to high-quality practices by professional accountants; promoting the value of professional accountants worldwide; speaking out on public interest issues where the accountancy profession's expertise is most relevant.



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# REQUEST FOR COMMENTS

This Exposure Draft 47, *Financial Statement Discussion and Analysis*, was developed and approved by the International Public Sector Accounting Standards Board (IPSASB).

The proposals in this Exposure Draft may be modified in light of comments received before being issued in final form. **Comments are requested by July 31, 2012.**

Respondents are asked to submit their comments electronically through the IPSASB website, using the "Submit a Comment" link. Please submit comments in both a PDF and Word file. Also, please note that first-time users must register to use this feature. All comments will be considered a matter of public record and will ultimately be posted on the website. Although IPSASB prefers that comments are submitted via its website, comments can also be sent to Stephenie Fox, IPSASB Technical Director at stepheniefox@ipsasb.org.

This publication may be downloaded free of charge from the IPSASB website: www.ipsasb.org. The approved text is published in the English language.

## Objective of the Exposure Draft

The objective of this Exposure Draft (ED) is to propose an authoritative Standard for the preparation of financial statement discussion and analysis by public sector entities.

## Guide for Respondents

The IPSASB would welcome comments on all of the matters discussed in this Exposure Draft. Comments are most helpful if they indicate the specific paragraph or group of paragraphs to which they relate, contain a clear rationale and, where applicable, provide a suggestion for alternative wording.

The Specific Matter for Comments requested for the Exposure Draft are provided below.

**Specific Matter for Comment 1:**

Do you agree that the material presented in this Exposure Draft should be developed as an IPSAS, with the same level of authority as the accrual based IPSASs, which applies to all entities that prepare financial statements in accordance with IPSASs?

**Specific Matter for Comment 2:**

Do you agree that IPSAS 1 should be amended to clearly indicate that financial statement discussion and analysis is not a component of the financial statements?

**Specific Matter for Comment 3:**

Is the scope of financial statement discussion and analysis clearly defined so as to distinguish it from other issues being addressed by the IPSASB (e.g., financial statements, service performance reporting, reporting on the long-term sustainability of public finances)?

**Specific Matter for Comment 4:**

Is the required content for financial statement discussion and analysis appropriate?

**Specific Matter for Comment 5:**

Do you agree with the transitional provisions?

**Specific Matter for Comment 6:**

Is the Implementation Guidance useful to understanding the requirements of the proposed IPSAS?

**Specific Matter for Comment 7:**

Is the Illustrative Example a useful way of illustrating the requirements of the proposed IPSAS?

# IPSAS XX (ED 47)—FINANCIAL STATEMENT DISCUSSION AND ANALYSIS

## CONTENTS

International Public Sector Accounting Standard XX (ED 47), *Financial Statement Discussion and Analysis* is set out in paragraphs 1–36. All the paragraphs have equal authority. IPSAS XX (ED 47) should be read in the context of its objective, the Basis for Conclusions, and the *Preface to International Public Sector Accounting Standards*. IPSAS 3, *Accounting Policies, Changes in Accounting Estimates and Errors* provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

## Objective

1. The objective of this Standard is to prescribe the manner in which financial statement discussion and analysis should be prepared and presented. To achieve this objective, this Standard sets out overall considerations for the guidance for its structure, minimum requirements for the content and presentation to allow entities to prepare financial statement discussion and analysis for their specific circumstances to assist users to understand the financial statements.

## Scope

2. **An entity that prepares and presents general purpose financial statements ("financial statements") in accordance with IPSAS 1, *Presentation of Financial Statements*, shall prepare and present financial statement discussion and analysis. Financial statement discussion and analysis shall be prepared for the same reporting entity that prepares and presents financial statements under the accrual basis of accounting.**

3. This Standard applies only to financial statement discussion and analysis. It does not apply to other information included in public documents issued in conjunction with the financial statements.

4. **This Standard applies to all public sector entities other than Government Business Enterprises.**

5. The *Preface to International Public Sector Accounting Standards* issued by the IPSASB explains that Government Business Enterprises (GBEs) apply IFRSs issued by the IASB. GBEs are defined in IPSAS 1.

## Requirement for Financial Statement Discussion and Analysis

**6. An entity shall issue the financial statement discussion and analysis when it issues financial statements.**

7. IPSAS 1 requires financial statements to be prepared at least annually. Some entities may prepare condensed interim financial information. This Standard requires an entity to issue financial discussion and analysis in conjunction with the entity's annual financial statements.

## Definition

8. **The following term is used in this Standard with the meaning specified:**

   **<u>Financial statement discussion and analysis</u> is an explanation of the significant items, transactions, and events presented in an entity's financial statements and the trends and factors that influenced them.**

   **Terms defined in other IPSASs are used in this Standard with the same meaning as in those Standards, and are reproduced in the *Glossary of Defined Terms* published separately.**

## Qualitative Characteristics

9. **Financial statement discussion and analysis shall include information that possesses the qualitative characteristics of general purpose financial reports identified in Appendix A of IPSAS 1.**

## Structure and Content of Financial Statement Discussion and Analysis

10. **Financial statement discussion and analysis shall be consistent with the financial statements, and based on currently-known facts and supportable assumptions.**

### Identification of Financial Statement Discussion and Analysis

11. **Financial statement discussion and analysis shall be identified clearly, and distinguished from the financial statements.**

12. Separate identification of financial statement discussion and analysis enables users to distinguish:

    (a) Financial statements prepared and presented under the accrual basis of accounting in accordance with IPSASs; and

    (b) Other information presented in an annual report or other document that may be useful to users but is not the subject of requirements in IPSASs.

### Compliance with this IPSAS

13. **An entity whose financial statement discussion and analysis complies with this IPSAS shall make an explicit and unreserved statement of such compliance. Financial statement discussion and analysis shall not be described as complying with this IPSAS unless it complies with all the requirements of this IPSAS.**

14. In some jurisdictions, preparation and presentation of financial statement discussion and analysis is required by legislative, regulatory, or other externally-imposed regulations. Entities are encouraged to disclose information about compliance with those requirements.

### Minimum Required Content

15. **To the extent it does not replicate information in the financial statements, financial statement discussion and analysis shall include, at a minimum:**

    (a) **An overview of the entity;**

    (b) **Information about the entity's objectives and strategies;**

    (c) **An analysis of the entity's financial statements, including variances and trends; and**

    (d) **Information about the entity's risks and uncertainties, including its risk management strategy.**

16. Financial statement discussion and analysis provides useful information to users for accountability and decision-making purposes. However, some matters may be required to be included in the financial statements by relevant IPSASs that may also be required to be included in financial statement discussion and analysis in accordance with this Standard. In those cases, financial statement discussion and analysis should not merely repeat what is in the financial statements, but it should complement and supplement the financial statement explanations by providing insights and perspectives thereon.

17. Although the specific information contained in an entity's financial statement discussion and analysis will vary depending on the facts and circumstances specific to the entity, certain essential elements are important to all financial statement discussion and analysis, as discussed below.

*Overview of the Entity*

18. An overview of the entity helps users to understand the entity and how the environment in which it operates affect an entity's financial statements. This information is the starting point in assisting users' understanding of an entity's financial statements. Information provided about an entity's operations in financial statement discussion and analysis may include current information, and changes from the prior year, about:

    (a) The entity's mission and vision;

    (b) The entity's governance (e.g., legislative or regulatory structure, management structure);

    (c) The entity's relationships with other entities (e.g., funding arrangements);

    (d) External trends, events and developments in the legal, regulatory, social, political, and macro-economic environment specific to the entity, which have or may have a material impact on the entity's financial position and financial performance (e.g., the impact of a regional or international financial crisis on employment, the tax base, or interest rates in the jurisdiction); and

    (e) The entity's main operations, including service delivery methods (e.g., outsourcing, service concession arrangements) and significant changes in them.

*Information about the Entity's Objectives and Strategies*

19. Financial statement discussion and analysis should discuss the entity's objectives and strategies in a way that enables users of the financial statements to understand the entity's priorities and to identify the resources that must be managed to achieve its objectives. Financial statement discussion and analysis should also explain how the achievement of the entity's financial objectives (e.g., debt reduction strategy) will be measured.

20. Financial statement discussion and analysis should discuss significant changes in an entity's objectives and strategies from the previous period or periods.

*Analysis of the Entity's Financial Statements*

21. Financial statement discussion and analysis should describe the significant events and activities that have affected the financial statements, without simply reiterating the information presented in those financial statements. A brief discussion of the purpose of, and information provided by, each component of the financial statements set out in IPSAS1, and their interrelationships should also be provided. In addition, there should be a discussion of significant commitments, contingencies, and events occurring after the reporting date.

22. If financial performance measures that are not required or defined by IPSASs are included within financial statement discussion and analysis, those measures should be defined and explained, including an explanation of the relevance of the measure to users. When financial performance measures are derived or drawn from the financial statements, those measures should be reconciled to measures presented in the financial statements that have been prepared in accordance with IPSASs. In addition, narrative explanations of such illustrations should be provided if necessary to accurately and completely present the information.

23. Comparative information should be included in financial statement discussion and analysis when it is relevant to an understanding of the current period's financial statements.

24. Financial statements can have a predictive or prospective role. This Standard does not require the entity to disclose forward-looking information, such as forecasts or projections. However, financial statement discussion and analysis should explain significant changes and trends in an entity's financial position and financial performance. An analysis of trends includes those financial statement items that are important and significant to gaining a better understanding of an entity's financial position and performance and changes in financial position and performance over a period of time.

25. Identification of the main events, trends, and factors influencing the current reporting period may provide information about the entity's intended actions in relation to such events, trends, and factors because the party responsible for the preparation of the entity's financial statement discussion and analysis possesses informed expectations regarding the entity's future operations based on its detailed knowledge of the entity's current operations.

26. To the extent such information is not included in the financial statements, financial statement discussion and analysis should include information about significant positive and negative variances between:

    (a) Actual results and the budget; and

    (b) The prior year and current year financial statements, by explaining significant changes and highlighting trends.

*Risks and Uncertainties*

27. Information about the entity's risks and uncertainties helps users to evaluate the impact of risks in the current period (e.g., contingent liabilities disclosed in the financial statements) as well as expected outcomes. Information provided may include its main exposures to risk and changes in those risks, its opportunities, along with its policies and strategies for mitigating the risks and capitalizing on opportunities. It may also include the entity's evaluation of the effectiveness of its risk management strategies. It is noted, however, that these need to be fact-based and take into account currently-known conditions. In addition, underlying assumptions need to be disclosed.

28. Information about the entity's risks and uncertainties may include a discussion of such matters as a summary of the entity's investment policy and other means of managing its risks, insurance coverage, and other controls intended to safeguard the entity's assets. It may also include the relevant legislation, regulation or body that sets the risk management policies for the entity (e.g., when risks are managed at a government-wide level).

