DECISION PAPER
Measurement of Assessed Contributions Receivables

Executive Summary

The aim of this paper is to identify those IPSAS compliant options for measurement of assessed contributions receivables that are presently under consideration by United Nations System organizations and support Task Force Members in their decision either to:

A. Establish a range of options that organizations are able to apply as they implement IPSAS, so that the extent of policy diversity in this area can be monitored going forward; or

B. Agree a single system-wide option applicable to all organizations.

In choosing between these two positions, Task Force Members are encouraged to take into account the constraints due to establishment of a stable policy platform and the benefits of a harmonized approach, which are described in **Appendix 1**.

Assessed contributions receivables: The three options are:

1) Direct reduction: Establishment of allowances as direct reductions (or write offs) of specific assessment receivables;

2) General allowance: Establishment of a general allowance for doubtful assessments; and

3) Discounting approach: Fair value of receivables calculated as the estimated discounted cash flows arising from assessed contribution receivables to be collected in the future (discounting approach).

This paper describes these three options, their advantages and disadvantages, and outlines further considerations in order to support an informed decision at the system wide level on treatment of assessed contributions receivables.

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1. Introduction

1 This paper identifies three possible options for measurement of assessed contributions receivables to support Task Force Members in their decision either to:

A. Establish a range of options that organizations are able to apply as they implement IPSAS, so that the extent of diversity in this area can be monitored going forward; or

B. Agree a single system-wide option applicable to all organizations.

2 In choosing between these two positions, Task Force Members are encouraged to take into account the constraints due to establishment of a stable policy platform and the benefits of a harmonized approach, both of which are described in **Appendix 1**.

2. Background

UNSAS and IPSAS

3 Measurement of assessed contributions receivables is an important area of change in the transition from UNSAS to IPSAS. UNSAS paragraph 32 states that "the organization may make a provision for delays in the collecting of the outstanding contributions". In other words, the establishment of a provision is allowed, but there is no specific requirement to do so.

IPSAS requirements inconclusive

4 IPSAS 23 is focused on the initial recognition of revenue from non exchange transactions. Example 20 of IPSAS 23 (IG 40 to 43) provides support for establishment of allowances[1] for doubtful debts from assessed contributions. In particular it illustrates that the nominal value receivables should be adjusted to provide a relevant and reliable measure. But this support is part of implementation guidance and the Standard itself does not contain requirements on the subsequent measurement of these assets.

5 Subsequent measurement needs to be consistent with IPSAS qualitative characteristics and IPSAS general measurement requirements, with a key requirement being that the asset be accurately and reliably reported; neither over- nor under-stated. A recently issued draft Standard, *ED 38 Financial Instruments Recognition and Measurement*, based on *IAS 37 Financial Instruments Recognition and Measurement*, is relevant to this issue. ED 38 requires organizations to write off uncollectible receivables.

6 The final version of ED 38 is likely to be open to interpretation in terms of whether assessed contributions receivables are within the Standard's scope. ED 38's scope is restricted to financial instruments that are "of a contractual nature." ED 38's

[1] Terminological issue: It is common for contra-asset amounts to be described as "provisions." While the use of the word "provision" with this contra-asset meaning is not prohibited by IPSAS, it can be confusing given that IPSAS defines "provision" differently. To avoid confusion, this paper uses the expressions "allowance for doubtful assessed contributions' receivables" and "contra-asset/ credit adjustment used to determine the carrying value of assets."

guidance on the meaning of this term is not conclusive. ED 38 *will* have relevance indirectly through the accounting policy hierarchy in IPSAS 3 (paragraph 14(b)) and represents a source of authoritative support for direct write off of uncollectible receivables (Option 1 below), because it sets out the accounting treatment of a "similar issue" i.e. the treatment of ordinary accounts receivable.

3. Three Options to Measure Assessed Contributions Receivables

7 While IPSAS establishes that the nominal value of assessed contributions receivables must be adjusted and that the asset must be accurately and reliably reported; neither over- nor under-stated, if the final Standard based on ED 38 does not apply directly to assessed contributions, how best to achieve this requirement remains open. Judgment will be required to choose among alternative options to arrive at an accurate and reliable value. This paper identifies the following three options:

1) Direct reduction: Establishment of allowances as direct reductions (or write offs) of specific assessment receivables, based on known payment arrangements or estimated amount of uncollectible debt (discussed in system-wide accounting paper *#27 Accounting for Assessed Contributions*).

