

Summary of comments

PAAinE Discussion Paper

Elements of the Framework Debate

The Conceptual Framework – Starting from the right place?

About the PAAinE

EFRAG and the European National Standard Setters have agreed to pool some of their resources and work together more closely so that Europe as a whole can participate more effectively in the global accounting debate. It was agreed that this initiative should in the beginning concentrate on long-term pro-active work. The objective of the initiative is to stimulate debate on important items on the IASB agenda at an early stage in the standard-setting process before the IASB formally issues its proposals. The initiative has the joint ambitions of representing a European point of view and exercising greater influence on the standard-setting process. This initiative is known as the 'Proactive Accounting Activities in Europe' (or PAAinE) initiative.

Several projects have commenced under the PAAinE initiative, and this paper was the result of the PAAinE project that relates to the joint IASB/FASB project on the Framework.

Work carried out under the PAAinE initiative can take a number of different forms and the full objectives of the initiative are:

- to stimulate, carry out and manage pro-active development activities designed to encourage the debate in Europe on accounting matters and to enhance the quality of the pro-active input to the IASB;
- to co-ordinate and resource monitoring work of IASB and FASB projects; and
- to try to ensure, as far as is practicable, that the messages Europe gives the IASB are consistent.

A further description of the PAAinE initiative is available on the EFRAG website (www.efrag.org).

A summary of the comments received in response to the PAAinE Discussion Paper on Elements of the Framework Debate: *The Conceptual Framework—Starting from the right place?*

Introduction

- 1 In late 2004 the IASB and the FASB ('the Boards') started a joint project on the conceptual framework for financial reporting. The objective of the project is to improve and converge the Boards' existing frameworks. It is envisaged that the project will take until at least until 2011 and probably later to complete.
- 2 The Framework project is of fundamental importance to global financial reporting and therefore to financial reporting by European entities. It follows that it is important that Europe participates fully in the global debate that it will create (and is already creating). With that in mind, the European National Standard-Setters and EFRAG decided—as part of their PAAinE initiative—to carry out work of their own on the Framework in order to stimulate timely debate on the subject within Europe, and thereby help Europe to be in a better position to participate actively and influentially in the global debate.
- 3 The first output of the PAAinE project was a discussion paper entitled 'The Conceptual Framework—Starting from the right place?'¹ The paper was used as a basis for discussion with a number of interested parties. Written comments on the paper were also invited, and twelve comment letters were received. A list of respondents is set out in Appendix 1 but, to summarise:
 - (a) Comments were received from:

• Preparers and representative bodies of preparers	1
• Users and representative bodies of uses	1
• Accounting firms	2
• Accountancy bodies	2
• Standard-setters	5
• Others	1
 - (b) The responses were received from the following geographic areas:

• Denmark	1
• Germany	1
• Italy	1
• Netherlands	2
• UK	4
• Pan-European	1
• Global	2
- 4 The purpose of this note is to summarise those comments. The summary is being published on the websites of the issuers of the PAAinE Discussion Paper and on the websites of some other European National Standard-Setters. It is also being

¹ The Discussion Paper was issued in October 2006 by the French standard-setter, the CNC (Conseil national de la comptabilité) and EFRAG. The paper (in near-final draft form) was considered at the quarterly meeting between EFRAG and representatives of the European national standard-setters in October 2006, and the representatives of the standard-setters confirmed that they were content for the paper to be issued.

sent to all those who were kind enough to respond in writing to the paper. We are very grateful to them for those responses.

Overview and summary

- 5 When the two Boards started working on their Framework project, they decided to break the project down into a number of phases. In July 2006, they issued a discussion paper on Phase A of their work (which dealt with the objectives of financial reporting and the desirable (or qualitative) characteristics of financial information). When the PAAinE Project Team (henceforth 'we')² looked at the Phase A work we thought it assumed a number of fundamental things that we thought needed to be debated. We therefore developed a paper that discussed some of those issues. Those issues were:
 - (a) The purpose and status of the revised framework
 - (b) Identifying the user needs that financial reports are intended to meet
 - (c) Type and size of entities within the scope of the revised Framework
 - (d) Extending the scope of the Framework to financial reports.
- 6 Respondents generally welcomed this initiative and thought the paper represented a useful contribution to the debate (although some thought it would have been better had the paper been issued earlier).
- 7 Respondents seemed generally to agree that the issues raised in the paper were appropriate issues to raise at this point in the debate. A number also expressed concerns about how the two Boards are structuring the Framework project. For example, FEE suggested that:

It would have been preferable if the IASB had developed an overview of the whole project, with a description of each phase and the related issues at stake, to clarify the long-term vision of the project. The separation into several phases makes it difficult to assess the implications of the concepts proposed. Moreover, discussions are made more complex without knowing the scope of the project. We suggest that the Board first discuss the role and purpose of financial statements today. Once all parts of the project have been dealt with, we suggest that the complete proposed Framework be exposed again for comment to reconsider decisions taken in the different phases.
- 8 One respondent (the DASB) was a bit concerned though that the PAAinE paper was a little unrealistic in what it expected of the IASB/FASB project:

In a number of instances we see the view expressed that further research is necessary. That is laudable but to be pro-active also means to be constructive. A certain level of common sense and pragmatism may be required in order to expedite projects. This may imply acceptance of the fact that further research is not always be possible on every position taken by IASB/FASB, at least not when you want to achieve a timely impact in the standards-setting process.
- 9 Perhaps the issue here is that there is some ambiguity as to what exactly the IASB/FASB project is trying to do. We had thought initially that it was seeking

² The project team is being led by staff of the French Standard-setter, the CNC, and is assisted in its work by a pan-European advisory panel. The panel comprises members from a variety of countries and backgrounds, and includes standard setters, academics, preparers, and auditors. A list of working group members is set out in Appendix 1.

simply to converge the two Frameworks and make some relatively uncontroversial changes to the Frameworks in the process; and we agree that in the context of such a project some of the PAAinE paper's calls for additional research might be unrealistic. However, the more thorough the IASB/FASB project becomes, the more reasonable we believe it is to carry out thorough research to support the assertions made.

- 10 Below we very briefly summarise the comments received on the PAAinE paper. A more detailed analysis of comments is set out in paragraphs 11 to 49.
- (a) The PAAinE paper discussed what the revised Framework's role ought to be in the preparation of financial statements, and it concluded that it should play a similar role as the existing IASB Framework does. In other words, it should be part of the hierarchy, but should not be mandatory or override existing standards. The vast majority of those commenting on this issue agreed with that conclusion.
 - (b) According to the two Boards, the revised Framework will guide them in their work but will not be mandatory. The PAAinE paper argued however that a Framework is most useful to the standard-setting process if the standard-setter is required to comply with it. A majority of those commenting on this issue agreed with that conclusion.
 - (c) The PAAinE paper concluded tentatively that there is little evidence that the information needs of investors and creditors encompass most of the information needs of other users of general purpose financial reports. It therefore questioned whether the notion of general purpose financial reporting was really valid. Six respondents commented specifically on this and five agreed with the PAAinE Paper.
 - (d) The PAAinE paper considers whether investors and creditors are a sufficiently homogeneous group to be used as the primary users and therefore as a key determinant of the information to be provided in the financial statements. The paper tentatively concludes that investors and creditors have different information needs. Respondents were fairly evenly split over this issue, with some saying investors and creditors did have different needs and that was a problem and the others saying that even if they did have different needs it was not a problem.
 - (e) The PAAinE paper invited views on whether the users of financial reports of small, large, listed and unlisted entities have similar needs. Four respondents thought they are the same, and four thought they are different. However, respondents generally did not seem to believe that, even if there were different user information needs, it meant a single Framework could not deal with all with all profit-oriented entities, regardless of size and accountable.
 - (f) The PAAinE paper discussed whether the scope of the IASB/FASB Framework work should be broadened to include the not-for-profit sector, and ending up not criticising the Boards' current focus just on the profit-oriented sector. The vast majority of respondents also supported the Boards' approach.
 - (g) Although the proposal is that the revised Framework will apply to financial general purpose financial *reporting* (rather than just general purpose financial *statements*), the IASB/FASB Discussion Paper proposes not to

define 'general purpose financial report' until later. The PAAinE paper criticised this proposal, arguing that, if the Boards wished their constituents to comment on the appropriateness of the paper's proposals, those constituents needed to know to which financial reports the Boards intended the proposals to apply. There was general agreement amongst respondents that the two Boards need to define the term now. There was also general agreement that, although it was a good idea to extend the scope of the Framework to include reports other than the financial statements, that should be done only after considering the implications more thoroughly than they have to date.

- (h) The PAAinE paper then went on to consider whether financial statements and other types of financial reporting have similar objectives and similar qualitative characteristics. The PAAinE paper's tentative conclusion on this was that further research was needed before a conclusion could be drawn about objectives, but the qualitative characteristics required did appear to be different. A wide variety of views were expressed by respondents on the first issue, but there seemed to be general agreement that the qualitative characteristics would differ.
- (i) The final issue the PAAinE paper considered was whether all kinds of financial reporting could be dealt with by the same framework. It tentatively concluded that financial statements and some other forms of financial reporting might have to be dealt with in separate frameworks. Respondents thought it depended very much on how 'financial reports' was defined and how detailed the Framework was.

