# Issue Paper #6

# Accounting Policy
# and
# External Review of Budget

The Budget Process Review Panel

An independent panel appointed to recommend improvements
to the budgeting and financial management
of the Province of British Columbia

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## Issue

This issue paper is about two potential mechanisms for adding credibility to the budget process – accounting policy and external review. These are not the only mechanisms for adding credibility to the process. The other ways include disclosure of expected and actual results (covered in Issue Paper #3 – Accountability and Performance Management) and disclosure of assumptions and the basis of forecasting (to be covered in Issue Paper #7 – Revenue and Expenditure Forecasting). However, accounting policy and external review are closely linked and have been emphasized by the Auditor General as important ways of adding credibility to the process.

The specific questions to be addressed by the Panel are:

- How should Government's accounting policies and the interpretation of those accounting policies be established?
- Should the accounting policies apply to the budget and Estimates?
- Should there be external review of budget practices or information?

## Suggested Reading

Chapter 2 of the Auditor General's report deals with the issues described above in several different sections.

## Terms of Reference and OAG Recommendations

The Panel's Terms of Reference include the following:

> Specifically the panel will be asked for advice on:
>
> E. Any changes in the form or content of information provided by government in its annual planning and its reports on results to improve clarity and usefulness to readers.

That would include content regarding accounting policies and any external review of budget practices or information.

The Auditor's General's report includes the following relevant recommendations:

> 2.3 The government require the Auditor General to annually comment on the accounting policies used in preparing the Estimates.
>
> 2.8 The government adopt policies and establish practices to help make the presentation of the Province's fiscal conditions, as well as of economic factors and fiscal measures underlying the budget and the Estimates, more transparent.
>
> 2.12 The government guard the reliability of all information provided in the Estimates and budget documents by ensuring it is supportable and free from error and bias, and is based on prudent planning discipline and appropriate accounting.
>
> 2.13 The government provide in the annual Estimates detailed information and explanation that improve Estimates comparability with other accountability documents, especially the summary financial statements of the Province.
>
> 2.14 The government improve understandability of information in the annual Estimates by, for example, ensuring it is prepared on a gross basis of accounting, explaining the nature and use of special accounts, and describing how the data in

the Estimates was developed, compiled and reviewed.

## Discussion

### *Problems Arising from Accounting Policies*

There are a number of ways that accounting policy can affect the summary financial information such as the deficit, debt, total expenditure, growth in expenditure, etc. This is a problem if accounting policy is used or set with the intention of making the results appear to be different than they would be using an alternative set of policies. Some of the types of problems encountered are described below.

#### The Entity

This issue is discussed in detail in Issue Paper #2. A comprehensive accounting entity is needed to ensure that government's financial statements give a full picture of the size of government and its financial position. One problem that can arise is that, if the entity is not comprehensive and defined in accordance with appropriate principles it is possible to affect the summary results and the reported deficit by manipulating what operations and functions are included in the entity.

There are two issues at present. The first is that budgeting is done using a relatively narrow entity referred to as the Consolidated Revenue Fund (CRF) while the Public Accounts are based on a broader entity, known as the Summary Entity that includes all Crown corporations and some other public bodies as well as the CRF. The second issue is the appropriate definition of the Summary Entity and specifically whether some or all of the schools, universities, colleges and health (SUCH) sector should be included.

#### Dividends

This is another issue that is related to the entity question. If the government continues to use the CRF instead of the Summary Entity for budgeting purposes, it is possible to manipulate the CRF deficit through the amount and timing of dividend payments. When dividends are received from a body that is not consolidated, the amount is treated as revenue. For example, results can be manipulated by requiring Crown corporations to retain earnings for a period and then pay a large dividend equal to several years' net earnings all at once. If the Crown corporation were consolidated, the amount of the dividend in any given period would not matter because the corporation's results would be consolidated into the summary results, with appropriate adjustments, including the elimination of transfers such as dividend payments, to eliminate double counting.

#### Budgets vs. Public Accounts

It is important that the accounting basis used to prepare the budget is the same as that used to report the ultimate results, or the two will not be comparable. The accounting methodology used in budgets is not always consistent with that used in the Public Accounts. While that does not seem to have been a major problem in British Columbia to date, it is an issue with considerable potential. One example might be the inclusion of the payment for the Downstream Benefits[1] in the 1995/96 budget. That transaction may not have been certain enough to be included in the Public Accounts and its treatment as a lump sum rather than amortization over the life of the agreement may not have been consistent with the government's accounting policies.

