

29 September 2008

Sir David Tweedie, Chairman
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Dear Sir David:

**Exposure Draft of An improved Conceptual Framework for Financial Reporting:
Chapter 1—The Objective of Financial Reporting
Chapter 2—Qualitative Characteristics and Constraints of Decision-useful Financial
Reporting Information**

Deloitte Touche Tohmatsu is pleased to comment on the Exposure Draft of *An improved Conceptual Framework for Financial Reporting* (“the ED”).

As we indicated during the Discussion Paper phase of this project, we support the global convergence of high quality financial reporting. To achieve this outcome, it is important to have a well established conceptual framework which underpins accounting standards and standard setting activities. As capital markets become increasingly complex and global, the conceptual framework will become a critical element in developing meaningful accounting standards which provide useful information to the marketplace. We commend the efforts that the Board has made to develop a mutually agreeable high quality conceptual framework to meet this high hurdle.

We wish to acknowledge that in our opinion, the proposed Framework as expressed in the ED has been significantly improved from the Discussion Paper phase of this project. We find the proposed Framework is now well organised and we generally agree with the notions expressed therein. More specifically, we agree with the dual focus of the expressed objective of financial reporting on both cash flow generation and management stewardship and also agree that decision useful information has several qualitative characteristics of which relevance and faithful representation are the most fundamental. However, we think that comparability, verifiability, timeliness and understandability are supporting components (not ‘enhancing characteristics’) that need to be present to render financial information relevant and representationally faithful. In addition, there are certain aspects of the proposed Framework which we continue to believe may be enhanced. We have included our comments on these aspects in the Appendix to this letter.

Please note that, given there are other phases of the proposed Framework that have not yet been undertaken and/ or are still in progress, it is possible that our views on the two chapters in this phase might continue to evolve.

We believe that the individual chapters of the conceptual framework should not be finalised (or at least not made effective) until all of the chapters are finalised to ensure that the overall Framework forms a cohesive set of principles.

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Re: Exposure Draft: *An Improved Conceptual Framework for Financial Reporting (Chapters 1 and 2)*

The Appendix to this letter contains our responses to the questions raised in the Invitation to Comment accompanying the Exposure Draft.

We appreciate the opportunity to comment on the Exposure Draft. If you have any questions concerning our comments, please contact Ken Wild in London at +44 (0) 207 007 0907.

Yours truly,

A handwritten signature in black ink, appearing to read "Ken Wild", written over a horizontal line.

Ken Wild
Global IFRS Leader

APPENDIX
Deloitte Touche Tohmatsu
Reponses to IASB's Invitation to Comment

Chapter 1: The Objective of Financial Reporting

Question 1: The boards decided that an entity's financial reporting should be prepared from the perspective of the entity (entity perspective) rather than the perspective of its owners or a particular class of owners (proprietary perspective). Do you agree with the boards' conclusion and the basis for it? If not, why?

We support the notion that information provided by general purpose financial reporting should focus on the needs of all capital providers, and not just those of a particular group. Based upon the arguments presented in the ED, we support the Board's decision that financial reports should reflect the perspective of the entity.

However, we believe that the discussion supporting the selection of the "entity approach" should be enhanced further. Given that the decision to adopt the entity approach is a fundamental choice, we believe that more analysis is required to support its superiority over other approaches, in particular the proprietary and parent approaches.

We would encourage the Board to explain more clearly what the fundamental principles of each approach are; the benefits and consequences of each approach; and a reasoned conclusion as to why one is better than the others. If it is not included in Chapters 1 or 2, we think this discussion should be undertaken in another chapter of the Framework.

Question 2: The boards decided to identify present and potential capital providers as the primary user group for general purpose financial reporting. Do you agree with the boards' conclusion and the basis for it? If not, why?

The ED notes that while there are various types of users of general purpose financial reporting, it is necessary to identify a primary user group. The Board has expressed that in their view, capital providers have the most critical need for financial information because they have provided economic resources to the entity in exchange for an interest in those resources. We agree with the conclusion that capital providers represent the primary users of general purpose financial reporting due to the nature of their relationship with the entity; that is, that they are seeking to obtain a return on as well as a return of their investment. We also agree that this primary user group does not have sufficient access to an entity's records to obtain the information needed to meet their needs. Accordingly, standard-setting should be performed keeping the needs of this user group foremost in mind. We also agree that the primary user group should include both present and potential capital providers. The identification of a primary user group represents a significant improvement in the proposed framework since the Discussion Paper phase.

However, we believe that the definition of the users of financial information could still be enhanced. While it is true that other users of general purpose financial reporting, such as governments, customers and suppliers would likely find information directed at capital providers to be useful for their needs as well, we disagree that their need is not as direct or immediate as that of capital providers. In our opinion, while it is important to satisfy the primary user group, financial information might end up being less balanced if the Framework does not give consideration to the needs of other potential users.

