



Australian Government

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CANADA

Dear Stephenie

IPSASB Exposure Draft ED 46
Reporting on the Long-Term Sustainability of a Public Sector Entity's Finances

The Australian Accounting Standards Board is pleased to submit its comments on Exposure Draft ED 46 to the International Public Sector Accounting Standards Board.

The AASB considers this to be a very important project of the IPSASB, particularly from the viewpoint of the probable usefulness to users of the information involved and because it brings much needed focus onto the identification of the boundaries of general purpose financial reporting.

The scope of general purpose financial reporting

The AASB generally agrees with the proposals in the Exposure Draft. Its main concern is that, whilst it considers that some information useful for assessing long-term fiscal sustainability (LTFS) belongs within the scope of general purpose financial reporting, it is likely that not all information useful for that purpose belongs within that scope. The AASB considers that usefulness of information, per se, is not a sufficient discriminator to decide what is part of general purpose financial reporting. If it were, annual reports, and more, would fall within the scope of GPFRs. Accordingly, criteria are needed to determine what is part of financial reporting and what is not.

This project illustrates that there is a gap in the conceptual framework. Whilst the IPSASB is addressing the scope of financial reporting in Phase 1 of its conceptual framework project, it has tentatively decided that the scope of financial reporting should evolve in response to users' information needs – this decision addresses the scope by reference to useful information but not financial reporting information.

Strategically, the AASB supports the IPSASB's fostering of fiscal sustainability reporting through guidance, but would like to see rigour, over time, in delineating the financial reporting aspects thereof and helping others to see what falls to them. We do not envisage that accounting standards would be the source of guidance or requirements for everything

that might be embraced by the topic. This scope issue is also seen in relation to the IPSASB's project on service performance reporting.

The AASB recommends that, to resolve the scoping issue, it is crucial that the IPSASB adequately defines general purpose financial reporting in its Conceptual Framework project.

General relevance of long-term fiscal sustainability reporting

Conceptually, the AASB sees no reason why financial sustainability is not a legitimate subject of every entity's financial reporting, whether in the public sector or the private sector, and whether for profit or not for profit. Conversely, it would be misleading for financial statements to be produced that ignore the anticipated consequences of existing or changed policies, changes in markets or changes in other environmental circumstances. Users' attention ought to be drawn to these to correct impressions about sustainability that might flow from just presenting basic financial statements.

We would urge that the IPSASB not treat the topic as if it were unique to reporting by governments or even the public sector. The prime examples seen to date of such reporting are focused on the fiscal sustainability of governments' current policies, but that should not be the limit of fiscal sustainability reporting. We also see no reason why a component or segment of an entity could not be the subject of such reporting.

Relationship to other current IPSASB projects

It would be worthwhile for the IPSASB to consider the links between fiscal sustainability reporting and other areas of general purpose financial reporting that it is presently addressing – in particular, financial statement discussion and analysis, and service performance reporting. Information reported under all of these projects could be clearly linked. For example, where service performance reporting is likely to emphasise information concerning the current reporting period and, to some degree, the short-term future, the service capacity dimension of fiscal sustainability reporting could extend this information over the long-term horizon. Therefore, entities reporting information under requirements or guidelines arising out of one or another of these projects might be expected to report information under all of them.

The linkage between all of these projects that are addressing financial reporting beyond the current scope of general purpose financial statements might be derived from identifying in the Conceptual Framework the types of information that would serve the objectives of financial reporting. For example, information about liquidity, sustainability and flexibility in various dimensions and timeframes may respond to the objectives, providing a platform for linking the different reporting threads. At present, the developing Framework largely refers to these different areas as separate information needs of users of financial reports. A better articulation of the linkages would be useful.

The AASB recognises that reporting information about LTFS is an evolving area, and further experience with such reporting will provide further insights into the ways in which the information can best be communicated and the part with which financial reporting can assist.

Other comments

The AASB's comments on the Specific Matters for Comment and other aspects of the proposals are set out in the attachment to this letter.