Another accounting policy issue with budgets is the fact that they are, by their nature, comprised of estimates and forecasts. The accounting standards include standards for future-oriented financial information. It has been suggested that the budget accounting policies should include specific policies respecting future-oriented financial information, consistent with the CICA standards. An excerpt from the standards is included in Appendix 6-A of this Issue Paper.

**Non-recurring Items**

It is often politically expedient to record some or all of the cash received from a non-recurring transaction, like the sale of an asset, as revenue in the period when it is received but to record associated costs as expenses over the life of the agreement.

An example of this is "sale/lease-back" arrangements whereby an asset is sold and the leased back from the new owners. This can be a legitimate way of financing a capital asset instead of using debt financing when there is a business case that shows that the benefits outweigh the costs based on reasonable assumptions. It can also be motivated by a desire to show one-time revenue with the costs spread out over the life of the lease, in which case there may be an incentive to accept a net cost in present value terms. This can be done if the lease is treated as an operating lease rather than a capital lease.[2] Under current CICA guidance it is possible to structure most leases as operating leases. PSAB will release draft guidance in July 1999 that will address this problem for the public sector but the CICA has yet to address it for the private sector.

In addition to sale/lease-backs there are other non-recurring items such as the sale of assets. Depending on the specifics of the transaction, the treatment of non-recurring items can be a question of interpretation. Some suggest that, to the extent non-recurring items are included as one-time entries, they should be at least disclosed separately as extraordinary items. It should be noted that "extraordinary items" are usually not related to the core business of an organization but in the case of land at least, government is in the business of selling Crown land. It would be difficult to distinguish between extraordinary sales and sales made in the normal course of business.

Others believe that accounting policies should require most of these transactions to be amortized over an appropriate period. Another suggestion is that, where there is a more prudent and a less prudent interpretation of accounting policies, the more prudent interpretation should be required to prevail.

## Net vs. Gross Accounting

Net accounting refers to netting revenue against expenditure for a particular program or netting expenditure against revenue for a revenue source (e.g. commissions and tax expenditures[3]). An example is the Product Sales and Services sub-vote in the Ministry of Finance and Corporate Relations Estimates, which recovers all of its costs from the value of products and services sold.

There are good and valid reasons for netting. It is appropriate to manage certain government functions on a business-like basis to ensure that, for example, the expansion of appropriate and profitable activities is not prevented by a sole focus on expenditure control. It may also be appropriate to dedicate a new revenue source to a new government program, if they are directly related or the revenue source was specifically created to fund the expenditure.

However, netting also tends to make total revenue and expenditure look smaller than they actually are, although it has no impact on the deficit. It can also, if practised too aggressively, severely limit government's flexibility to reallocate expenditure.

It has been suggested that this problem be resolved by showing expenditure and revenue on both a gross and a net basis. The Alberta Estimates uses that approach. The Ministry of Finance and Corporate Relations reporting committee[4] is working on principles for netting and appropriate disclosure.

In practice that means that, on line-by-line basis, revenue and expense would be shown on a net basis. However, on the summary statements, an adjustment would be made to show total expense and revenue on a gross basis, with appropriate disclosure of the details of the adjustment on a supporting schedule.

### ***The Basis for Accounting Policies***

In British Columbia, government sets accounting policies in accordance with the *Financial Administration Act*. On the face of it, that implies that government could choose any accounting policy that it wishes. In practice, government's discretion is limited by the fact that the Auditor General can and does criticise government for accounting policies that the Auditor General believes do not represent appropriate financial disclosure.

The government and the Auditor General have had some ongoing disputes about elements of accounting policy, not least of which is the definition of the reporting entity. Nonetheless, Treasury Board Staff (TBS), the Office of the Comptroller General (OCG) and the Office of the Auditor General (OAG) have all indicated that they enjoy a constructive working relationship within which accounting policy issues are discussed well in advance and most are resolved to the satisfaction of all parties. An example is the treatment of capital contributions to public bodies, which are now treated as prepaid capital advances instead of loans to the public bodies (see Issue Paper #2).

