



Australian Government
Australian Accounting
Standards Board

AASB 8-9 June 2011
Agenda paper 13.2

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X June 2011

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CANADA

Dear Ms Fox

IPSASB Conceptual Framework Exposure Draft 1 *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities: Role, Authority and Scope; Objectives and Users; Qualitative Characteristics; and Reporting Entity*

The Australian Accounting Standards Board (AASB) is pleased to provide its comments on the above named Exposure Draft (ED). In formulating these comments, the AASB considered the views received from Australian constituents.

The AASB supports the International Public Sector Accounting Standards Board's (IPSASB's) development of a conceptual framework for public sector entities as a high priority project. The AASB has some noteworthy concerns regarding the proposals in the ED and recommendations for addressing them. The more substantive concerns are set out below.

The AASB considers the rationale that the scope of financial reporting will evolve in response to users' information needs is insufficient. If the IPSASB does not define the scope of financial reporting at this stage, it should at least specify criteria for assessing how the scope of financial reporting should evolve in response to users' information needs.

The AASB does not support having two objectives of general purpose financial reporting because accountability is subsumed within the decision making objective and, in any event, the information identified in the ED as useful to meet an accountability objective is similar to the information that is useful for decision making. Instead, the AASB recommends the IPSASB Conceptual Framework identifies a single objective of financial reporting, namely, to provide information useful for decision making by users of financial reports and at the same time explaining the relationship of accountability to decision making.

The AASB considers 'economic phenomena' a broad notion encompassing scarce resources, claims to scarce resources, and inflows and consumptions of scarce resources. The AASB acknowledges the difficulty, in global standard setting, with choosing

terminology that does not cause translation problems and therefore the use of ‘economic phenomena’ may need elaboration. However, the AASB is concerned that the references to phenomena other than economic phenomena in the ED implicitly expand the scope of financial reporting, and considers that such matters should be dealt with explicitly in the ‘scope of financial reporting’ component of the Conceptual Framework.

The AASB acknowledges that the development of the IPSASB’s Conceptual Framework is not an IASB convergence project. However, the AASB supports the principle of transaction neutrality (because of, amongst other reasons, the benefits such an approach can bring to the quality of global financial reporting) and considers that the IPSASB’s Conceptual Framework should differ from the revised IASB Conceptual Framework only when there is a public sector specific reason to do so. The AASB will find it difficult to incorporate aspects of the IPSASB Conceptual Framework in its own Framework to the extent differences exist without appropriate rationale.

The AASB’s responses to the specific matters for comment in the ED are set out in Appendix A.

Other AASB comments on the ED are set out in Appendix B.

If you have any queries regarding matters in this submission, please contact me or Mischa Ginns (mginns@aab.gov.au).

Yours sincerely

Kevin Stevenson
Chairman and CEO

APPENDIX A

AASB's comments on the Specific Matters for Comment on the ED

1. Role, authority and scope of the Conceptual Framework

Role and authority of the Conceptual Framework

The AASB generally supports the proposed role and authority of the Conceptual Framework.

The AASB recommends that, as a matter of priority, the IPSASB addresses in IPSAS 3 *Accounting Policies, Changes in Accounting Estimates and Errors* the status of its Conceptual Framework in the hierarchy of authoritative guidance for issues not specifically addressed by IPSASs. The AASB considers that the status of the IPSASB Conceptual Framework should be equivalent to that of the IASB Conceptual Framework in IFRSs, including in particular IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. The AASB notes that, presently, paragraph 14 of IPSAS 3 refers to the definitions, recognition and measurement criteria set out in other IPSASs, and paragraph 15 of IPSAS 3 refers to the IASB Framework.

Scope of financial reporting

The AASB considers the rationale that the scope of financial reporting will evolve in response to users' information needs is insufficient. If the IPSASB does not define the scope of financial reporting at this stage, it should at least specify criteria for assessing how the scope of financial reporting should evolve in response to users' information needs. The AASB's reasons for these comments are set out below.

The AASB does not consider usefulness a sufficient criterion for determining which information types should fall within the scope of financial reporting. It is quite probable that not all useful information belongs within that scope. This point is acknowledged in paragraph BC1.10 of the ED's Basis for Conclusions on Chapter 1. Consistent with this point, the AASB's submission on the IPSASB Consultation Paper *Reporting on the Long-Term Sustainability of Public Finances* expresses a view that information about the long-term affordability of a government's policies may be useful for decision making by users of the government's financial reports but would not be suitable for general purpose financial reporting.

Therefore, the AASB considers it unclear which useful information the ED would conclude belongs within the scope of financial reporting and which useful information falls outside the scope of financial reporting. It encourages the IPSASB to conceptually define the scope of general purpose financial reporting to help resolve this issue.