2) General allowance: Establishment of a general allowance for doubtful receivables based on the estimated amount of uncollectible assessments (raised in Focus Groups' comments on system-wide accounting paper *#53 Guidance Note 3 Assessed Contributions*).

3) Discounting approach: Fair value of receivables calculated as estimated discounted cash flows arising from outstanding assessed contribution to be collected in the future (discussed in system-wide accounting paper *#53 Guidance Note 3 Assessed Contributions*).

8 **Table 1** below summarized the main advantages and disadvantages of each option on both a technical and institutional ground.

4. Calculation Methods for the Three Options

9 Different calculation methods can be used for each option identified above. **Appendix 2** provides an overview of the main calculation methods.

Table 1 Options: Advantages and Disadvantages

	Option	Advantages	Disadvantages
1)	**Direct Reduction**	• Supported by the most recent version of ED 38 on Financial Instruments and IPSAS 23, Example 20 (IG 40 to 43) • Already applied by some International Organizations (i.e. IFAD and other International Financial Institutions) and GAAP • Reliability, based on specific information about significant delays or Member States' inability to pay an assessment	• Problematic on institutional/political ground: lack of authority to make direct reductions of specific assessments or to establish a provision on a specific receivable without precise instructions from GA/governing bodies • Perceived implications of an allowance/expense for doubtful assessments[2] • Financial regulations of some organizations do not allow write offs other than the 100% provision for former states/members that lost their voting rights
2)	**General Allowance**	• Supported by IPSAS 23, Example 20 (IG 40 to 43) • Reliability, based on calculation methods (i.e. use of historical data on arrears collected over time, general assumptions, % of allowance based on length of overdue time) • General allowance does not have implications on the legal obligation for the member state to pay outstanding assessed contributions	• Perceived implications of an allowance/expense for doubtful assessments[3]
3)	**Discounting Approach**	• Focuses on future cash flows rather than on assumptions on uncollectible receivables • Accurate methodology to measure present value of contributions receivable under specific payment plans (i.e. 10 to 20 years) • Factors in the present value of receivables which are likely to be collected in the future or that may never be collected • A fair value adjustment to reflect present value of future cash flows is conceptually more acceptable than an allowance to rectify the nominal value of overdue assessments	• Complicated method, perhaps more subjective than the others • Difficulty in reliable measurement of future cash flows (i.e. quantification and timing of cash flows) • Debatable discount rate to be applied

[2] This issue was raised by few organizations in the Focus Groups' comments to accounting paper 27 and is well summarized by the IFAD accounting policy paper EB/88/34/R.34, par. 28: "the effect of making a provision (…) is primarily to reduce the value of the asset and thereby explicitly to assure that these amounts are withheld from resources which are committed (…)". Does the establishment of an allowance interfere with the full usage of the resources approved in the regular budget? Does it have other implications i.e. a cross-subsidization of the non-paying states by the ones who regularly pay? Given the different basis of accounting between budgeting and reporting and the need to reconcile their values, there would be ways to avoid budgetary consequences of writing an allowance/expense for uncollectible assessments.

Appendix 1 Accounting Policy Harmonization and Diversity

1. Introduction

A1 This Appendix briefly describes the benefits of a harmonized approach, the constraints on further harmonization due to establishment of a stable policy platform, and a framework for managing diversity in accounting policies and practices across different United Nations System organizations. Such a framework needs to include:

- Clarification of the level of system-wide harmonization that already exists;
- Processes to protect the existing stable policy platform so as to provide policy stability during organizations' IPSAS implementation, while still providing a mechanism to amend policies where necessary;
- A process to track policy and practice diversity over time and support the emergence of further harmonization in these areas, which should include an evaluations of whether harmonization is increasing or decreasing over time and whether or not diversity is within acceptable limits; and
- Factors likely to impact on the extent of accounting policy and practice harmonization during the short to medium term.