In spite of the fact that most accounting policy issues are being dealt with in a mutually agreeable fashion, concern has been expressed about the fact that government has absolute discretion to set accounting policies and could choose to adopt policies that would not lead to appropriate financial disclosure.

As noted in Issue Paper #2, the Canadian Institute of Chartered Accountants (CICA) established the Public Sector Accounting Board (PSAB) in 1981 to set standards for public sector accounting in Canada. The objective is to improve comparability and consistency in accounting policy across the public sector.

The CICA Public Sector Accounting Handbook, often referred to as the PSAB Handbook, sets out recommended accounting policies for the Canadian public sector. Both the government (OCG) and the OAG generally agree that the PSAB Handbook provides an appropriate basis for provincial accounting policy.

The PSAB Handbook establishes a standard for most of the elements of public sector accounting.[5] The accounting policies of specific jurisdictions will always have to deal with the specific circumstances of the jurisdiction in question, as corporate accounting policies must do in the private sector. The question is "Why not limit government's discretion in setting accounting policy to policies that are consistent with the PSAB Handbook?"

The advantages of placing this type of limit of government accounting policy are the same as requiring private sector corporations to prepare their financial statements in accordance with Generally Accepted Accounting Principles (GAAP). It ensures comparability over time and with other similar entities, allows for change as the standards evolve and provides a basis set by disinterested professionals.

Two disadvantages have been suggested to that approach. Some suggest the PSAB Handbook is not developed sufficiently to form the basis for accounting policy. There are public sector accounting issues that have not been fully addressed as yet and the PSAB Handbook is quite young compared to the CICA Handbook used by the private sector. However, to the extent that the handbook would just form the "basis" for accounting policy that may not be a serious problem.

The other disadvantage cited by some is that the PSAB Handbook tends to lag improvements in accounting practice. PSAB was created because public sector accounting significantly lagged private sector accounting practice. While PSAB has consistently moved to improve those practices, it has also done so in such a way that most jurisdictions can remain in or close to compliance. PSAB has done that by allowing its standards to evolve without making radical changes in a short period of time.

That suggests that it may be appropriate to seek a balance between standardized, professionally sanctioned accounting policies and the need to be able to improve reporting ahead of the standard, thus helping the standard to evolve over time.

For example, the approach currently taken in British Columbia to the presentation of results related to the capitalization of assets is not supported by the PSAB handbook, although it is supported by the Auditor General. PSAB allows assets to be capitalized and provides guidance about when it is appropriate to do so, how the assets values should be amortized and other related matters. However, PSAB defines the surplus/deficit as being equal to the change in net debt,[6] consistent with the PSAB focus on net debt as the most appropriate fiscal indicator.

That means that the deficit must include the operating deficiency of expenditure over revenue (i.e. the deficit as reported in British Columbia) plus any changes in debt for working capital purposes and any changes in debt related to capital assets. That means that although revenue and expense may be reported on an accrual basis, the results of capitalizing assets must be reversed on the statement of operations for the purpose of calculating the deficit.

As indicated above, the deficit or surplus reported in British Columbia is the operating deficiency or excess of revenue over expense. That is the amount of current costs that are being passed on to future generations and is consistent with the private sector full accrual accounting definition of deficit or surplus. Debt used to purchase capital assets is also a cost being passed on to future taxpayers but unlike the operating costs, there are also benefits associated with the capital assets that will be enjoyed by those future taxpayers.

The question is, given the objectives of financial reporting, what is the most appropriate definition of the deficit and what is the appropriate basis for accounting policies to ensure results are reported appropriately?

Table 6-1 outlines legislated accounting policies in various jurisdictions. It shows that the only Canadian jurisdictions to refer to GAAP or professional accounting standards are Ontario and the federal government and then only for Crown corporations. However, it is clear from Australia and New Zealand that there is some movement in the Commonwealth countries to such legislative provisions.

### ***Setting and Interpreting the Specific Accounting Policies***

Some have suggested that, even if there is additional statutory guidance to government about the basis for its accounting policies that may not be sufficient to maintain appropriate policies over time. There is also the issue of how the government's policies will be interpreted in various circumstances. There may be political pressure for a particular interpretation in some cases.