Applicability

The AASB considers it important to clarify in paragraph 1.8 that, whilst GPFs of government business enterprises (GBEs) as separate reporting entities are not within the scope of the IPSASB Conceptual Framework, information about GBEs included in the GPFs of governments and other not-for-profit public sector entities is within the scope of

the IPSASB Conceptual Framework. The present wording of paragraph 1.8 has caused some confusion for Australian commentators on the ED.

2. Objectives of financial reporting by public sector entities and the primary users of GPFs of public sector entities and their information needs

Objective of financial reporting

Whilst acknowledging the range of views on this matter held by IPSASB constituents, the AASB does not support having two objectives of general purpose financial reporting. Instead, the AASB suggests the IPSASB Conceptual Framework identifies a single objective of financial reporting, namely, to provide information useful for decision making by users of financial reports. This would help with identifying the financial information needs of users that GPFs should strive to meet and that Standards should be developed to require. The AASB does not support identifying accountability as a separate objective because:

- (a) the information identified in the ED as useful to meet an accountability objective is similar to the information that is useful for decision making. Therefore, it is unclear how identifying two objectives would help the IPSASB identify information that should be required by IPSASs;
- (b) accountability is subsumed in the decision making objective and can be explicitly acknowledged as such, and therefore given sufficient acknowledgement, in a Conceptual Framework along the lines of the approach taken by the IASB; and
- (c) accountability is an imprecise notion. Therefore, if it is identified as a separate objective, it could unintentionally open up general purpose financial reporting to providing all kinds of information, such as social responsibility reporting. Whilst acknowledging the interrelationship between objectives and scope, the intended scope of financial reporting should be addressed directly rather than defining it inadvertently through articulation of the objective.

In expressing these views, it is important to note that the AASB regards discharging accountability as a key role of GPFs of public sector entities. However, it considers this role would be achieved by providing financial information useful for decision making purposes. In support of this conclusion, the AASB notes that the ED adopts a broad view of decision making, by identifying voting and lobbying decisions as the kinds of decisions it includes.

Therefore, consistent with (b) above, the AASB considers the relationship between discharging accountability and providing information for decision making should be made more explicit. This would involve explaining that the importance of GPFs in discharging accountability of public sector entities (and their managements) does not necessarily mean accountability should be identified as an objective.

The AASB considers that the ED's guidance on decision making should be enhanced in two respects:

- (a) it should provide a more comprehensive description of decision making. Although the ED's guidance usefully identifies voting and lobbying decisions as the kinds of decisions included in decision making, it does not specifically describe 'decision making'. The AASB recommends elaborating on the nature or types of decisions encompassed by the references to 'decision making'; and
- (b) in meeting (a), the discussion of decision making should refer to 'evaluating past decisions'. Information useful for such evaluations would possess confirmatory value. Including this guidance would strengthen the link between decision making and accountability. This could help address concerns that some users, such as recipients of services, do not make decisions about allocating resources to the entity. Even if a user of a financial report takes no action as a result of evaluating past decisions, this reflects the user's decision not to act.

Primary users

The AASB does not support the proposed identification of 'primary' users of GPFRs in the IPSASB Conceptual Framework. Although it is useful to consider categories of users to help identify users' common information needs, identifying 'primary' users may inappropriately imply the needs of some users should be disregarded.

However, if the IPSASB decides to proceed with identifying 'primary users' it should include, among others, all parties performing a review or oversight function on behalf of other users. The AASB considers it inconsistent to identify as primary users parties performing a representative (review or oversight) function on behalf of other primary users, but only when they are legislators/parliamentarians.

3. Qualitative characteristics of, and constraints on, information included in GPFRs of public sector entities

Faithful Representation

The AASB supports using faithful representation instead of reliability as a qualitative characteristic. Consistent with its view outlined in the covering letter, the AASB supports the use of terminology that is consistent with the IASB Conceptual Framework because, in this case, there is not a public sector specific reason for the IPSASB's Conceptual Framework to differ from the revised IASB Conceptual Framework.

Economic phenomena

The AASB considers 'economic phenomena' a broad notion encompassing scarce resources, claims to scarce resources, and inflows and consumptions of scarce resources. It would also include phenomena external to the entity that may be assessed in relation to scarce resources and changes therein. This notion would therefore include information such as output information. The AASB acknowledges the difficulty, in global standard setting, with choosing terminology that does not cause translation problems and therefore the use of 'economic phenomena' may need elaboration. However, the AASB is concerned that the references to phenomena other than economic phenomena in the ED implicitly

expand the scope of financial reporting, and considers that such matters should be dealt with explicitly in the ‘scope of financial reporting’ component of the Conceptual Framework. The AASB is also concerned that references to other phenomena open the door to reporting items, such as deferrals, that do not represent phenomena that have a dimension that is external to the entity. The ED does not explain the meaning of such other phenomena, and if retained, the IPSASB should explain its reference to providing information about phenomena other than ‘economic phenomena’.

