

Statement of Accounting Concepts

SAC 2
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Objective of General Purpose Financial Reporting

Prepared by the **Public Sector Accounting Standards Board** of
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STATEMENT OF ACCOUNTING CONCEPTS

SAC 2 "OBJECTIVE OF GENERAL PURPOSE FINANCIAL REPORTING"

Citation

- 1 This Statement may be cited as Statement of Accounting Concepts SAC 2 "Objective of General Purpose Financial Reporting".

Application and Operative Date

- 2 This Statement applies to each reporting entity in relation to its first reporting period that ends on or after 31 August 1990, and in relation to subsequent reporting periods.

INTRODUCTION

- 3 The purpose of this Statement is to establish the objective of general purpose financial reporting by reporting entities in the private and public sectors. The Statement identifies the users of general purpose financial reports, the common information needs of such users and the broad types of information, consistent with those needs, that general purpose financial reports should provide.
- 4 Although the specification of an objective will have implications for the type of information to be included in general purpose financial reports and for the manner in which such information is to be communicated to users, this Statement contains no conclusions regarding the particular qualities that information should possess to meet this objective, the number, nature and form of the financial statements to be prepared, and the nature and measurement of the elements of such statements. These matters are the subject of other Statements of Accounting Concepts.

DEFINITIONS

- 5 For the purposes of this Statement:

"accountability" means the responsibility to provide information to enable users to make informed judgements about the performance, financial position, financing and investing, and compliance of the reporting entity;

"compliance" means adherence to those statutory requirements, regulations, rules, ordinances, directives or other externally-imposed requirements in respect of which non-compliance may have, or may have had, a financial effect on the reporting entity;

"financial position" means the economic condition of a reporting entity, having regard to its control over resources, financial structure, capacity for adaptation and solvency;

"financing and investing" means those activities of a reporting entity that relate to the financing of its operations and the investment of its resources;

"general purpose financial report" means a financial report intended to meet the information needs common to users who are unable to command the preparation of reports tailored so as to satisfy, specifically, all of their information needs;

"performance" means the proficiency of a reporting entity in acquiring resources economically and using those resources efficiently and effectively in achieving specified objectives; and

"reporting entity" means an entity (including an economic entity) in respect of which it is reasonable to expect the existence of users dependent on general purpose financial reports for information which will be useful to them for making and evaluating decisions about the allocation of scarce resources.

DISCUSSION

Scope and Applicability

- 6 The objective specified in this Statement applies to general purpose financial reporting by all reporting entities.
- 7 General purpose financial reporting focuses on providing information to meet the common information needs of users who are unable to command the preparation of reports tailored to their particular information needs. These users must rely on the information communicated to them by the reporting entity.
- 8 Some users have specialised needs and will possess the authority to obtain the information to meet those needs. Examples of such users are taxation authorities, central banks and grants commissions. Although such users may make use of the information contained in general purpose financial reports, because they have the authority to

command the information they require they do not need to rely on information provided to other groups. Special purpose financial reports directed at the needs of such users are beyond the scope of this Statement.

- 9 This Statement encompasses general purpose financial reporting by business and non-business reporting entities in the public and private sectors. It covers general purpose financial reporting by all types of reporting entities, whether legal, administrative or economic entities, and therefore encompasses all types of government entities, including government departments, statutory authorities, and, as a whole, Federal, State, Territorial and local governments; investor-owned entities, including companies and unit trusts; mutual co-operative entities, including building societies and credit unions; human service entities, including churches, foundations, professional associations and charities; superannuation plans; partnerships; and sole proprietorships.
- 10 Financial reporting encompasses the provision of financial statements and related financial and other information. Financial reports, comprising financial statements, notes, supplementary schedules and explanatory material intended to be read with the financial statements, are the principal means of communicating financial information about a reporting entity to users. However, other information can best be provided, or can only be provided, outside financial reports. Financial reports are not the only source of relevant information about a reporting entity, and users of financial reports may need to consult other sources to satisfy their information needs. This Statement does not attempt to draw a clear distinction between financial reports and financial reporting, nor does it attempt to define the boundaries of general purpose financial reporting. Distinctions will be made and boundaries drawn, as required, in other Statements of Accounting Concepts and in Accounting Standards.

