



Accounting Standards Board

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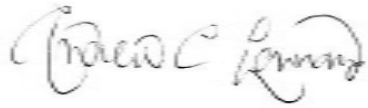
Dear Stephenie

Re: 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.*
1. The Accounting Standards Board (ASB) welcomes the opportunity to respond to the above Exposure Draft (ED).
 2. We consider that it would be unfortunate if the Conceptual Framework for public sector entities were to diverge markedly from that used in the private sector. We therefore emphasise the importance of the IPSASB and the IASB continuing to work closely together to minimise any differences between their projects on this subject, and to ensure that any significant differences are limited to issues where the differences are required by the different economic circumstances that prevail in each sector.
 3. Whilst we agree with many of the proposals in the ED, there are some we have concerns, namely:
 - Some aspects of the Scope;
 - The current description of 'faithful representation'; and
 - Materiality is entity-specific and should not be considered a constraint on information.
 4. Each of these issues and some other comments are expanded upon in the Appendix which addresses the Specific Matters for Comment.

5. If you require any further information please contact me or Joanna Spencer (j.spencer@frc-asb.org.uk or telephone +44 (0) 20 7492 2428).

Yours sincerely

A handwritten signature in black ink that reads "Andrew Lennard". The signature is written in a cursive style with a large initial 'A'.

Andrew Lennard

Director of Research

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Specific Matters for Comment

SMC 1

Role of the Conceptual Framework

We agree that the role of the Conceptual Framework (CF) is to establish the concepts that underpin general purpose financial reports (GPFs) by public sector entities applying accrual accounting.

Authority of the Conceptual Framework

We agree that the CF should not establish authoritative requirements for the preparation of public sector GPFs, but rather be used as guidance for issues not dealt with specifically by IPSASs.

Scope of the Conceptual Framework

Whilst we agree that the scope of the CF could include all financial reporting, in our view this may in reality prove to be difficult.

Scope of financial reporting

We are concerned that although the ED states that the scope of financial reporting establishes the boundary around what should be reported in the GPFs, the proposals do not actually articulate what this boundary should be. Therefore, the scope appears to be open-ended and consequently too wide. Paragraph BC1.5 of the Basis for Conclusions, for example, clarifies what may be included in GPFs and therefore could be elevated to be included in the main text as this may assist in understanding the intended scope. Further clarity could be obtained by including the helpful diagram 'Figure 1: Information needs of users' that was given in paragraph 1.14 of the 2008 Consultation Paper.

We note that phases 2 and 3 of the CF project have focused on financial statements rather than financial reporting as a whole; it would also be important to establish clear boundaries for financial statements.

Scope of information

We agree that it is important that the scope includes both past and forward-looking information but these should be based on the same qualitative characteristics.

Process for determining the scope

We are also concerned that the ED states that the scope will be determined by the objectives of financial reporting and the needs of users. However, neither of these

issues were discussed prior to the scope being determined. In order to determine what should be included in the GPFR, surely it is necessary to determine first what the objectives of the GPFR are. In redeliberating the CF, only once the objectives have been determined, should the scope of the CF be revisited.

SMC 2

Objectives

We agree that the objectives of financial reporting for public sector entities should be to provide information which will assist in fulfilling accountability and be useful for decision-making purposes.

However, we are of the view that not all information can fulfil both objectives equally well and that some information may be weighted more heavily towards one objective than the other e.g. accountability may be a more important objective for past events. Whilst decision usefulness may be more relevant for prospective information this is not to imply that the two objectives are mutually exclusive but the weighting of each objective may be dependent on the type of information provided. It is important to determine which objective is principally being addressed by different parts of financial reporting.

Users

We agree that the users of GPFRs are service recipients and resource providers and therefore citizens should be considered to be primary users. Whilst it would obviously never be possible to produce GPFRs that every citizen could easily understand, we agree that citizens are informed by their representatives and others such as the media and therefore GPFRs should be produced to address these needs.

SMC 3

Relevance

We agree that any information provided in GPFRs must be relevant in achieving the objectives of accountability and/or decision making. We further agree that such information must also have either a confirmatory and/or predictive value.