Materiality

The AASB does not support treating materiality as a constraint on reporting useful information in GPFRs. Consistent with the IASB’s revised Conceptual Framework, the AASB considers materiality to be an entity-specific aspect of relevance. This is because, unlike cost, materiality is not a constraint on a reporting entity’s ability to report information; and materiality does not affect standard setters’ decisions because it is an entity-specific consideration.

The AASB does not support the IPSASB’s reasoning for treating materiality as a constraint set out in paragraph BC3.32 of the ED. The AASB considers that, if an item of information is irrelevant, meeting the other qualitative characteristics does not make it useful.

‘Fundamental’ and ‘enhancing’ qualitative characteristics

The AASB notes that the ED does not replicate the revised IASB Conceptual Framework’s dichotomy between ‘fundamental’ and ‘enhancing’ qualitative characteristics. Although the AASB has concerns, in principle, with that dichotomy adopted by the IASB, it considers there is no apparent public sector specific reason for the IPSASB’s Conceptual Framework to differ from the revised IASB Conceptual Framework on this issue. This is particularly so given the benefits of a common conceptual framework applicable to all kinds of entities, whether for-profit or not-for-profit, in the private or public sectors. Consistent with its view outlined in the covering letter, the AASB considers that differences from the IASB Conceptual Framework should only occur when there is a public sector specific reason for them.

4. The basis on which a public sector reporting entity is identified and the circumstances in which an entity should be included in a group reporting entity

The AASB supports the IPSASB’s intention to identify the boundaries for determining those entities that should prepare GPFRs and identify the circumstances in which consolidated financial statements should be prepared. However, it considers that in the public sector, there is likely to be a need for criteria to identify which entities should, in concept, be required to prepare GPFRs. For example, it may be unclear whether government departments should prepare GPFRs. It is less clear than in the private sector to identify which entities that are components of entities preparing GPFRs should also prepare GPFRs. The AASB therefore suggests including guidance for identifying the characteristics of entities with users dependent on their GPFRs for decision making; and that should therefore prepare GPFRs. The focus of the guidance could, in effect, be on identifying which public sector entities need not prepare GPFRs.

The AASB considers the proposed boundaries of a group reporting entity are in principle consistent with the notion of control adopted by standard-setters in various jurisdictions and

recommends explicitly acknowledging this in the IPSASB Conceptual Framework. Although the AASB acknowledges the reasons for the IPSASB's approach that focuses on the components of group reporting entity relationships without referring to control, it considers the arguments for referring to 'control' are stronger. The arguments include that IPSASs are developed with reference to IFRSs and are applied or referred to by many parties who are strongly conversant with IFRSs. Therefore, it is important not to create the appearance of substantive differences from IFRSs where none exists.

The AASB is concerned that paragraph BC4.21 of the ED suggests the concept of a group reporting entity is incomplete. This is because it says that whether applying the proposed boundaries of a group reporting entity will provide useful information in various circumstances will need to be considered in developing authoritative requirements in each jurisdiction.

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APPENDIX B

Other AASB Comments on the ED

Paragraphs	Comment
1.6	Whereas Footnote 2 on page 11 of the ED clarifies that information about “anticipated future service delivery activities and resource needs” need not be provided in every GPFR, paragraph 2.14 (second sentence, particularly third bullet point) says GPFRs will need to provide information about such matters and paragraph 2.23 gives a similar impression. It would seem best if the IPSASB Framework were to say such information is included within the scope of general purpose financial reporting in view of its usefulness, but that a broad scope is not intended to indicate each GPFR should provide this information.
2.24 and 2.25	The AASB considers paragraphs 2.24-2.25 imply that narrative reports would only include information about financial and service delivery performance. This could unintentionally narrow the scope of the information that should be included in a narrative report. The AASB suggests amending wording and including some examples of other information that may be included in a narrative report, such as information about risks, resources, objectives, strategies, relationships and nature of business.
3.40	The AASB suggests replacing “relevant” with “useful” in the last sentence. Under the present wording, timeliness and understandability are components of relevance, although Chapter 3 identifies them as qualitative characteristics in their own right (see paragraph BC3.7, third sentence).
4.8	The second sentence implies services delivered are not financial benefits. The AASB disagrees with that implication, and therefore suggests replacing “financial” in the second line of the first sentence with “in the form of cash flows”.
BC4.14	This paragraph essentially repeats the proposal in Chapter 4 regarding the boundaries of a group reporting entity, and therefore is not a basis for a conclusion. The AASB suggests providing the basis for concluding that these boundaries are necessary to satisfy the objectives of financial reporting.