29. A discussion of how the entity's manages its risks helps users obtain a complete picture of the entity's exposure to risks that directly affect financial statement items and disclosures, which allows them to evaluate the entity's financial position and financial performance. Such disclosure may include the entity's decision to "self-insure", or to mitigate risk by transferring or sharing it, or through insurance.

30. Additional information may be provided about uncertainties such as environmental issues, and significant events after the reporting date (see IPSAS 14, *Events After the Reporting Date*), which may affect the entity's future operations (e.g., debt issuance, guarantees issued in relation to a financial crisis, or entering into a new service concession arrangement). Information may also be provided about the entity's opportunities; however in reporting such information, care must be taken to ensure it is fact-based, and neutral. This means that the assumptions made are based on conditions that exist at the reporting date and events that occurred in the current period.

31. A discussion of the risks the entity faces also provides relevant information to users about exposure or vulnerability to concentrations of risks such as significant loans to particular regions or industries, or dependence on a particular source of revenue.

32. Risks and uncertainties may have a pervasive effect on the financial statements, therefore information pertaining to risks and uncertainties may be reported separately, or in relevant sections throughout the financial statement discussion and analysis.

## Transition

33. **All provisions of this Standard shall be applied from the date of first adoption of this Standard.**

34. **An entity that has applied the transitional provision in IPSAS 1 to present only current period information in the financial statements to which accrual accounting is first adopted in accordance with IPSASs is permitted to omit the comparative information described in paragraph 23 from its financial statement discussion and analysis for that period.**

## Effective Date

35. **An entity shall apply this Standard to financial statement discussion and analysis that relates to annual financial statements covering periods beginning on or after MM DD, YYYY. Earlier application is encouraged. If an entity applies this Standard for a period beginning before MM DD, YYYY, it shall disclose that fact and apply IPSAS 1 and IPSAS 24, *Presentation of Budget Information in Financial Statements* at the same time.**

36. When an entity adopts the accrual basis of accounting as defined by IPSASs for financial reporting purposes subsequent to this effective date, this Standard applies to the entity's financial statement discussion and analysis covering periods beginning on or after the date of adoption.

**Appendix A**

## Amendments to Other IPSASs

## IPSAS 1, Presentation of Financial Statements

**A new paragraph is inserted after paragraph 21 as follows:**

## Components of Financial Statements

21. **A complete set of financial statements comprises:**

    (a) **A statement of financial position;**

    (b) **A statement of financial performance;**

    (c) **A statement of changes in net assets/equity;**

    (d) **A cash flow statement;**

    (e) **When the entity makes publicly available its approved budget, a comparison of budget and actual amounts either as a separate additional financial statement or as a budget column in the financial statements; and**

    (f) **Notes, comprising a summary of significant accounting policies and other explanatory notes.**

<u>21A. Financial statement discussion and analysis is not a component of the financial statements. IPSAS XX (ED 47), F*inancial Statement Discussion and Analysis* requires financial statement discussion and analysis to be presented in conjunction with its financial statements.</u>

**A new paragraph is inserted after paragraph 24 as follows:**

24. Public sector entities are typically subject to budgetary limits in the form of appropriations or budget authorizations (or equivalent), which may be given effect through authorizing legislation. General purpose financial reporting by public sector entities may provide information on whether resources were obtained and used in accordance with the legally adopted budget. Entities that make publicly available their approved budget(s) are required to comply with the requirements of IPSAS 24, *Presentation of Budget Information in Financial Statements*. For other entities, where the financial statements and the budget are on the same basis of accounting, this Standard encourages the inclusion in the financial statements of a comparison with the budgeted amounts for the reporting period. Reporting against budget(s) for these entities may be presented in various different ways, including:

    - The use of a columnar format for the financial statements, with separate columns for budgeted amounts and actual amounts. A column showing any variances from the budget or appropriation may also be presented for completeness; and

    - Disclosure that the budgeted amounts have not been exceeded. If any budgeted amounts or appropriations have been exceeded, or expenses incurred without appropriation or other form of authority, then details may be disclosed by way of footnote to the relevant item in the financial statements.

24A. When an entity elects, under IPSAS 24, to explain, in financial statement discussion and analysis rather than by way of note disclosure, material differences between the budgeted and actual amounts identified in paragraph 24, it applies the guidance in IPSAS XX (ED 47).

**Paragraphs 27 and 28 are amended as follows:**

## Overall Considerations

### Fair Presentation and Compliance with IPSASs

27. **Financial statements shall present fairly the financial position, financial performance, and cash flows of an entity. Fair presentation of the financial statements requires the faithful representation of the effects of transactions, other events, and conditions in accordance with the definitions and recognition criteria for assets, liabilities, revenue, and expenses set out in IPSASs applicable to the financial statements. The application of these IPSASs, with additional disclosures when necessary, is presumed to result in financial statements that achieve a fair presentation.**

28. **An entity whose financial statements comply with IPSASs applicable to the financial statements shall make an explicit and unreserved statement of such compliance in the notes. Financial statements shall not be described as complying with IPSASs unless they comply with all the requirements of those IPSASs.**

**Paragraph 62 is amended as follows:**

### Identification of the Financial Statements

…

62. IPSASs apply to financial statements and financial statement discussion and analysis, and not to other information presented in an annual report or other document. Therefore, it is important that users can distinguish information that is prepared using IPSASs from other information that may be useful to users but is not the subject of those requirements.

**A new paragraph is inserted after paragraph 153D as follows:**

## Effective Date

153E. **Paragraphs 21A and 24A were inserted and paragraphs 27, 28 and 62 were amended by IPSAS XX (ED 47) issued in Month 201X. An entity shall apply those amendments for annual financial statements covering periods beginning on or after Month DD, 201X. Earlier application is encouraged. If an entity applies the amendments for a period beginning before Month DD, 201X, it shall disclose that fact and at the same time apply IPSAS XX (ED 47) and the amendments to paragraphs 14, 19 and 54A of IPSAS 24.**

## IPSAS 24 Presentation of Budget Information in Financial Statements

**Paragraph 14 is amended as follows:**

## Presentation of a Comparison of Budget and Actual Amounts

14. **Subject to the requirements of paragraph 21, an entity shall present a comparison of the budget amounts for which it is held publicly accountable and actual amounts, either as a separate additional financial statement or as additional budget columns in the financial statements currently presented in accordance with IPSASs. The comparison of budget and actual amounts shall present separately for each level of legislative oversight:**

    (a) **The original and final budget amounts;**

    (b) **The actual amounts on a comparable basis; and**

    (c) **By way of note disclosure, an explanation of material differences between the budget for which the entity is held publicly accountable and actual amounts, unless such explanation is included in either the financial statement discussion and analysis or other public documents issued in conjunction with the financial statements, and a cross reference to those documents is made in the notes.**

**Paragraph 19 is amended as follows:**

19. ~~Management~~ IPSAS XX (ED 47), *Financial Statement Discussion and Analysis* requires presentation of a financial statement discussion and analysis~~, operations review, or other public reports~~ that provides commentary on the performance and achievements of the entity during the reporting period~~,~~. It can include ~~including~~ explanations of any material differences from budget amounts~~,~~. Alternatively, this explanation could be included in other public documents ~~are often~~ issued in conjunction with the financial statements. In accordance with paragraph 14(c) of this Standard, explanation of material differences between actual and budget amounts will be included in notes to the financial statements, unless (a) included in the financial statement discussion and analysis or other public reports or documents issued in conjunction with the financial statements, and (b) the notes to the financial statements identify the reports or documents in which the explanation can be found. When an entity presents the actual-to-budget comparison in financial statement discussion and analysis, it applies the guidance in IPSAS XX (ED 47).

**A new paragraph is inserted after paragraph 54 as follows:**

## Effective Date

54A. **Paragraphs 14 and 19 were amended by IPSAS XX (ED 47) issued in Month 201X. An entity shall apply those amendments for annual financial statements covering periods beginning on or after Month DD, 201X. Earlier application is encouraged. If an entity applies the amendments for a period beginning before Month DD, 201X, it shall disclose that fact and at the same time apply IPSAS XX (ED 47) and the amendments to paragraphs 21A, 24A, 27, 28, 62 and 153E of IPSAS 1.**

## Basis for Conclusions

*This Basis for Conclusions accompanies, but is not part of, IPSAS XX (ED 47).*

### Scope and Authority

BC1. The IPSASB approved a project in March 2008 to address "narrative reporting". In developing this Standard, the IPSASB clarified that the scope of the project is to address only those reports that provide discussion and analysis specifically pertaining to an entity's general purpose financial statements ("financial statements") as set out in IPSAS 1, and not broader types of reports that may be considered general purpose financial reports as envisaged in the IPSASB's Conceptual Framework.

BC2. In undertaking this project, the IPSASB considered, under its *Criteria for Modifying IASB Documents*, whether to develop guidance that was converged with *Management Commentary*, an IFRS Practice Statement. The IPSASB did not consider this approach to be appropriate because:

(a) The users identified in the Practice Statement are investors. IPSAS 1, *Presentation of Financial Statements*, identifies different users, which results in different information needs related to the financial statements.

(b) Additionally, in the private sector there may be a strong influence from the securities exchanges and their regulators which help ensure and reinforce the information needs of the investors. In the public sector there may not be a comparable regulator, which participates in the process of standardizing financial statement discussion and analysis for a jurisdiction, and therefore reliance on the private sector guidance may result in loss of accountability in the public sector.

BC3. Financial statement discussion and analysis is intended to address similar matters to reports that may be termed "management discussion and analysis" and "management commentary" in various jurisdictions. However, the IPSASB did not consider those terms to accurately describe the nature of the report in relation to the financial statements. The IPSASB decided it was important to link financial statement discussion and analysis to the financial statements because the financial statement discussion and analysis is intended to explain the financial statements, and not to stand alone. The IPSASB considers the term "financial statement discussion and analysis" clearly defines the scope of applicability of this Standard and its close linkage to the financial statements.

BC4. The IPSASB considered whether public sector entities that prepare and present financial statements in accordance with International Public Sector Accounting Standards (IPSAS):

(a) Should be required to prepare financial statement discussion and analysis; and

(b) If so, whether financial statement discussion and analysis should be included as an integral part of the general purpose financial statements.

BC5. The IPSASB considers that financial statement discussion and analysis provides additional information necessary to meet the objectives of financial statements. The IPSASB concluded that all entities that prepare and present their financial statements in accordance with IPSASs should be required to prepare financial statement discussion and analysis in accordance with this IPSAS, which has the same level of authority as accrual based IPSASs.

BC6. The IPSASB decided it was important to develop a standard that provided principles for financial statement discussion and analysis, while allowing reporting on specific information most relevant to an entity. Accordingly, this Standard has been developed from a principles-based perspective that can be applied to all public sector entities. In addition, entities are encouraged to prepare financial statement discussion and analysis that meets their specific circumstances.

