

April 25, 2012

Mr. François Lequiller
The Director, Directorate D: Government Finance Statistics
European Commission - Eurostat D4
GFS Quality Management and Government Accounting
Office : Bech B4/401
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By email: ESTAT-IPSASconsultation@ec.europa.eu

Dear François:

PUBLIC CONSULTATION ON THE SUITABILITY OF INTERNATIONAL PUBLIC SECTOR ACCOUNTING STANDARDS (IPSASs) FOR EU MEMBER STATES

The International Federation of Accountants (IFAC) values the opportunity to comment on the public consultation paper issued by Eurostat on February 15, 2012, on the suitability of International Public Sector Accounting Standards (IPSASs) for EU Member States. Through its membership, currently 167 professional accountancy bodies in 127 countries and jurisdictions, IFAC represents approximately 2.5 million accountants in public practice, industry and commerce, government, and education.

IFAC Support for IPSASs

IFAC strongly supports the use of IPSASs by EU Member States, and commends the European Parliament for asking Eurostat to assess their suitability. In our view the adoption of IPSASs by EU Member States would be a historic step in the direction of governmental transparency that would be welcomed by citizens and capital markets alike. The critical need for government financial reporting arrangements that promote high levels of transparency and accountability could not be made more apparent than has been done by the sovereign debt crisis.

IPSASs are written specifically with the public sector in mind, and are suitable for implementation by all types of governments and public sector entities. Although the accrual basis of the standards are based on the International Financial Reporting Standards (IFRSs), issued by the International Accounting Standards Board (IASB)—where the requirements of those Standards are applicable to the public sector—IPSASs also deal with public sector specific financial reporting issues that are not dealt with in IFRSs.

While IFAC recognizes that many people would consider the standards to be quite complex, it is evident that the fiscal positions of governments have become markedly more complex over the years, particularly through the interventions of governments during the financial crisis. Cash-based accounting—which itself often involves complex arrangements and professional judgments pertaining to recording and measurement—has virtually no capacity to deal with these added complexities, leaving the financial statement user seriously uninformed.



To mitigate the negative consequences of using what might be seen as being more complex reporting arrangements, it is important that governments enhance the role and competency of professional accountants engaged in the public sector. In many countries this will involve working closely with national professional accountancy organizations to enhance public sector accounting capacity and expertise.

IFAC fully understands that the adoption and implementation of IPSASs in many countries would involve a lengthy process, which would require considerable political will and support. However, these difficulties must be overcome, given the potential significant risks of not acting now. Accrual-based financial reporting by governments is commonplace today, proving that it can be implemented. Nearly 40 jurisdictions around the world use IPSASs and/or accrual-based public sector accounting, and some countries, such as Australia and New Zealand, have been doing so for around 20 years. Countries using accrual-based accounting and/or IPSASs recognize the risks associated with making decisions based on short-term agendas and incomplete information, the significant threats to long-term sustainability, and the burdens placed on future generations. Having high-quality, complete, and adequate financial information available for decision-makers mitigates these threats.

Advantages of Adopting and Implementing IPSASs

The adoption of IPSASs has several advantages. Most notably, the production of financial reports using a high-quality reporting framework such as IPSASs, and the development and use of financial information systems required for such reporting, will improve the reliability of economic and financial information. This results in enhanced quality and reliability of all reporting, including economic statistics provided to Eurostat under the European System of Accounts, and the reporting of Government Finance Statistics required by the International Monetary Fund.

Other significant advantages include:

- Promoting consistency of reporting across different countries, and within the same jurisdiction, for comparative purposes, including fiscal management and compliance with fiscal rules;
- Improving the completeness of financial information, including the recording of all physical assets, liabilities (including all long-term liabilities), and net worth; and
- Providing appropriate incentives for enhanced political decision making.

Governance Arrangements for the IPSASB

We note that Section 2 of your public consultation paper is devoted to a discussion of IPSASs and the International Public Sector Accounting Standards Board (IPSASB).

While the paper correctly indicates that the IPSASB is an independent standard-setting board, we are conscious that the independence of standard-setting boards, and governance arrangements in place to protect and enhance their independence, are often questioned by governments and regulators when considering the adoption and implementation of standards. For example, questions were raised about the governance arrangements of the IASB several years ago at the height of the global financial crisis.

As the body that provides logistical, financial, and staff support the IPSASB, IFAC considers it important that governance arrangements of the IPSASB are clearly enunciated and understood; this includes



proposed measures to further enhance the robustness of these arrangements and the independence of the board. With this in mind, we offer the following information about the governance arrangements of the IPSASB.

IFAC outlines its views on the importance of robust governance arrangements for standard setting in its Policy Position Paper 3, *International Standard Setting in the Public Interest*.¹ In this paper, it is noted that:

Current arrangements for international standard setting encompass a combination of public and private sector roles, and provide a structure and process that operate and are seen to operate in the public interest, in a context in which there are needs for legitimacy, independence, transparency, performance (encompassing technical competence, responsiveness, and efficiency) and accountability.

Although all of the arrangements outlined in this paper currently do not apply to the IPSASB—for example, the IPSASB is currently not subject to oversight by the Public Interest Oversight Board (PIOB)—the general principles of independent, transparent, accountable, and high-performing boards that promote the legitimacy of the standards is applicable for the IPSASB. The IPSASB has due process arrangements, nominations processes, board composition and representation requirements, and resourcing arrangements similar to those of the other boards supported by IFAC, as described in this policy position paper. Furthermore, the IPSASB conducts its meeting in public (and welcomes observers to these meetings), it makes public all meeting papers and exposure drafts, and undertakes annual performance monitoring of its board members.

