



Accounting Standards Board

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The Technical Director  
International Public Sector Accounting Standards Board  
International Federation of Accountants  
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Per e-mail

31 July 2012

Dear Stephenie,

**COMMENT ON THE EXPOSURE DRAFT ON FINANCIAL STATEMENT DISCUSSION AND ANALYSIS**

We welcome the opportunity to comment on the Exposure Draft of *Financial Statement Discussion and Analysis*.

Our comment to you is set out in three parts: Part I outlines comment to the specific matters for comment, Part II outlines general comment on the Exposure Draft and Part III outlines editorial and other minor comment.

Overall, we are supportive of the proposal to develop a framework for the preparation and presentation of financial statement discussion and analysis. We believe that this would result in consistent, comparable and useful information being provided to users for accountability and decision-making purposes. We do, however, have reservations about the type of pronouncement that the IPSASB intends to issue on financial statement discussion and analysis, ie an IPSAS, as explained in our response to specific matter for comment no 1.

The comment in the Exposure Draft is that of the Secretariat and not the Accounting Standards Board (Board). In formulating the comment on the Exposure Draft, the Secretariat consulted with a range of stakeholders including auditors, preparers, consultants, professional bodies and other interested parties.

Board Members: Ms T Coetzer, Mr B Colyvas, Mr V Jack (Chairperson), Ms CJ Kujenga, Mr K Kumar,  
Mr T Makwetu, Mr F Nomvalo, Mr G Paul, Ms N Ranchod, Ms R Rasikhinya  
Chief Executive Officer: Ms E Swart



Please feel free to contact me should you have any queries relating to this letter.

Yours sincerely,

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

**Erna Swart**

**CEO: Public Sector Accounting Standards Board**

## **PART I – SPECIFIC MATTERS FOR COMMENT GENERAL COMMENTS**

### **Specific Matter for Comment 1**

*Do you agree that the material presented in this Exposure Draft should be developed as an IPSAS, with the same level of authority as the accrual based IPSAS, which applies to all entities that prepare financial statements in accordance with IPSASs?*

We note the IPSASB's view in BC 11 that introducing a new type of pronouncement that has equivalent authoritative status to the IPSASs will be confusing to its constituents, and that an IPSAS is therefore the most appropriate type of pronouncement to apply to financial statement discussion and analysis. If the pronouncement is issued as an IPSAS, we have the following concerns:

- Users may consider the financial statement discussion and analysis to be part of the financial statements while the Exposure Draft's explicitly states otherwise, ie that it is not part of the financial statements but merely an explanation of the financial statements. What confuses the issue is the statement that financial statement discussion and analysis is not seen as stand-alone (see BC 3).
- Uncertainty will also exist around whether the information presented in the financial statement discussion and analysis have been subjected to the same audit requirements compared to the information presented in the financial statements.
- If an authoritative IPSAS is issued while specifically excluding it from the financial statements, it could create an unintended conflict in that, on the one hand, the financial statements would be expected to achieve fair presentation on their own, while on the other hand it would imply that management commentary outside the financial statements is necessary to achieve fair presentation. There are thus two issues of concern (a) achieving fair presentation; and (b) compliance with all IPSASs. It would be difficult to prove (b) when the opening paragraph of the pronouncement requires an entity to prepare financial statement discussion and analysis if you prepare financial statements in accordance with IPSASs.

We therefore propose that the proposed Exposure Draft should be issued as part of a new suite of pronouncements that are not part of the financial statement reporting framework. This will allow entities to make an explicit and unreserved statement of compliance with IPSASs, which is limited to the financial statements only.

Because the IPSASB may issue additional mandatory requirements for reports outside the General Purpose Financial Statements, the IPSASB can address this issue holistically rather than making ad-hoc changes to, for example, IPSAS 1.

If the proposed Exposure Draft is issued as part of a new suite of pronouncements, entities not applying an accrual basis of accounting may also consider and/or adopt the pronouncement. The IPSASB may also consider not to limited the scope of the pronouncement to entities applying the accrual basis of accounting.