BC7. The IPSASB considered whether a requirement to issue financial statement discussion and analysis when an entity issues financial statements prepared in accordance with IPSASs would be an impediment to the adoption of IPSASs. The IPSASB considered that the users of financial statements in such jurisdictions may even have a greater need for the benefit of financial statement discussion and analysis to help explain the financial statements.

BC8. The IPSASB considers that in all cases, the benefits of providing financial statement discussion and analysis would outweigh the costs of preparing it, as the information is used in the preparation of the financial statements, and tailored to the specific circumstances of the entity. The IPSASB therefore concluded that financial statement discussion and analysis should be prepared by all entities that prepare their financial statements in accordance with IPSASs.

BC9. IPSAS 1 defines the scope of the financial statements. The IPSASB does not consider financial statement discussion and analysis to be part of the financial statements prepared in accordance with IPSASs despite its close link to the financial statements. The IPSASB did not, therefore, amend IPSAS 1 to include financial statement discussion and analysis as an integral part of the financial statements. Nevertheless, the IPSASB has clarified the close link between the financial statements and financial statement discussion and analysis.

BC10. The IPSASB noted the concern that, if this Standard were an IPSAS, it could still be considered part of the financial statements and there could be confusion as to whether it would be subject to the same audit requirements as the financial statements. This could cause difficulties in some jurisdictions if the inclusion of financial statement discussion and analysis resulted in a qualified audit report on the financial statements. While the audit of financial statement discussion and analysis is desirable, the IPSASB considers that imposing an audit requirement on such information exceeds its mandate. However, it is noted that an audit of financial statements would not automatically require audited financial statement discussion and analysis. The term “financial statements” ordinarily refers to a complete set of financial statements as determined by the requirements of the applicable financial reporting framework. The financial reporting framework for public sector entities is described in IPSAS 1, and does not include financial statement discussion and analysis.

BC11. To date, IPSASs have addressed only matters that pertain to the content of the financial statements themselves. The IPSASB considered whether it would be appropriate to allow for a new type of pronouncement that had equivalent authoritative status to the IPSASs. The IPSASB is of the view that introducing a new type of pronouncement would be confusing to its constituents. Accordingly, the IPSASB has decided that an International Public Sector Accounting Standard (IPSAS) is the appropriate type of pronouncement to apply to the financial statement discussion and analysis.

### Qualitative Characteristics

BC12. The IPSASB also concluded that the information in financial statement discussion and analysis should possess the qualitative characteristics and constraints in IPSAS 1. Accordingly, IPSAS XX (ED 47) contains requirements that financial statement discussion and analysis contain information that is consistent with those qualitative characteristics.

### Structure and Content of Financial Statement Discussion and Analysis

BC13. Paragraph 21 of IPSAS 1 states that a complete set of financial statements comprises:

(a) A statement of financial position;

(b) A statement of financial performance;

(c) A statement of changes in net assets/equity;

(d) A cash flow statement;

(e) When the entity makes publicly available its approved budget, a comparison of budget and actual amounts either as a separate additional financial statement or as a budget column in the financial statements; and

(f) Notes, comprising a summary of significant accounting policies and other explanatory notes.

The IPSASB noted that in some of the minimum required content in paragraph 15 of IPSAS XX (ED 47) may also be required under other IPSASs for financial statements. IPSAS XX (ED 47) therefore requires financial statement discussion and analysis include significant items, transactions, and events that are presented in an entity's financial statements to the extent it does not replicate information in the financial statements.

BC14. The IPSASB noted that the content and format of presentation of financial statement discussion and analysis should be determined by the entity, in a way that best reflects its circumstances, noting that the specific information contained in an entity's financial statement discussion and analysis will vary depending on the facts and circumstances specific to the entity. The IPSASB wishes to avoid a checklist approach that may result in an entity reporting less relevant information. Accordingly, some flexibility is provided in the content and format. However, the Standard contains certain essential required content that is important to all financial statement discussion and analysis.

BC15. In determining the matters that should be required in financial statement discussion and analysis, the IPSASB reviewed and compared existing national standards, guidance, and regulatory requirements for financial statement discussion and analysis (or its equivalent) in the public sector. The existing approaches, identified in conducting the research, were used to help form the basis for the required content of financial statement discussion and analysis.

BC16. In some cases an IPSAS permits certain information to be included in separate reports (e.g., financial statement discussion and analysis) rather than in the financial statements. The IPSASB did not consider it necessary to duplicate the financial statement disclosure in the financial statement discussion and analysis and has accordingly provided guidance to that effect.

### Forward-Looking Information

BC17. This Standard does not require the entity to disclose forward-looking information, such as forecasts or projections. However, the IPSASB noted that information in financial statements also has predictive ability about the entity's operations, and that financial statement discussion and analysis could enhance that ability. For example, information about an entity's risk management policies, and trend analyses of significant financial statement items, may assist users in assessing the extent to which resources will be available to support future service delivery objectives and the amounts and timing of future cash flows necessary to service and repay existing claims to the entity's resources. The IPSASB has thus provided guidance on how such information could be included in financial statement discussion and analysis.

### Transitional Provisions

BC18. The IPSASB determined that a transitional provision was required to address the case when an entity has used the exemption under IPSAS 1 to not include comparative information in respect of the financial statements to which accrual accounting is first adopted in accordance with IPSASs. This Standard states that comparative information should be included in financial statement discussion and analysis when it is relevant to an understanding of the current period's financial statements. However, where an entity has applied the transitional provision in IPSAS 1 it is unlikely to have comparative information and thus it would not be possible to provide such comparative information.

## Alternative View of Mr. Thomas Müller-Marqués Berger

AV1. This member is of the view that ED 47 should require entities to disclose forward-looking information, such as forecasts or projections. As outlined in the IPSASB's Conceptual Framework Exposure Draft 1, the objectives of financial reporting by public sector entities are to provide information about the entity that is useful to users of GPFRs for accountability purposes and for decision-making purposes.

AV2. In the view of this member, the decision not to require entities to disclose forward-looking information does not completely fulfill user needs as the objective of decision-making is not sufficiently addressed.

## Implementation Guidance

*This guidance accompanies, but is not part of, IPSAS XX (ED 47).*

IG1. The purpose of this Implementation Guidance is to illustrate certain aspects of the requirements of IPSAS XX (ED 47).

IG2. This Implementation Guidance is divided into three sections as follows:

(a) Section A: Qualitative Characteristics of General Purpose Financial Reports—Applicability to Financial Statement Discussion and Analysis;

(b) Section B: Examples of Information about the Entity's Financial Statements; and

(c) Section C: Examples of Information about Variances and Trends.

## Section A: Qualitative Characteristics of General Purpose Financial Reports—Applicability to Financial Statement Discussion and Analysis

A.IG1. Financial statement discussion and analysis is intended to explain the significant items, transactions, and events presented in an entity's financial statements and the trends and factors that influenced the financial statements to assist users to understand the financial statements. It should, therefore, possess the same qualitative characteristics as for financial statements described in IPSAS 1, namely:

(a) Understandability;

(b) Relevance;

(c) Reliability; and

(d) Comparability.

A.IG2. Financial statement discussion and analysis should aim to achieve a balance between the qualitative characteristics to meet the objectives of providing the information. In some cases, depending on the circumstances of the entity, the relative importance of a particular qualitative characteristic may be greater than in others.

A.IG3. Application of the qualitative characteristics to financial statement discussion and analysis is set out in paragraphs A.IG.4–A.IG.20.

### Understandability

A.IG4. Information provided in financial statement discussion and analysis should be clear and concise to explain and interpret the complex transactions, events, and conditions presented in the financial statements in a readable and simple manner. Financial statement discussion and analysis is understandable when it uses descriptions that are not overly technical, does not provide excessive detail, and clearly describes those transactions, events, and conditions.

### Relevance

A.IG5. The matters that are relevant to an entity are also specific to that entity. Financial statement discussion and analysis reflects detailed knowledge of the items, transactions, and events, presented in the entity's financial statements and of the policies that govern the entity's operations. This means that financial statement discussion and analysis may not include some matters that are material to the components of the financial statements set out in IPSAS 1, or it may include some matters that are not material to the financial statements.

A.IG6. Financial statement discussion and analysis needs to be clear and concise to be useful, therefore the most important, or material, matters must be selected to be included, descriptions should be non-technical, and an appropriate but not excessive level of detail should be provided. Inclusion of information about immaterial items could make the more important information difficult to find.

A.IG7. Generic or “boilerplate” information that does not relate to the specific operations, practices and circumstances of the entity is unlikely to be relevant and should not be included in financial statement discussion and analysis. When practicable, duplication of the disclosures made in the notes to its financial statements should be avoided. Financial statement discussion and analysis that recites financial statement information without analysis or explanations, or presents discussions that do not provide insight into the entity’s past performance is unlikely to provide information that is relevant to users of the financial statements, and may create an obstacle for users to identify and understand the most significant matters the entity faces. For example, commentary on the economy that relates specifically to the entity’s financial statements and expected impacts on the entity would be relevant information for users.

A.IG8. When dealing with qualitative or forward-looking information (e.g., expectations about financial results in the future), it is not generally possible to specify a uniform quantitative threshold above which a particular type of information becomes material.

A.IG9. Financial statement discussion and analysis provides additional perspectives and insights about the financial statements, which increases the relevance of the information.

**Reliability**

A.IG10. Information presented in financial statement discussion and analysis should be:

(a) Based on, and consistent with, the underlying financial statements;

(b) Neutral in discussing both positive and negative facts and views;

(c) Based on currently-known facts, decisions, or conditions; and

(d) Based on verifiable and supportable assumptions.

A.IG11. It is important that information presented in the financial statement discussion and analysis is supported by information in the financial statements, and does not go beyond or contradict the information presented in the financial statements.

A.IG12. Information that excludes certain facts (e.g., negative) is incomplete and thus could be not neutral. In cases when financial statement discussion and analysis presents ratios, tables, or charts, they should not distort the information in the financial statements by, for example, using a scale that exaggerates a positive or negative trend.

A.IG13. Financial statement discussion and analysis should contain information specific to the entity and related to that reporting period. While the information provided in financial statement discussion and analysis may reflect information outside of the financial statements (e.g., economic indicators such as changes in the tax base or the employment base), that information should be related to the reporting period and should be from a reliable source.

A.IG14. The underlying assumptions and methodologies (including formulae) used to determine ratios and to prepare tables and charts included in financial statement discussion and analysis should be disclosed (e.g., those used in analyses of trends and variances). In addition, the methodologies adopted in compiling the information, and the factors and circumstances that support the discussion and analyses, need to be transparent. Disclosure of this information permits users to assess the reliability of the information provided.

A.IG15. Assumptions should be mutually compatible. Assumptions are mutually compatible when they reflect economic relationships in the jurisdiction (e.g., interest rates, employment rates, GDP). For example, all assumptions that depend on the tax base for a given future period would assume the same tax base level in that period.

