

Private/Confidential

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International Federation of Accountants
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27 July 2012

Exposure Draft 47 Financial Statement Discussion and Analysis

Dear Ms Fox,

The global organization of Ernst & Young is pleased to comment on the above Exposure Draft (ED).

General comments:

We commend the efforts of the International Public Sector Accounting Standards Board (IPSASB) in developing guidance for the preparation of Financial Statement Discussion & Analysis (FSD&A) by public sector entities. We believe such guidance would be useful to preparers, as it sets out guidance on the structure, content and how information should be presented in the FSD&A, and also improve the quality of narrative reporting by public sector entities. We also believe that such guidance would be helpful to users in comparing information presented by public sector entities.

We observe concerns in some jurisdictions regarding the proposed requirement of mandating these disclosures and the potential conflict between these requirements and existing requirements in particular jurisdictions where similar requirements exist. It would be helpful if there is further consideration and more guidance issued by the Board as to how the proposed guidance could be applied alongside existing requirements. As for countries without such disclosure guidance in their reporting framework, we see the proposed guidance as filling the gap for such countries in this area.

In addition, we believe that more work needs to be done in order for the future IPSAS to be operational. Specifically, the scope of the guidance and linkage with other IPSAS requirements need to be refined regarding overlapping requirements with other IPSASs. Therefore we are unsure whether it is currently appropriate that the proposed guidance should be developed as

an IPSAS. We suggest that the Board consider this project together with the proposals in the Service Performance Reporting project and the Conceptual Framework Phase 4: Presentation and Disclosure project, before making final decisions on the requirements for FSD&A to ensure that these components of the general purpose financial report (GPFR) fit together cohesively.

More considerations should also be given to the implication of issuing this as an IPSAS from an audit perspective. We are concerned that issuing this ED as an authoritative standard while specifically excluding it from the financial statements may create an unintended conflict as the financial statements would be expected to achieve fair presentation on their own, but it would also imply that the FSD&A disclosed outside of the financial statements is necessary to achieve fair presentation. In our view, the disclosures in the FSD&A should be a standalone document that complements the financial statements. If the IPSASB believes that there are deficiencies within the disclosure requirements in existing standards, the existing standards need to be amended rather than establishing reliance on information presented outside of the financial statements.

Specific matters for comments and other comments

Our views on the specific matters for comments on which the IPSASB is seeking answers are set out in Appendix A of this letter. In addition, we have included other unsolicited comments following Appendix A.

Please contact Mr. Thomas Müller-Marqués Berger, Global Leader for International Public Sector Accounting, at +49 711 9881 15844 or thomas.mueller-marques.berger@de.ey.com should you have any questions on the letter.

Appendix A

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 IPSASs, which applies to all entities that prepare financial statements in accordance with IPSASs?

Although we believe that the FSD&A provides information that would facilitate sound and well-informed decision making that leads to an efficient resource allocation, and brings together the material information about a public sector entity's performance in a way that reflects the social and environmental context within which it operates, we currently have concerns as mentioned previously in the general comments section whether it should be developed as an IPSAS.

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?

We agree that the FSD&A should not be a component of the financial statements and it should be stated clearly within IPSAS 1 that the FSD&A is not a component of the financial statements.

In addition, IPSAS 1 should also highlight that separate compliance statements be made:

- 1) for the compliance of recognition, measurement and disclosure of IPSAS standards;
and
- 2) for the compliance of information presented in accordance with other IPSAS guidance (such as FSD&A, long term fiscal sustainability and service performance information).

In the context of paragraph 15-21 of the ED, we do not agree that the FSD&A should disallow duplicate information to be presented. Preparers should be able to make judgment on which piece of relevant information to be replicated in the FSD&A with relevant cross-references made back to the financial statements when necessary. We believe that the FSD&A guidance should be principles-based, and allow preparers to select information that would be relevant to users. Also, this prohibition could potentially be misleading and confusing to preparers who would be forced to provide information that is essentially already disclosed in the financial statements but expressed in a different manner.

We also recommend that a statement similar to a disclaimer should be disclosed in the FSD&A itself; that it should be read in conjunction with the full financial statements, and that FSDA itself is not able to provide a full picture of the financial situation of an entity.

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)?

The scope paragraph in the ED currently does not distinguish FSD&A explicitly from other reporting requirements being addressed by the IPSASB including service performance reporting and long-term sustainability of public finances.

We recommend that the scoping paragraphs discuss how the requirements for FSD&A interact with service performance reporting and long-term sustainability reporting (and vice versa). Besides clarifying the scope, it would be useful to define the objective of this guidance in consideration of the other reporting issues, and with reference to phase 4 of the conceptual framework project, and how the objectives of presentation and disclosures are achieved through the requirements of this ED.

We also find the scope and linkage of the proposed guidance to the rest of the financial report to be unclear. Firstly, we are unsure whether it is limited to financial information or also covers non-financial information such as service performance reporting. Secondly, the relationship of FSD&A with financial statements needs to be clarified. The ED states that the FSD&A is not part of the financial statements (and amends IPSAS 1 to distinguish it), but creating a physical separation does not help explain the relationship between the two sets of information, given that there is overlap between the information that would be required in FSD&A and information (e.g. notes to the financial statements) that is already required under other IPSASs.