As an alternative, the IPSASB could also consider expanding the disclosure requirements in existing IPSASs to cover the minimum required information as set out in paragraph .15 of this Exposure Draft. Amending the disclosure requirements in existing IPSASs to include

issues identified during the financial statement discussion and analysis will provide users with useful and reliable information rather than to establish reliance on information that is presented outside the financial statements. If the IPSASB supports this alternative proposal, we propose that the disclosure requirements to be included in existing IPSASs should be more prescriptive compared to what is currently required and prescribed in the Exposure Draft.

### **Specific Matter for Comment 2**

*Do you agree that IPSAS 1 should be amended to clearly indicate that financial statement discussion and analysis is not a component of the financial statements?*

Based on our response to specific matter for comment 1 where we propose that the Exposure Draft should be issued as part of a new suite of pronouncement, IPSAS 1 would not need to be amended to indicate that financial statement discussion and analysis is not a component of the financial statements. If financial statement discussion and analysis forms part of General Purpose Financial Reporting (GPFR) entities should be required to include two distinct statements of compliance with IPSASs and other pronouncements – one for the financial statements and one for other information presented outside the financial statements.

If the IPSASB considers the alternative view expressed in specific matter for comment 1 where the disclosure requirements in existing IPSASs will be expanded to require the minimum required information as set out in paragraph .15 of this Exposure Draft, such a statement will also not be necessary as the required information will be included as presented as part of the financial statements.

### **Specific Matter for Comment 3**

*Is the scope of financial statement discussion and analysis clearly defined so as to distinguish it from other issues being addressed by the IPSASB (e.g., financial statements, service performance reporting, reporting on the long-term sustainability of public finances)?*

We agree that the scope of financial statement discussion and analysis is clearly defined to distinguish it from other issues being addressed by the IPSASB, but we propose that the paragraph should be expanded to clarify that the financial statement discussion and analysis should be separately identified to ensure that it is distinguished from any other information.

We are, however, of the view that certain areas relating to the scope isn't clearly dealt with in the body of the text. For example, the scope relates to information about the annual financial statements, but the proposed pronouncement requires information about strategies and risks, which doesn't really relate to the annual financial statements.

We also believe that in future, the scope of this report should be expanded to deal with other issues, so that one report is prepared to cover all issues, i.e. performance information, sustainability and financial issues.

The inclusion of an example in paragraph .03 (ie service performance information) will also be useful in understanding what "other information included in public documents issued in conjunction with the financial statements" entails.

#### **Specific Matter for Comment 4**

*Is the required content for financial statement discussion and analysis appropriate?*

Yes, the content appears to be appropriate and provides sufficient guidance.

We do however propose that specific additional criteria should be included for each of the disclosure sections, particularly if the intention is for this Exposure Draft to become an authoritative Standard. The lack of specific disclosure criteria would make it difficult for preparers and auditors to verify compliance with the standard in practice.

We further propose that the term “may” should be amended to “should” in paragraphs .16 to .32 (where appropriate), as the information required in these sections should prescribe the minimum requirements for the content and presentation of financial statement discussion and analysis, as required in paragraph .15.

We also have some suggestions on specific content paragraphs. These proposals are set out in Part II of our comment letter (see general comment 4 to 14).

#### **Specific Matter for Comment 5**

*Do you agree with the transitional provisions and effective date?*

Yes, the transitional provisions appear to be appropriate.

#### **Specific Matter for Comment 6**

*Is the Implementation Guidance useful to understanding the requirements of the proposed IPSAS?*

Yes, we found the implementation guidance to be useful to understanding the requirements of the proposed IPSAS.

We do have some suggestions on certain paragraphs included in the implementation guidance. These proposals are set out in Part II of our comment letter (see general comment 16 to 18).

#### **Specific Matter for Comment 7**

*Is the Illustrative Example a useful way of illustrating the requirements of the proposed IPSAS?*

Yes, the illustrative example is useful in illustrating the requirements of the proposed IPSAS. However, as financial statement discussion and analysis should be prepared for the same reporting entity that prepares and presents financial statements, it may be more useful to include examples of different levels of reporting entities as it will be more representative of reporting entities. The current illustrative example seems to be aimed at a central government or at a whole-of-government reporting entity.