2. Harmonized accounting policies and practices: United Nations System

IPSAS adoption delivers harmonization

A2 IPSAS adoption will significantly increase the consistency and comparability of United Nations organizations' financial reporting. This is because IPSAS is far more detailed and prescriptive than UNSAS. Member States view this increase in harmonization as an important benefit of IPSAS adoption. This harmonization contributes towards Member States' aim for United Nations System organizations to harmonize their business practices[3].

System-wide policies, practices, guidance and training provide further harmonization

A3 In addition to the large increase in harmonization due to IPSAS adoption, the Task Force has developed a level of harmonized practices above that delivered by IPSAS compliance. This higher level of harmonization is given effect through the Task Force's approval of harmonized accounting policies and recommended accounting practices, and through development of system-wide guidance papers and system-wide IPSAS training products, which support both IPSAS adoption and a consistent United Nations system-wide interpretation of IPSAS requirements.

Completion of IPSAS adoption means a <u>very high</u> level of system-wide harmonization

A4 To gain the benefits of the work done by the Task Force requires that all organizations fully implement IPSAS. Once that is achieved, the agreed set of policies and practices, the extent of IPSAS understanding achieved through the system-wide guidance papers and IPSAS training is expected to result in a very higher level of

[3] The system-wide coherence report describes the importance of coherence, also called harmonized business practices, and Member States support the package of business harmonization initiatives proposed by the High Level Committee on Management.

consistency; higher than usually exists across a single industry group within a national jurisdiction.

Policy and practice differences will remain

A5 Despite this very high level of harmonization, differences in terms of policy and practice will remain. This is normal in any reporting environment. No set of financial reporting standards provides exhaustive coverage of all reporting issues. While the Task Force's commitment to consistency has reduced the extent of policy and practice diversity that will exist once IPSAS is fully implemented, diversity remains. This diversity arises in the following ways:

- *Explicit policy decisions* to allow organizations to choose between two options in a Standard. (For example, the policy that allows organizations to report their cash flows on either a gross or a net basis).
- *Differences of application* of a Standard when applying it to organizational specifics. (For example, organizations may have different ways of classifying their voluntary funding agreements with the result that different revenue recognition points are used for revenue from similar funding agreements.)
- *Gaps in IPSAS*, where there is no Standard addressing an issue with the result that a number of different accounting treatments are acceptable. (For example, how to account for the value of a building that has been provided to an organization for a nominal (pepper corn) rent.)

Differences in accounting treatment that reflect differences in substance

A6 Policy and practice diversity focuses on different reporting of the same substance or different reporting of the same set of information. For example, an organizations' cash flow from operations can be reported on either a gross or a net basis – the information will look different but the underlying substance is the same. That is diversity. By contrast, two organizations may have different depreciation rates for their vehicles, because the experience of the two organizations is that their vehicles have different useful lives. The difference in depreciation rates reflects the different substance of the event (the vehicles usage and resulting useful life). This is simply a necessary difference in accounting treatment to reflect a difference in substance. It is *not* an example of lack of system-wide harmonization; and, it is *not* an example of diversity in system-wide policy or practice. If the *substance* of an event or transactions is different, then it is important that the accounting rules correctly report that difference.

Normal to have a 'tidy up' period after a major accounting change

A7 In addition, a major accounting change such as IPSAS adoption usually includes areas of accounting treatment uncertainty that are only resolved during a 'tidy-up' period after the major change has been implemented. That is part of the transformation process. That phenomenon needs to be appreciated and processes put in place to ensure that further progress occurs to identify and address 'unresolved' areas and topics that were particularly difficult and challenging during implementation.

A8 For example, despite Task Force agreement on the system-wide papers addressing controversial issues such as control over assets, it is likely that different organizations will apply the system-wide guidance in different ways. Some of the resulting diversity

will correctly reflect organizations' different specific arrangements. Some of the diversity may reflect different applications of the guidance applied to essentially the same under-lying economic substance. The list of controversial items encountered by United Nations System organizations as they adopt IPSAS is small compared to what normally exists when a national public sector adopts accrual accounting for the first time.

