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Mr David Boymal
Chairman
Australian Accounting Standards Board
PO Box 204
COLLINS STREET WEST VIC 8007

16 October 2006
Our ref: DR:SC

Dear David

Re: Request for Comment on IASB Discussion Paper “Preliminary Views on an improved Conceptual Framework for Financial Reporting: *The Objective of Financial Reporting and Qualitative Characteristics of Decision-useful Financial Reporting Information*”

Deloitte Australia welcomes the opportunity to comment on the IASB Discussion Paper “Preliminary Views on an improved Conceptual Framework for Financial Reporting: *The Objective of Financial Reporting and Qualitative Characteristics of Decision-useful Financial Reporting Information*”.

Although we agree with many of the proposals in the Discussion Paper as they apply to for-profit entities in the private sector, we have a number of concerns which we have outlined below. As the other phases of this project progress, our views on these two chapters may continue to evolve.

The Objective of Financial Reporting

Stewardship

The financial reporting objective should indicate that producing information that is useful for assessing management stewardship is as important as producing information for decision-making. Stewardship is about assessing the use of the entity's resources in the past. An entity may have excellent financial prospects, but poor management, or vice versa. Subsuming stewardship within decision-usefulness in the framework could weaken the focus on past management of existing resources. We believe that in developing appropriate financial reporting requirements, the Boards ought to consider both decision usefulness (in terms of expectations about future cash flows) and stewardship (management of resources in the past).

Cash Flow Focus

Paragraph OB13 contends that providing information about the ability of an entity to generate net cash inflows should be the primary focus of financial reporting because such information helps satisfy the needs of investors and creditors. Present and potential investors and creditors view cash flow information as essential data for their decision-making. They also value other information not specifically tied to cash flows. For example, many noncash transactions such as asset write-downs and share-based payments lend insight into management stewardship and the impact of current economic factors on the entity's assets and liabilities. Other statistical information such as sensitivity or trend analyses might prove equally useful. For this reason, we consider that the focus of the conceptual framework should transcend providing information about an entity's ability to generate net cash inflows.

The Discussion Paper's focus on cash flows raises a question as to whether the Objective of Financial Reporting phase of the conceptual framework leads to an ultimate endorsement of fair value accounting. The Boards could address this concern by reminding readers that they have yet to deliberate the measurement phase of the conceptual framework project and that a focus on cash flows does not preordain a measurement outcome.

Qualitative Characteristics of Decision-Useful Financial Reporting Information

Verifiability

The Discussion Paper's discussion of verifiability does not indicate that direct verification is preferable, nor does it limit the use of indirect verification only to those situations for which direct verification is not available or the costs of direct verification exceed the related benefits. As noted in the Discussion Paper, indirect verification does not guarantee the appropriateness of the method used for measurement; for this reason it is a less preferable method. The Framework should explicitly express a bias for direct verification and indicate that indirect verification should be used only in limited circumstances.

We note that the project initially focuses on business entities in the private sector. The IASB and FASB have indicated once concepts for those entities are developed, they will consider the applicability of those concepts to financial reporting by other entities such as not-for-profit entities in the private sector and, in some jurisdictions, business entities in the public sector.

We do not consider that the proposed two chapters are appropriate for not for-profit entities in the private or public sector in their current form and additional 'Aus' paragraphs will be required in respect of these entities. Further comments in respect of not-for-profit entities and for-profit entities in the public sector are provided in Matters for Specific Comment.

Due to the later IASB submission deadline for the Discussion Paper, the global firm of Deloitte Touche Tohmatsu has not finalised its views in relation to the matters raised. Furthermore, in this letter we have highlighted issues and concerns in the Australian context that may not have the same degree of relevance internationally or which may not be considered of sufficient significance to warrant separate comment by the global firm of Deloitte in its submission. Therefore, the views presented in this document should be read in this context and may not necessarily represent the view of the global firm of Deloitte.

As noted above, our responses to the AASB specific questions raised in the Discussion Paper are outlined below.

If you have any questions concerning our comments, please contact Darryn Rundell on (03) 9208 7916.

Yours sincerely

A handwritten signature in black ink, appearing to read "Darryn Rundell". The signature is written in a cursive, flowing style.

Darryn Rundell
Partner

MATTERS FOR SPECIFIC COMMENT

Question 1 The IASB-FASB joint conceptual framework project has an initial focus on for-profit entities in the private sector. In relation to the topics of “objective” and “qualitative characteristics” covered by the Discussion Paper, what matters do you consider require attention if this revised Framework were also to be applied in Australia to not-for-profit entities in the private and public sectors and for-profit entities in the public sector?

Applying the proposed “Objective” to not-for-profit entities in the private sector.

We have the following comments regarding application of the proposed “Objective” to not-for-profit entities in the private sector:

- There is insufficient emphasis on stewardship. As discussed earlier in our submission, we consider that stewardship should be a separate objective for all entities. Stewardship is even more important for not-for-profit entities due to the pursuit of objectives other than profit. In addition, we consider that safeguarding assets is too narrow a view of stewardship for these entities as they are also accountable for the efficient and effective delivery of services.
- There is a need to broaden the identified users and establish an alternative primary user group. In the context of the not-for-profit sector, additional users would include present and future funders and supporters; and
- the pervasive cash flow focus adopted by the proposed framework is inappropriate for not-for-profit entities. We consider that users are often more interested in how well the organisation has met its non financial objectives.

Applying the proposed “Qualitative Characteristics” to not-for-profit entities in the private sector

In addition to the matters raised in respect of the Objective which may also be relevant to , Qualitative Characteristics we note that different cost-benefit assessments may be appropriate when considering not-for-profit entities because of their different objectives, different primary user group and because of the different incidence of benefits and costs.

Applying the “Objective” and “Qualitative Characteristics” to not-for-profit entities in the public sector.

Each of the significant issues raised above are also an issue in the context of public sector not-for-profit entities. In particular, we consider that stewardship is a key objective of financial reporting for public sector not-for-profit entities.

Public sector not-for-profit entities also have additional and sometimes different users. They include funders and financial supporters, including the public through the payment of taxes. They also have governing or oversight bodies that are likely to use information to assess the entity’s achievements against objectives including how efficiently and effectively goods and services have been provided.

In the case of public sector not-for-profit entities, both funders and financial supporters and oversight bodies should be encompassed within the primary user group.

In relation to the scope of financial reporting, budgets have a major significance for public sector not-for-profit entities and therefore the boundaries of financial reporting may be too narrow to meet the needs of users for these types of entities.

In addition, because the objective of these entities is not the making of a profit, information about the service performance of the entities is likely to be necessary to meet the needs of users.

Applying the “Objective” and “Qualitative Characteristics” to for-profit entities in the public sector

Subject to our comments in respect of for profit entities in the private sector we do not consider that there are any further matters which require attention in respect of for-profit entities in the public sector. We consider that they should apply the same requirements as the private sector.

Question 2: Are the proposals in the Discussion Paper in the best interests of the Australian economy?

We believe that the adoption of IFRS as converged Australian Standards will improve the ability of Australian entities to compete for funds in global capital markets. Accordingly, we believe that there must be no change made by the AASB to the IFRS Framework when issuing the AASB equivalent, other than any amendments applicable to not-for-profit and public-sector entities that are considered absolutely necessary.