A.IG16. Financial statement discussion and analysis should clearly describe the basis for how the information is reported, including the unit of measurement. For example, in cases when financial statement discussion and analysis presents ratios, tables, or charts, they should not distort the information in the financial statements by, for example, using a scale that exaggerates a positive or negative trend. Thus, when financial statement discussion and analysis contains charts or graphs showing trends, disclosure of the unit of measurement is necessary to ensure such information can be properly interpreted. When such information is presented, the scale of such illustrations should be on a basis that faithfully represents the relationships of the items being analyzed.

A.IG17. In some cases it may not be possible to verify the accuracy of all qualitative and quantitative explanations of such information until a future period, if at all. For example, if the entity's strategy and risk management are described in financial statement discussion and analysis, such information would be less verifiable than, for example, a ratio calculated from information provided in the financial statements.

**Comparability**

A.IG18. Information in financial statement discussion and analysis should be comparable. Comparability applies to information related to different entities and to the entity over periods of time.

A.IG19. Comparability is enhanced when financial statement discussion and analysis is presented on a basis consistent with that in prior years and when the same principles and practices are used for each period for such items as determining ratios and preparation of tables and charts included in financial statement discussion and analysis. In addition, disclosure of those principles and practices, including underlying assumptions and formulae, is useful in interpreting the analyses. Changes to the principles and practices used to prepare financial statement discussion and analysis from one period to the next should be disclosed.

A.IG20. Enhancing the inter-period comparability of information assists users in making and evaluating decisions, especially by allowing the assessment of trends in financial information for predictive purposes. In some circumstances, it is impracticable to reclassify comparative information for a particular prior period to achieve comparability with the current period. For example, data may not have been collected in the prior period(s) in a way that allows reclassification, and it may not be practicable to recreate the information.

## Section B: Examples of Information about the Entity's Financial Statements

This Implementation Guidance includes guidance on how an entity may prepare and present financial statement discussion and analysis that includes information about all significant items, transactions, and events presented in the financial statements that are most relevant to enhancing users' understanding of the financial statements.

*Financial Position*

B.IG1. Information about the financial position will help users to identify the resources of the entity that can be used to provide particular services in future periods and claims to those resources at the reporting date. This will provide information useful as input to assessments of such matters as:

- The extent to which the entity has discharged its responsibilities for safekeeping and managing its resources;
- The extent to which resources are available to support future service delivery objectives; and
- The amounts and timing of future cash flows necessary to service and repay existing claims to the entity's resources.

*Financial Assets*

B.IG2. Financial statement discussion and analysis may include the following information pertaining to an entity's financial assets:

(a) Changes in financial assets to illustrate volatility in the sources of funds;

(b) Provisions for loan losses;

(c) The rates of return on investment;

(d) Composition of investments;

(e) A government's investment in GBEs as a percentage of the total financial assets;

(f) Taxes receivable to total tax revenues; and

(g) Restricted and designated assets set aside for specific purposes.

*Property, Plant, and Equipment*

B.IG3. Financial statement discussion and analysis may include the following information pertaining to an entity's property, plant, and equipment:

(a) An analysis of required maintenance, including future expenditure requirements for maintenance and replacement, to allow users to make informed decisions regarding the ability of the capital assets to sustain and provide services in the future;

(b) An analysis of the change in the net book value of property, plant, and equipment by major class and an explanation of what the net book value and changes in it mean (e.g., a description of why the net book value has increased or decreased is useful in understanding asset replacement and usage);

(c) The average age and average useful life for each category of property, plant, and equipment; and

(d) An assessment of the assets' physical condition carried out by a technical expert in such assessments.

B.IG4. Asset management systems may contain information about an asset's physical condition, but the absence of an asset management system does not necessarily preclude reporting on the physical condition.

B.IG5. Asset condition assessment methodologies and frequency of assessments can be different for major classes of property, plant, and equipment. For example, they could be different for bridges when compared to buildings.

B.IG6. It may not be possible to complete a physical examination of all items of property, plant, and equipment. However, the physical condition could be estimated based on a combination of factors including, for example, age, construction materials and methods, breaks per kilometer, geological, and soil conditions.

B.IG7. Financial statement discussion and analysis may provide the average age and either the average remaining useful life or estimated average useful life of property, plant, and equipment in each major class. Information about the average age and the useful life allows users to assess the timing of rehabilitation and replacement expenditures.

B.IG8. Financial statement discussion and analysis may contain a description and the quantity of the major components of property, plant, and equipment in each major class of asset. Providing this information gives users an understanding of the nature and extent of the stock of property, plant, and equipment.

B.IG9. The quantity could be based on a unit of measurement that represents the common characteristics of the class of property, plant, and equipment being assessed or components thereof (e.g., lanes or kilometers for roads, kilometers of pipes for sewer for water systems, or the number of water treatment plants). This summary level unit of measure provides users with a reference that is useful in assessing the magnitude of the classes and components of items of property, plant, and equipment.

B.IG10. The information required to promote a better understanding of an entity's property, plant, and equipment explains information in the financial statements. Reporting on the physical condition of property, plant, and equipment assists users when assessing:

(a) The effects on service potential of past resource allocation and funding decisions;

(b) The trends in the physical condition;

(c) The adequacy of existing maintenance, replacement and renewal funding; and

(d) The extent of current and future revenues needed to maintain, renew, and replace property, plant, and equipment.

*Other Assets*

B.IG11. Financial statement discussion and analysis may include the following information pertaining to an entity's other assets, to the extent they are material (e.g., inventories of supplies—see IPSAS 12, *Inventories*, and prepaid expenses):

(a) The nature, extent and purpose of inventories of supplies (e.g., maintenance materials, strategic stockpiles, and land/property held for resale); and

(b) The nature, extent, purpose, and timing of any prepaid items such as insurance.

*Liabilities*

B.IG12. Financial statement discussion and analysis may include the following information pertaining to an entity's liabilities:

(a) A breakdown of the entity's debt by domestic issues versus foreign issues.

(b) A description of the entity's debt management policies and strategies, and the general terms and conditions associated with the debt, including whether the entity has complied with any debt covenants.

(c) An analysis of the entity's total debt. Specific ratios or indicators may also be useful to highlight the magnitude of the entity's debt and the changes in it over time. For example, an analysis of the total debt outstanding at year end to the total liabilities of the entity may be provided. The impact of the debt servicing cost, expressed as public debt charges to revenues, may also be included. An assessment of any unfunded retirement and other employment or post employment benefit liabilities. This may include a discussion related to the timing of when the unfunded liability needs to be provided for.

(d) An analysis of revenues that are not earned at the end of the period including the terms and conditions (e.g., commitments) associated with them. The entity is not entitled to these revenues until it performs specific actions as outlined in the terms and conditions of the related contract or agreement. For example, in the case of service concession arrangements in which the operator is compensated by the entity granting it the right to earn third-party revenues, there may be substantial liabilities of this type.

(e) The nature of financial liabilities under service concession arrangements.

(f) An analysis of any sinking funds available for the discharge of long-term liabilities.

*Net Assets/Equity*

B.IG13. An analysis of net assets/equity provides users with information relevant in assessing the entity's overall financial position, and whether it has improved or deteriorated. Providing significant explanations and a trend analysis related to the net assets/equity provides users with an indication as to whether the entity's liabilities are growing and allows them to make assessments about whether current levels of taxes or other charges are sufficient to maintain the volume and quality of services currently provided or to undertake any planned enhancements. For example, explanations and a trend analysis related to the assets/equity may indicate to users that while debt is growing, the entity is accumulating resources, such as property, plant, and equipment.

**Financial Performance**

B.IG14. Information about the financial performance will inform assessments of matters such as whether the entity has acquired resources economically, and used them efficiently and effectively to achieve its service delivery objectives. Information about the costs of service delivery and the amounts and sources of cost recovery during the reporting period will enable users to determine whether operating costs were recovered from, for example, taxes, user charges, contributions and transfers or were financed by increasing the level of indebtedness of the entity.

B.IG15. Any currently-known conditions that have significantly affected revenues or expenses in the current period, as well as those that may impact future revenues or expenses, should be disclosed to assist users in determining trends.

*Revenues*

B.IG16. Financial statement discussion and analysis may include the following information pertaining to an entity's revenues:

(a) An overview of total revenues by major source to indicate trends and dependencies on specific sources.

(b) Ratios may also be provided to highlight the level of dependence the entity has on particular sources of revenues, for example:

(i) Public-to-public transfers to revenues generated by the entity (e.g., taxes, user fees, licences); and

(ii) Revenues generated by the entity as a percentage of total revenues.

(c) The impact of the  of government business enterprises on the entity as a whole, which may be relevant especially if there are restrictions placed on the use of a government business enterprise's net assets.

(d) An analysis of the change in revenues by major source.

*Expenses*

B.IG17. Financial statement discussion and analysis may include the following information pertaining to an entity's expenses:

(a) An overview of total expenses by nature (e.g., depreciation, purchases of materials, transport costs, employee benefits, and advertising costs).

(b) An overview of total expenses by function.

(c) An analysis of debt servicing costs as a percentage of total expenditures, which helps to highlight the magnitude of expenses that is required to service past obligations and thus reduces the amount of funds that can be directed to various programs. Alternatively, debt servicing costs as a percentage of revenues could be provided.

(d) An analysis of significant changes in expenses by nature and function.

*Surplus or Deficit for the Period*

B.IG18. An analysis of the surplus or deficit for the period provides users with information relevant in determining whether the entity was able to raise enough revenues in the period to cover its costs and spending and whether the trend is likely to continue in the future.

B.IG19. Financial statement discussion and analysis may include the following information pertaining to an entity's surplus or deficit for the period:

(a) An analysis of net revenues or expenses by nature (for example, depreciation, purchases of materials, transport costs, employee benefits, and advertising costs).

(b) A comparison of direct / identifiable program revenues to expenses by function, to illustrate the amount of program spending funded through taxation.

(c) Analyses of specific, significant non-recurring transactions or events such as:

(i) Write-downs of inventories to net realizable value or of property, plant, and equipment to recoverable amount or recoverable service amount as appropriate, as well as reversals of such write-downs;

(ii) Restructurings of the activities of an entity and reversals of any provisions for the costs of restructuring;

(iii) Disposals of items of property, plant, and equipment;

(iv) Privatizations or other disposals of investments;

(v) Discontinuing operations;

(vi) Litigation settlements; and

(vii) Other reversals of provisions.

In these cases, the nature of the revenue or expense and a discussion of its impact on future operations would be disclosed.

### Cash Flows

B.IG20. Information about the cash flows contributes to assessments of financial performance and the entity's liquidity and solvency. It indicates how the entity raised and used cash during the period, including its borrowing and repayment of borrowing and its acquisition and sale of, for example, property, plant, and equipment. It also identifies the cash received from, for example, taxes and investments and the cash transfers made to, and received from, other governments, government agencies, or international organizations. Information about cash flows can also support assessments of the entity's compliance with spending mandates expressed in cash flow terms, and inform assessments of the likely amounts and sources of cash inflows needed in future periods to support service delivery objectives.

