

Financial Reporting
Advisory Board

From the Chairman

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2 April 2009

Dear Stephenie

RE: CONSULTATION PAPER “Conceptual Framework for General purpose Financial Reporting by Public Sector Entities:

- **The objectives of Financial Reporting**
- **The Scope of Financial Reporting**
- **The Qualitative Characteristics of Information Included in General Purpose Financial Reports**
- **The Reporting Entity**

Introduction

1. The Financial Reporting Advisory Board (the Board) welcomes the opportunity to comment on the Consultation Paper *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities* (the Paper). This letter summarises the Board's views and the attached Appendix A provides more detailed comments on the Paper.

2. The Board welcomes the IPSASB's decision to issue this material in the form of a consultation paper, thereby providing an opportunity for the Board to contribute to the debate on, and the development of a conceptual framework for the general purpose financial reporting by public sector entities.

Background to the Board and its interest in the Conceptual Framework

3. The Financial Reporting Advisory Board (the Board) acts as an independent element in the process of setting accounting standards for government. The Treasury is required by the Government Resources and Accounts Act 2000 to consult the Board on financial reporting principles and standards. The Board exists to promote the highest possible

standards in financial reporting by government and to ensure that any adaptations of, or departures from, Generally Accepted Accounting Practice are justified and properly explained. In conducting this process the Board ensures that an even and sector neutral accounting approach is consistently applied. The Board reports annually to Parliament about its activities and highlights areas of concern. More details about the work of the Board can be found on its website at www.hm-treasury.gov.uk/psr_frab_index.htm.

4. The Board views the proposed Conceptual Framework as fundamentally important to the future development of International Public Sector Accounting Standards (IPSASs), and consequently this has subsequent implications for Public Benefit Entities, i.e. those not for profit entities within the public sector, in jurisdictions applying IPSASs.

General comments on the Paper

5. The Board agrees with many of the views expressed in the paper. Some general comments on the paper are included below.

The Framework

6. The Board would not wish to see unintended differences arising in application and emphasis as a result of having two separate conceptual frameworks, and views that there should only be a departure from the IASB framework if there is good reason to do so, and hopes that any differences can be resolved as the frameworks develop.

Objectives of Financial Reporting

7. It is agreed that the objectives of financial reporting by public sector entities are to provide information about the reporting entity useful to users of GPFRs for accountability (stewardship) purposes and for decision usefulness. Whilst the relative importance of the objectives at any given time may depend upon the specific circumstances of the utilisation of the financial reports, in general, accountability is particularly important in the public sector context, and particularly in relation to general purpose financial statements.

Scope of Financial Reporting

8. As set out in the paper, the scope of financial reporting is very wide in nature. There is a need to distinguish between the types of information that would fall to be included in general purpose financial statements, and those types of information that will fall to other forms of financial reporting.

Qualitative Characteristics of Information

9. Our previous view to the International Accounting Standards Board on this issue was that the qualitative characteristic of 'reliability' is preferred to 'faithful representation' as the former is likely to lead to more consistent financial reporting because the latter is a less well-understood term by those involved in general purpose financial statements. However, the Board acknowledges that the IPSASB is seeking to maintain alignment with the IASB framework and considers that the advantages that will come from the alignment outweigh its concern over not using 'reliability'.

The Board's comments on the preliminary views in the paper

10. Appendix A to this paper sets out the Board's views on each of the preliminary views reached in the Consultation Paper. The Board looks forward to the opportunity to further contribute to the work of the IPSASB in the development of its conceptual framework.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Elwyn Eilledge', with a large circular flourish at the beginning.

p.p. ELWYN EILLEDGE

Signed on behalf of the Chairman in his absence

Appendix A

Financial Reporting Advisory Board response to the IPSASB Consultation Paper “Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities:

- **The objectives of Financial Reporting**
- **The Scope of Financial Reporting**
- **The Qualitative Characteristics of Information Included in General Purpose Financial Reports**
- **The Reporting Entity**

Preliminary View 1 – The Authority of the IPSASB Framework (following paragraph 1.7)

The IPSASB Framework will not establish new authoritative requirements for financial reporting by public sector entities that adopt IPSASs, nor will it override the requirements of existing IPSASs.

In selecting accounting policies to deal with circumstances not dealt with in IPSASs or other guidance issued by the IPSASB, public sector entities will refer to, and consider the applicability of, the definitions, recognition criteria, measurement principles, and other concepts identified in the IPSASB Framework.

The Board agrees with this view.

Preliminary View 2 – General Purpose Financial Reports (GPFRs) (following paragraph 1.15)

GPFRs are financial reports intended to meet the common information needs of a potentially wide range of users who are unable to demand the preparation of financial reports tailored to meet their specific information needs.