## **PART II – GENERAL COMMENT**

### **Definition of financial statement discussion and analysis**

1. We are of the view that the term “significant” in the definition of financial statement discussion and analysis should be deleted in the proposed definition since IPSASs apply to items, transactions and events that are significant. It is therefore not necessary to include a specific reference to “significant” in the definition.
2. We also propose that the definition should require management’s view on significant risks and uncertainties.

(Refer to the amendment proposed in comment 6 below)

### **Compliance with IPSAS**

3. Paragraph .13 requires an entity whose financial statement discussion and analysis complies with the proposed IPSAS to make an explicit and unreserved statement of such compliance. A similar requirement is included in IPSAS 1.28 where an entity, whose financial statements comply with IPSAS, is required to make an explicit and unreserved statement of such compliance in the notes.

Because the financial statement discussion and analysis will not form part of the financial statements, entities will be required to include two compliance statements – one for the financial statements that comply with IPSASs, and another for the financial statement discussion and analysis as required by paragraph .13. This requirement could be explained in the Exposure Draft. However, with reference to our response to specific matter for comment 1, such statements may be confusing to users in understanding what is included and what is excluded from the financial statements, and in understanding what information have been subjected to the audit requirements.

### **Minimum required content**

4. Paragraph .15 and paragraphs .18 to .32, list the minimum requirements for the content and presentation of financial statement discussion and analysis. We propose that a statement should be made that even though the information required in paragraph .15 and .18 to .32 are the minimum requirements to be included in financial statement discussion and analysis, entities are encouraged to provide additional information if it will provide useful information to users for accountability and decision-making purposes.
5. The disclosure guidance included in paragraph .16 appears to imply that the requirements of the proposed IPSAS are not satisfactory, and that additional information is required to ensure fair presentation. The requirements in paragraph .16 could be seen as contradicting the requirements in existing IPSASs as the information required in other IPSASs should already be sufficient to ensure fair presentation.

### *Overview of the entity*

6. Paragraph .18(a) and (b) requires information about an entity’s vision, mission and governance (eg legislative or regulatory structure, management structure). During the

consultation on the Exposure Draft, stakeholders questioned how the disclosure information required under paragraph 18(a) and (b) links to the definition of financial statement discussion and analysis, as information about an entity's vision, mission and its governance will not necessarily be presented in its financial statements.

We therefore propose that the definition for financial statement discussion and analysis be amended as follows (taking into account the comment in 1 and 2 above):

Financial statement discussion and analysis is an explanation of the ~~significant~~ items, transactions, and events presented in an entity's financial statements, the environment in which it operates and significant risks, uncertainties, trends and factors that influenced them.

#### *Information about the entity's objectives and strategies*

7. Paragraph .19 provides guidance on the required disclosure relating to the entity's objectives and strategies. This paragraph can also be interpreted broadly and could result in overlapping requirements with, for example, service performance information, as the paragraph requires an explanation on how the achievement of the entity's financial objectives will be measured.

We therefore propose that this potential overlap between information required for financial statement discussion and analysis and other information that are presented in reports that are outside the financial statements, should be further explained.

#### *Analysis of the entity's financial statements*

8. We propose that paragraph .23 should be expanded to include examples of circumstances where comparative information should be included in financial statement discussion and analysis.
9. We propose that "prospective role" in paragraph .24 should be deleted as it is not clear from the discussion that follows what is meant by a prospective role.
10. We propose that paragraph .25 be expanded to state clearly that sufficient information should be presented about an entity's financial statements to allow users to make their own forecasts and projections. The information presented in financial statement discussion and analysis should have a predictive value to allow users to develop their own forward-looking projections, rather than management making such assessments.
11. Paragraph .26 requires an entity to disclose the variance between actual and budget as part of the financial statement discussion and analysis to the extent that the information is not included in the financial statements. This requirement will, however, contradict the exemption provided in IPSAS 24 as paragraph .26 does not seem to consider the impact on entities whose budgets are not made publically available. If the requirement in paragraph .25 is retained, it would mean that entities would now have to disclose a comparison between actual and budget information to ensure compliance with the requirements of this paragraph, irrespective of the exemption allowed in IPSAS 24.