B.IG21. Financial statement discussion and analysis may include the following information pertaining to an entity's cash flows from operating, investing, and financing activities:

(a) An analysis of the cash flows arising from operating activities such as:

(i) The gross cash receipts and payments arising from the normal operations of the entity (e.g., the gross cash receipts from taxation, user fees or transfers from other entities).

(ii) Significant cash requirements or payments made during the period (e.g., payments to and on behalf of employees).

(b) An analysis of cash flows arising from investing activities such as:

(i) Expenditures made to acquire resources (e.g., property, plant, and equipment, investment property, and intangible assets) intended to generate future cash flows and service potential; and

(ii) Significant changes in such investments, including any additions or disposals during the current year.

(c) An analysis of financing activities, which provides information relevant in assessing future cash flow requirements due to debt financing arrangements. This analysis may highlight cash proceeds from debt issues or redemptions. It may also highlight significant changes in capital leases. Further, it may be helpful in explaining the need for borrowing even though the entity has reported a surplus in its statement of operations.

(d) Analysis of whether the entity has complied with any spending mandates expressed in cash flow terms.

(e) Trend analyses of operating, investing and financing cash flows, or components thereof.

**Commitments, Contingencies, and Events after the Reporting Date**

B.IG22. Where they are significant to the entity, information may be required pertaining to events occurring after the reporting date and planned future events, such as those described in paragraph B13(c), but which did not occur in the reporting period, and are therefore not reflected in the entity’s financial statements. Such information assists users in assessing future revenue requirements of the entity.

(a) Financial statement discussion and analysis may include the following additional information:

(b) A subsequent issue of debenture debt;

(c) Litigation;

(d) Capital and operating leases;

(e) Service concession arrangements; and

(f) Various types of guarantees.

B.IG23. Although such disclosures are required to be provided in the notes to the financial statements in accordance with various IPSASs, further elaboration of such transactions and events may assist in providing greater insight as to how such events may affect the entity's future operations.

## Section C: Examples of Information about Variances and Trends

C.IG1. Paragraph 15(c) requires financial statement discussion and analysis to include information about the entity's financial statements, including variances and trends. This Implementation Guidance includes guidance on the type of information an entity may provide in its discussion and analysis to satisfy that requirement.

### Actual-to-Budget Variances

C.IG2. Paragraph 29(b) of IPSAS 24, *Presentation of Budget Information in Financial Statements*, requires explanations of material differences between actual and budget amounts to be included in the notes to the financial statements, unless (a) included in other public reports or documents issued in conjunction with the financial statements, and (b) the notes to the financial statements identify the reports or documents in which the explanation can be found.

C.IG3. In cases where this exemption is followed and the explanations are presented in financial statement discussion and analysis, paragraph 14 of IPSAS 24 requires a cross-reference to those documents to be made in the notes to the financial statements. Where such a comparison is included in financial statement discussion and analysis, a cross-reference to the financial statements should be provided in the financial statement discussion and analysis.

### Year-to-Year Variances and Trends

C.IG4. Financial statement discussion and analysis may include an analysis of trends in an entity's financial position and financial performance that provides information that is useful beyond the date of the financial statement discussion and analysis. For example:

(a) Analysis of changes in the nature and extent of financial assets provides information regarding the amount of resources available to be converted to cash if necessary. In addition, specific ratios and analysis of cash flows may be useful to highlight liquidity.

(b) Analysis of changes in revenues by major source may indicate trends and dependencies on specific revenue sources (e.g., government business enterprises (GBEs), transfers, or royalties).

(c) Analysis of changes in expenses may demonstrate the entity's allocation and use of resources, provide insight into the cost of programs and services, and assist in evaluating the cost of borrowing to finance spending.

(d) Discussion of significant changes in commitments, contingencies, and subsequent events assists users in assessing future revenue requirements of the entity.

C.IG5. In some cases, a significant change may have occurred during the reporting period, but the financial statements and quantitative analyses may not illustrate a significant variance because of offsetting factors. Explanations contained in financial statement discussion and analysis may identify and explain significant variances between the current year and prior year such as variances due to changes in how a service is delivered, changes in programs and services provided, and changes due to the level of revenues raised or costs incurred. Some of these may be within the control of the entity (e.g., taxation rates, new or discontinued programs or services, restructuring operations, or changing the method of service delivery), while others may be more due to external factors (e.g., a downgraded credit rating, a decreased tax base, wage contracts, and unexpected events such as a natural disaster). Such explanations may assist users in assessing possible future changes in current services and commitments of the entity.

C.IG6. Trend analysis may cover several prior years if the information is available and can be presented in a consistent manner. In such cases, the source of information related to periods not covered by the comparative information in the financial statements to which the financial statement discussion and analysis pertains would be disclosed.

C.IG7. In cases where the presentation of the underlying financial statements has changed in accordance with paragraph 42 of IPSAS 1, the presentation of any information in the financial statement discussion and analysis based on the changed financial statements should also change.

C.IG8. When historical information is not be readily available on which to base trend analyses for some or all of the entity's operations an entity should, on a best-efforts basis, include in the financial statement discussion and analysis, the information it possesses that meets the qualitative characteristics and indicate that historical information is not readily available. When the data is available for only part of the reporting entity, the financial statement discussion and analysis should be provided on a limited-scope basis, and clearly describe the scope of information including the fact that information related to certain activities is not available. This allows an entity to begin trending the relevant data.

C.IG9. Other changes may affect the trend analysis. For example, when an entity restructures its operations or chooses an alternative method of service delivery, this may affect certain trends. In cases where such changes have significantly affected a trend, the financial statement discussion and analysis should describe the reasons for the changes in the trend to assist users in understanding and assessing the financial effect of those changes.

## Illustrative Example

*This example accompanies, but is not part of, IPSAS XX (ED 47).*

The purpose of this example is to illustrate the information that a national government may include in its financial statement discussion and analysis. This example is one illustration of the format and content of information an entity could disclose in order to meet the requirements set out in this Standard. However, this illustration is not intended to be a template for financial statement discussion and analysis. For example, other information may be appropriate to the circumstances of departments, agencies, and other public sector entities. All entities are encouraged to report financial statement discussion and analysis in a way that best informs readers about their own significant matters related to their specific circumstances, including the use of diagrams, charts, and graphs.

# GOVERNMENT OF COUNTRY A ("THE GOVERNMENT")

## Financial Statement Discussion and Analysis

This section of the Government of Country A's ("the Government") annual financial report presents our discussion and analysis of the Government's financial position and financial performance during the year ended December 31, 20X9 [*if the entity is required to provide financial statement discussion and analysis by way of legislation or regulation, it may state the relevant requirements here*]. This Financial Statement Discussion and Analysis has been prepared in accordance with IPSAS XX (ED 47), *Financial Statement Discussion and Analysis.*

This Financial Statement Discussion and Analysis is not part of the Government's financial statements; however it should be read together with the Government's financial statements on pages XX to XX of this report.

## Overview of the Financial Statements

Financial statements are prepared for the Government as a whole as specified in the *Government of Country A Public Sector Finance Act 2000* (PFA). The PFA also requires this financial statement discussion and analysis, which explains the significant items, transactions, and events presented in the financial statements and the trends and factors that influenced them, to accompany the Government's financial statements.

Parliamentary and state sector entities and organizations for which statements are prepared include: Ministries, Departments, Offices of Parliament, state-owned enterprises, and the Government of Country A Reserve Bank. A full list of government reporting entities can be found in the Supplementary Information section of this financial report as at December 31, 20X9 (see "Government Reporting Entity").

Our report consists of the financial statement discussion and analysis (this section) and the financial statements. The financial statements consist of:

- A Statement of Financial Position – which provides information about the accumulated deficit—the difference between the Government's total liabilities and total assets. It provides information about:
  - The extent to which resources are available to support the Government's future service delivery objectives; and
  - The amounts and timing of future cash flows necessary to service and repay existing claims to the Government's resources.
- A *Statement of Financial Performance* – which measures the net surplus or deficit— the difference between revenues and expenses. It provides information about:
  - Costs of service delivery; and
  - The amounts and sources of cost recovery (e.g., through taxes, user charges, contributions and transfers, or by increasing the level of indebtedness).

The annual surplus or deficit is presented on an accrual basis of accounting, recognizing revenue in the period it is earned and expenses when incurred, regardless of when the associated cash is received or paid.

- A *Statement of Changes in Net Assets/Equity* – which highlights the sources of changes in Government of Country A's overall financial position, including:
  - Gains and losses that directly affect the Government's total assets less liabilities;
  - Changes due to the surplus or deficit for the period.
- A *Cash Flow Statement* – which provides information about the Government of Country A's liquidity and solvency, including:
  - How the Government raised and used cash during the period, including its borrowing and repayment of borrowing and its acquisition and sale of, for example, property, plant, and equipment; and
  - The cash received through taxes and investments and the cash transfers made to, and received from, other entities, government agencies, and international organizations.

  In contrast to the Statement of Financial Performance, the Government's net cash flow measures the difference between cash coming in to the Government and cash going out.
- A comparison of budget and actual amounts – which highlights:
  - Whether resources were obtained and used in accordance with the approved budget; and
  - Reasons for material departures from the approved budget for which the entity is held publicly accountable.
- Notes – which assist users in understanding the financial statements and comparing them with financial statements of other entities. Notes comprise a summary of significant accounting policies and other explanatory notes:

  (a) Present information about the basis of preparation of the financial statements and the specific accounting policies used;

  (b) Disclose the information required by IPSASs that is not presented on the face of the statement of financial position statement of financial performance, statement of changes I net assets/equity, or cash flow statement; and

  (c) Provide additional information that is not presented on the face of the statement of financial position, statement of financial performance, statement of changes in net assets/equity, or cash flow statement.

## About the Government[1]

Country A has a small open economy which operates on free market principles. It has sizable manufacturing and service sectors complementing a highly efficient agricultural sector. Country A is highly dependent on the primary sector with commodities accounting for around half of total goods exports. Exports of goods and services account for around one third of GDP.

[1] This section addresses relevant information from the "Overview of the Entity" requirement. Since the Government of Country A is a government and not a sub-entity of a government, some details (e.g., mission and vision and description of the entity's governance and management structure) are not addressed in this example. In addition, some of the details in this section pertain to risks and uncertainties due to global risks.

Exhibit 1 and Exhibit 2 show breakdowns of the GDP by production group and by industry group respectively.