Purpose of General Purpose Financial Reporting

- 11 General purpose financial reporting is not an end in itself, but is a means of communicating relevant and reliable information about a reporting entity to users. The objective specified in this Statement derives from the information needs of those identified as the users of general purpose financial reports. Those needs depend, in turn, on the activities of reporting entities and the decisions users make about them.
- 12 Reporting entities control resources and influence members of the community through providing goods and services, levying prices,

charges, rates and taxes, and acquiring and investing resources. The community interest is best served if scarce resources controlled by reporting entities are allocated to those entities which will use them in the most efficient and effective manner in providing goods and services. Efficient use of resources raises output, has desirable macroeconomic effects by enhancing employment and the standard of living, and enables social policy objectives to be achieved at the lowest cost. Members of the community make resource allocation decisions in respect of reporting entities - that is, they make reasoned choices among alternative uses of scarce resources. For example, investors decide whether to invest in an entity; creditors decide whether to lend resources to an entity; governments and parliaments decide, on behalf of constituents, whether to fund particular programmes for delivery by an entity; taxpayers decide who should represent them in government; donors decide whether to donate resources to an entity; individuals decide whether to contribute to a superannuation plan; employees decide whether to sell their services to a particular entity; owners/members of reporting entities decide whether they should contribute resources to the entity and who should manage the entity on their behalf; and ratepayers decide whether they should support the particular programmes of their local government and who should represent them on the local government council.

- 13 Efficient allocation of scarce resources will be enhanced if those who make resource allocation decisions, such as those groups identified above, have the appropriate financial information on which to base their decisions. General purpose financial reporting aims to provide this information.
- 14 General purpose financial reporting also provides a mechanism to enable managements and governing bodies to discharge their accountability. Managements and governing bodies are accountable to those who provide resources to the entity for planning and controlling the operations of the entity. In a broader sense, because of the influence reporting entities exert on members of the community at both the microeconomic and macroeconomic levels, they are accountable to the public at large. General purpose financial reporting provides a means by which this responsibility can be discharged.
- 15 Although the subsequent discussion of users and their information needs at times distinguishes between business and non-business entities, the common objective specified in this Statement reflects the inherent similarities between the two types of entities. While business entities seek to earn profits or desired rates of return and non-business entities pursue primarily non-financial objectives, both

types of entities provide goods and services to the community and use scarce resources in the process; both obtain these resources from external sources and are accountable to the providers of the resources or their representatives; both control stocks of resources; both incur obligations; and both must be financially viable to meet their operating objectives.

Users of General Purpose Financial Reports

- 16 Many individuals and organisations base resource allocation decisions on their relationship with and knowledge about reporting entities and are therefore potentially interested in the information provided in general purpose financial reports. The following three categories of user groups are identified as the primary users of general purpose financial reports, and those whose common information needs should dictate the type of information to be disclosed by such reports: resource providers, recipients of goods and services, and parties performing a review or oversight function.

Resource providers

- 17 Providers of resources include those who may be compensated either directly or indirectly for the resources they provide. The former category includes employees, lenders, creditors, suppliers and, in the case of business entities, investors and contributors. The latter category includes donors, members of non-business entities such as clubs, societies and professional bodies, and, in the case of public sector bodies, parliament, taxpayers and ratepayers.

Recipients of goods and services

- 18 Recipients of goods and services are those who consume or otherwise benefit from the goods and services provided by the reporting entity. This category comprises customers and beneficiaries. In many non-business entities recipients of goods and services include resource providers, for example, ratepayers, taxpayers and members of professional associations.