On the other hand, there is a well-established principle that management is responsible for the financial statements, including accounting policy. To take responsibility for setting government accounting policy away from Treasury Board would not be consistent with that principle. Also, the OCG has a statutory duty that arguably includes interpreting government's accounting policy, although that is subject to Treasury Board direction.[7]This could be changed in several ways. In most other Provinces the Comptroller General has Deputy Minister status (as was the case in British Columbia until 1981) and the Comptroller General could be given stronger statutory independence. Alternatively, there could be an independent advisory function created for the purpose of recommending accounting policies and interpretations.

In a 1998 Private Members Bill in British Columbia,[8] it was proposed that a reporting policy committee recommend accounting policies to the Legislative Assembly, which would be responsible for setting the policies. The committee would be comprised of the Auditor General, the Comptroller General and a Chartered Accountant appointed by the Canadian Institute of Chartered Accountants.

Another approach to the advisory committee would be to establish a committee comprised of accounting professionals without any government representation that would provide advice to government through public reports. Although the advice would not be binding on government, independent professional advice delivered in public would be difficult to disregard. This could be a forum for the resolution of disagreements between the Auditor General and the government on policy and interpretation issues.

### *Review of Budget and Estimates*

The Auditor General has recommended that, to improve the credibility of the budget and accountability process, the Auditor General should be annually required to comment on the **accounting policies** used in the preparation of the Estimates. There are a number of types of review of the Estimates and budget information that could be implemented. For example, there could be:

- a review of key assumptions used in preparing the Estimates, as is done in the United Kingdom;[9]
- a review of the methodology used to forecast revenue and/or expenditure;
- more extensive audit of the revenue Estimates to review the methodology, assumptions and information as is done in Nova Scotia;

**Table 6-1 – Legislative Accounting Policy Provisions in Various Jurisdictions**

| Jurisdiction | Legislative Provision |
|---|---|
| Canada | Financial Administration Act (FAA) 131(4) Each parent Crown Corporation shall cause financial statements to be prepared … in accordance with Generally Accepted Accounting Principles, augmented or supplemented by sub-section (6).<br>(6) Treasury Board may, for the purposes of subsection (4) make regulations respecting financial statements … but such regulations shall … only supplement or augment generally accepted accounting principles.(6) |
| British Columbia | FAA, 10. The financial statements of the government for each fiscal year must be prepared in accordance with the government's accounting policies as established by the Treasury Board and must<br>(a) contain the government's accounting policies as established by the Treasury Board, |
| Alberta | FAA, Definition of financial statements requires financial statements to include “a statement of accounting policies followed in preparation of financial statements.” |

| | |
|---|---|
| Saskatchewan | FAA 16(1) Financial statements of government … shall be prepared in accordance with the accounting policies established by the board. |
| Manitoba | FAA 65(1) (a) … prepare public accounts that include financial statements prepared in accordance with the accounting policies of the government set out in the financial statements. |
| Ontario | Legislates PSAB as basis for accounting policy **(Check)** |
| Québec | None specified. |
| New Brunswick | 48(3) (a) financial statements … (must include) a statement of the accounting policies followed. |
| Nova Scotia | None specified **(Check)** |
| PEI | None specified. |
| Newfoundland | 59 (1) the public accounts shall show … statements that may under good accounting practice be required to show the financial positions … at year end. |
| Australia | Charter of Budget Honesty Act 1998 requires the budget, the midyear report and the final report (Public Accounts) to be "(a) based on external reporting standards; and (b) identify, in general terms, the external reporting standards upon which it is based and any ways in which the report departs from those standards" External reporting standards is defined with reference to the accounting professions standards setting body. |
| New Zealand | Fiscal responsibility Act, 1994 5. All financial statements included in reports required under this Act shall be prepared in accordance with generally accepted accounting practices. GAAP is defined in the Public Finance Act with reference to the accounting profession's standards setting body. |

- an independent council established to advise government on the economic forecast, as has already been done in British Columbia;
- a review of the accounting policies used, including the policies related to future-oriented financial information and both the revenue and expenditure sides of the budget;
- a review of the budget and Estimates development systems;
- a review of the information contained in the Estimates.