We recommend that the Board consider noting that there is a second class of users consisting of non-capital providers which should also be considered in financial reporting. We think the Framework should note that the primary goal of standard-setting should be to satisfy the needs of the primary user group; where a board are choosing between one or more alternatives on a particular matter, and all the alternatives would provide useful information for the primary user group, it should specifically consider and place weight on whether any of the alternatives appears clearly superior in the information it provides for users in other groups. We believe that consideration of the needs of other users will actually result in more complete information for the primary user group, as information that is important to the secondary users will likely be meaningful to capital providers as well.

Question 3: The boards decided that the objective should be broad enough to encompass all the decisions that equity investors, lenders and other creditors make in their capacity as capital providers, including resource allocation decisions as well as decisions made to protect and enhance their investments. Do you agree with that objective and the boards' basis for it? If not, why?

We are very supportive of the changed emphasis in the ED (as compared to the Discussion Paper) that decision-useful financial reporting helps users to assess more than just an entity's cash flow prospects. We agree that decision useful information also enables users to assess management's performance in discharging its responsibilities with respect to protecting an entity's economic resources, ensuring their efficient and profitable use and ensuring an entity complies with applicable laws, regulations etc.. The ED recognises that capital providers are interested in both how much return their resources can be expected to generate as well as how well their resources are being protected and better ensures that financial reporting will provide the information that users need to make a wide range of decisions.

We do believe however, that the Framework would be enhanced by acknowledging explicitly that financial statements should reflect the business model followed by management. We think that information presented from this perspective is important to users who are trying to assess management's performance.

Other Comments on Chapter 1

Focus on General Purpose Financial Reporting

The ED proposes that the Framework will apply to general purpose financial reporting which includes, but is not limited to, general purpose financial statements. However, what falls within the scope of financial reporting has not yet been defined. The Board has acknowledged that the term 'financial reporting' is very broad, and could include a range of reports such as management commentary, press releases and forecasts, amongst others. Given the nature of these reports is so different, we are not certain that the proposed Framework would be equally suitable to each one. Accordingly, once the scope of financial reporting is defined, the Board may have to revisit the conclusions reached in Chapter 1 and 2 to ensure they remain appropriate.

Until such time as the boundaries of general purpose financial reporting are defined, we would encourage the Board to be explicit when setting IFRSs as to whether a standard addresses general purpose financial statements or general purpose financial reporting. Where a standard is meant to address the latter, the Board should be specific as to that scope.

Chapter 2: Qualitative Characteristics and Constraints of Decision-Useful Financial Reporting Information

Question 1: Are the distinctions – fundamental and enhancing qualitative characteristics and pervasive constraints of financial reporting – helpful in understanding how the qualitative characteristics interact and how they are applied in obtaining useful financial reporting information? If not, why?

Do you agree that (a) relevance and faithful representation are fundamental qualitative characteristics (b) comparability, verifiability, timeliness and understandability are enhancing qualitative characteristics and (c) materiality and cost are pervasive constraints? If not, why?

In our opinion, it is correct to classify relevance and faithful representation as ‘fundamental’ and therefore in some sense, more important than other characteristics such as timeliness or comparability.

However, we do not agree with the ED’s characterisation of comparability, verifiability, timeliness and understandability as ‘enhancing’. The Board’s proposal frames these characteristics as desirable but not necessarily required: in our view, each one of the ‘enhancing’ characteristics is actually a supporting component of relevance and faithful representation.

We understand that there are complex relationships amongst all of the characteristics and their interactions with one another in producing decision useful information. However we believe it would be rare for high quality information not to be, for example, verifiable or understandable at all. We believe the Framework would be improved by referring to these characteristics as ‘supporting components’ of relevant and faithfully representative information that would be expected to be present in almost all cases. We would encourage the Board to state explicitly that all of these supporting components need to be present—it would be inappropriate to forgo completely any one qualitative characteristic in favour of achieving the others because the resultant information would be unlikely to be relevant to users or faithfully representative of underlying economic phenomena.

Pervasive Constraints

We agree with the view that materiality and cost are pervasive constraints on financial reporting. However, we believe that they do not have the same effect on financial reporting and therefore should be described differently in the Framework. We elaborate this comment in our response to Question 4 below.

Question 2: Are the fundamental qualitative characteristics appropriately identified and sufficiently defined for them to be consistently understood? Are the components of the fundamental qualitative characteristics appropriately identified and sufficiently defined for them to be consistently understood? If not, why?

