HM Treasury

Financial Reporting Advisory Board

Accounting for Social Benefits

Issue:	Clarification of accounting treatment for social benefits following discussion at FRAB and updates to the wording suggested for inclusion in the FReM.
Impact on guidance:	Wording to be added to the FReM for clarification only
IAS/IFRS adaptation?	No adaptations or interpretations proposed.
Impact on WGA?	No material impact.
IPSAS compliant?	The current accounting treatment for social benefits in the UK public sector is considered to be substantially compliant with IPSAS 42.
Interpretation for the public-sector context?	No adaptations or interpretations proposed.
Impact on budgetary regime and Estimates?	None
Alignment with National Accounts	No impact on National Accounts alignment.
Recommendation:	For the Board to agree to implement the suggested wording in the FReM to provide clarity on current accounting treatment for social benefits.
Timing:	To impact December 22/23 FReM update.

DETAIL

1. The issuance of the new International Public Sector Accounting Standards Board (IPSASB) standard IPSAS 42, Social Benefits, prompted HMT to review the current accounting treatment for social benefits in the UK public sector per previous discussions at FRAB.

2. HMT was asked by FRAB members to clarify the current accounting treatment for social benefits and to draft wording for inclusion in the Financial Reporting Manual (FReM).

3. We have considered points raised by FRAB members at the November 2021 and June 2022 FRAB meetings and we have updated the wording proposed at the June 2022 meeting. We are now asking FRAB members to agree to its inclusion in the December 22/23 FReM update.

Background

4. At the November 2021 FRAB meeting, a review of the IPSASB standard, IPSAS 42, Social Benefits, was presented (FRAB 145 (12)), covering the background to the Standard and comparing it to the existing accounting treatment for social benefits in the UK public sector.

5. FRAB had previously discussed the accounting treatment of social benefits over a number of years, agreeing to the continuation of the current treatment until the IPSASB standard was available to review. In 2001-02, FRAB accepted the view that benefits should be accounted for in the year in which amounts to be paid fall due following proper approval of a claim. It was agreed that it would be inappropriate to recognise any longer-term liability for such expenditure because social benefit payments were analogous to executory contracts in FRS 12: Provisions, Contingent Liabilities and Contingent Assets.

6. Under an executory contract, both the right and obligation are conditional upon each other. Accordingly, the right and the obligation cannot be separated.

7. It was agreed at the November 2021 FRAB meeting that there was no need to adapt existing practice in the UK public sector in light of IPSAS 42, but that clarification was needed in current guidance as to how social benefits should be accounted for.

8. Subsequently, at the June 2022 FRAB meeting the Board considered suggested wording for inclusion in the FReM in order to set out the existing accounting treatment.

9. HMT proposed the following wording to the Board:

   Expenditure in respect of social benefit payments should be recognised in financial statements as closely as possible to the time of the underlying activity that gives rise to a liability. The underlying activity is defined as the point at which the claimant is deemed to be eligible to receive the social benefit, per the underlying legislation. Only the expenditure for the period of entitlement that falls within the accounting year should be recognised.

   Social benefits may be defined as current transfers received by households intended to provide for the needs that arise from certain events or circumstances, for example, sickness, unemployment, retirement, housing, education, or family circumstances.

10. This wording was suggested after consultation with the National Audit Office (NAO), the Department for Work and Pensions (DWP), the Relevant Authorities, the Resource Accounts Special Interest Group (RASIG) and the User and Preparer Advice Group (UPAG), and drew on statistical definitions, which is in line with the basis for definitions in IPSAS 42 (see Annex 1 for full definitions).

11. After discussion, this wording was not agreed at the June 2022 meeting. Instead, it was agreed that HMT would further consider certain points raised by FRAB members and how the suggested wording should apply in practice in accounting for social benefits.

Points for consideration raised by FRAB members

12. Several specific points raised by FRAB at the June 2022 meeting have been considered below, including:
    - Comparison with accounting for mis-sold PPI in the private sector;
    - Differences in practice;
    - The scope of the wording; and
    - The trigger point for recognition for social benefits.