The Board agrees with this view.

Preliminary View 3 – The users of GPFRs (following paragraph 2.7)

As a mechanism for focusing on their common information needs, the potential users of GPFRs of public sector entities are identified as:

- *recipients of services or their representatives;*
- *providers of resources or their representatives; and*
- *other parties, including special interest groups and their representatives.*

The legislature is a major user of GPFRs. It acts in the interests of members of the community whether as recipients of services, providers of resources, or citizens with an interest in, or need for, particular services or activities.

The Board agrees with the preliminary view in that there are common information needs required by the potential users of GPFRs. However, in a public sector context there is inevitably greater focus on the information needs of providers of resources consistent with the objectives of financial reporting outlined in preliminary view 4 below.

Preliminary View 4 – The Objectives of Financial Reporting (following paragraph 2.22)

The objectives of financial reporting by public sector entities are to provide information about the reporting entity useful to users of GPFRs for:

- *accountability purposes; and*
- *Making resource allocation, political and social decisions.*

The Board agrees this view, with particular emphasis on the importance attached to accountability (stewardship) in the public sector context, particularly related to general purpose financial statements.

Preliminary View 5 – The Scope of Financial reporting (following paragraph 3.18)

The scope of financial reporting encompasses the provision of financial and non-financial information about:

- *economic resources of the reporting entity at the reporting date and claims to those resources;*
- *the effect of transactions, other events, and activities that change the economic resources of the reporting entity and claims to those resources during the reporting period, including cash inflows and outflows and financial performance;*
- *the reporting entity's compliance with relevant legislation or regulation and legally adopted or approved budgets used to justify the raising of monies from taxpayers and ratepayers;*
- *the reporting entity's achievement of its service delivery objectives; and*
- *prospective financial and other information about the reporting entity's future service delivery activities and objectives, and the resources necessary to support those activities.*

It also encompasses explanatory material about: (a) the major facts underlying the financial performance of the entity, the achievement of its service delivery and other

objectives and the factors which are likely to influence its performance in the future; and (b) the assumptions underlying and major uncertainties affecting the information included in GPFRs.

The Board agrees with the preliminary view put forward covering the general scope of financial reporting, that is acknowledged to be wide in nature. However, it would be helpful to first distinguish between the types of information that would normally be expected to be included within general purpose financial statements, and that information that would normally fall to be included within other types of financial reporting.

Preliminary View 6 – Evolution of the Scope of Financial Reporting (following paragraph 3.22)

The scope of financial reporting should evolve in response to users' information needs, consistent with the objectives of financial reporting.

The Board agrees with this view.

Preliminary View 7 – The Qualitative Characteristics of Information Included in GPFRs (following paragraph 4.40)

The qualitative characteristics of information included in GPFRs of public sector entities are:

- *relevance, which encompasses confirmatory value, predictive value, or both;*
- *faithful representation, which is attained when depiction of economic or other phenomena is complete, neutral, and free from material error;*
- *understandability;*
- *timeliness;*
- *comparability; and*
- *verifiability (including supportability).*

Constraints on financial reporting are materiality, cost and achieving an appropriate balance between the qualitative characteristics.

In its response to the IASB Discussion Paper on this issue the Board expressed the view that 'faithful representation' is a less well-understood term than 'reliability', which would be differently interpreted in practice, and consequently would be unlikely to lead to consistency in financial reporting. However the Board acknowledges that the IPSASB is seeking to

maintain alignment with the IASB framework and considers that the advantages that will come from the alignment outweigh its concern over not using ‘reliability’.

Preliminary View 8 – Characteristics of a Reporting Entity (following paragraph 5.10)

The key characteristic of a reporting entity is the existence of users who are dependant on GPFs of the entity for information for accountability purposes, and for making resource allocation, political, and social decisions.

A public sector reporting entity may be an entity with a separate legal identity or other organisational structure or arrangement.

The Board agrees with this preliminary view. Public sector reporting entities that are directed by the Government to report may take various organisational or structural forms, which may or may not have a separate legal identity.

Preliminary View 9 – The Composition of a Group Reporting Entity (following paragraph 5.35)

A group reporting entity will comprise the government (or other public sector entity) and other entities when the government (or other public sector entity):

- has the power to govern the strategic financing and operating policies of the other entities (a “power criterion”); and*
- can benefit from the activities of the other entities, or is exposed to a financial burden that can arise as a result of the operations or actions of those entities; and can use its power to increase, maintain, or protect the amount of those benefits, or maintain, reduce, or otherwise influence the financial burden that may arise as a result of the operations or actions of those entities (a “benefit or financial burden/loss” criterion).*

The Board agrees with this view.