

**INTERNATIONAL PUBLIC SECTOR ACCOUNTING STANDARDS BOARD
(IPSASB): CONCEPTUAL FRAMEWORK PROJECT**

Initial Issues Paper:	The scope of financial reporting
National Standard Setter	South Africa
Primary Author:	Erna Swart

1. The purpose of this component of the project is to set out proposals for consultation on the scope of financial reporting by public sector entities.

Key issues to be addressed

2. The key issues to be addressed in this component of the project are:
 - Financial reporting versus financial statements
We believe we should be addressing financial reporting and not just financial statements. Service delivery objectives and key accountability issues differ significantly from the private sector. These issues are normally reported on, outside the financial statements, but in the annual report. Auditing considerations generally determine where the information will be reported. Issues to be considered include what our involvement throughout the reporting life cycle should be, including budgeting and year end reporting (annual report). An issue that should be considered is our role in the budget compilation stage and reporting stage.
 - Performance Reporting
Performance in the public sector is generally measured in terms of service delivery and not profit. There are two aspects within this area that should be considered:
 - Reporting of Performance (an assessment of economy, efficiency and effectiveness), and
 - The reporting of performance information (looking at both financial and non-financial performance information and in particular the setting of measurable objectives, determining output, output performance measure/service delivery indicators, and reporting actual performance against the targets set, in summary service accomplishments).
 - Budget Reporting
What is our role with regards to budget compilation and presentation? From reporting to the man on the street, this is the one financial document issued by government with the highest public profile. Budgets in the private sector are not made public, but from a public sector perspective it is an important component of the accountability cycle.
 - Prospective financial information

Those countries that have adopted medium term expenditure frameworks include prospective financial information for up to three years in the framework. Once again, in the private sector the three year or five year plans are not public documents. The private sector, economists and financial analysts are very interested in the information and the assumptions made by government. Do we have a role with the compilation and presentation of that information and should there be reporting of that information in the annual report.

- Long term sustainability of government programmes
Many social programmes provide benefits that extend over the long term. Measurement of these programmes and reporting the sustainability of these programmes are particularly challenging. The usual elements of assets, liabilities, revenue and expenses cannot easily be used to report the impact. Where, if at all, should the impact of these programmes be reported – as part of the budget or as part of the annual report? What should the disclosures be in the annual financial statements – should it be disclosed as commitments? Is there a common understanding of a commitment as commitment accounting is often used in the public sector, but has a different meaning? Is this an aspect that should be addressed in general purpose financial reports or should we be looking at special purpose reporting?
- Sector neutrality
We are committed to converging with IASB where possible, but based on our scope and user needs, we may have to re-assess whether the disclosure requirements of the current suite of standards address our objectives.
- Environmental reporting
GRI has addressed the reporting of environmental issues in the financial reports of for-profit entities. Global-warming and its impact are becoming more topical. We should assess the public sector's response to the GRI initiative.
- Narrative reporting
Terms also used are management commentary and management discussion and analysis. The role of narrative reporting in public sector reporting should be considered.

The inter-relationship between performance reporting, budget reporting, prospective financial information and fiscal sustainability need to be considered and as the number of topics are rapidly increasing we may need to consider the role of summary financial statements.

3. Work on proposals for the objectives of financial reporting in the public sector is being led by the United Kingdom Accounting Standards Board. There will be a need for close liaison given the interrelationships between the two components, in particular in determining whether the objectives

- should focus on general purpose financial statements or general purpose financial reports.
4. Work on proposals on the qualitative characteristics is being led by Norway. There will be a need for close liaison given the interrelationships between long term sustainability reporting and the reliability of the information.

Coverage in existing International Public Sector Accounting Standards (IPSASs) and other publications issued by IFAC

5. The coverage in the current IPSASs is limited. In the accrual IPSASs:
- Scope of financial reporting is not addressed in any specific IPSAS.
 - Presentation of Budget Information in Financial Statements is addressed in IPSAS 24 and amendments to the Cash Standard.
 - Study 7 “Performance Reporting” issued in January 1996.
 - Study 11 “Governmental Financial Reporting” issued in May 2000.
 - Research Report on “Budgeting” issued in May 2004.