Faithful Representation

Reliability and faithful representation

We do not consider that the terms 'reliability' and 'faithful representation' are interchangeable as they embody different concepts. Both should be identified as qualitative characteristics.

We support the principle of reliability, which is presently defined as “free from material error and bias, and can be depended on by users to represent faithfully that which it purports to represent or could reasonably be expected to represent” (see BC3.10).

In our view, faithful representation does not adequately focus on information representing what it purports to represent. Although the idea of ‘what it purports to represent’ appears in the first sentence of paragraph 3.10, it is not developed or discussed further, but is followed by a statement that appears to define faithful representation. There appears to be a risk that the concept of ‘purports to represent’ is lost by reading the definitional sentence in isolation.

This can suggest that there is only one ‘representationally faithful’ representation of an asset or liability which is its fair value. We would disagree with this view especially where it is used to justify a ‘mark to model’ technique which often does not result in a useful number. In our view, it is inevitable that accounting can often only report a selected attribute of an asset or liability. For example, it may be representationally faithful for an asset to be stated at historical cost, which is a complete statement of its acquisition cost. This would not reflect other aspects of the asset, such as its fair value, but would reflect all that a historical measure purports to represent.

The use of the term ‘economic phenomenon’ may be unhelpful as it can imply that there is only one true answer for any economic phenomenon, which we consider to be incorrect. For example, if there is an accounting policy choice available over the capitalisation of borrowing costs there will be two answers for one economic phenomenon – one which includes those costs in the carrying amount of the asset and one that does not. In many cases the economic phenomenon will be a transaction; it might be preferable to make this clear, by referring to a ‘transaction or other economic event’.

Summary

In summary we suggest the *Framework* should include use of both reliability and faithful representation as qualitative characteristics provided that the discussion of faithful representation adequately encompasses ‘what it purports to represent’, and the use of ‘economic phenomenon’ is reconsidered

Understandability

We agree that understandability is a qualitative characteristic that information should possess.

Timeliness

We agree that timeliness is a qualitative characteristic that information should possess.

Comparability

We agree that comparability is a qualitative characteristic that information should possess.

Verifiability

Although we have no specific concerns with the use of the term 'verifiability' we note that it is a difficult concept to use in relation to prospective information. Therefore we suggest that a term such as 'supportability' be used instead as it is wider in concept and can be applied to both past and forward-looking information.

Materiality

We do not agree that materiality should be classified as a constraint on information or that standard-setters should be making the determination as to what is and is not considered material.

Materiality is an entity-specific component of relevance, because what is material to one entity may not be material to another, therefore it is for the preparers of GPFs to make this determination. We agree with the IASB that a CF cannot specify a uniform quantitative threshold for materiality or predetermine what could be material in a particular situation.

SMC 4

The Reporting Entity and the Group Reporting Entity

We agree that a key characteristic of a reporting entity is the existence of users by which we mean that there is a legitimate demand for the information that the GPFs would provide. In determining whether individual GPFs should be produced this must of course be tempered by a consideration of the costs and benefits of involved.

To achieve the objective of accountability to citizens it follows that all entities that raise or consume resources are reporting entities and we agree that in practice

legislation, regulation or another authority will identify which entities will be required to prepare GPFRs. However, we note that paragraph 4.4 suggests that GPFRs might be prepared for individual activities. We question this; in our view a reporting entity should be a cohesive economic unit (see ASB 'Statement of Principles for Financial Reporting' paragraph 2.3). Where information is required about, say individual activities, users' needs are more likely to be met by special purpose reports that do not contain all the components required for GPFRs.

Regarding group reporting entities, we consider that the proposed text is not as articulate as it could be. The CF would benefit from having a definite statement about when a group exists, for example by stating that a group reporting entity will exist where one entity has the authority and capacity to direct the activities of another entity. As noted before, we found that some of the text in the Basis to be more helpful than the actual CF text (e.g. paragraphs BC4.11 and BC4.14 are particularly helpful).