Importance of establishing a way to manage accounting policy diversity

A9 The existence of diversity and the benefits of harmonization provide an argument in favor of a way to manage diversity, with a central part of this management being monitoring the extent of diversity that exists and establishing an on-going mechanism to maintain or even increase the level of harmonization, with the most important period for this task being the years immediately after IPSAS implementation. This is discussed further in **Section 4** below.

3. Constraints due to establishment of a stable policy platform

Stable policy platform – constraint on further restrictions on policies and practices

A10 A stable policy platform was established in 2007. As discussed above, this platform will ensure a high level of consistency across United Nations System organization, once organizations have adopted IPSAS. Further policy development generally is only expected to occur in response to new issues raised by new and revised Standards[4]. This is important to ensure policy stability for all organizations, whether they have already implemented, plan to implement in 2010, or are progressively implementing individual Standards using the flexibility available under UNSAS. Organizations expecting to implement by 2010 should have already determined the majority of their accounting policies by the end of 2008, so that changes to procedures, training, and information systems can be identified and put in place by the end of 2009.

Changes to existing policies – limited scope

A11 In rare cases a change to an existing policy may be proposed. Change should not occur unless either *all* early adopters and *all* organizations planning to adopt effective 2010 – without exception – have agreed to the proposed policy change; or, the changed policy is necessary to ensure IPSAS compliance after a new or revised Standard has made the system-wide policy non-compliant.

Development of new policies and definition of acceptable practices

A12 Development of a new policy, where no system-wide policy has previously been developed, and definition of acceptable practice at a more detailed level than that which presently exists have the same potential to cut across decisions already made by early adopters and organizations adopting effective 2010. The same preconditions should be met as those for a change to an existing policy before either a new policy or a detailed definition of acceptable practice is approved by the Task Force.

[4] The IPSASB is in process of issuing a set of 'convergence' standards based on existing International Financial Reporting Standards (IFRS). Where system-wide policies applicable to the existing IFRS have already been developed and the IPSAS-equivalent to that IFRS does not change the accounting requirements, the policies are not changed other than to align the reference paragraphs to those in the IPSAS. When a new 'convergence' IPSAS includes changes of substance that introduce new options that were not in the previous IFRS, a system-wide policy needs to be developed.

Expansion of options

A13 Where an organization comes to a view that a particular system-wide policy is inappropriate and would like to be able to apply a different policy, it is possible to propose that the preferred option be allowed *in addition to* the approved system-wide policy. If the Task Force agrees to widen the range of allowable treatments, this would allow the individual organization to adopt a different policy, while protecting early adopters and 2010 organizations from policy change. But the effect would be to decrease the level of policy harmonization. A better alternative would be to gain 100% agreement from early adopters and the Task Force Member for a change of policy.

4. Management of policy and practice diversity

A14 Management of any phenomenon begins with information about that phenomenon. Management also involves an understanding of the factors that impact on the phenomenon and ways to address those factors. A framework to manage accounting policy and practice diversity is provided below:

1. Clear expectations: Establish a clear agreed understanding of the overall level of harmonization that is being pursued (the goal), the types of diversity that are acceptable and those that are not acceptable, and the expected benefits of policy harmonization.
2. Baseline: Establish a *baseline* that identifies the areas where diversity exists, classifies the different types of diversity, and grades the extent to which policies and practices are different.
3. Monitor changes: Gather information on changes to organizations' policies and practices such that the overall picture on the extent of policy and practice diversity can be kept reasonably current and it is possible to report reliably on whether the level of policy and practice diversity is decreasing, steady, or increasing.
4. Change factors: Identify factors that could impact on diversity and monitor those factors. Factors that are likely to impact on organizations' accounting policies and practices include:
    a. IPSAS changes: Standards will be developed to address previously unaddressed areas. Options in Standards may be removed.
    b. Application and allowable option changes: Organizations' understanding of an issue may change or auditors' comments may indicate that some practices are more acceptable than others with the result that organizations may decide to apply a different practice.
    c. Task Force decisions: Task Force approved policies and recommended practices may change. The Task Force may amend a system-wide policy to delete an allowed option or may establish further policies and recommended practices that constrict (or enlarge) organizations' options in areas where IPSAS is not definitive.
5. Processes: Establish processes (monitoring, reporting on trends and factors, decision making,) that support harmonization, provide scope to further increase harmonization consistent with the overall goal, and allow for an appropriate level of diversity.