Purpose and status of the revised framework

<i>Issue 1—What is the intended purpose and status of the revised Framework?</i>
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- 11 The IASB/FASB Phase A Discussion Paper contained an initial draft of what two of the chapters of the revised Framework might look like and asked for comments on that initial draft. Frameworks can be of use to standard-setters and/or in the preparation of financial reports, and they can be mandatory or non-mandatory. The PAAinE paper argued that the purpose and status of the revised Framework will be a factor in determining the content of the Framework and the level of detail involved, so to comment on whether the draft Framework was 'fit for purpose' it was necessary to know its intended purpose and status. It is therefore important that the Framework's purpose and status is made clear at an early stage in the project.
- 12 However, although the IASB/FASB Paper made it clear that the revised Framework was to be used to help the standard-setters as a guide, it stated that the role that the revised Framework would have in the preparation of financial statements would not be decided until later in the project.
- 13 The PAAinE paper criticised the two Boards for deferring this decision until later. It then considered what the revised Framework's role ought to be in the preparation of financial statements. It noted that, although the IASB's existing Framework plays a role in the preparation of IFRS-compliant financial statements because it is part of the IAS 8 hierarchy, FASB's existing Framework does not play an equivalent role in the preparation of FAS-compliant financial statements. The PAAinE paper tentatively concluded that the revised Framework should play a similar role in the preparation of financial statements as the existing IASB Framework does.

- 14 Nine respondents agreed with this tentative conclusion.³ The other two⁴ that commented on the issue thought that, in a financial reporting model based on high-level principle-based standards, the Framework (assuming it too is written at the right level and is principle-based) should act as a check to ensure that the financial statements reflect economic reality. In other words, the Framework should override IFRS where necessary. The CRUF, for example, said:

We believe that the framework should be used in the preparation of financial reporting to ensure that the accounts present the economic reality of the business rather than accounting or legal form. Both management and auditors need to be able to look to high-level principles in the conceptual framework to ensure that they can do so.

We do not share the concern that this may drive subjective interpretations. As users our concern is that company reporting should not become merely a compliance function but be one of communication. We welcome companies taking subjective decisions which ensure that their reporting more closely reflects the underlying economics of their business, rather than blindly reporting in accordance with detailed rules which may actually obscure the reality of their results.

Issue 2—Should the Framework be mandatory for standard-setters?

- 15 As already explained, the IASB/FASB Paper made it clear that the revised Framework was to be used by standard-setters as a guide. The PAAinE paper considered whether it would be preferable for the revised Framework to be mandatory for standard-setters. It tentatively concluded that a Framework is most useful to the standard-setting process if the standard-setter is required to comply with it.⁵
- 16 Seven⁶ of the twelve respondents agreed with this tentative conclusion. Several of them argued that the need to deviate from the Framework would depend on the level of detail at which the Framework is written. For example:
- [Revising the Framework (FW)] would not be necessary if the FW is built on a theoretical basis that only takes accounting principles into account. BY doing so, the FW will not be as detailed as now, but it will be able to last longer without any need for modification. (FSR)
- 17 Two other respondents also thought it depended on the level of detail involved.
- (a) Grant Thornton thought the revised Framework proposed in the IASB/FASB Paper was “not well suited to entities that do not have public accountability”. Therefore, if changes are not made to make it more suited to such entities, it should not be mandatory for standard-setters.

³ Hundred Group, OIC, PricewaterhouseCoopers, SR, UK ASB, ICAEW, FEE, DRSC and DASB.

⁴ CRUF and Pieterse van Wijck

⁵ The PAAinE paper did say that standard-setters should be allowed to diverge from the Framework, though only if the exception was both temporary (because the standard-setter has given a commitment to revise the Framework to eliminate the inconsistency) and infrequent (ie the Framework should not be subjected to frequent change).

⁶ Hundred Group, OIC, FEE, DASB, PricewaterhouseCoopers, DRSC and FSR

- (b) In the CRUF's view, a truly high-level principle-based Framework should be mandatory for standard-setters. However, "if what is on offer is detailed, prescriptive and impenetrable to the average reader of accounts, then we have strong reservations about mandatory status." The CRUF does not comment on into which category it believes the proposed revised Framework set out in the IASB/FASB Paper falls.

- 18 The UK ASB stated that it fundamentally disagreed with the conclusion that to be effective a Framework should be mandatory for standard-setters.

New thinking in accounting often occurs when new problems or innovative transactions are being analysed. Such new thinking is often incorporated in new standards and it is only over time that the framework is revised to reflect such changes. To make the framework mandatory will mean that such changes will need to be reflected in the framework before any new standards may be issued, making the whole process extremely cumbersome. It is therefore not pragmatic to consider that all standards will be in line with the framework at all times.

The ICAEW had similar concerns.