The diversity of IPSASB membership is described in the “Call for Nominations 2013” paper, available on the IFAC website.² For your convenience, an extract of the IPSASB section of this paper is attached to this letter (refer Attachment 1). This extract outlines, among other things, the IPSASB mission, its work plan for 2013, the general qualifications for nominees, and the requirements for board membership.

There are existing proposals to further enhance these governance arrangements, including: seeking Monitoring Group (MG) (of which the European Commission is a member) approval to have the IPSASB subject to oversight by the PIOB; and the appointment of a full time independent chair of the board. Subject to available resourcing, it is hoped that these proposals will be implemented in the next two years. The MG has recently issued its public consultation—with responses due by June 22, 2012—on the governance of the MG, the PIOB, and the standard-setting boards supported by IFAC.³ In its consultation paper the MG discusses the benefits, challenges, and issues associated with introducing public oversight of the IPSASB. It poses several questions for consideration, including:

- Would you support the IPSASB being subject to PIOB oversight? Why?
- What conditions, if any, would you impose on such oversight? Would you see as a factor to take into account the fact that IPSASB deals with accounting rules instead of auditing ones?

¹ www.ifac.org/sites/default/files/publications/files/PPP3%20Standard%20Setting%20in%20the%20Public%20Interest.pdf

² www.ifac.org/sites/default/files/uploads/NomCom/IFAC-Call-For-Nominations.pdf

³ www.iosco.org/monitoring_group/pdf/MG%20Governance%20Review.pdf?v=1



Public Sector Financial Management Transparency and Accountability

IFAC considers that the adoption and implementation of high-quality, accrual-based accounting standards (IPSASs) is an integral and essential part of ensuring that governments implement the necessary institutional arrangements required to enhance public sector financial management transparency and accountability. The use of IPASSs promotes greater transparency and accountability in public sector finances and allows for enhanced monitoring of government debt and liabilities for their true economic implications. IFAC's position, in this regard, is presented in its Policy Position Paper 4 *Public Sector Financial Management Transparency and Accountability: The Use of International Public Sector Accounting Standards*.⁴

IFAC is of the view that the sovereign debt crisis, and the consequences that are being felt around the globe, illustrate the implications of government balance sheet management failures and the inability of organizations such as global financial institutions, investors in government debt, and credit rating agencies to adequately monitor the financial positions of governments. IFAC notes that government debt and deficits alone do not provide a comprehensive picture of fiscal soundness, and that full disclosure of all assets, liabilities, and contingent liabilities is vital for assessing the true economic implications of public sector financial management. Furthermore, IFAC believes that when all liabilities are disclosed—including the long-term obligations of government (e.g., pension obligations)—government leaders may be encouraged to make decisions that are driven by long-term financial sustainability, rather than short-term political incentives.

In March this year IFAC convened a seminar titled *The Sovereign Debt Crisis, a Matter of Urgency – from Lessons to Reform*, which included presentations, debates, and discussion involving key decision makers, politicians, and public sector finance management leaders. The outcomes from the seminar included the identification of the compelling and urgent need for governments to address seriously the quality of public sector financial management systems and institutions. There was a call for the adoption of accrual accounting and budgeting to better measure and manage fiscal positions; noting that the current crisis emphasized the deficiencies associated with cash-based arrangements. A common theme that emerged was that in many countries the risks associated with the poor fiscal measurement and management exposed by the sovereign debt crisis are amplified by the fiscal risks associated with the aging population.

More generally, IFAC's views about public sector financial management, transparency, and accountability—including perspectives on institutional changes required—have been outlined in letters of recommendations to the G-20 in each of the last four years. The most recent letter—dated April 6, 2012⁵ included:

IFAC is of the view that what is needed is urgent and fundamental work to consider the nature of the institutional changes that are required to protect the public and to protect investors in government bonds. It strongly encourages the G-20 to initiate such work through the FSB, making it explicit that it is seen as

⁴ www.ifac.org/publications-resources/public-sector-financial-management-transparency-and-accountability-use-intern

⁵ www.ifac.org/sites/default/files/publications/files/IFAC%20G20%20Letter%20One%202012.pdf



a critical part of the FSB's role. As such, a separate working group should be established within the FSB to specifically address public sector reporting and accounting matters.

In undertaking its work, the G-20 (and FSB) should look to the institutional arrangements for public finances in jurisdictions in which fiscal positions have been well managed, and should recognize that the problems that need to be addressed are ones in which governments are self-interested parties. As noted in IFAC's 2010 submission to the G-20, arrangements that might be considered as part of this work include:

- *High-quality and timely accrual-based financial reporting;*
- *Audited financial statements released within six months of year end;*
- *Budgeting, appropriations, and reporting on the same accrual basis;*
- *Full transparency in fiscal positions ahead of general elections, ensuring that voting is fully informed; and*
- *Limitations on deficit spending, or at least full transparency around the reasons for deficit spending and explanations of how, over an economic cycle, fiscal balance will be restored.*

Please do not hesitate to contact me should you wish to discuss any of the matters raised in this letter, or require any further information about the governance arrangements of the IPSASB. IFAC is committed to advancing the global adoption and implementation of IPSASs, and is willing to assist Eurostat in any way during this current assessment project.

Sincerely,

A handwritten signature in black ink, appearing to read 'Ian Ball', written in a cursive style.

Ian Ball
Chief Executive Officer

Attachment