Coverage in the IASB-FASB joint Conceptual Framework project and other relevant material

6. The International Accounting Standards Board (IASB) issued a Discussion Paper (DP) in July 2006 ‘Preliminary Views on an improved Conceptual Framework for Financial Reporting: The Objective of Financial Reporting and Qualitative Characteristics of Decision-useful Financial Reporting Information’ as the first output from the joint conceptual framework project being undertaken with the US Financial Accounting Standards Board (FASB).
7. The preliminary views set are clearly of relevance to this component of the IPSASB project. A group of chairs and senior staff of the standard-setters of Australia, Canada, New Zealand and the UK (the ‘Group of Four’) are monitoring the applicability of the conceptual framework project to not-for-profit entities in the public and private sectors (public-benefit entities). A report from the group (authored by Kevin Simpkins) issued in July 2006 highlighted the inappropriateness of the pervasive cash flow focus the IASB/FASB’s proposed objective of financial reporting. It does however become relevant when including prospective financial information and fiscal sustainability in a wider financial reporting project and not limiting it to financial statements.
8. A number of national standard-setters and other organisations are developing material on reporting performance.

9. FEE issued in 1991 a publication “Developments in Performance Measurement and Financial Management”.
10. We should assess our own response to issues raised by Mr Kevin Simpkins in his paper to the Australian Financial Reporting Council, “The use of a sector neutral framework for the making of Australian Accounting Standards” and the reports issued by him as part of the monitoring of the IASB framework project.
11. The IASB has issued a discussion paper on management commentary. The UK has issued a standard and so have some of the other national standard setters.
12. Any academic research that other members of the project group may have access to would be welcomed.

**South African Accounting Standards Board
6 February 2007**

IPSASB PUBLIC SECTOR CONCEPTUAL FRAMEWORK

**INITIAL ISSUES PAPER PREPARED BY PRIMARY AUTHORS OF
GROUP 1 PAPERS**

The Reporting Entity – Australia - AASB

<u>Initial Issues Paper</u>	The reporting entity
<u>Lead Standard Setter</u>	AASB
<u>Primary Author</u>	Ahmad Hamidi

The issues mentioned below are quite detailed. Whether each of them is analysed in the draft Consultation Paper prepared for consideration by the IPSASB and its Conceptual Framework Subcommittee will depend on feedback on this initial issues paper, the constraints of the project timetable, and whether, in developing the draft Consultation Paper, project staff find that some of these issues are less relevant than originally thought.

Purpose

1. The purpose of this component of the project is to set out proposals for consultation on the concept of reporting entity in a public sector context.

Key Issues to be Addressed

2. This component of the project will address the following key issues:
 - (a) Should the reporting entity concept address which entities should be required to prepare general purpose financial reports and should be the focus of IPSASs? If so:
 - (i) What is an entity? For example, must it have a separate legal identity?
 - (ii) How should a reporting entity be defined with this objective in mind?
 - (iii) Which factors/indicators should be considered in determining whether an entity is a reporting entity?
 - (iv) Which of the following entities should be identified as reporting entities:

- (A) Entities below the ultimate controlling entity?
 - (B) The parent entity?
 - (C) Sectors or segments of government—e.g., core government (the budget sector/GGS)?
 - (D) Statutorily autonomous and independent entities?
 - (E) Government departments and ministerial portfolios?
- (b) What should be the basis for determining the boundaries of the individual or group reporting entity?
 - (i) How relevant is the concept of control?
 - (ii) The definition of control used in IFRSs is proposed as a starting point and, if the concept of control were thought to be an appropriate basis for determining the boundaries of a reporting entity, consideration would be given to the following:
 - (A) Should it be broadened or otherwise amended for application in the public sector?
 - (B) Should it be limited to direct control or also include indirect control?
 - (C) Does it matter whether control is only temporary?
 - (D) Should it be different from the concept of control used in relation to the definition of an asset?
 - (E) Does it apply to financial resources (and changes in them) or also control of non-financial outcomes—i.e., can an entity with constitutional or other legal autonomy of decision-making (such as a court) be controlled if it must deploy its resources to provide specified services?
 - (iii) Should the determination of the boundaries of reporting entity be based on other concepts? For example:
 - (A) The fund concept;
 - (B) Ownership; or
 - (C) Common control.