Specific Matter for Comment 4:

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

The following are our suggestions and comments on how the content for FSD&A should be improved:

1. Paragraph 15 should be expanded (possibly in the implementation guidance section) to include more specific guidance on what is required for each criterion.
2. In the context of paragraph 18, we suggest that paragraph 18 (c) explicitly refer to the financial dependencies and relationships that an entity has and recommend the following amendment: "... entity's relationships with other entities, in particular, relationships of financial relevance (e.g. funding arrangements)". Some public sector entities have relationships in many ways to a lot of entities but we believe there should be an emphasis on financial support.

3. It is unclear what type of information is required, whether the information disclosed under paragraph 18 should relate only to historical information or should also incorporate future information. In particular, paragraph 18(d) refers to trends, events and developments which 'have or could have' a material impact on the entity's financial position and financial performance. Given that the FSD&A is supposed to relate to historical financial statements, the requirements described in this paragraph seem to indicate that future trends be analyzed and discussed. If the IPSASB had intended it to relate only to past information, we believe the paragraph should be in the past tense, i.e. using 'had' instead of 'have or could have'.
4. Paragraph 19 is unclear as to whether financial or non-financial objectives and/or strategies such as service performance objectives and strategies should be discussed. The second sentence of paragraph 19 specifically refers to 'financial objective', but the first does not, which raises the following issues:
 - a. If the requirement only relates to financial objectives, this needs to be clarified
 - b. If the requirements do not cover non-financial objectives/strategies, in particular, service performance objectives/strategies, it is likely that providing information about the entity's objectives and strategies will be significantly incomplete for many entities. However, it might be difficult for the IPSASB to include requirements on non-financial information for FSD&A at this stage, until the Board has completed the service performance reporting project.
5. Paragraphs 24 and 25 are unclear as to what is or is not required in future-oriented information. On one hand, paragraph 24 states that it is not required, on the other hand, paragraph 25 seems to suggest that it is.
6. Paragraph 26(b): Here it needs to be considered that in the case of first-time adoption of accrual basis IPSASs, entities are not required to present comparative information (as tentatively decided by the IPSASB in June 2012). As paragraph 26(b) is currently phrased, an entity electing not to present comparative information in its first IPSAS financial statements would be required to present such information. Therefore, paragraph 34 should provide a reference to paragraph 26(b).
7. Also, paragraph 26 does not take into consideration the impact on entities that do not publish their budget publicly and are exempted from IPSAS 24 *Presentation of Budget Information in Financial Statements*. A reference to IPSAS 24 should also be provided in paragraph 26a.
8. Paragraph 28: It only explicitly refers to assets, and not liabilities. Based on the experiences of the current sovereign debt crisis, discussions about risks may also refer to the liability situation (including unrecognized contingent liabilities) of an entity and what this means for an entity's financial management.
9. Paragraph 29 should be amended to include all risks, not just financial risks as that will provide users with a more complete view of their exposures, and what measures management has/will implement to mitigate those risks.
10. Paragraph 30: "... care must be taken to ensure it is fact-based, and neutral" (also repeated in paragraph 27) - should these be the overall characteristics of the information presented in the FSD&A? Instead of repeating it in different paragraphs of

the proposed standard, we recommend the IPSASB move this to the 'Qualitative characteristic' section of this guidance (paragraph 9).

11. Overall comment on paragraphs 27-32: There seems to be a large amount of overlap between these requirements and other IPSASs, in particular, IPSAS 14 *Events after the Reporting Date* and IPSAS 30 *Financial Instruments: Disclosures*. While the scope of the ED appears to be broader than IPSAS 30, we would expect considerable overlap of information.

We believe that extensive work needs to be completed to refine the FSD&A guidance before the proposals are operational. We also agree with the alternative view that forward-looking information be disclosed to provide users with better and more complete information for decision-making purposes. Furthermore, we believe it is also difficult not to discuss forward-looking information in order to fulfill the disclosure objectives of paragraphs 18, 24-25 and 27-32.

Specific matter for comment 5:

Do you agree with the transitional provisions?

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?

The implementation guidance is useful for setting best practice guidelines that should be followed when making such narrative disclosures.

Specific matter for comment 7:

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

The illustrative example provided is that of a country. It would be more useful if the set of illustrative examples could include example disclosures other public sector entities such as municipalities and ministries as there would presumably be more preparers in these categories.

We question the appropriateness of some of the content in the illustrative example. Firstly, the section on 'about the government', it largely contains information about the economy of the country that the government governs, rather than the government itself, which we would have

thought should be the main focus of that section.

Secondly, the discussion of 'objectives and strategy' seems more in the nature of a political party's election campaign document. For example, the 'Highlights of the EAS' shows that this government's strategy has resulted in only good news all round, and no bad news, which would be unusual. It would be useful for preparers for more realistic/practical examples to be included.

Other comments

- The definition of FSD&A in paragraph 8 is very broad and it is not clear how the FSD&A links with the notes to the financial statements. We suggest that the definition be refined to include the aim/objective of FSD&A.
- Amendments to IPSAS 1.27: Based on the amendments one could conclude that the principle of fair presentation does not apply to FSD&A. We assume that this is not intended by the IPSASB. Therefore, we would think that it should also apply to FSD&A. We suggest that the IPSASB clarify the relationship between fairly presented financial statements and fairly presented FSD&A.

Yours sincerely,

Ernst & Young GmbH
Wirtschaftsprüfungsgesellschaft

Prof. Dr. Peter Oser

Thomas Müller-Marqués Berger