Identifying the user needs that financial reports are intended to meet

- 19 Put very simply, the objective of preparing a financial report is to provide information that is useful. It follows that, in order to decide what form a financial report should take and what information it should provide, it is necessary first to decide which information needs the report should be attempting to meet. Typically this involves asking:

- (a) Who are the users of the financial report?
- (b) What are the information needs of those users?
- (c) Which of those information needs is the financial report intended to meet?

- 20 When we studied the IASB/FASB Phase A Framework Discussion Paper, we found much of the material about users, users' information needs and the objectives of general purpose financial reports unconvincing. The PAAinE Paper focussed on just two of the concerns we had.

- (a) With barely no discussion the paper introduced the notion of 'general purpose financial reports', asserted that financial statements prepared in accordance with the EU Accounting Directives (hereafter 'statutory financial statements') are an example of such reports, and assumed that a single set of general purpose financial statements can meet the information of a wide variety of users of general purpose financial reports. The PAAinE Paper asked whether these assumptions about general purpose financial statements are valid.
- (b) The IASB/FASB Discussion Paper noted, reasonably in our view, that information that meets the needs of investors and creditors is also likely to be useful to other users, but then drew two much more contentious conclusions from that.
 - (i) As investors and creditors have a common interest in the ability of an entity to generate net cash flows, it follows that information about that ability is the primary focus of financial reporting because it helps satisfy the needs of investors and creditors.

- (ii) By focusing primarily on the needs of present and potential investors and creditors, the objective of financial reporting encompasses the needs of a wide range of users.

The PAAinE paper considers whether investors and creditors are a sufficiently homogeneous group to be used as the primary users.

Issue 3: The validity of the Boards' assumption that a single set of financial statements can meet the information needs of a wide variety of users

- 21 The third issue discussed in the PAAinE paper relates to the validity of the Boards' assumption that a single set of financial statements can meet the information needs of a wide variety of users. We think that, if there is little overlap between the information needs of the various users who cannot satisfy their information needs through special purpose reports (general purpose financial report users), it follows that the notion of a general purpose financial report is an unrealistic one. However, the IASB/FASB Phase A Discussion Paper suggested that, by focusing primarily on the needs of investors and creditors, the objective of financial reporting encompasses the needs of a wide range of users. We wondered whether evidence exists to support this assertion.
- 22 The PAAinE paper concluded tentatively that there is little evidence that the information needs of investors and creditors encompass most of the information needs of other users of general purpose financial reports.
- 23 Six respondents commented specifically on this and five (Grant Thornton, OIC, PricewaterhouseCoopers, FSR and FEE) agreed with the PAAinE Paper. However, one (the ICAEW) did not:

We disagree with the tentative views expressed in the discussion paper, which express scepticism as to both general purpose financial statements and the identification of actual and potential investors and creditors as their key users (3.2.15). While we accept that different users' needs may well diverge, it would not be feasible to prepare a different set of financial statements to meet every different set of users' needs. For that reason, general purpose statements are practically inevitable.

Issue 4—Are investors and creditors sufficiently homogenous to be used as the primary user group?

- 24 The IASB/FASB Phase A Discussion Paper identified investors and creditors as the primary users. The PAAinE paper considers whether investors and creditors are a sufficiently homogeneous group to be used as the primary users and therefore used as a key determinant of the information to be provided in the financial statements. The paper argues that this is an important question because focusing on users that do not have the same information needs could result in conflicting or at least sub-optimal decisions being taken as to the type of information that needs to be provided and the attributes it should possess.
- 25 The Paper's tentative conclusions on this issue were that:
 - (a) although investors and creditors have some common information needs, for some types of investor and creditor the focus is different; and that means the information needs could be different.

- (b) it would be preferable to focus the financial statements on a group of users that have common information needs. These users should include investors, but could include other user groups if research indicates that they have the same information needs as investors.

- 26 Six respondents⁷ agreed with the tentative conclusion in the PAAinE Paper that, if a type of user is to be included as part of the primary user group, that type of user should have similar information needs to those of the other primary users.

With respect to the definition of the primary user group we think homogeneous information needs are of fundamental importance. Otherwise it is not possible to reach unambiguous conclusions, i.e. deduce appropriate accounting policies. We therefore prefer a definition which does not include different user groups. In our view investors and creditors are not homogeneous user groups. They have different interests and different information needs. (DRSC)

- 27 However, five respondents⁸ thought investors and creditors can be treated as the primary users even if their information needs are not homogenous.

We disagree with the premise of this question: that the primary users of financial statements have to be homogeneous (3.4). Clearly it is easier to meet the needs of a group of homogeneous users, but primary users are primary users whether their needs are homogeneous or heterogeneous. A more important issue in our view is whether the framework is sufficiently broadly based to meet an acceptable range of needs of a spectrum of users. (ICAEW)

- 28 Grant Thornton thought the primary user group issue was relevant only if a proprietary perspective is being applied.

