

June 10, 2011

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Dear Ms Fox

**Phase I of the 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**

We would like to thank you for the opportunity to provide the International Public Sector Accounting Standards Board (IPSASB) with our comments on the Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities (hereinafter referred to as “the framework”).

The IDW recognizes that there is a distinct need for a conceptual framework for general purpose financial reporting by the public sector. We continue to believe that, as stated in our letter to you dated 31 March 2009, the discussion is of fundamental importance for the future development of International Public Sector Accounting Standards. As, in the meantime, the IPSASB has substantially completed its conversion project establishing public sector specific financial reporting standards based on those for the private sector as

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**page 2/6** to the comment letter to the IPSASB dated 10 June, 2011

promulgated by the IASB, it is opportune for the IPSASB to concentrate significant resources on bringing this important project forward.

We support the IPSASB's work in seeking to gain the views of its constituents in order to identify areas of difference between the public and private sectors. However, as developing a conceptual framework is not merely a matter of gaining information as to constituents' preferences, this exercise can only be seen as one part of the process of establishing this framework. In our opinion, a further essential step involves the alignment of ideas, where appropriate, between the IPSASB and the IASB, since deviations that are not founded on public sector specifics would only serve to "irritate" those users who deal with both sectors, including but not limited to those providing financial support such as financial institutions and suppliers. Indeed, the IDW has repeatedly encouraged the IASB to accelerate its own framework project in order to have a sound conceptual basis for private sector standard setting activities and would welcome further cooperation and coordination between the two boards in this context.

In view of this, we are concerned that the IPSASB's timetable may be overly optimistic, as it would essentially mean that the IPSASB would complete the project independently – and thus likely ahead – of the IASB's conceptual framework project. Whilst we accept that, in view of the fact that there are significant differences between the public and private sector which need to be addressed, the IPSASB is not intending this to be a further conversion project as such, we nevertheless believe that at a conceptual level there are likely to be significant areas of common ground between the two sectors. It would therefore be inappropriate for the two Boards to independently come to different conclusions on matters of common ground. We therefore strongly believe that a mere monitoring of the IASB's own project may be insufficient, and suggest the respective frameworks be aligned in this area, except in areas where there are compelling arguments to the contrary. Indeed, without alignment of the conceptual frameworks, we do not see how the IPSASB will be able to fulfil its strategy to continue maintaining the alignment of IPSAS with IFRS where appropriate for the public sector as it has stated.

Subject to the above, our responses to the issues raised for comment in the exposure draft are as follows:

page 3/6 to the comment letter to the IPSASB dated 10 June, 2011

*1. Role, authority and scope of the Conceptual Framework*

We broadly agree with the role, authority and scope of the framework. We appreciate the fact that the suggestion we made in our letter dated 31 March 2009 concerning the impact of the conceptual framework on existing IPSAS is reflected in BC 1.2. However, we suggest this issue be included in paragraph 1.2 of the framework itself, since it clarifies the authority of the framework in the direct context of current standards already set by the IPSASB, which is not clear from the first sentence of that paragraph. We therefore suggest a sentence be added following the first sentence of paragraph 1.2 to read: "If an IPSAS currently in effect conflicts with the Conceptual Framework, the IPSASB should review that IPSAS and, applying the due process for standard setting, revise it."

*2. Objectives of financial reporting by public sector entities and the primary users of GPFRs (General Purpose Financial Reports) of public sector entities and their information needs*

Objectives:

We agree with the proposed objectives: "to provide information about the entity that is useful to users of GPFRs for accountability and decision-making purposes". We also believe that the subsequent discussion of the various users and their potential decisions in paragraphs 2.3- 2.6 is appropriate for the public sector and highlights differences to the private sector.

Primary users and their information needs:

We also agree that a wide definition of primary users is appropriate in a public sector context. However, as we noted in our previous letter, their information needs are likely to be diverse. This is one area in which there is likely to be significant common ground with the private sector, for example, those providing external funding such as banks but also suppliers will have very similar, if not identical information needs in this capacity, which, in turn, means that qualitative characteristics such as the relevance of information may be equally important to them; the same is likely to apply to certain other users.