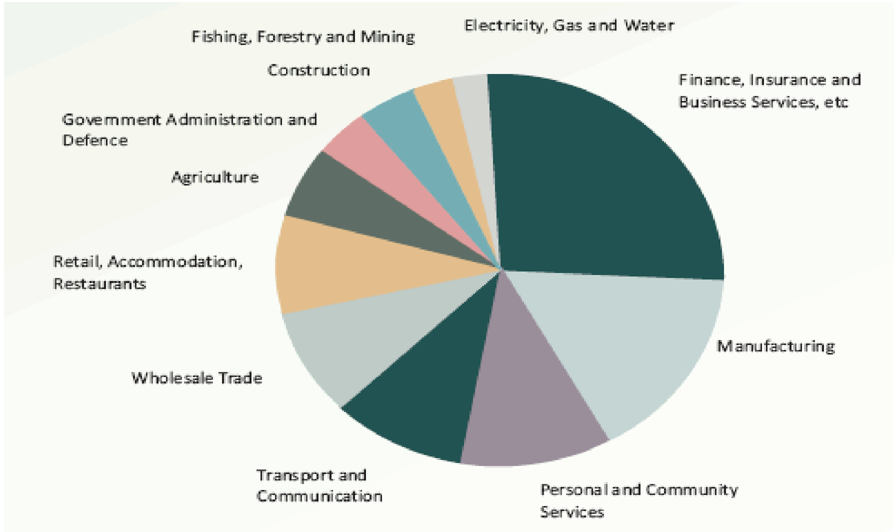
**Exhibit 1 – Gross Domestic Product by Production Group[2]**

The following table shows Gross Domestic Product by major industries:

| | GDP (millions of Currency Units) Year ended December 31 | | | | | |
|---|---|---|---|---|---|---|
| | **20X5** | **20X6** | **20X7** | **20X8** | **20X9** | **20X9 % of Total** |
| **Finance Insurance & Business Services** | 326,150 | 339,960 | 350,250 | 362,280 | 367,930 | 27.6% |
| **Manufacturing** | 195,730 | 196,840 | 185,970 | 185,970 | 176,120 | 13.2% |
| **Personal & Community Services** | 148,220 | 151,240 | 152,160 | 155,040 | 159,470 | 11.9% |
| **Transport & Communication** | 129,030 | 133,870 | 135,360 | 143,040 | 143,340 | 10.7% |
| **Retail, Accommodation, Restaurants** | 94,060 | 98,260 | 100,980 | 104,100 | 100,420 | 7.5% |
| **Wholesale Trade** | 98,240 | 100,770 | 100,900 | 105,230 | 99,730 | 7.5% |
| **Govt Administration & Defence** | 52,010 | 54,920 | 59,540 | 63,740 | 66,730 | 5.0% |
| **Agriculture** | 61,430 | 65,040 | 66,470 | 64,720 | 63,100 | 4.7% |
| **Construction** | 61,900 | 65,010 | 63,310 | 65,920 | 60,100 | 4.5% |
| **Fishing, Forestry, Mining** | 26,340 | 27,550 | 27,090 | 34,190 | 33,350 | 2.5% |
| **Electricity Gas & Water** | 25,260 | 24,410 | 26,020 | 25,090 | 25,220 | 1.9% |
| **Gross Domestic Product** | 1,263,930 | 1,303,830 | 1,315,000 | 1,353,670 | 1,334,860 | 100.0% |
| **Annual Average % change** | 3.7% | 3.2% | 0.9% | 2.9% | (1.4%) | |
| **Primary Industries** | 88,660 | 93,590 | 94,510 | 100,510 | 98,010 | 7.3% |
| **Goods Producing Industries** | 283,230 | 286,510 | 276,790 | 278,330 | 263,050 | 19.7% |
| **Services Industries** | 843,700 | 875,050 | 896,090 | 928,980 | 935,040 | 70.0% |
| **Gross Domestic Product** | 1,263,930 | 1,303,830 | 1,315,000 | 1,353,670 | 1,334,860 | 100.0% |

2 20X9 data estimated. Prior year's data revised.

**Exhibit 2 – Gross Domestic Product by Industry Group**




Throughout 20X8 and into early 20X9, the global economy continued its recovery from the deepest and most synchronized recession since the 1930s. During this time, global financial market conditions improved and commodity prices rebounded.

Reflecting Country A's solid economic and fiscal fundamentals, together with the impact of its *Economic Action Strategy* (EAS – see details below)[3] and monetary policy stimulus, Country A's economy has recovered more strongly from the recession more than all of the employment lost during the downturn.

Growth in Country A's economy has been fuelled by a strong rebound in domestic activity. Growth in real consumer spending on goods and services averaged more than 3 percent per quarter in 20X8. Business investment in machinery and equipment was even stronger, growing on average by more than 17 percent per quarter. In the first half of 20X9, domestic demand in Country A remained strong, with consumption and business investment continuing to expand. In particular, business investment in machinery and equipment grew by more than 16 percent. The strength of the domestic economy, however, has been dampened by weak demand for Country A's exports, particularly from its largest trading partner, Country B.

The economic recovery has underpinned a strong rebound in Country A's labor market. By August 20X9, the economy had created about 600,000 jobs relative to its trough in July 20X0—more than offsetting the jobs lost during the global economic downturn of that period. Furthermore, most of the jobs created over the recovery have been full-time and in relatively high-wage industries.

The level of economic activity in 20X8 was considerably higher than in 20X0. Real GDP increased by 3.2 percent in 20X8. Nominal GDP (the broadest single measure of Country A's tax base) increased by 6.3 percent as a result of the increase in real GDP together with a significant rebound in global commodity prices.

However, in more recent months, the global economic recovery has become uneven and more fragile and downside risks have become more significant. Weakening global economic growth, particularly in

3 In Budget 20X0, the Government introduced its EAS in response to the worst economic and financial crisis since the 1930s. To learn more about individual elements visit the EAS web site.

the U.S. and Europe, combined with ongoing concern about sovereign debt in Europe, have led to increasing volatility in global equity, bond and foreign exchange markets. Country A will not continue to be immune from these external developments.

Real GDP contracted slightly in the second quarter of 20X9—the first quarter of negative growth since mid-20X0. The outlook for Country A looking forward is for positive but modest growth. However, risks remain to this outlook, given the recently renewed uncertainty surrounding the global economic situation.

## Objectives and Strategy[4]

### Economic Action Strategy

The Government of Country A's *Economic Action Strategy* (see Exhibit 3 for highlights) is directed towards lifting the performance of the economy and achieving higher living standards for citizens of Country A. It helped lay the foundation for long-term prosperity by supporting key drivers of economic growth—innovation, business investment, families, communities, education and training—in a responsible manner that preserves Country A's fiscal advantage.

**Exhibit 3 – Highlights of the Economic Action Strategy**

**HIGHLIGHTS OF THE EAS**

As a short-term strategy, the EAS was designed to support economic growth and job creation, and its implementation has been effective at shielding citizens from the worst impacts of the global recession. The EAS has:

- Reduced tax rates.
- Helped the unemployed through enhanced benefits and training programs.
- Prevented layoffs by enhancing the work-sharing program.
- Made significant investments in infrastructure.
- Provided support to the housing sector through the Residence Renovation Tax Credit.
- Advanced Country A's knowledge economy by improving infrastructure at colleges and universities and supporting research and technology.
- Supported industries and communities most affected by the global downturn.
- Improved access to and the affordability of financing for Country A households and businesses.

These measures have been implemented across a large number of departments, agencies and state-owned corporations, often in partnership with other levels of government.

Because the stimulus in the EAS was designed to provide temporary support to the economy, the vast majority of initiatives announced in Budget 20X9 ended as planned on December 31, 20X8. In

[4] This section addresses relevant information from the "Information About the Entity's Objectives and Strategies" requirement.

order to provide additional flexibility to the Government's partners, the completion deadline for four state and municipal infrastructure programs was extended to September, 20X9. As a result of this decision, the economic benefits and job creation impact of stimulus projects were continued for an additional construction season.

Sustained and steady growth in citizens' incomes is a central means of improving their living standards. Economic growth enables choices by individuals and provides the means to acquire many of the things we value. It also gives the Government choices; this includes how it funds education, health, environmental protection, physical and social infrastructure, and assistance to those in need.

Higher living standards also incorporate elements that are broader than increases in consumption and income. These determinants of an individual's well-being are likely to include such things as good health, a satisfying job, and a high-quality natural environment. And beyond individual well-being, most citizens of Country A also place a high value on social inclusion, freedom, security, democracy, equality of opportunity, and our physical environment. These dimensions of well-being are clearly important in their own right, and some are also important contributors to economic performance.

To that end, the next phase of Country A's Economic Action Strategy will take steps to advance the Government's long-term objective of building a stronger economy that generates high-wage jobs.

The next phase is centered on four strategic areas:

- **Supporting Job Creation:** Creating the right environment for businesses and entrepreneurs to invest in Country A and succeed in the global economy, leading to higher rates of productivity growth, more and better-paying jobs for citizens of Country A, and a higher standard of living.
- **Supporting Families and Communities:** Ensuring that all citizens of Country A can enjoy a high quality of life and benefit from the opportunities that long-term growth creates.
- **Investing in Innovation, Education and Training:** Promoting the research and development that will give our firms a competitive advantage in global markets and providing citizens of Country A with the opportunity and incentives to acquire the education and skills needed for increasingly complex, high-wage jobs.
- **Preserving Our Fiscal Advantage:** Maintaining a strong environment for growth by ensuring the Government will return to fiscal balance in the medium term, providing confidence and certainty to citizens and businesses of Country A.

By focusing on the drivers of growth, the next phase of the Economic Action Strategy will help individuals, entrepreneurs and businesses create the wealth Country A needs to invest in health care, infrastructure and other services that promote vibrant communities and maintain our high quality of life. Budget 20X9 introduced a number of targeted measures to support these objectives.

However, subsequent to the issuance of the Budget, the global economic crisis has further deepened and The Government of Country A is now considering amendments to the EAS to respond to these new challenges.

### Strategic Reviews

The Government of Country A conducts reviews of its strategic reviews of its existing spending on a four-year cycle to:

- **Increase efficiency and effectiveness**. Change the way the Government delivers programs and services to be more effective and efficient.

- **Focus on core roles**. Focus on providing programs that are consistent with federal roles and responsibilities, and ensure services are delivered by those best positioned to do so.
- **Meet the priorities of citizens of Country A**. Align federal activities with the needs and priorities of citizens of Country A and eliminate programs that are no longer necessary.

The second and third of these goals are not addressed directly in the general purpose financial statements[5].

Budget 20X10 delivers over CU500 million in new ongoing savings from the 20X9 round of strategic reviews, which were undertaken to ensure that programs are achieving their intended results, are effectively managed, and are appropriately aligned with the priorities of citizens of Country A and federal responsibilities. When combined with the previous three rounds of reviews, the strategic review process has provided more than CU2.8 billion in ongoing savings.

**Responsible Fiscal Management**

Fiscal policy is one tool for achieving a government's economic and social objectives. The PFA requires the Government to outline its fiscal policy intentions in the annual *Fiscal Strategy*. This fiscal strategy is undertaken through the setting of long-term fiscal objectives relating to expenses, revenue, the operating balance, debt and net worth over a period of at least 10 years.