- 29 Perhaps inevitably because of the views summarised above, there was a wide variety of views as to which users should be identified as primary users.

- (a) Three respondents favoured 'investors and creditors' (the Hundred Group, PricewaterhouseCoopers and the ICAEW), although the ICAEW thought the primary users might be different for owner-managed companies.
- (b) FEE did not support 'investors and creditors', but did not indicate who it thought the primary users should be.
- (c) Three respondents supported 'investors' (CRUF, DRSC, and DASB). The CRUF argued that, although reporting which focuses on the needs of equity owners would not *meet* the needs of all users, it would still *serve* their needs:

We believe that reporting which focuses on the needs of equity owners serves the needs of all stakeholders. Because groups such as creditors, employees, suppliers and so on enjoy other protections under contractual or other specific legal rights, reporting which serves the interests of the shareholders – which do not enjoy such additional protections and so are most economically exposed to all aspects of company performance – will also serve the needs of other stakeholders. Financial reporting which tries directly to address the needs of all stakeholders is liable to produce a lack of clarity; stakeholder interests will be better served by narrative reporting which more directly addresses their various concerns. We believe that reporting from an entity perspective can support and add

⁷ OIC, FSR, FEE, CRUF, Pieterse van Wijck, and DRSC.

⁸ Grant Thornton, PricewaterhouseCoopers, ASB, ICAEW, and DASB.

value to reporting from a parent perspective, but we do not believe it would be a substitute for such reporting.

To summarise, we believe that accounts designed to meet the needs of all stakeholders would tend to obscure more than they reveal and that the reporting needs of stakeholders will best be met in practice by reporting which focuses on the needs of equity owners. We favour the parent approach as the principal approach but we recognise that reporting from an entity perspective can provide additional insights.

- (d) A further two respondents (OIC and FSR) thought the primary users should be investors plus any other user group that research shows to have the same information needs as investors.
- (e) Pieterse van Wijck thought that, *if* it is worth identifying a primary user group, perhaps the focus could be on users with the greatest risk:

The issue is whether or not a distinction can be made between primary and non primary users. It can be suggested that the distinction could be based on the risk perspective of the various users. If the group with the highest risk is designated as primary users, i.e. as the group which has the highest need for information in order to assess their risk, a new element comes up. If the information needs of the primary users are met, are in that case the information needs of all other resource providers met as well? It is beyond the scope of this document to address that question.

- (f) The UK ASB thought further research was needed before a decision should be taken as to which users are to be treated as the primary user.
- (g) Grant Thornton argued it was not necessary to identify a primary user group.

We believe that the entity perspective and general purpose financial statements for all stakeholders is a valid concept and should be a core feature of a conceptual framework. The core of an entity perspective is that there are certain commonalities in all financial statements based on accounting records, regardless of the type of entity. The common need of all users could be described in terms of a degree of transparency into the books of the reporting entity and thereby into the financial position of the entity, the operations of the reporting entity and the results of operations. Those common needs have been expressed in the objective in the SME Exposure Draft as: "information about the financial position, performance and cash flows of the entity that is useful for economic decision-making." Under an entity approach, the content of the information in financial statements could be independent of the intended use by an unspecified user. We believe that this is the original meaning of the term general purpose financial reporting.

We acknowledge, however, the objective in the Preliminary Views document, with its focus on information about future cash flows to inform resource allocation decisions by investors and creditors, is *de facto* a proprietary perspective. The central argument for the proprietary perspective is that the content of the information should be dependent on the intended use of the information. Therefore, it is necessary to define a specific user.

It is not clear whether such financial statements should still be considered to be general purpose financial statements. The FASB and IASB have tried to make that case in the Preliminary Views document: nearly half of chapter one consists of arguments to establish that financial reporting based on a proprietary perspective still qualifies as general purpose

financial reporting (paragraphs OB3-OB15). Those arguments are to a large degree based on the unproven assertion that information that meets the needs of investors and creditors (narrowly defined) for resource allocation decisions will meet the needs of other users. If one accepts those arguments, then we believe that this will create a different meaning of the term general purpose financial reporting. If a proprietary perspective is adopted, then general purpose financial statements in the traditional sense may not be a valid concept going forward.

Type and size of entities within the scope of the revised Framework

- 30 As already explained, general purpose financial reports are prepared to provide information that is useful, and information is useful only if it meets one or more needs. It follows from this that the objective of a general purpose financial report and the characteristics that good financial information is expected to exhibit might vary depending on the information needs it is intended to meet.
- 31 We *think* the information needs of users might vary depending on the type of entity involved. Following the logic of the previous paragraph, this could have implications for the objectives of general purpose financial reporting and the qualitative characteristics of good financial information.