Parties performing a review or oversight function

- 19 Certain parties, including parliaments, governments, regulatory agencies, analysts, labour unions, employer groups, media and special interest community groups, perform oversight or review services on behalf of the community. Members of this group tend to have indirect or derived interests in general purpose financial reports since they advise or represent those who have direct interests.

Managements and governing bodies

- 20 Managements and governing bodies are another category of user interested in the information provided in general purpose financial reports. However, managements and governing bodies need, in addition to the information contained in general purpose financial reports, management accounting and other information to carry out their planning and control responsibilities. Since this type of reporting has to be tailored to meet the specialised needs of these users, and since they will have the ability to determine the form and content of any such reports, this reporting is in the nature of special purpose financial reporting and is therefore beyond the scope of this Statement.

Purposes for which User Groups Require Financial Information

Resource providers

- 21 Providers of resources want to know whether the reporting entity is achieving the objectives which formed the reason for the provision of resources in the past and is operating economically and efficiently and using resources as prescribed. In the case of investor-owned business entities, investors and other resource providers will want to know whether the entity is operating profitably and generating favourable cash flows in the process, since their decisions relate to amounts, timing and uncertainties of expected cash flows. In the case of public sector entities and non-business entities in the private sector, taxpayers (and ratepayers) and contributors, respectively, want to know whether the entity is delivering the services expected of it, that is, whether it is achieving its objectives, and is doing so economically and efficiently. Other providers of resources to public sector entities and non-business entities in the private sector, for example, employees, suppliers, creditors and lenders, will principally be interested in the entity's ability to generate cash flows for timely payment of the entity's obligations to them. However, they will be indirectly concerned about the extent to which the entity is achieving its objectives since the ability of the entity to generate future cash flows will depend on its performance in this regard. Information provided in general purpose financial reports to enable resource providers to make these assessments will assist them in determining whether continued support of the entity's activities is warranted and in predicting the level of resources necessary to support those activities.

Recipients of goods and services

- 22 Recipients of goods and services may want to assess the ability of the reporting entity to continue to provide goods and services in the future, the likely level at which the goods and services will be provided and the likely cost of the goods and services. In this regard, as with resource providers, they want to know whether the entity is achieving its objectives and is operating economically and efficiently in the provision of the goods and services.
- 23 In the case of business entities, the focus of this user group is on the ability of the entity to generate favourable cash flows, since only by obtaining sufficient cash to pay for the resources it uses and to meet its other obligations will the entity be able to continue to provide the goods and services in the future. Assessments by these users will affect their decisions to seek alternative suppliers of the goods and services.
- 24 In the case of non-business entities, and to an extent public sector business entities, the focus of this user group is on the extent to which the entity is using resources in their interests. Assessments made by this category of users in relation to public sector entities may influence their voting preferences and representations made to parliamentary and other representatives, and may lead to the continuation, expansion, contraction or even cessation of the entity's activities. Assessments made by this category of users in relation to private sector non-business entities may influence their voting preferences concerning the existing management or governing body of the entity and their decisions as to whether to continue to obtain the goods and services provided by the entity.

Parties performing a review or oversight function

- 25 Parties performing review or oversight services of interest to members of the community want to know whether the reporting entity has been operating in the interests of such members. Like resource providers and recipients of goods and services, they want to know whether the entity is achieving its objectives and is operating economically and efficiently in carrying out its operations. Assessments by these users of the extent to which the entity is operating satisfactorily in these respects will influence the decisions they make about the activities of the entities and, in respect of the advice they give to their constituents, will affect the decisions of those constituents. These users may have specific guidelines against which to assess the operations of the entity, and some may be able to

demand special purpose financial reports to enable them to carry out this function.