- (c) Notions of the reporting entity under statistical reporting models and accounting reporting models.

Cross-cutting issues

- 3. This component of the project will address the following cross-cutting issues:
 - (a) Links between the reporting entity concept and the objective of financial reporting/ information needs of users;
 - (b) Interaction with the Scope component of the project – for example, whether to apply differential reporting, and the nature or content of the financial reports that should be prepared, are interactive issues;
 - (c) Whether the concept of control of an entity (if used) should be the same as the concept of control of an asset (cuts across future work on Elements); and
 - (d) Whether the boundaries of a reporting entity include only resources that are controlled, or also include resources administered or held in a custodial capacity for other entities (cuts across future work on Elements).

Coverage in existing International Public Sector Accounting Standards (IPSASs)

- 4. The coverage in the current IPSASs is limited. In the accrual IPSASs:
 - (a) IPSAS 6 ‘Consolidated and Separate Financial Statements’ deals with control for financial reporting purposes, determination of control, and the relevance of regulatory power and purchase power to the concept of control (paragraphs 28-42);
 - (b) IPSAS 1 ‘Presentation of Financial Statements’ has references to “reporting entity”, indicating an implicit recognition of the concept in accrual IPSASs (paragraphs 63, 111, 138 and page 45); and
 - (c) The Preface to International Public Sector Accounting Standards notes that “The IPSASs are designed to apply to the general purpose financial statements of all public sector entities.” (paragraph 12)
- 5. The Cash Basis IPSAS has numerous references to “reporting entity”, indicating an implicit recognition of the concept in that IPSAS. For example, Paragraph 1.1.3 of the IPSAS notes that the Standard applies equally to the general purpose financial statements of an individual entity and to the consolidated general purpose financial statements of an economic entity, such as a whole-of-government, and requires the preparation of a statement of cash receipts and payments that recognizes the cash controlled by the reporting entity.

Coverage in the IASB-FASB joint Conceptual Framework project and other relevant material

6. The International Accounting Standards Board (IASB) has discussed the concept of reporting entity in a number of meetings during 2005 and 2006 and is expected to publish its preliminary views in the second quarter of 2007 on the subject. Perhaps its most significant tentative decision with potential implications for the scoping of this project is its decision that the reporting entity concept should not specify (or provide guidance on) which entities should be required to prepare general purpose financial reports.
7. A group of chairs and senior staff members of the standard-setting bodies of Australia, Canada, New Zealand and the United Kingdom is monitoring the applicability to not-for-profit entities in the private and public sectors of the concepts proposed under the IASB/FASB Conceptual Framework Project. Three reports from the group (authored by Kevin Simpkins) issued in March, September and December 2006 highlight a number of issues relevant to the reporting entity concept that the IPSASB will need to give particular attention to, including:
 - (a) when reporting should be necessary at a level below the ultimate controlling entity;
 - (b) whether and when it is appropriate for a core government entity to report;
 - (c) whether, when and how reporting at the level of Ministers (or equivalents) is appropriate;
 - (d) statutorily autonomous and independent entities in the public sector; and
 - (e) whether full consolidation is always appropriate for all entities within a group.
8. A number of national standard setters have also issued material that is relevant to this component of the project. For example, the Australian Accounting Standards Board has issued the Statement of Accounting Concepts SAC 1 *Definition of the Reporting Entity* and the UK Accounting Standards Board's *Statement of Principles for Financial Reporting* includes a chapter on the reporting entity.

**Australian Accounting Standards Board (AASB)
1 March 2007**