<i>Issue 5: Does the size of the entity or whether it is publicly accountable matter?</i>

- 32 The IASB/FASB Phase A Discussion Paper envisages a single Framework for all profit-oriented entities, regardless of size and whether the entity is publicly accountable. As different user information needs might have implications for the objective of general purpose financial reporting and the qualitative characteristics, the PAAinE paper invited views on whether the users of financial reports of small, large, listed and unlisted entities have similar needs.
- 33 Seven respondents specifically commented on whether the information needs of users were the same regardless of the size or accountability of the entity.
- (a) Four (Hundred Group, Pieterse van Wijck, DASB and the CRUF) thought the information needs of users are the same.

The users of financial reporting of small, large, listed and unlisted entities will have in general similar information needs. However, the specific information needs of users will differ as do the accounting resources and expertise available to the reporting entities involved will differ. These differences need to be addressed during the standard setting process. During the standard setting process the balance should be struck between costs and benefits for certain types of entities: simplifications and approximations that are necessary for certain types of entities seem less necessary for others. (DASB)

- (b) Four (FSR, FEE, DRSC and ICAEW) thought they are different.

Users of financial reporting of listed entities usually have greater needs for detailed information from the financial statements than do users of unlisted entities. This is mainly because of the controlling effect of the financial statement. The financial statement is audited, which means that all financial information given by the entity throughout the year will be indirectly proved by the independent auditor when the financial report is prepared. Unlisted entities are not forced to, and normally do not, release information during the year. Furthermore, they usually only have one or a few investors who often are also members of the board of directors or

even managing the entity. Of course, these kinds of investors get the information they want from the entity, and in the form they want it. Thus, rules to fulfil their needs are not necessary. (FSR)

We think that different user groups have different information needs, as the decisions these different user groups have to make are dissimilar. Consequently, the most favourable information system for one user group will not be most favourable for another user group. Nevertheless, information given under one user group's most favourable information systems contain also information meeting the information needs of other user groups too. (DRSC)

- (c) Grant Thornton thought whether the information needs of users were the same regardless of the size or accountability of the entity would depend on the perspective adopted.

Under a proprietary perspective, we consider that the needs of users of financial statements of larger, listed companies differ from those of smaller, unlisted companies. Shareholders in listed companies are constantly making resource allocation decisions. Thousands or millions of shares may be traded on any given day that markets are open. The users of smaller, unlisted companies make also make resource allocation decisions, but typically much less frequently.

Our answer may change if one adopts an entity perspective. We believe that under an entity perspective, the needs of users of general purpose financial statements of small, large, listed and unlisted companies are fundamentally the same. However, the costs and benefits of providing that information may not always be the same and should be taken into consideration by standard setters when establishing reporting requirements.

- 34 However, respondents generally did not seem to believe that, even if there were different user information needs, it meant a single Framework could not deal with all with all profit-oriented entities, regardless of size and accountable. For example, nine respondents⁹ thought a single Framework could deal with all such entities. Having said that, some of those did add caveats:

- (a) the ICAEW also said the Framework would “need to recognise differences in user needs and cost-benefit outcomes for different types of entity. The OIC made a similar point;
- (b) the Hundred Group thought it necessary for the Framework to be at a “suitably high level”. The FSR made a similar point, referring to the need for the Framework to be “made on a theoretical foundation” and not too detailed; and
- (c) the Hundred Group thought the Framework should focus on publicly listed entities to begin with. In a similar vein, the DRSC suggested the focus initially should be listed companies: “potential differences for small and medium sized entities should be discussed further.” The CRUF also suggested focusing initially on listed entities.

⁹ ICAEW, OIC, CRUF, PricewaterhouseCoopers, Pieterse van Wijck, DASB, DRSC, Hundred Group and DRSC.

Issue 6: Not-for-profit entities

- 35 There has been much discussion about whether the IASB/FASB Framework work would benefit from being focused on both the profit-oriented and the not-for-profit sectors. We wondered whether that would actually be possible in a single Framework, because users of financial reporting of profit-oriented and non-profit oriented entities might not similar information needs.
- 36 However, although the PAAinE paper discussed the issue, it was rather inconclusive. It did though agree that the IASB/FASB Phase A Paper's focus on profit-oriented entities is consistent with the IASB's objective of helping participants in the world's capital markets in their decision making and reflects the priority given to profit-oriented entities in the IASB's standard setting activity.
- 37 Eight respondents agreed with this tentative conclusion (and therefore the approach adopted in the IASB/FASB Phase A Discussion Paper).¹⁰ Of those:
- (a) the CRUF went on to suggest that there might be lessons to be learned from not-for-profit entities that might improve the Framework for profit-oriented entities; and
 - (b) Grant Thornton suggested that whether it would be possible to extend the scope of the Framework to include not-for-profit entities would depend on the perspective on which the Framework is based.
- 38 The UK ASB disagreed with the PAAinE and IASB/FASB tentative conclusion; in its view the Framework should cover both types of entity.