Comparison with mis-sold Payment Protection Insurance

13. At the June 2022 FRAB meeting, a member raised a point around accounting for claims for mis-sold payment protection insurance (PPI) in the private sector and how this compared to accounting for social benefits in the public sector and whether there was a discrepancy between the two that meant accounting for social benefits in the public sector was not IFRS-compliant.

14. The FRAB member highlighted that with mis-sold PPI claims it does not matter if a customer has raised a claim or not, but that the correct treatment is to provide for everything that individual would be entitled to.

15. In comparison, in relation to social benefits in the public sector, until a benefit claimant is deemed eligible, there is no obligation to pay out benefits and so the liability should not be recognised until eligibility criteria have been deemed to be met.

16. However, obligations in relation to mis-sold PPI claims relate to a prior period, to provide redress for monies taken erroneously in the past, where social benefits provide support in the future during periods of entitlement.

17. Accounting for social benefits in the public sector is not contradictory to accounting for PPI claims in the private sector so no change is deemed necessary to the practice or the suggested wording. (See Annex 2 for further consideration of accounting for PPI claims).

Differences in Practice

18. Additionally, the consideration of differences in practice in accounting for social benefits was raised at the previous FRAB meeting.

19. In previous conversations, the NAO have set out, specifically in relation to DWP, that there should not be any recognition point until the benefits claim has been approved. This relates to the executory element of accounting for social benefits, as previously agreed at FRAB whereby there is no obligation to the benefit payment until the right has been determined.

20. In practice we found that there was a slight difference with how the Department for Communities Northern Ireland (DfC) were accounting for new claims. DfC currently does accrue for claims where the eligible period of entitlement is before the financial year end.

21. DfC have been consulted on the wording and are keen to engage with best practice and so will review their approach after the outcome of FRAB and the publication of the FReM guidance.

22. The amount that relates to these claims is likely immaterial in practice and so this should not impede application of the guidance.

Scope of Guidance

23. HMT were also asked to clarify the scope of the wording on accounting for social benefits.

24. In the case of other payments made to address a current concern, e.g., Covid-related grants, which do not meet the proposed definition of social benefits these would be considered grants and normal IFRS principles would apply. Additionally, IAS 37 and Grantor Accounting guidance has been issued by HMT to assist with grantor accounting.

Trigger point for recognition

25. HMT were also asked to clarify the trigger point for recognising social benefit expenditure. To do this, we have removed the previous wording around recognising expenditure "as closely as possible to the time of the underlying activity that gives rise to a liability." This wording had previously raised questions and confusion.

26. It is considered that the assessment of an individual being eligible is the underlying activity that gives rise to a liability as, for most social benefit schemes, there is no expectation that the benefit will be paid unless it is claimed. Therefore, the guidance states that expenditure should be recognised at the point at which the claimant is deemed to be eligible to receive the benefit, per the underlying legislation. We do not think this represents a substantive change from the previous wording presented to FRAB, rather it simplifies the guidance.

27. Under this approach, there should not be any recognition point until the benefits claim has been approved. In the case of new claims, no accrual should be made at financial year end if the claim has not yet been approved as the obligation has not yet arisen. For ongoing claims, expenditure is accrued if it relates to the financial year. (See Annex 3 for an illustrative example).

Updated wording

28. Considering the points raised by FRAB members and discussions with other groups, the following wording is now suggested for inclusion in the FReM:

> *Expenditure in respect of social benefit payments should be recognised in financial statements at the point at which the claimant is deemed to be eligible to receive the social benefit, per the underlying legislation. Only the expenditure for the period of entitlement that falls within the accounting year should be recognised.*
>
> *Social benefits may be defined as current transfers received by households intended to provide for the needs that arise from certain events or circumstances, for example, sickness, unemployment, retirement, housing, education, or family circumstances.*

29. This wording has also been reviewed by the NAO, RASIG and the Relevant Authorities Working Group. Support for the wording has specifically been received by the NAO, Northern Ireland, and Wales.