However, because of the wide range of different users in the public sector, in our view, it remains questionable as to whether it is really possible to identify and respond to common needs in GPFRs. The IPSASB recognizes this point such that the discussion included in paragraph 2.14 et seq. highlights one essential difference in information needs from the private sector. However, our concern is whether all such reports would truly be "general purpose" or whether

page 4/6 to the comment letter to the IPSASB dated 10 June, 2011

certain reports may simply respond to the information needs of specific users or classes of users, rather than really common information needs applicable to all users. This is an aspect that will require further exploration on a case by case basis, as GPFRs evolve beyond GPFs (General Purpose Financial Statements), and which ought to be discussed in the framework.

In this context, we had also previously commented that in developing GPFRs care will need to be taken to ensure that the Board deals with financial information and narrative information related thereto, but not non-financial information, which ought to be subject to separate reporting. This issue is particularly important in considering projects such as service reporting where the IPSASB will need to establish clear delineation.

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

*In particular, whether:*

(a) *“Faithful representation” rather than “reliability” should be used in the Conceptual Framework to describe the qualitative characteristic that is satisfied when the depiction of an economic or other phenomenon is complete, neutral, and free from material error; and*

(b) *Materiality should be classified as a constraint on information that is included in GPFRs or as an entity-specific component of relevance;*

In our view, the qualitative characteristics of public sector financial information identified at a conceptual framework level are unlikely to differ from that applicable to the private sector. However, their application and interaction with one another may differ in some respects.

*In response to a)*

Since the Consultation Paper on Phase I of the project was issued, a number of jurisdictions within Europe have experienced and are continuing to experience problems related to their sovereign debt and individual credit ratings. Such occurrences have re-emphasized how essential it is that reliable financial information be produced by public sector entities.

Against this background, and whilst we recognize that the IASB has chosen to substitute *reliability* with *faithful representation* in establishing fundamental qualitative characteristics, we still do not fully support this change. We continue

page 5/6 to the comment letter to the IPSASB dated 10 June, 2011

to believe that information must, in the first place, be sufficiently reliable for it to be useful, and that faithful representation follows on from there, rather than the other way round. In the above-mentioned letter dated 31 March 2009, we had previously mentioned the IDW Concept Paper “Additional Issues in Relation to a Conceptual Framework for Financial Reporting” of September 17, 2007<sup>1</sup>, which drew upon the IASB’s conceptual framework proposals of the time. We would like to mention this Paper again, as it not only deals with the context in which we had first drawn your attention to this paper, but also suggests that reliability is still needed as a separate concept, and further suggests that those responsible for the preparation of financial statements should support the information therein with appropriate accounting evidence derived from reliable accounting processes and document that evidence to achieve truly reliable financial information. On the basis of this paper, we would also like to suggest that the quality of a public sector entity’s processes, controls and documentation should be addressed within the IPSASB’s Conceptual Framework somewhere both to ensure reliability and also because the ability to obtain such accounting evidence is also a factor that needs to be taken into account by the IPSASB when considering new GPFR requirements. In addition, a recent report by PwC in the UK<sup>2</sup> highlights the pressures facing financial reporting within the public sector, which are also factors which the IPSASB will need to bear in mind when setting robust standards capable of consistent application.

*In response to b)*

We agree with this approach. In particular, as the recent Discussion Paper “The Evolving Nature of Financial Reporting: Disclosure and Its Audit Implications” by the IAASB indicates, recent trends for increasingly copious notes to the financial statements have resulted in a lack of understandability of GPFS, in part because there is often a tendency in practice on the part of preparers to include disclosures even though they may not be material.

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.*

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<sup>1</sup> <http://www.idw.de/idw/portal/d423366/index.jsp>

<sup>2</sup> [http://download.pwc.com/ie/pubs/2011\\_cutting\\_costs\\_and\\_cutting\\_fraud.pdf](http://download.pwc.com/ie/pubs/2011_cutting_costs_and_cutting_fraud.pdf)

page 6/6 to the comment letter to the IPSASB dated 10 June, 2011

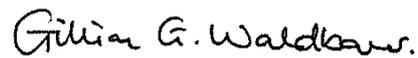
The basis discussed appears appropriate in a public sector context and it essentially follows the same principle as established in IAS 10, which was issued recently. We have no additional comments on this issue.

We hope our comments will be useful to the IPSASB in drafting this phase of the framework. We would be pleased to answer any questions that you may have or discuss any aspect of this letter.

Yours sincerely



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Chief Executive Officer



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