There are two principal arguments against some level of external review of the budget and Estimates. The first argument is that review by the Auditor general or some other external party would overshadow the budget development and decision-making process. On of the principles adopted by the Panel is that government is responsible for developing expenditure proposals for approval by the Legislature. Having an external review during the actual budget building exercise might be inconsistent with that principle, conferring on the Auditor General a real or perceived ability to comment on the appropriateness of government's decisions.

Perhaps a review by the Auditor General limited to systems and practices used in preparing the Estimates and budget information, including forecasting systems and practices, would overcome this concern. Such a review would not have to be done in conjunction with a particular budget or reported upon on budget-day. The broad powers in the *Auditor General Act* to inquire into government programs and practices would already support this type of review.

The second argument against an external review of the budget and Estimates is that it would add time and resource requirements to an already very onerous annual exercise. That seems especially to be a concern as it applies to decisions that are made late in the budget process.

It seems unlikely that last-minute budget decisions can be altogether avoided since the difficult decisions associated with reconciling the aggregate of many individual revenue and expenditure decisions with an overall fiscal plan must, by their nature, be take at the end of the process.

It should be noted that that is true regardless of the financial circumstances. It is often just as difficult to decide how to allocate a surplus as it is to reduce a deficit.

## Summary of Consultations

### *External Input*

The Chartered Accountants of B.C. (CABC) have made three recommendations related to this Issue paper:

> 3. The CABC recommend that the government of B.C. adopt CICA accounting standards as set out in the CICA Accounting Handbook, and the CICA Public Sector Accounting Handbook, including the principles of future-oriented financial information.
>
> 4. Legislation should be changed so that the responsibility for setting accounting standards is moved from being an internal process through the Treasury Board, to an external process through the CICA standards.
>
> 8. The CABC recommend that an independent opinion from the Auditor General be obtained on the accounting policies and basic assumptions used in the Estimates Process."

The Canadian Bankers' Association suggests:

> Ultimately, we must remember that the government is accountable to the people. A budget is, by definition, a plan … governments are judged by the people on whether their plans are good or bad and whether or not they are successful … We are concerned that independent third parties reviewing budget plans for reasonableness (of accounting policy, economic assumptions, revenue projections, etc.) would add to the bureaucracy in these independent agencies without necessarily adding benefits.

### *Immediate Public Sector Input*

In interviews with immediate public sector officials, the following points were made:

- There should be some mechanism for strengthening the OCG's professional role in establishing accounting policy without eliminating the government's ultimate responsibility for reporting its results.
- Accounting policy should clearly be the responsibility of the OCG and planning the responsibility of government, with the independence of the OCG protected through legislation.
- Concern was expressed about the possibility of the Auditor General commenting on subjective elements of the budget information such as prudence of projections or decisions and about the time and effort that external review of budget information would entail.
- There are problems with the legislation of the PSAB standards as the basis of accounting policy but it may be useful to have some reference to external standards as a starting-point. Reporting is too important to be left to accountants whose benchmark is the private sector. Current checks and balance role of the Auditor General may be sufficient.
- There is no need for independent review of budgets because problems become evident quickly enough. The best protection is a free press.
- Independent review by OAG of the basis and systems for the budget can be done in advance and add credibility to the process.
- If the process becomes more transparent and effective through better planning and better disclosure of assumptions and decisions, what would be added by independent review except time and effort?
- If the Auditor General did a full review of the budget information, there would be a danger of the OAG usurping government's authority and responsibility for public policy. Government must decide what it is going to do and there should not be a subjective opinion expressed about whether its fiscal and other public policy decisions are prudent or appropriate.

## Options

### *Accounting Policy Basis*

1. **Status quo** – government remains responsible for setting accounting policy with the Auditor General playing a check and balance role. There would continue to be no specific accounting policy requirement for the budget and Estimates.
2. **Require accounting policies to be based on CICA standards** – would establish the PSAB standards, standards for future-oriented financial information and other CICA standards as the basis for British Columbia accounting policy.
3. **Option 2 with the ability to vary from the standard where it improves reporting –** would establish professional accounting standards as the base and allow for the

continued evolution of those standards.