Decision needed: Does FRAB agree to approve the suggested wording in relation to accounting for social benefits for inclusion in the FREM?

Annex 1 – Definitions

30. "*Social benefits*" have been defined using OECD statistical definitions.

31. The term "*Current transfers*" is defined by the OECD as "*… all transfers that are not transfer of capital. Current Transfers are classified into two main categories: -general government -other sectors*"

32. The term "*Household*" is also a statistical term and, per the OECD, refers to "*… either (a) a one-person household, that is to say, a person who makes provision for his or her own food or other essentials for living without combining with any other person to form part of a multi-person household or (b) a multi-person household, that is to say, a group of two or more persons living together who make common provision for food or other essentials for living. The persons in the group may pool their incomes and may, to a greater or lesser extent, have a common budget; they may be related or unrelated persons or constitute a combination of persons both related and unrelated. A household may be located in a housing unit or in a set of collective living quarters such as a boarding house, a hotel or a camp, or may comprise the administrative personnel in an institution. The household may also be homeless.*"

33. The OECD definition is based on the definition of social benefits in SNA08—this is the UN's statistical framework for national accounts upon which ESA10 is based. ESA10 is broadly consistent with SNA08 but contains more detail in a number of subjects.

34. The ESA10 definition of social benefits is as follows:

> *Social benefits are transfers to households, in cash or in kind, intended to relieve them from the financial burden of a number of risks or needs, made through collectively organised schemes, or outside such schemes by government units and NPISHs; they include payments from general government to producers which individually benefit households and which are made in the context of social risks or needs.*

35. IPSAS 42 sets out the following definitions in relation to accounting for social benefits:

> *5. Social benefits are cash transfers provided to:*
>
> *(a) Specific individuals and/or households who meet eligibility criteria;*
>
> *(b) Mitigate the effect of social risks; and*
>
> *(c) Address the needs of society as a whole.*
>
> *AG9. Social risks relate to the characteristics of individuals and/or households–for example, age, health, poverty, and employment status. The nature of a social risk is that it relates directly to the characteristics of an individual and/or household. The condition, event, or circumstance that leads to or contributes to an unplanned or undesired event arises from the characteristics of the individuals and/or households. This distinguishes social risks from other risks, where the condition, event, or circumstance that leads to or contributes to an unplanned or undesired event arises from something other than the characteristics of an individual or household*

36. This is in line with the definitions set out above in relation to accounting for social benefits in the UK public sector.

37. Under IPSAS 42, transactions under IPSAS 39 Employee Benefits and IPSAS 41 Financial Instruments (based on IFRS 9 Financial Instruments) are excluded from the scope of the social benefits standard.

38. The wording for accounting for social benefits in the UK public sector wording applies to transactions that meet the definition of a social benefit and so does not apply to cash transfers that are accounted for in accordance with other standards, e.g., IAS 37.

Annex 2 – Accounting for mis-sold PPI claims

39. In November 2014, the Supreme Court ruled in Plevin v Paragon Personal Finance Ltd (Plevin) that a failure to disclose to a client a large commission payment on a single premium PPI policy made the relationship between a lender and the borrower unfair under section 140A of the Consumer Credit Act 1974 and customers could reclaim any amounts that they had paid.

40. There is a difference between accounting for financial redress as determined by a court ruling setting the criteria for, and accounting for government-distributed social benefits as paid out to individuals (or households) who demonstrate entitlement to the benefit for a particular period as set out in legislation.

41. For social benefits, the obligating event for future periods has not yet been determined. For example, for the UK State Pension social security benefits are only payable if the claimant meets the entitlement conditions.

