EUROPEAN COMMISSION
Budget

The Accounting Officer of the Commission

Brussels,
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**NOTE FOR THE ATTENTION OF PROF DR ANDREAS BERGMANN,
CHAIRMAN OF THE IPSAS BOARD**

Subject: Comments on the Conceptual Framework Exposure Drafts 2: Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities: Elements and recognition in financial statements

Thank you for giving me the opportunity to comment on the Exposure Draft 2 of the Conceptual Framework project. The following comments are made in my capacity as Accounting Officer of the European Commission responsible for, amongst other tasks, the preparation of the annual consolidated accounts of the European Union which comprise more than 50 European Agencies, Institutions and other Bodies with an annual budget of more than EUR 140 billion.

As a general comment, I would like to congratulate the IPSAS Board for issuing this high quality exposure draft and for the significant progress made on the work on the Conceptual Framework. Please find my comments on specific matters of this exposure draft in the Annex to this note.

I look forward to our continued co-operation in the area of public sector accounting and remain at your disposal for any question you may have on the comments.

Manfred Kraff

Annex: Comments on specific matters

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Annex: Comments on specific matters

Specific Matter for Comment 1:

Do you agree with the definition of an asset? If not, how would you modify it?

Comment:

We agree with the definition of an asset as presented in this exposure draft. However, we would like to draw your attention to the definition of a "resource" in paragraph 2.2. The asset definition refers to a "resource, with the ability to provide an inflow of service potential or economic benefits ..." A resource is defined as "an item, with the ability to provide an inflow of service potential or economic benefits." The need to define a "resource" in the same way as an "item" is not very clear in the paper and needs more explanation. Without additional explanation, the introduction of "item" seems redundant.

Specific Matter for Comment 2:

a) Do you agree with the definition of a liability? If not, how would you modify it?

Comment:

We agree in general with the definition of a liability as presented in this exposure draft. However, we would encourage the board to clarify better the notion of "little realistic alternative to avoid an outflow of service potential or economic benefit." In the paragraphs following the definition of a liability, this distinction is not explained any further and this could cause uncertainty as to when the definition of a liability is met. If the word "little" refers to the uncertainty of future events and the fact that one can never be certain (100%) but only virtually certain, then we believe it could be useful for preparers to add a short clarification in this respect to one of the paragraphs. As we don't believe that a difference with IFRS was intended in this respect, a clarification would eliminate doubts.

Specific Matter for Comment 5:

a) Do you agree with the decision to define deferred inflows and deferred outflows as elements? If not, why not.

Comment:

We fully understand that there are good arguments to implement an inter-period equity concept, in particular when accrual accounting is combined with accrual budgeting. However, we believe that the benefits of this concept do not outweigh both conceptual and practical issues related to this concept as it is proposed, and thus we would, for the reasons outlined below, prefer not to define deferred in- and outflows as separate elements of financial statements.

From a conceptual point of view, we find most of the arguments expressed as the alternative view to the exposure draft convincing. In particular, we find it problematic to define resources that are not under the control of the transferor (outflows with restrictions only attached to it) as elements of the statement of financial position of the transferor. The transferor of a grant without conditions does not control the resource any longer and so the deferred reporting on the financial performance might be misleading for the addressees of financial reporting in particular when the service recipients (not resource recipients) are located in another jurisdiction than the transferor. Similarly, the recipient in a non-exchange transaction without conditions attached to it has gained control over the resource received and so the dynamic future consumption of economic benefits is completely under the discretion of the resource recipient.

The control-criterion in combination with the past event requirement is, for us, very important in this context as it is in most cases observable and thus reliable. Although we can see the advantages for the revenue/expense-led approach, we believe that it should not be implemented in the proposed way. The recognition of elements based on control and past events seems more reliable and less sensitive to manipulation.

We also believe that the deferred in- and outflows model in its proposed narrow form does not necessarily take the advantages of the dynamic approach into account. On the one hand it might be that the conditions attached (clearly specified future periods) are, for whatever reason, not always met and so for similar transactions, different accounting treatments would follow and on the other hand changes in estimation or other circumstances would again lead to bias in the inter-period equity.

We are, furthermore, of the opinion that the definition of deferred in- and outflows at the Conceptual Framework level for very specific types of non-exchange transactions with specific conditions attached may result in a mismatch with all other elements of financial statements. The conceptual extension of criteria that determine elements for such specific cases does not, in our opinion, justify the benefits intended as compared to all other transaction neutral elements of financial statements. We support a more principle based transaction neutral approach for the Conceptual Framework level.

As mentioned above, we do believe that there are particular transactions on the recipient's side where the inter-period equity approach would indeed present fairly the substance of the transaction. We therefore would like to encourage the board to reflect on how to solve this issue on a standards level. One possibility would be to reflect on the possibility of changing the definition of condition in IPSAS 23 in the sense that quasi conditions are included or stipulations where the transferor has the expectation that the recipient complies with the intention of the transferor.

Specific Matter for Comment 6:

a) Do you agree with the term net assets and net financial position and the definitions? If not, how would you modify the terms and/or definitions?

Comment:

Following our reply to SMC 5 the definitions of net financial position can be dropped as only the term net asset would remain.