The PFA requires the Government to pursue its policy objectives in accordance with the following principles of responsible fiscal management:

- Maintaining debt at a prudent level by ensuring that, on average, over a reasonable period of time, total operating expenses do not exceed total operating revenue.
- Achieving and maintaining net worth at levels which provide a buffer against factors which may adversely impact on net worth in the future.
- Managing prudently the fiscal risks facing the Government.
- Pursuing policies which are consistent with a reasonable degree of predictability about the level and stability of taxes for future years.

The PFA also requires the Government to present, in each financial year, two reports outlining government's fiscal policy: the *Budget* and the *Fiscal Strategy*. The *Annual Budget* has a short run focus setting out policy goals that will guide the Government's Budget decisions and priorities. The *Fiscal Strategy* is presented with the *Budget* and must state the Government's long-term objectives for fiscal policy over a period of at least 10 years and the Government's short-term intentions for fiscal policy over a period of three years.

The *Fiscal Strategy* must also provide projections of fiscal variables to show progress towards meeting the long term objectives.

In addition, the Government Treasury is required to publish, at least every four years, a *Report on Long-Term Fiscal Sustainability*. This has a horizon of at least 40 years and identifies how demographic and other changes may impact the fiscal position.

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[5] Such information would be reported in other general purpose financial reports of the Government such as those on service performance and long-term fiscal sustainability.

### Fiscal Strategy of the Government

The current government's fiscal strategy—set out in Budget 20X10—aims to deliver a fiscal position that is sustainable in the long term, contributes to economic stability and advances key priority policies.

The Government has sought to strengthen its fiscal position so that it is well placed to respond to future challenges such as those associated with population ageing.

The strategy aims to provide certainty to households, businesses and investors by keeping taxes and core government expenses around current levels. By keeping finance costs low, it will ensure flexibility in meeting future fiscal pressures by maintaining a low level of debt.

Budget 20X10 set out a three-point plan for returning to balanced budgets over the medium term by:

- Winding down the stimulus provided in the Government of Country A’s *Economic Action Strategy* as the economy recovers.
- Implementing targeted measures to restrain growth in direct program spending.
- Undertaking a comprehensive review of government administrative functions and overhead costs.

The Government of Country A has been clear and consistent that it will not raise taxes or cut transfers to persons, including those for seniors, children and the unemployed, or transfers to other levels of government in support of health care and social services, equalization payments, and the gas tax transfer to municipalities.

The emphasis on the careful management of direct program spending reflects the Government's fundamental belief that the private sector will continue to be the engine of growth and wealth creation.

### Planned Borrowing Activities for 20X9-20X10

The *Debt Management Strategy* (see Exhibit 4 for highlights) sets out the Government of Country A’s objectives, strategy and plans for the management of its domestic and foreign debt, other financial liabilities and related assets. Borrowing activities support the ongoing refinancing of government debt coming to maturity, the execution of the budget plan, and other financial operations of the Government, including investing in financial assets needed to establish a prudent liquidity position and borrowing on behalf of some state-owned corporations.

The *Financial Administration Act* requires that the Government table in Parliament, prior to the start of the fiscal year, a report on the anticipated borrowing to be undertaken in the year ahead, including the purposes for which the money will be borrowed. This legislative requirement was fulfilled with the tabling of the 20X10–20X11 *Debt Management Strategy*.

For 20X9–20X10, the aggregate borrowing limit that was approved by Parliament to meet updated Budget 20X9 financial requirements and provide a margin for prudence was CU300 billion, the same amount requested and approved for 20X8–20X9.

Actual borrowing and uses of funds compared with those forecast will be reported in the 20X9–20X10 *Debt Management Report*, and detailed information on outcomes will be provided in the *20X11 Public Accounts of the Government of Country A*. Both documents will be tabled in Parliament in Q4 of 20X10.

**Exhibit 4 – Highlights of the Debt Management Strategy**

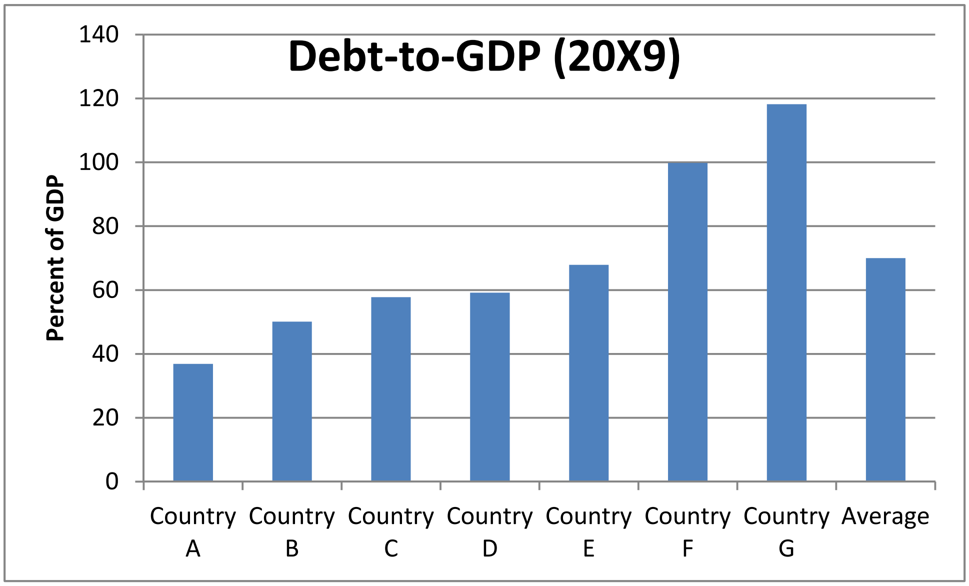
**HIGHLIGHTS OF THE DEBT MANAGEMENT STRATEGY**

- Updated Budget 20X10 financial requirements for 20X10-20X11 are projected to be higher than in 20X9-20X10 at CU47 billion versus CU36 billion.
- The debt program for 20X10-20X11 has been developed in the context of a new medium-term debt management strategy focused on stability and reduced financing risk.
- For 20X10-20X11, gross issuance of domestic marketable bonds is planned to be approximately CU102 billion. At the end of 20X10-20X11, the stock of marketable bonds is projected to be CU461 billion.
- Four new maturity dates have been introduced to reduce rollover risk. These new dates are expected to greatly reduce single-day rollover of maturing debt, with noticeable improvements beginning as early as 20X11-20X12.
- Benchmark target range sizes in the 2-, 3- and 5-year sectors have been increased to facilitate the transition to the adjusted maturity dates in those sectors.
- Regular bond buyback program operations are planned to be CU8 billion in 20X10-20X11, about CU3 billion higher than in 20X8–20X9. For 20X10-20X11, buyback operations on a cash basis will be reintroduced for longer-dated bonds.
- By the end of 20X9–20X10, the treasury bill stock is projected to be CU150 billion, about CU13 billion higher than the year-end level for 20X8–20X9.
- To improve prudential liquidity management, over the next three years, the Government will borrow an additional amount of CU35 billion to safeguard its ability to meet payment obligations in situations where normal access to funding markets may be disrupted or delayed. This financing activity will have no material impact on the federal debt as the cost of the additional borrowing will be offset by a corresponding increase in returns on interest-bearing assets.

According to the Organisation for Economic Co-operation and Development (OECD), Country A's total government liabilities-to-GDP[6] ratio stood at 36.9 percent in 20X9 (see Exhibit 5). This is the lowest level among G7 countries, which the OECD estimates will record, on average, a debt-to-GDP ratio of 71.4 percent for that same year.

[6] 20X9 GDP was CU1,705,017 (millions).

**Exhibit 5 – Debt-to-GDP (20X9)**




## Financial Statement Highlights

- Overall, net assets increased by CU142,250,000 (17%), mainly due to an increase in the surplus for the period.
- The Government of Country A's total current assets decreased by CU13,860 (2%). This resulted from a decrease of CU10,500,000 (2%) in its most liquid assets—cash and cash equivalents and receivables, which was offset by a increases in inventories and other current assets. Current liabilities decreased by CU139,320 (30%). The Government's short-term liquidity, as measured by the change in current assets—current liabilities, improved by CU125,460,000.
- The increase in the 20X9 surplus over the 20X8 surplus of CU55,750,000 (85%) was largely due to increased revenues from taxes, fees and transfers from other governments, as well as modest decreases in overall expenses for the period of CU6,383,000 (1.9%). The Government of Country A introduced measures to reduce costs during 20X9, and it is expected that for 20X10 further cost savings will be realized.
- The growth in tax revenues of CU24,400,000 (9.3%) was mainly due to the increase in personal tax revenues, which was caused by strong growth in wages and employment during the year. Recent data published by the government's Statistics Department suggests that this growth will not continue due to lower employment figures and wage increases resulting from a weakening economy.
- The Government of Country A's long-term borrowing position improved overall by CU40,000,000 (25%). Its total liabilities, which are a claim on future resources, also decreased by CU199,950,000 (29%).

## Risks and Uncertainties

A large proportion of the risks and uncertainties around the outlook for Country A relate to the global economic outlook, especially around global financial markets and international commodity prices. If global growth falters and credit conditions tighten again, both businesses and households will be adversely affected. Country A's performance through the crisis has, however, demonstrated a degree of resilience, with no major bank failures, only a moderate fall in GDP from peak to trough, and with modest growth resuming from Q2 20X10. Risks remain around a resumption in domestic demand in the near term, particularly if the labor market deteriorates more rapidly than anticipated. The path taken by the exchange rate is an additional source of uncertainty.

### Debt Management Strategy

The fundamental objective of debt management is to raise stable and low-cost funding to meet the financial needs of the Government of Country A. An associated objective is to maintain a well-functioning market in Government of Country A's securities, which helps to keep debt costs low and stable.

### Foreign Currency Strategy

The purpose of the Exchange Fund Account (EFA) is to aid in the control and protection of the external value of the Country A currency unit (CU). Assets held in the EFA are managed to provide foreign currency liquidity, support market confidence, and promote orderly conditions for the Country A CU in the foreign exchange markets, if required.

The Government has access to a range of direct sources of funding for its foreign currency assets, including a short-term U.S.-dollar paper program, medium-term note issuance in various markets, international bond issues, purchases and sales of Country A CUs in foreign exchange markets, and cross-currency swaps involving the exchange of domestic liabilities for foreign-currency-denominated liabilities.

As part of the planned increase in prudential liquidity and ongoing International Monetary Fund commitments, the level of foreign exchange reserves will increase by about CU10 billion by the end of 20X9–20X10. The mix of funding sources used to finance this increase will depend on a number of considerations, including relative cost, market conditions, and the objective of maintaining a prudent foreign-currency-denominated debt maturity structure. The medium-term debt strategy assumes that all foreign liabilities maturing during the year will be refinanced. However, the amount of foreign currency funding may vary from the plan, depending on market conditions and government foreign currency needs.

Further information on managing foreign currency reserves and funding objectives is provided in *Management of Country A's Official International Reserves*, which is available on the Government Treasury website.