Objective of General Purpose Financial Reporting

- 26 In view of the information needs of the users of general purpose financial reports identified in the preceding paragraphs, the position adopted in this Statement is that the objective of general purpose financial reporting is to provide information to users that is useful for making and evaluating decisions about the allocation of scarce resources.
- 27 When general purpose financial reports meet this objective they will also be the means by which managements and governing bodies discharge their accountability to the users of the reports. The provision of information for accountability purposes is an important function of the process of general purpose financial reporting, particularly in relation to public sector entities and non-business entities in the private sector. However, the rendering of accountability by reporting entities through general purpose financial reporting is encompassed by the broader objective of providing information useful for making and evaluating decisions about the allocation of scarce resources, since users will ultimately require the information for resource allocation decisions.

Types of Information Relevant to Users' Needs

- 28 The particular information users require for making and evaluating resource allocation decisions will overlap since all users will be interested, to varying degrees, in assessing whether the reporting entity is achieving its objectives and is operating economically and efficiently in the process, in assessing the ability of the entity to continue to provide goods and services in the future, and in confirming that resources have been used for the purposes intended. General purpose financial reports can provide information useful for these purposes by disclosing information about the performance, financial position, and financing and investing of the reporting entity, including information about compliance. The information useful for these purposes may be both historical and prospective in nature. Paragraphs 29 to 40 provide examples of information that users may require for making and evaluating decisions about the allocation of scarce resources.

Performance

- 29 Aspects of the performance of a reporting entity can be measured in financial and non-financial terms. Disclosure of the revenues generated by the entity during the reporting period and the expenses incurred in generating this revenue, together with the assets, liabilities and equity of the entity at the end of the reporting period, will provide users with information to assist them to assess the financial performance of the entity over the reporting period. The information will be useful in determining the cost of providing goods and services and the change in the entity's control over resources during the reporting period. In relation to business entities, users will be able to evaluate the change in the entity's control over resources by reference to the resources or funds employed by the entity in achieving the change. In terms of the purposes for which users require information, as identified in paragraphs 21 to 25, this information is relevant to the users of general purpose financial reports of business entities in predicting both the capacity of the entity to generate cash from its existing resource base and the effectiveness with which it would employ additional resources. In relation to non-business entities, the information is useful in assessing the resources necessary to enable the entity to continue to provide services in the future and the likely cost of those services.
- 30 Non-financial measures of performance may also be relevant to users for the purposes identified, particularly in relation to non-business entities. The absence of a profit or rate of return objective for these entities means that financial measures of performance are unlikely to be sufficient to assess fully the extent to which those entities have achieved their objectives, which typically include social as well as financial dimensions. The extent to which non-financial performance measures can be considered to fall within the scope of general purpose financial reporting will be the subject of a separate Statement of Accounting Concepts.
- 31 In the public sector, information about government policies that affect a reporting entity's operations may be relevant to assessments of performance. For example, it may be relevant that an entity is subject to a government policy of break-even pricing or a stipulated target rate of return on assets.

Financial position

- 32 Disclosure of information about the financial position of the reporting entity involves disclosure of information about its control

over resources, financial structure, capacity for adaptation and solvency.

- 33 The disclosure of information about the resources over which the entity has control, that is, disclosure of its assets, is relevant to users for making and evaluating decisions about the allocation of scarce resources. In terms of the purposes for which users require information, as identified in paragraphs 21 to 25, the information is useful in predicting the ability of the entity to continue to meet its objectives, whether these relate to the generation of positive cash flows in the future or the continued provision of goods and services.
- 34 The disclosure of information about the financial structure of the entity, that is, the sources, types and time patterns of finance, whether debt or equity, and the types of assets used by the entity, is relevant to users for making and evaluating decisions about the allocation of scarce resources. In particular, it is useful in predicting the future distribution of cash flows among providers of resources and the ability of the entity to attract resources in the future, and in assessing the extent to which restrictions and limitations on the uses to which the entity's resources can be put will affect the ability of the entity to meet its objectives.
- 35 The disclosure of information about the capacity of the reporting entity to modify the composition of the resources under its control is relevant to making and evaluating decisions about the allocation of scarce resources. Such modification may be required by changes in the environment within which the entity operates or in response to directives from controlling bodies. In this respect, disclosure of information on the location, realisable value and current state of repair of the entity's assets would be relevant to users, as would disclosure of any restrictions that may have been imposed on the entity regarding its use of the assets.
- 36 Information about the solvency of the entity, that is, information about the availability of assets to meet financial commitments as they fall due, is relevant for making and evaluating decisions about the allocation of scarce resources. This information, such as disclosure of the liquidity of the entity's assets and the availability of cash from sources external to the entity, is useful in predicting the ability of the entity to meet its financial commitments as they fall due and, therefore, in predicting the ability of the entity to continue to provide goods and services in the future.
- 37 In the public sector, the ability of an entity to continue to provide goods and services in the future will, in addition to the dimensions