We agree that relevant information is information that is capable of making a difference in the decisions made by users. We note that we have recommended above that the Board considers broadening the concept of ‘users’ in the Framework – accordingly, relevant information, in our opinion, could be information that could affect the decisions of more than just the capital providers. We also agree that relevant information has both confirmative and predictive value

We are supportive of the conclusion that information that is a faithful representation of an underlying economic phenomenon is complete, neutral and free from bias. However, we believe the notion expressed in QC11 that “some minimum level of accuracy is also necessary for an estimate to be a faithful representation” could be enhanced further, and seems slightly at odds with the previous sentence, which refers to appropriate inputs, etc. It would be helpful for the Board to clarify what level of uncertainty renders information unable to achieve a faithful representation.

Question 3: Are the enhancing qualitative characteristics appropriately identified and sufficiently defined for them to be consistently understood and useful? If not, why?

We have noted above that we do not agree with the Board’s characterisation of comparability, verifiability, timeliness and understandability as ‘enhancing’ because we believe that each of these characteristics is in fact a supporting component of relevance and faithful representation.

Therefore, we would encourage the Board to consider adding wording to the Framework which states clearly that the absence of any one qualitative characteristic entirely would not be appropriate. For example, we do not believe that information that is not at all verifiable, even if it meets the other qualitative thresholds, could be considered useful to financial statement users. The ED cites management estimates as one example of information that is not always verifiable but in our opinion, estimates when based on economic data or established modelling techniques can still be assessed for reasonableness; they are therefore still verifiable. If information was altogether unverifiable i.e. could not even be assessed for reasonableness, we believe it would not meet the relevance/faithful representation threshold. In the same way, we believe the other qualitative characteristics have an equally important role to play and a single characteristic cannot be completely forgone.

We also recommend that the Board clarifies in the Framework which type of user is being contemplated in the standard-setting process because in our opinion, the ED is not well defined in this regard. In QC24, the Board has noted that “Users of financial reports are assumed to have a reasonable knowledge of business and economic activities and to be able to read a financial report. In making decisions, users should review and analyse the information with reasonable diligence”. We agree that the assumed level of sophistication of users should be as noted above – that is, that users, though not necessarily accounting experts, are assumed to be intelligent, financially literate individuals who can understand financial information. We believe this notion of the theoretical user is a very important anchor for the Framework that applies to all of the qualitative characteristics, not just understandability and should therefore be well-defined and separately identified in the Framework. It would be useful for there to be a separate heading in the Framework which describes the theoretical user.

Question 4: Are the pervasive constraints appropriately identified and sufficiently defined for them to be consistently understood and useful?

Cost

The cost-benefit constraint is an important consideration in the Framework. We believe that the cost of providing financial information should be weighed against the benefit obtained. We also agree that the cost-benefit constraint is pervasive to the standard-setting process and should therefore be separately identified within the Framework.

We understand the difficulty of carrying out assessments in this area, as explained in BC2.61 and BC2.62. Nevertheless we believe that ongoing cost-benefit research should be a major component both of developing new standards and of assessing the continuing appropriateness of what is already in place. In our opinion, the Framework should note the need to continuously look to improve the methods employed in the standard setting process; in particular, where meaningful quantitative assessments can be performed, we believe that the Framework should note that the resultant information is preferable for use in the cost-benefit assessment to information that is not based on empirical quantitative information.

We believe that the proposed Framework could also be enhanced if the Board defined from whose perspective the cost-benefit trade-off should be considered. The discussion in this area might be improved if it stated clearly that there are two sides to the costs-benefits equation - the perspective of the providers of the information (management) as well as the users - and the balance in deciding on an issue should be struck with more weight on the user perspective. For example, if the cost of providing information is too high because it is difficult, complex or time consuming to do so from management's perspective, this would not have the same 'weight' as a foregone benefit to the primary user group, if indeed the information is very relevant or better reflects underlying economic phenomena.

Materiality

In our opinion, the discussion of materiality needs to be distinguished from that of cost. In the context of general purpose financial reporting, materiality is considered by both management and by users. Management makes an assessment of materiality when deciding whether to include an item in the financial statements or to adopt a particular accounting treatment—this assessment is made from a 'cost to the preparer' point of view. Users, when assessing management's assertions about the financial statements, will consider materiality from the point of view of whether the omission of such information, or the accounting treatment adopted would render those financial statements neither relevant or representationally faithful—a 'cost to users' perspective. We encourage the Board to consider elaborating on this analysis.

Other Comments

Scope

The preface to the ED explains that in developing the Framework, the Board has decided to focus initially on concepts that are applicable to profit oriented entities in the business sector and then consider the applicability of the concepts to other entities at a later stage.

We encourage the Board to consider the needs of other organisations during this phase to avoid significant re-work at a later stage in time.

Finalisation of Chapters 1 and 2

We believe that the individual chapters of the Framework should not be finalised (or at least not made effective) until all of the chapters are finalised to ensure that the overall Framework forms a cohesive set of principles.