If you have queries regarding any matters in this submission, please contact me or Clark Anstis (canstis@aab.gov.au).

Yours sincerely,

A handwritten signature in black ink that reads "K.M. Stevenson". The signature is written in a cursive style with a long, sweeping underline.

Kevin M. Stevenson
Chairman and CEO

Specific AASB comments on IPSASB Exposure Draft ED 46 *Reporting on the Long-Term Sustainability of a Public Sector Entity's Finances*

Specific Matters for Comment

The AASB provides the following comments on the IPSASB's Specific Matters for Comment set out in the Exposure Draft.

Specific Matter for Comment 1

Do you agree that the characteristics of an entity that indicate whether users exist for information on long-term fiscal sustainability are those set out in paragraph 15? If you consider that there are more appropriate indicators please provide them.

The AASB agrees that users of LTFS information are likely to exist for entities that reflect the characteristics set out in paragraph 15 – entities that have the power to change their policies on the raising of revenue and other resources (such as debt) or the provision of goods and services in order to affect trends in the entity's long-term fiscal sustainability.

However, as indicated in our covering letter, the AASB's view is that the reporting of long-term fiscal sustainability (LTFS) information conceptually is relevant to all reporting entities. LTFS reporting is just as relevant to entities that do not have such powers. If their LTFS information reveals negative trends, then it is likely that the entity's operating model or parameters will need to be changed by those entities that do have the powers to change the policies. This would appear to be useful information in relation to such entities. LTFS reporting by such entities need not require extensive disclosures, if that is unnecessary to provide the relevant information to users of their general purpose financial report.

Therefore, the AASB does not agree with the unstated implication of paragraphs 14 and 15 in the ED that LTFS reporting essentially should be or is expected to be restricted to entities exhibiting the stated characteristics. Although paragraph 14 does refer to an entity needing to assess "initially" whether there are potential users of its prospective information, nothing further is said about the relevance of LTFS reporting beyond that initial assessment. This should be addressed in the pronouncement.

Specific Matter for Comment 2

Do you agree that the "dimensions" of long-term fiscal sustainability in paragraphs 27–37 provide a viable framework for narrative reporting on the long-term sustainability of an entity's finances that complements and interprets the projections? If not, how would you modify this approach?

The AASB considers that the dimensions appear to be useful components of fiscal sustainability reporting, particularly the discussion of relevant indicators to portray the dimensions. However, the AASB strongly supports the indication in paragraph 27 that faithful representation of LTFS information can be satisfied by presenting information along those dimensions – without implying that any other approach would be inappropriate. That implication, though, should be made explicit, so that it is clear that the dimensions

discussed in the document are not the only basis upon which LTFS information might be provided.

This approach also would be justified on the grounds that the IPSASB's project on service performance reporting is presently at an early stage. It could well be that that project begins to develop dimensions of service performance reporting that reflect upon LTFS reporting as well, given that LTFS includes a service capacity dimension under the framework set out in the ED.

Specific Matter for Comment 3

Do you agree with the guidelines in this ED on disclosure of principles and methodologies, including risks and uncertainties? If not, how would you modify these guidelines?

The AASB generally agrees with the guidelines proposed in the ED concerning the principles and methodologies underlying the preparation of projections, and provides some specific comments in the following paragraphs. The AASB also notes that paragraphs 38-51 concern more than disclosure of the basis of preparation of projections, and thus the heading before paragraph 38 is too limiting.

In relation to paragraph 39, the AASB is concerned with the implication that annual updating of projections is the preferred frequency. The ED does not specify a recommended frequency of LTFS reporting, which is supported by the AASB. However, it may be appropriate to state the principle that LTFS reporting should be at least as frequent as necessary to ensure that the most recently published LTFS information for an entity does not become misleading. The patronising reference in paragraph 39 to sub-national entities that might be reporting on projections for the first time certainly should be deleted.