Although we agree that a focus on profit-oriented entities would "avoid diluting the reporting requirements" however, we firmly believe that a framework should be sufficiently broad based to meet the general needs of not-for-profit entities as well. We acknowledge that in doing so some principles would need to be re-expressed and others would need a change of emphasis before they can be applied to that sector. As you are aware, the ASB is collaborating with a group of national standard setters in a project that considers the implications of the IASB/ FASB conceptual framework project for the not-for-profit and public sectors. This project has followed the IASB's debate at each phase of the project and provides direct input to the IASB staff and Board on the potential implications for not-for-profit and public sectors.

- 39 Pieterse van Wijck argued that the purpose of financial reporting is to report on the outcome of reporting entity's conversion of inputs into outputs. Thus users' information needs are the same regardless of whether or not the entity is profit-oriented.

The distinction 'profit or non-profit oriented' is merely a distinction in purpose of the conversion and exchange process the entity is engaged in. In profit oriented entities that purpose is clear: profit. And profit is exactly the reward some resource providers are fully dependant on and their reward is thus fully at risk. In a non-profit oriented entity the purpose is not clear, it might be anything. But whatever the purpose, the same reasoning can be applied: it is the achievement of the purpose that is at risk for those resource providers whose reward depends on just that achievement.

¹⁰ Hundred Group, OIC, FEE, PricewaterhouseCoopers, Grant Thornton, DRSC, DASB and CRUF.

Users of financial reports of profit and non-profit oriented entities have similar needs. All want to be informed on the achievement of the purpose of the conversion and exchange process in relation to their risk.

Extending the scope of the framework to financial reports

Issue 7: Does 'financial reports' need to be defined now?

- 40 The existing IASB Framework sets out the concepts and principles to be applied in the preparation of financial general purpose financial *statements*; the IASB/FASB Discussion Paper proposed to extend this scope to include other types of general purpose financial *report*. However, although the IASB/FASB Discussion Paper acknowledges that 'general purpose financial report' is a very broad term that encompasses for example press releases, it states that the Boards will not decide until later to which types of financial report the revised Framework should apply.
- 41 We found the Boards' logic here difficult to follow. It seemed to us that it was self-evident that some financial reports (for example some press releases that include financial information) have very different objectives to some other financial reports (for example statutory financial statements), and it was also possible that the information provided in different types of report would need to exhibit different qualities in order to be useful. Therefore, it seemed to us that, if the Boards wished their constituents to comment on the appropriateness of the paper's proposed objective for all general purpose financial reports and proposed single set of qualitative characteristics, those constituents needed to know to which financial reports the Boards intended the proposed revised Framework to apply. With those thoughts in mind, the PAAinE paper explored the issues involved further.
- 42 Respondents generally found the issues set out below difficult to discuss without making some assumptions about which 'financial reports' would be included within the scope of the revised Framework. For that reason there was general agreement amongst respondents that the two Boards need to define the term now, rather than leave the term undefined until a later phase of the project, and that, although it was a good idea to extend the scope of the Framework to include reports other than the financial statements (only FEE seems to disagree with this), that should be done only after considering the implications more thoroughly than the Boards' Discussion paper does.
- 43 PricewaterhouseCoopers went further, suggesting that what was needed was a fundamental review of the corporate and financial reporting models.

Companies today face a multiplicity of corporate reporting requirements. At the same time, on a voluntary basis, companies increasingly use and site financial information in those parts of their communications where they consider investors will find it most useful and accessible.

Further, our country and industry-specific research has shown that the measures that both management and investors regard as important are not just financial measures but also non-financial measures. This type of contextual information is becoming as important to the market as the more traditional financial data.

For these and other reasons, we suggested the Boards should consider:

1. The need for a framework for the whole corporate reporting model, rather than simply financial reporting

2. The need to develop a view of the future corporate reporting model by understanding investors' expectations
3. The need to address the purpose of the primary statements
4. The need for a consistent set of global corporate reporting standards that are founded on broad principles.

Issue 8: Do all general purpose financial reports have similar objectives and similar qualitative characteristics?