4. **Apply consistent accounting policies to budget and reporting information –** would ensure that budgets are prepared to the same standard as the reporting information. Would also require that the budget information be created and presented in accordance with accounting policies regarding future-oriented financial information consistent with CICA standards, if CICA standards are used as the basis for accounting policies.

### *Setting and Interpretation of Specific Accounting Policy*

1. **Status Quo** – government remains responsible for setting and interpreting accounting policy with the Auditor General playing a check and balance role.

2. **OCG responsible for setting and interpreting accounting policy** – the role of the OCG would be strengthened and made more independent and it would be given the duty of setting specific accounting policy and determining the interpretation of those policies. The Auditor General would continue to play a check and balance role.

3. **Advisory panel established** – an independent advisory panel of accounting professionals would advise government on accounting policy and would provide non-binding recommendations to resolve disputes between the government and the Auditor General on specific accounting policies and their interpretation.

### *External Review of Budget and Estimates*

1. **Status Quo –** no specific required external review but the Auditor General would continue to have the ability to examine systems and practices used in the budget process

**2. Auditor General review of accounting policy and methodology –** the Auditor General would undertake a required independent review of the accounting policies used and methodology (i.e. systems and practices) used in preparing the budget and Estimates but would not opine on the specific decisions taken or information presented. The timing of this annual report could coincide with release of the budget or could be on a completely different schedule.

**3. Auditor General review of budget and Estimates Information –** in addition to reviewing accounting policy and methodology, the Auditor General would be required to annually review whether the information presented is consistent with the established policies and methodology and is fair and complete disclosure of material information.

## Appendix 6-A – Future-Oriented Financial Information Accounting Principles

Section 4250 CICA Accounting Handbook below defines future-oriented financial reporting.

PURPOSE AND SCOPE

.01 This Section establishes standards for the measurement, presentation and disclosure of future-oriented financial information when presented for external users of financial information in the format of general purpose financial statements or in such special purpose format as agreed by the parties. This Section does not apply to historical pro-forma statements issued, for example, in conjunction with business combinations and prospectuses (see BUSINESS COMBINATIONS, Section 1580 and PROSPECTUSES, Section 4000).

.02 The objective of presenting future-oriented financial information is to provide external users with information that assists them in evaluating any entity's financial prospects.

## DEFINITIONS

.03 Future-oriented financial information is information about prospective results of operations, financial position and/or cash flows, based on assumptions about future economic conditions and courses of action. Future-oriented financial information is presented as either a forecast or a projection.

.04 A forecast is future-oriented financial information prepared using assumptions all of which reflect the entity's planned courses of action for the period covered given management's judgment as to the most probable set of economic conditions.

.05 A projection is future-oriented financial information prepared using assumptions that reflect the entity's planned courses of action for the period covered given management's judgment as to the most probable set of economic conditions, together with one or more hypotheses that are assumptions which are consistent with the purpose of the information but are not necessarily the most probable in management's judgment.

.06 General purpose future-oriented financial information is future-oriented financial information prepared for external users with whom the entity is not negotiating or dealing directly.

.07 Special purpose future-oriented financial information is future-oriented financial information prepared for external users with whom the entity is negotiating or dealing directly.

## MEASUREMENT

### Assumptions

.08 Future-oriented financial information should be prepared using assumptions appropriate in the circumstances. [OCT. 1989]

.09 Management is responsible for the process of developing assumptions and for ensuring that the assumptions developed are appropriate in the circumstances. The quality of future-oriented financial information is largely dependent on the completeness and reasonableness of the assumptions. The process used to develop assumptions would provide for relevant information that is reasonably available when the future-oriented financial information is prepared. Plans and budgets prepared for internal use may provide a basis for developing appropriate assumptions.

.10 Assumptions are frequently interdependent and one assumption may affect many parts of a business and lead to the formulation of other assumptions. The assumptions, therefore, need to be internally consistent. For example, an assumption that sales volume will increase would in most circumstances be coupled with an assumption that wages and raw material costs will also increase.