Appendix 2 Calculation Methods for the Three Identified Options

1 This Appendix offers an overview of calculation methods that give effect to each of the three options described in the main part of this paper. These calculation methods have either been mentioned in accounting papers #27 and #53, in the December 2007 survey on "Allowance for Outstanding Assessments" (Appendix 4, accounting paper #53) or been identified through e-mail exchanges with United Nations system organizations developing or reviewing existing accounting policies in this area. Reference to the source of information is provided for each method.

Option 1) Direct Reduction

2 Calculation methods (i) through (v) below are applicable to Option 1) Direct Reduction:

i. Allowance is established only "for exceptional and agreed technical reasons", while normally "no allowance for loss is recorded with respect to receivables related to member countries' assessed contributions" (*OECD, notes to the financial statements*);

ii. Allowance (100%) is established for contributions where a country formally refuses to pay an assessment amount (*FAO, survey 2007*);

iii. Allowance (100%) is limited to the arrears of former member states and those member states that have lost the right to vote (*ILO, survey 2007; WIPO, survey 2007*);

iv. Allowance (100%) is established for those outstanding assessed contributions that generate the risk of losing voting rights, i.e. outstanding for over 24 months (*ICAO, survey 2007*);

v. Allowance (100%) is established for all assessed contributions that have been outstanding for 24 months or more, or in other words for all assessed contributions outstanding at the end of each administrative period/biennium (*WHO survey 2007, IFAD survey 2007*).

3 Methods (i) through (v) represent a continuum, which ranges from a stricter to a broader inclusion of the categories of outstanding assessments for which organizations would establish allowances. Further variation could exist in practice - positioned somewhere between the five points on the continuum shown above.

Option 2) General Allowance

4 Calculation methods (i) through (iii) below are applicable to Option 2) General Allowance:

i. Allowance calculated as percentage of the nominal value of outstanding contributions based on historical data on % of consolidated arrears/not collectable assessments (*Similar calculation is proposed in Accounting Paper 53, par. 14*). This percentage may vary over time and average rates might be used to offset variations.

ii. Allowance calculated as percentage of the nominal value of outstanding contributions divided in classes based on the length of payment overdue time. (*UNIDO/UNESCO email exchange 11/08/2009*). Different percentages are applied to each class of outstanding contributions, i.e:

- contributions outstanding for over 24 months = 100% allowance;
- contributions outstanding for 12 to 24 months = xx% (< 100%) allowance;
- contributions outstanding for 6-12 months = yy% (< xx%) allowance.

Quantification of xx% and yy% can be based on historical analysis of uncollected arrears and uncollected overdue contributions.

iii. Option 1.5 above (all outstanding amounts at the end of each biennium) can be used as well to calculate a general allowance for doubtful receivables. Difference between 2.3 and 1.5 is conceptual rather than practical.

Option 3) Discounting Approach

5 The discounting approach represents a pragmatic way to avoid reducing/writing off specific assessments and as such it requires that the expected cash flows from receivables over time be quantified. Calculation methods (i) and (2) below illustrate to ways to achieve this quantification:

iii. Historical data on percentages of arrears collected in i.e. 0-6, 6-12, 12-24 or over 24 months from the end of the biennium could be used to quantify future cash flows over time. Proper discount rates should be applied to each class of identified receivables to obtain the discounted value of the future inflows.

iv. A further approach to quantify cash flows is to assume that for arrears overdue for more than 3 years the corresponding States will request an agreement to settle their obligations over a period from 10 to 20 years and to discount accordingly the future payments so determined (*ICAO, survey 2007*).

6 As a further note, the identification of the appropriate discount rate is important to ensure a meaningful and IPSAS compliant calculation method. Depending on the method used to quantify the future payment flows, different rates could be applied to receivables based on the expected collection lapse or an average rate could be applied to the overall estimated inflow.