## Variances and Trends[7]

### Budget 20X9 Restraint Measures Are On Track

*Budget 20X9* implemented targeted measures to restrain direct spending growth and close tax loopholes that are expected to generate savings of CU17.6 billion over five years. The Government is on track to meet this spending restraint commitment as:

- The Department of National Defence is on track to achieving the savings required to meet the commitment to restrain growth in defence spending.
- In 20X8–20X9, The Government of Country A fulfilled its commitment to double international assistance. International Assistance funding has now been capped at CU5 billion.
- Savings of CU300 million in 20X8–20X9 have been achieved as departments and agencies absorbed the 1.5 percent wage increase for the federal public administration.
- The operating budgets of departments remain frozen at their 20X8–20X9 levels for two years.

### Building On Budget 20X9 Restraint Actions

Budget 20X10 builds on the actions taken in *Budget 20X9* by announcing the following measures that could achieve an additional CU17.2 billion in savings over five years:

- Delivering on the 20X9 round of strategic reviews.
- Taking action to close tax loopholes.
- Launching a comprehensive one-year Strategic and Operating Review aimed at improving the efficiency and effectiveness of government operations and programs to ensure value for taxpayer money.

### Revenues

Revenues totaled CU228.8 billion in 20X8–20X9. Exhibit 6 illustrates the composition of revenues for 20X8–20X9.

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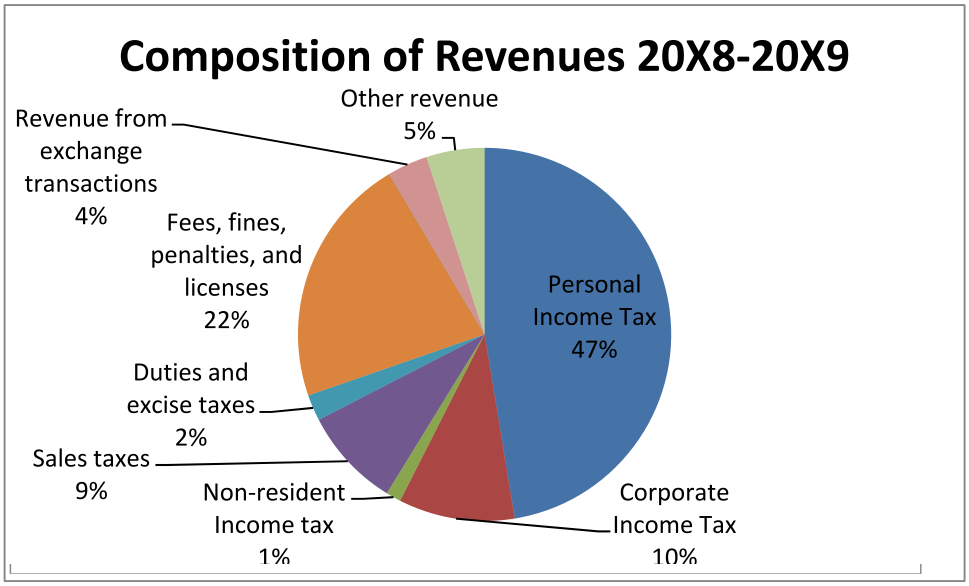
[7] It is assumed that detailed actual-to-budget comparisons are reported elsewhere and are thus not duplicated in the financial statement discussion and analysis.

**Exhibit 6 – Composition of Revenues 20X8-20X9**




The largest overall source of revenues is income taxes. Personal income taxes accounts for 47 percent of total revenues. Revenues from this source increased 7.8 percent from 20X7–20X8, reflecting higher employment, even though average personal tax rates were reduced. Corporate income taxes also increased, by 8.3 percent from 20X7–20X8 reflecting higher corporate profits.

Sales taxes also increased from 20X7–20X8 due to increased consumer spending on goods and services.

This trend of increased tax revenues from all sources is not expected to repeat in 20X9–20X10 due to the expected impact of the global recession on Country A.

Exhibit 7 shows the changes in significant revenue sources from 20X8.

**Exhibit 7 – Change in Revenues**

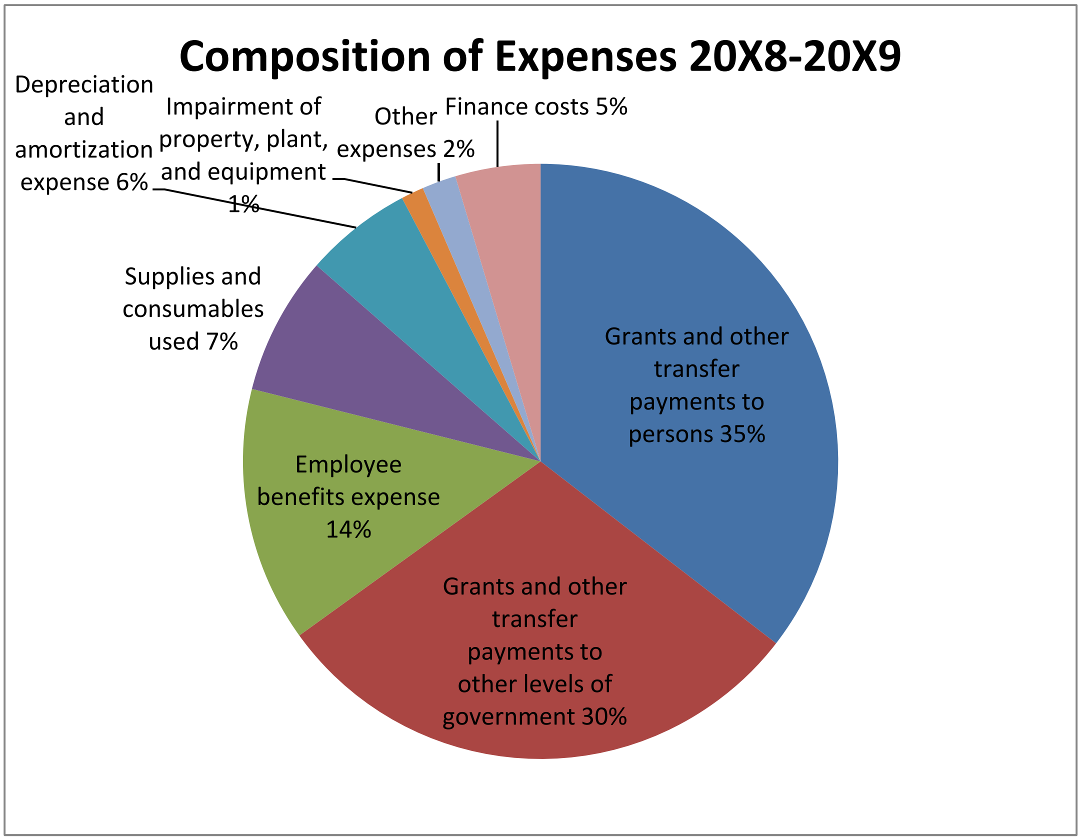
(in millions of currency units)

| **Revenues** | **20X9** | **20X8** | **Net Change (CU)** | **Net Change (%)** |
|---|---|---|---|---|
| Income Taxes | | | | |
| Personal | 194,684 | 180,532 | 14,152 | 7.8 |
| Corporate | 41,333 | 38,141 | 3,192 | 8.3 |
| Non-resident | 5,361 | 5,524 | -163 | -3.0 |
| Other taxes and duties | | | | |
| Sales taxes | 35,500 | 30,932 | 4,568 | 14.8 |
| Duties and excise taxes | 9,322 | 6,671 | 2,651 | 39.7 |
| Total Tax Revenues | 286,200 | 261,800 | 24,400 | 9.3 |
| Fees, fines, penalties, and licenses | 89,400 | 80,600 | 8,800 | 10.9 |
| Revenue from exchange transactions | 14,400 | 12,600 | 1,800 | 14.3 |
| Other revenue | 20,667 | 11,300 | 9,367 | 82.9 |
| **Total Revenues** | 410,667 | 366,300 | 44,367 | 12.1 |

**Expenses**

Expenses totaled CU228.8 billion in 20X8–20X9. Exhibit 8 illustrates the composition of expenses for 20X8–20X9.

**Exhibit 8 – Composition of Expenses 20X9-20X9**




Expenses consist of transfer payments, program expenses and public debt charges. In 20X8–20X9, expenses amounted to CU324.5 billion, down CU6.38 billion, or 1.9 per cent, from 20X7–20X8.

Major transfers to persons (income supplements, social security payments, and children's benefits) and to other levels of government (the Health Transfer, the Social Transfer, fiscal arrangements, and transfers to cities and communities) were the two largest components of expenses in 20X8–20X9, representing 35 percent and 30 percent of expenses, respectively.

Transfers to persons increased 6.7 percent from 20X8 due to increased spending under the EAS on:

- Helped the unemployed through enhanced benefits and training programs.
- Prevented layoffs by enhancing the work-sharing program.
- Provided support to the housing sector through the Residence Renovation Tax Credit.

Transfers to other levels of government increased 4.3 percent for:

- Investments in infrastructure (e.g., by improving infrastructure at colleges and universities, expansion of the subway system in Country A's largest municipality, rehabilitation of the transnational highway).
- Advancement of Country A's knowledge economy by supporting research and technology investment.
- Support of industries and communities most affected by the global downturn.

After major transfers to persons and to other levels of government, the next largest component of expenses was the cost of programs and services provided by government departments and agencies, excluding National Defence, at 18.4 per cent. Program costs include items such as salaries and benefits, facilities and equipment, and supplies and travel.

The largest increase in this category from 20X8 was in consumables and supplies. This was due to printing of forms and brochures related to new programs (e.g., Residence Renovation Tax Credit). Employee salaries and benefits increased by 4.7 percent mainly due to new collective agreements with unions covering the largest group of public servants.

Public debt charges amounted to 5 percent of expenses in 20X8-20X9. This is expected to increase in the coming year due to future borrowing requirements resulting from the impacts of the global recession, as discussed previously.

The Exhibit 9 shows the changes in significant expenses from 20X8.

**Exhibit 9 – Change in Expenses**

(in millions of currency units)

| **Expenses** | **20X9** | **20X8** | **Net Change (CU)** | **Net Change (%)** |
|---|---|---|---|---|
| Grants and other transfer payments to persons | 115,100 | 107,900 | 7,200 | 6.7 |
| Grants and other transfer payments to other levels of government | 96,000 | 92,000 | 4,000 | 4.3 |
| Costs of programs and services | | | | |
| Employee salaries and benefits | 45,000 | 43,000 | 2,000 | 4.7 |
| Supplies and consumables used | 24,417 | 17,000 | 7,417 | 43.6 |
| Depreciation and amortization | 19,000 | 17,000 | 2,000 | 11.8 |
| Impairment of property, plant, and equipment | 4,000 | – | 4,000 | – |
| Other expenses | 6,000 | 5,500 | 500 | 9.1 |
| Finance costs | 15,000 | 18,000 | -3,000 | -16.7 |
| Restructuring costs | – | 30,500 | -30,500 | – |
| **Total Expenses** | 324,517 | 330,900 | -6,383 | -1.9 |

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