- 44 The eighth issue the PAAinE paper considered was whether financial statements and other types of financial reporting have similar objectives and similar qualitative characteristics. The PAAinE paper's tentative conclusion on this was that further research into users' information needs is required to clarify whether the objectives of financial statements are compatible with those of other forms of financial reporting.
- 45 Of the respondents that commented on this issue, only the Hundred Group seems to believe that the objective for general purpose financial reporting proposed in the IASB/FASB Phase A Discussion Paper did or might apply to all general purpose financial reports.
- (a) Both Pieterse van Wijck and the CRUF suggested that a single objective might apply to all general purpose financial reports, though not the objective set out in the Boards' paper. The CRUF suggested the objective should be to provide information that helps decision-making by investors; and Pieterse van Wijck suggested it should be to report on the outcome of reporting entity's conversion of inputs into outputs.
 - (b) The FSR thought different financial reports have different objectives, although financial statements and management commentary have the same objective. .
 - (c) The OIC agreed with the PAAinE paper's tentative view that more research into the issue is needed.
- 46 The PAAinE paper also tentatively concluded that the desirable characteristics of financial information provided by financial statements are different from the desirable characteristics of financial information provided by other forms of financial reporting. For example, other forms of financial reporting, such as management information, are more subjective or entity specific and therefore would probably not have the same comparability or satisfy the "faithful representation" characteristic.
- 47 Of the respondents that commented on this, only Pieterse van Wijck seemed to suggest that the qualitative characteristics for financial information proposed in the IASB/FASB Phase A Paper might apply to all general purpose financial reports.

Financial reporting of all types will have similar qualitative characteristics, because all these types of financial reporting have a similar objective: portray reality. Qualitative characteristics are in actual fact requirements that must be met in order to reach the desired quality of the view of reality. It may well be, that, if a financial report is aimed at one (or a limited number of the) aspect(s) of the outcome of the conversion and exchange process, a certain characteristics is of more importance than it is in a report on another aspect.

- 48 Although the Hundred Group thought the management commentary was an example of a financial report to which different qualitative characteristics probably applied, the FSR and FEE suggest that the same qualitative characteristics applied to both.

Issue 9: Can all kinds of financial reporting be dealt with by the same framework?

- 49 The final issue the PAAinE paper considered was whether all kinds of financial reporting could be dealt with by the same framework. It is of course difficult to answer this question when it is not known what form the Framework will eventually take or what the term 'financial report' will eventually be defined to mean. Nevertheless, the PAAinE paper's tentative conclusion was that financial statements and some other forms of financial reporting might have to be dealt with in separate frameworks.
- (a) The OIC agreed with the PAAinE paper's tentative conclusion.
 - (b) The Hundred Group thought it likely that all kinds of financial reporting can be dealt with in a single Framework if 'financial reporting' is narrowly defined. The FSR and DRSC thought that if 'financial reports' is defined to include just financial statements and management commentary then a single Framework would suffice.
 - (c) The CRUF thought a single Framework would be appropriate only if it is high-level and principles-based "and, we would argue, if it uses concepts which are already well understood". Similarly, Pieterse van Wijck thought that, as there is a "common objective, ie provide a view of reality, all kinds of financial reporting can be dealt with by the same framework."
 - (d) PricewaterhouseCoopers favours a single framework and argues that such a Framework could underpin the preparation of the standards and guidance to support principles necessary to cover all communications needed to ensure the efficiency and effectiveness of the markets.

Appendix 1

List of respondents

Letters of comment were received from the following respondents:

Preparers and representative bodies of preparers

- The Hundred Group of Finance Directors (UK)

Users and representative bodies of users

- The Corporate Reporting Users' Forum (CRUF) (UK)

Accounting firms

- Grant Thornton (Global)
- PricewaterhouseCoopers (Global)

Accountancy bodies

- Fédération des Experts Comptables Européens (FEE) (Pan-European)
- The Institute of Chartered Accountant in England and Wales (ICAEW) (UK)

Standard-setters

- Accounting Standards Board (UK ASB) (UK)
- Deutsches Rechnungslegungs Standards Committee (DRSC) (Germany)
- Foreningen af Statsautoriserede Revisorer (Denmark)
- Organismo Italiano di Contabilita (Italy)
- Raad Voor De Jaarverslaggeving (Netherlands)

Others

- P A Pieterse Van Wijck (Netherlands)

Appendix 2 Acknowledgements

This note has been prepared by the PAAinE Framework Project Team, which is led by staff of the French standard-setter, the CNC. The Team comprises Jerome Chevy and Philip Staines, who are both members of the CNC's staff, and Sigvard Heurlin, who is a member of EFRAG's staff.

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Mr Paul Ebling	Staff member of EFRAG	
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Mr Rolf Uwe Fülbier	WHU Otto Beisheim School of Management, StB Prof. Dr.	Germany
Ms Seema Jamil-O'Neil	Staff member of UK Accounting Standards Board	UK
Mrs Alicja Jaruga	University of Lodz, Professor Dr h.c	Latvia
Mr Steinar Sars Kvitte	Ernst & Young, Partner	Norway
Mrs Aurelija Lauruseviciute	The Institute of Accounting of the Republic of Lithuania, Senior expert of accounting	Lithuania
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