A number of specific disclosures are identified in paragraphs 38-51, but the level of detail varies considerably. For example, paragraph 48 specifies disclosure of the "approach" to inflation, but then goes on to identify four disclosures in relation to discount rates, including the reason for changes. The AASB recommends that the IPSASB consider including a general principle for disclosure of the basis of the preparation and presentation of projections and other LTFS information and changes therein. This would cover, for example, changes in the time horizon used for the projections – the Consultation Paper preceding the ED had referred to disclosing the reason for modifying the time horizon, but this does not appear in the ED.

Other Comments

Recommended Practice Guidelines

The AASB supports the issue of Recommended Practice Guidelines at this stage. The AASB also proposes that the IPSASB consider at a later stage whether to make the requirements mandatory for entities that exhibit the characteristics set out in paragraph 15, i.e. that have the power to change their revenue sources and their policies on the provision of goods and services.

The AASB considers that non-mandatory Guidelines do not require an effective date. As soon as they have been published by the IPSASB, it is up to each entity that reports LTFS information thereafter to decide whether to disclose the degree of compliance with the Recommended Practice Guidelines. An entity that considered it needed more time and experience with the subject matter before reporting its compliance with or departure from the Guidelines could simply choose not to report any comparison until it was ready to do so. An effective date therefore would not be useful.

Reporting boundary

The AASB considers that information about LTFS presented within a GPFR should not encompass information about entities outside the boundary of the reporting entity (paragraph 11 would appear to permit this). In that sense, the AASB agrees that the concept of a reporting entity should be reflected in IPSASB guidance on reporting information about LTFS. However, the AASB would not support limiting information about LTFS in GPFRs to being reported only in respect of an entire reporting entity. For example, the IPSASB should not preclude reporting of such information in respect of particular segments of an entity. This is an extension of the approach in paragraph 12, which refers to reporting LTFS information for the General Government Sector, which is a sector of the whole-of-government reporting entity.

The emphasis in paragraph 11 should be reversed – in the event that entities within the reporting boundary for LTFS differ from those for the general purpose financial statements, the LTFS report should disclose the differences and the impacts. This makes the financial statements the primary GPFR rather than the LTFS report.

Presenting projections of prospective inflows and outflows

The AASB supports the flexible approach in the ED to the presentation of LTFS information. The AASB had opposed the dichotomous approach in the Consultation Paper that LTFS information in GPFRs should be presented either through additional statements for details of projections or as summarised projections in narrative reporting. The important point is that guidance on LTFS reporting:

- (a) should not be too prescriptive as to the form of presentation of information about LTFS in an entity's general purpose financial reporting; and
- (b) should focus on whether an entity's GPFRs, collectively, provide all of the information that is useful to users of the entity's GPFRs for accountability and decision-making purposes.

Paragraph 20 refers to “a combination of narrative reporting, graphical presentation and the use of indicators”. It is not clear that these are distinct forms of presentation, and it would be better to use an alternative description.

Paragraph 22 refers to the risk of LTFS information presenting a misleadingly favourable picture, and indicates that consistent formats are important in this regard. The AASB considers that, as also noted in the paragraph, it is the explanation of changes in format that would be important. Consistent formats per se cannot reduce any skewness in the LTFS

information; indeed, consistent formats may serve only to maintain any skewness in the presentation of the information. The wording should be revised to avoid this difficulty.

Paragraph 23 also needs to be redrafted. It begins by referring to assets and liabilities recognised in the statement of financial position, and the assessment of short-term solvency – but including unrecognised assets and liabilities. It concludes with a reference to obligations and inflows that may not be settled for many years, however some of these will be recognised in the statement of financial position in any case. The logic of this paragraph is unclear, and the message needs to be clarified.

Definitions of indicators

The glossary in Appendix A to the proposed Guidelines defines various terms in accordance with GFS and other statistical sources. Therefore, it is uncertain whether it is intended that the calculation of such indicators should be in accordance with statistical requirements or IPSAS requirements. The AASB supports the latter approach. For example, ‘net worth’ is defined as total assets less total liabilities. This should be based on assets and liabilities as addressed in IPSASs, since there are differences between accounting standards and statistics on the scope of both assets and liabilities.