It is therefore proposed that the requirement in paragraph .26(a) be amended to require the disclosure of such information in financial statement discussion and analysis to the extent that the exemption in IPSAS 24 is not applicable.

#### *Risks and uncertainties*

12. Paragraph .27 requires information about an entity's risks and uncertainties in assisting users to evaluate the impact of such risks in the current period and on expected outcomes. Information about an entity's risks and uncertainties will not necessarily be included or presented in the financial statements, but information on how the entity *manages* such risks and uncertainties may well be, for example the information required on risks related to financial instruments.

We therefore recommend that the paragraph be amended to require presentation of information on how the entity manages its risks and uncertainties.

13. Paragraph .29 states that a discussion of how the entity manages its risks will help users obtain a complete picture of the entity's exposure to risks that directly affect financial statement items and disclosure. We are of the view that such a discussion will not necessarily provide a *complete* picture of the entity's exposure to risks, as other factors may also be relevant that will not necessarily be included in the financial statement discussion and analysis.

We therefore propose that the word "complete" be deleted from the statement.

14. We propose that paragraph .29 should highlight specific risk areas that could be considered to avoid requiring disclosure of sensitive or political risks.

#### **Basis for Conclusions**

##### ***Audit of financial statement discussion and analysis***

15. We are of the view that the conclusion reached in BC 10 could lead to the situation where financial statement discussion and analysis will not carry any significance because it is not subjected to audit. If financial statement discussion and analysis is to be issued as an IPSAS, information presented should be subjected to an audit. As the information to be used in preparing financial statement discussion and analysis must be based on currently known facts and verifiable assumptions, the reason not to subject it to an audit out of concern for a qualified opinion, is confusing.

#### **Implementation Guidance**

##### **Section A**

16. Some stakeholders were of the view that paragraph .09 of the Exposure Draft could be expanded with the information included in section A. We therefore propose that information that is relevant in understanding how the qualitative characteristics apply to financial statement discussion and analysis be included in the text of the Exposure Draft, rather than in an annexure.
17. The explanations included in paragraph A.IG 5 and A.IG 6 seems to be contradictory. IPSAS applies only to material items, and it is therefore viewed that 'relevant' information will always be 'material' due to the possible impact on decisions. The need to only include material information in financial statement discussion and

analysis is dealt with in A. IG 6, but in contrast, A. IG 5 states that “financial statement discussion and analysis may not include some matters that are material to the components of the financial statements set out in IPSAS 1, or it may include some matters that are not material to the financial statements”.

A.IG 5 should be reconsidered to avoid any contradiction.

## **Section B**

18. We are of the view that information about the economic, efficient and effective use of resources are beyond the proposed scope of this Exposure Draft. We propose that consideration be given to the information required about an entity’s financial performance as illustrated in B.IG14.

The requirement to provide information about whether the entity has acquired resources economically and used them efficiently and effectively to achieve its service delivery objectives, in our view, contradicts the requirement in paragraph .03 of the Exposure Draft which states that the Standard applies only to financial statement discussion and analysis and not to other information included in public documents that are issued in conjunction with the financial statements, ie service performance information. The information required in B IG14 will not necessarily be available in the statement of financial performance.

### PART III – EDITORIAL AND OTHER MINOR COMMENTS

The following editorial and other minor comments are proposed:

<b>Paragraph</b>	<b>Comment</b>
Paragraph .29 first sentence	Amend “entity’s” to “entity”. “A discussion of how the entity’s manages its risks ....”
Heading to paragraphs .33 and .34 “Transition” vs the heading “Transitional provisions” in the Basis for Conclusions	The reference to the transitional provisions should be consistent.