HM Treasury

Financial Reporting Advisory Board

Accounting for Social Benefits Update

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 to clarify correct accounting treatment
IAS/IFRS adaptation?	No adaptations or interpretations proposed.
Impact on WGA?	Any changes in accounting for social benefits at the individual department level will flow through into WGA consolidation.
IPSAS compliant?	The accounting treatment proposed for social benefits proposed in this paper 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?	Potential impact on budget cover required if applying guidance for first time.
Alignment with National Accounts	Likely misalignment with National Accounts requirements; if FRAB agree with HMT's recommendation, HMT will work with the ONS to implement this change.
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 25/26 FReM update.

Summary of issue

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. In 2001-02, FRAB discussed the accounting treatment of social benefits before the publication of IPSAS 42, agreeing to the continuation of the current treatment until the IPSASB standard was available to review.

3. 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. However, FRAB agreed not to introduce any specific guidance in this area until the forthcoming IPSASB standard was published.

4. At FRAB 145, November 2021, FRAB members concluded that no changes were needed to align the accounting treatment more closely with IPSAS 42. Instead, 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). In developing this guidance, we have closely considered points raised by FRAB members at the November 2021, June 2022 and November 2022 FRAB meetings.

5. This paper focuses on the trigger point for recognition for social benefits accruals, and in particular the recognition of first-time claims where a claim is required by the underlying legislation of the social benefit. The suggested guidance for inclusion in the FReM has also been updated.

Background to proposed changes

6. At the June 2022 FRAB meeting (FRAB 147 (15)), the Board considered suggested wording for inclusion in the FReM in order to set out the existing accounting treatment, which drew on statistical definitions, which is in line with the basis for definitions in IPSAS 42 (see Annex 1 for full definitions). After discussion, this wording was not agreed at the June 2022 meeting as the Board agreed that more clarity was needed over the correct accounting treatment.

7. At the November 2022 FRAB meeting (FRAB 148 (15)), alternative guidance was presented to clarify the current accounting practice for social benefits. The Board again did not agree to the proposed guidance but raised concerns with the current accounting practice around the application of IFRS principles to accounting for social benefits, specifically the point at which new claims are accounted for.

8. The Board's objections were that the current practice of not recognising a liability for claims made prior to the year-end but not yet approved by the year end is inconsistent with IFRS principles. This is because, in the view of some Board members, in this fact pattern conditions for a present obligation existed at the year end and therefore a liability should be recognised. HMT agreed to review this issue and present an updated paper at FRAB 150.

Current and proposed accounting practice and IFRS compliance

9. Previously, there has been no specific guidance in the FReM for accounting for social benefits. Again, the decision made by FRAB in 2001-02 was to defer setting out guidance until the conclusion of the IPSASB project on accounting for social benefits.

10. In the absence of central guidance on accounting for social benefits, departments have had to apply stand-alone accounting policies.

11. As an example, the Department for Work and Pension has until now applied an accounting policy that states that no amounts should be recognised in relation to a new benefit claim until the claim has been approved and the first payment has been made.

12. In contrast, MoD includes an accrual for claims received not yet registered for the War Pension benefit and uses historical claim and payment data to calculate this accrual, although this does constitute a relatively small proportion of the recognised expenditure.

13. After further discussion with relevant stakeholders, including the NAO, DWP, MOD, the Relevant Authorities and HMRC, HMT are now proposing that for social benefits that require a claim to be made, these should be accounted for with a recognition point based on the *period of eligibility of the applicant* (rather than the point the claim has been approved, as was proposed in previous FRAB papers).

14. For accruals relating to new claims, this means that:

    a. claims by eligible persons which have been received but not yet processed by the department before the year end should be included; and
    b. claims by eligible persons expected to be received but not yet received when the accrual is calculated should also be included.

15. HMT believe that the above approach is consistent with IFRS principles generally. The IFRS definition of a liability is *a present obligation of the entity to transfer an economic resource as a result of past events.* In assessing whether a present obligation (and therefore a liability) exists, Para 4.43 of the Conceptual Framework states the following:

    A present obligation exists as a result of past events only if:

    a) the entity has already obtained economic benefits or taken an action; and
    b) as a consequence, the entity will or may have to transfer an economic resource that it would not otherwise have had to transfer.[1]

16. The key question under consideration here is what the trigger point for is ‘past events’ to occur that give rise to a present obligation to transfer economic resources associated with social benefits (i.e. what is the trigger point to recognise a liability related to social benefits.

17. After consultation with departments, the NAO and independent Board members, HMT would now argue that ‘the past event’ that serves as a trigger point for the recognition of a liability occurs when a social benefit recipient becomes eligible for the benefit. At this point departments cannot take steps to avoid making payment and as a consequence a liability is created.