.11 A forecast is based on reasonable and supportable assumptions that management believes reflect the most probable set of economic conditions and planned courses of action. To be reasonable, these assumptions need to be consistent with the plans of the entity. Assumptions are consistent with the plans of the entity if they reflect the expected economic effects of anticipated strategies, programs, and actions, including those being planned in response to expected future economic conditions. To be supportable, assumptions need to be based on the past performance of the entity itself, the performance of other entities engaged in similar activities, feasibility studies, marketing studies or any other sources that provide objective corroboration of the assumptions used. The extent of detailed information supporting each assumption, and an assessment as to the reasonableness of each assumption, will vary according to circumstances, and will be influenced by factors such as the significance of the assumption and the availability and quality of the supporting information.

.12 As the period of time encompassed by future-oriented financial information is extended, an assumption that reflects management's judgment as to the most probable set of economic conditions and planned courses of action may no longer be supportable. In this case the assumption would be considered an hypothesis and the forecast would become a projection.

.13 A projection is based on reasonable assumptions that include one or more hypotheses. Once hypotheses have been formulated, assumptions would be developed to reflect the most probable set of economic conditions and planned courses of action should the hypotheses prove true. Hypotheses are assumptions that assume a set of economic conditions or courses of action that are not necessarily the most probable in management's judgment, but are consistent with the purpose of the projection, as in response to the question "What would happen if ...?". To be reasonable, hypotheses need to be consistent with the purpose of the projection and represent plausible circumstances. Hypotheses need not be supportable. For example, a projection might be used by an entity in its start up phase when certain key assumptions cannot be supported.

.14 Management's responsibility extends beyond ensuring that individual assumptions used to prepare the future-oriented financial information are appropriate in the circumstances, to ensuring that the assumptions taken as a whole are appropriate.

Time period

.15 The period covered by future-oriented financial information should not extend beyond the point in time for which such information can be reasonably estimated. [OCT. 1989]

.16 The length of the period for which management can present future-oriented financial information depends on factors such as the needs of users, the ability to make appropriate assumptions, the nature of the industry, and the operating cycle of the entity. The periods covered would normally coincide with those for which historical financial statements or information will be presented, e.g., on an annual or quarterly basis.

.17 Forecasts would not normally be prepared for periods beyond the following fiscal year except when there is reasonable assurance as to the operations in the forecast period. Projections may be presented for periods extending beyond the following fiscal year when there is a reasonable basis for making Estimates, although the degree of uncertainty normally increases with the length of the future period covered.

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[1] The Downstream Benefits refers to the value of electricity produced from a dam built on the Columbia River in British Columbia that was originally sold to a U.S. utility for an extended period but reverted to British Columbia in 1996/97 and a tentative agreement was made to again sell the power. An amount was included in the 1996/97 budget revenue but the deal subsequently fell through and the revenue was not received.

[2] If the lease is a capital lease the revenue from the sale must be deferred and brought into revenue over the life of the lease.

[3] Tax expenditures are tax policy provisions that use the tax system to deliver government programs. For example, there are a number of provincial sales tax exemptions for specific users such as bona fide farmers. Tax expenditures are estimated in the Budget reports but not accounted for in the Estimates or Public Accounts because of the difficulty in accurately determining the amount in most cases.

[4] The reporting committee is a committee comprised of the Deputy Minister of Finance and Corporate Relations and representatives of the OCG and TBS.

[5] As discussed below, PSAB is not a set of policies that can be adopted by every jurisdiction but a standard to guide the adoption of jurisdiction specific policies.  Policies need to vary to reflect the specific structures and programs of each jurisdiction.  The standard is open to interpretation, as are the policies adopted by various jurisdictions.

[6] See paragraph 1500.79 in the Public Sector Accounting recommendations published by the Canadian Institute of Chartered Accountants.

> [7] FAA, 9.  The Comptroller General must, subject to any direction of the Treasury Board, do all of the following:
>
> (a) develop and issue policies and guidelines and establish procedures for the financial management and recording of the revenues, expenditures, assets, liabilities and equity of the government;
>
> (b) issue directives respecting the methods by which the accounts of the government are kept;
>
> (c) administer and maintain the central accounts of the government;
>
> (d) provide functional control over all financial transactions entered into the central accounting system; …

[8] Bill M202 – 1998 Truth in Budgeting Act.

[9] In the U.K. the government refers specific assumptions to the Auditor General for review each year so that, over time the bases for all the key assumptions are reviewed.  There is not an annual review of the basis for each assumption.