42. Section 2(1) of the Pensions Act 2014 sets out the entitlement conditions for new State Pension, namely that if the claimant has reached State Pension age and has made 35 years of National Insurance Contributions, they will receive the full rate of new State Pension. Furthermore, Section 1(2) of the Social Security Administration Act 1992 states that no-one is entitled to any benefit unless they make a claim for it. Therefore, in order to receive the full rate of new state pension, a claim must be made by the individual in addition to meeting the entitlement conditions above

43. Within these criteria, 'being alive', is an implicit criterion and under the current accounting policy for UK social benefits, when assessing the recognition of a social benefit liability it cannot be certain that a specific individual who meets the eligibility criteria at the reporting date will be alive and, by implication, eligible for the entire period between benefit payments and therefore a 'present' obligation can only be considered up to the year end.

44. Similarly, IPSAS 42 also provides the following examples pertaining to the consideration of 'being alive' as a criterion:

    a) An unemployment benefit may only be payable to those who have become unemployed and are available for work (which implicitly includes being alive).
    b) Being alive may not be an eligibility criterion for the recipient of the social benefit. A child benefit may be paid to the parents or guardian of the child; the payment of the benefit may be dependent on the child being alive, and not on the status of the parent or guardian.
    c) Benefits may be transferred to a survivor following the death of the beneficiary.

45. In relation to pension benefits the FRAB has previously concluded that "the basic state pension should be recognised in the year in which the amounts fall due"[1] and that "an obligating event does not occur for non-contributory or contributory programs before the relevant threshold eligibility criteria are met, e.g. there is no obligating event for the payment of an old age pension until all eligibility criteria have been met, including the survival of the beneficiary to the required age for the pension to be paid."[2]

46. Comparatively, the court ruling for mis-sold PPI determined the eligibility for receiving a refund and put an obligation on the banks to repay the money by creating an obligation as a result of a past

[1] FRAB, *The Fifth Report 2001-2*
[2] FRAB, *The Twelfth Report 2008-9*

event. Furthermore, the ruling only applied to those customers that had not yet received a full refund for mis-sold PPI, allowing the banks to estimate the amounts still to be repaid.

47. In the case of court rulings that impact government, a liability would similarly be recognised if there was an obligation to pay out monies under this ruling.

48. For example, when HMRC faces a legal challenge by taxpayers in relation to tax already paid, a contingent liability is included in the consolidated Annual Report and Accounts where claims are possibly, rather than probably, likely to be successful and a provision where it is probable that the claim will be successful.

Annex 3 – Illustrative Example

Universal credit

If a person has lost their job or had a drop in income they may be entitled to Universal Credit.

Universal credit is a social benefit paid in cash, falling under the definition in the wording:

Social benefits may be defined as current transfers received by households intended to provide for the needs that arise from certain events or circumstances, for example, sickness, ***unemployment****, retirement, housing, education, or family circumstances.*

Universal credit addresses concerns with unemployment, sickness or family circumstances as a means-tested social benefit that mitigates the social risks associated with high unemployment or low income.

Example 1

Person A loses their job and prior to 31st March 2022 submits an application to receive Universal Credit.

This is the first time Person A has applied for Universal Credit.

Due to processing times, their application is processed, approved and paid 4 weeks post-31st March 2022.

No accrual is included in the 2021-22 ARA for DWP as there is no obligation to make the payment until Person A is "***deemed to be eligible to receive the social benefit***". To be deemed eligible to receive the social benefit, the claimant has to have their claim approved, which in this example does not happen until the following financial year.

This would then be accounted for as expenditure in the financial year 2022-23.

Example 2

Person B loses their job and prior to 31st January 2022 submits an application to receive Universal Credit. Their application is approved processed, approved and paid 5 weeks later in w/c 28th February 2022.

This is accounted for as expenditure in the financial year 2021-22.

They are due to receive another payment 5 weeks later around w/c 4th April 2022. They have not reported any changes in their circumstances from the original application and they are deemed eligible for this payment. The amount covering the period between the approval of the first claim and the year end would then be accrued and accounted for as expenditure in the financial year 2021-22.