18. Social benefit payments are given to support recipients when they meet qualifying conditions. If the conditions for eligibility are met at year-end, this is the underlying obligating event, and submission of a claim is the post year-end evidence process only as required by legislation.

19. This will bring accounting for new claims in line with the current practice for ongoing claims, where expenditure should be accrued if the period of eligibility for the recipient relates to the financial year.

Comparison with IPSAS 42

[1] https://www.ifrs.org/content/dam/ifrs/publications/pdf-standards/english/2021/issued/part-a/conceptual-framework-for-financial-reporting.pdf

20. Under the accounting treatment proposed in this paper, social benefits will be recognised in the year in which the recipient is eligible for the benefit, with an accrual raised for any amounts for claims not yet processed or received at the year-end. This is on the basis that fulfilling the eligibility criteria is a past event that creates a present obligation to individuals and/or households, and therefore gives rise to a liability for the department providing the social benefit.

21. Under IPSAS 42 the obligating event for the creation of a liability related to social benefits is similarly the point at which an individual or a household meets the eligibility criteria for the provision of the next social benefit payment and the next social benefit payment would be recognised in full, unless eligibility changes before the payment is made.

22. The main potential divergence between IPSAS 42 application and the accounting treatment proposed in this paper is a small timing difference in recognition.

23. Under IPSAS 42, the full amount of the next benefit payment payable after the year end is accounted for in the year.

24. Under the accounting treatment in this paper, the amount relating to the period of entitlement up to year end, but not beyond, that has not yet been paid is included as an accrual.

Practical implications of proposed requirements

25. HM Treasury are recommending that this guidance be applied for the first time in 2025-2026. This year is recommended in response to concerns raised by departments about the timing of implementation. Departments will need to prepare the data for collection in advance of needing to restate prior year balances, which under this implementation date would be 2024-25.

26. HM Treasury also recommend that this should be accounted for as a change in accounting policy that should be applied retrospectively in accordance with IAS 8. It is expected that it will be practicable for departments to restate prior period balances. First-year application in 2025-2026 will allow for departments to prepare the prior period balances for 2024-25.

27. There will be an in-year budgetary impact of this change for departments that do not currently account for social benefits in this way.. However, as per Consolidated Budgeting Guidance principles, departments will not be held any better or worse off for accounting policy changes outside of their control and budgets will be restated for the remainder of the SR period as necessary.

Other support payments given in response to external circumstances

28. In the course of previous discussion in this area, Board members raised the issue 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 payments 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.

29. Accruals under IAS 37 principles will continue to require entities to determine whether the obligation is a present obligation on a case-by-case basis, in agreement with the NAO. This assessment includes determining the point at which recipients become eligible, the level of communication and obligation and the level of discretion in issuing payments.

Updated wording

30. Considering the analysis above, the following wording is now suggested for inclusion in the FReM:

    Expenditure in respect of social benefit payments should be recognised at the point at which the social benefit claimant meets the eligibility requirements to receive the benefit. Only the expenditure for the period of entitlement that falls within the accounting year should be recognised.

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

31. See Annex 1 for more detail on the definitions used.

32. See Annex 2 for Illustrative Examples.

Decision needed: Is the Board content to confirm that they agree with accounting for social benefits and the suggested wording for inclusion in the 24-25 FReM?

Annex 1 – Definitions

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

2. 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*"

3. 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.*"

4. 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

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

6. 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.

Annex 2 – 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 meets the definition of social benefits set out in the body of the paper as it is paid in cash to eligible individuals and addresses concerns with unemployment, sickness or family circumstances as a means-tested social benefit that mitigates the social risks associated with unemployment or low income.

Example 1

Person A loses their job and on 25th March 202X submits an application to receive Universal Credit.

This is the first time Person A has applied for Universal Credit. Person A has met the eligibility criteria to be eligible to receive the benefit prior to the year-end.

Due to processing times, their application is processed, approved, and paid 4 weeks post-31st March 202X on the 27th April 202X.

An accrual for this claim should be included accrued and accounted for as expenditure in the financial year 202Y-2X as the conditions existed for the claimant to be eligible for the benefit prior to the year end.

Example 2

Person B loses their job and on 31st January 202X submits an application to receive Universal Credit. Their application is approved processed, approved, and paid 5 weeks later, on 4th March 202X.

This is accounted for as expenditure in the financial year 202Y-2X.

Person B is due to receive another payment on 4th April 202X. 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 of eligibility between the first payment and the year-end would then be accrued and accounted for as expenditure in the financial year 202Y-2X as the conditions existed for the claimant to be eligible for the benefit prior to the year end.