of financial position outlined in paragraph 32, be influenced by government policy objectives.

Financing and investing

- 38 Information about financing and investing, for example, disclosure of the sources and applications of funds during the reporting period, is relevant for making and evaluating decisions about the allocation of scarce resources. This information indicates the way in which the reporting entity has financed its operations and invested its resources during the reporting period. It is useful to users in confirming that resources have been used for the purposes intended and, as an input to assessing the solvency of the entity and analysing the change in the entity's financial position, it is useful in assessing the ability of the reporting entity to continue to provide goods and services in the future and in assessing whether the reporting entity is achieving its objectives.

Compliance

- 39 Information about compliance is relevant to making and evaluating decisions about the allocation of scarce resources because knowledge of non-compliance with externally-imposed requirements governing the reporting entity's operations may affect users' assessments of the reporting entity's performance, financial position, or financing and investing. For example, information about compliance with the following types of externally-imposed requirements may be relevant to users: conditions imposed by borrowing agreements, licencing agreements and grant arrangements; memorandum and articles of association and/or enabling legislation; spending mandates and borrowing limits; equal employment opportunity legislation; occupational health and safety legislation; environmental protection legislation; requirements to provide particular types or levels of service under a government grant programme or specific government directive; and requirements to observe specified tendering procedures for significant expenditures. Users should be able to presume that, in the absence of disclosures to the contrary, the reporting entity has complied with all externally-imposed requirements in respect of which non-compliance is relevant to assessments of the reporting entity's performance, financial position, or financing and investing. Information about compliance is relevant to users irrespective of the sector in which the reporting entity operates or whether the reporting entity is of a business or non-business nature.

- 40 The concept of compliance appropriate for general purpose financial reporting depends substantially on the types of information which are identified as being encompassed by general purpose financial reporting. If general purpose financial reports include non-financial information about an entity's performance, information about non-financial dimensions of compliance would be relevant to users. Because the boundaries of general purpose financial reporting will continue to evolve, the concept of compliance currently adopted in this Statement is consistent with the boundaries of general purpose financial reporting reflected in the current reporting practices of most reporting entities. Accordingly, the definition of compliance included in this Statement refers to adherence to externally-imposed requirements in respect of which non-compliance may have, or may have had, a financial effect on the reporting entity. As such, reporting about compliance as defined in paragraph 5 would entail disclosure of the nature and probable financial effect of any non-compliance by the reporting entity with externally-imposed requirements which has occurred and which is relevant to assessments of the reporting entity's performance, financial position, or financing and investing.

ACCOUNTING CONCEPTS

Discussion and Definitions

- 41 **The following concepts shall be interpreted in the context of paragraphs 1 to 40 of this Statement.**
- 42 **Paragraph 5 (definitions) shall be read as forming part of the accounting concepts set out in this Statement.**

Objective of General Purpose Financial Reporting

- 43 **General purpose financial reports shall provide information useful to users for making and evaluating decisions about the allocation of scarce resources.**

Accountability

- 44 **Managements and governing bodies shall present general purpose financial reports in a manner which assists in discharging their accountability.**

Information disclosures

- 45** **General purpose financial reports shall disclose information relevant to the assessment of performance, financial position, and financing and investing, including information about compliance.**