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AASB Research Report No. 1

Application of the Reporting Entity Concept and Lodgement of Special Purpose Financial Statements

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Foreword

The findings reported in this Research Report raise some fundamental questions about the adequacy of Australian financial reporting by entities that do not have ‘public accountability’ (as defined in AASB 1053 *Application of Tiers of Australian Accounting Standards*). Among other aspects, it identifies the incidence of financial statements lodged on public records that do not purport to fully apply (or do not disclose the extent of application of) accounting standards. The Report reveals widespread use of special purpose financial reporting by lodging entities of various types (including large proprietary companies).

Accounting standards are developed to serve the needs of users of general purpose financial statements (GPFSs). Those users are unable to demand the information they need to inform their economic decision-making. Accordingly, they depend on GPFSs as input to those decisions. Entities with such users, or the potential for such users, are ‘reporting entities’. Those entities are subject to accounting standards.

Many of the lodgement requirements specified by regulators rely on the use of size criteria, which do not necessarily align with the concept of a reporting entity. For example, the corporations law uses size criteria to identify which companies should lodge financial statements with the Australian Securities and Investments Commission (ASIC). Some of those entities may not have the prospect of external users dependent upon their financial reporting but nevertheless are required to lodge. Conversely, some entities that fail to meet the size criteria may be reporting entities as defined in accounting standards, but face no lodgement requirements.

By definition, special purpose financial statements (SPFSs) differ in some material way from GPFSs. They do not include some material information considered necessary by standard setters for external users of GPFSs. And yet they are often required by regulators to meet the test of being ‘true and fair’.

The corporations law and other laws, as well as auditing pronouncements, contain safeguards to protect users of financial statements, including when compliance with accounting standards is judged not to result in a true and fair view. Furthermore, the auditing pronouncements require qualified audit reports when applicable accounting standards are not followed in financial statements held out to be GPFSs and the consequences are material.

On the other hand, the preparers of SPFSs do not purport to apply all accounting standards, follow no known framework, and thus limit both the possibility of any audit qualification and the meaningfulness of an audit report. This is because SPFSs are largely the result of the preparing entity’s management setting an entity-specific benchmark for the entity’s reporting. I say ‘largely’ because some regulators set minimum requirements for lodged SPFSs – for example, the ASIC expects application of the recognition and measurement aspects of standards, and some presentation/disclosure standards, as a minimum.

The findings in this Report go to the heart of the fundamental question of how best to serve the needs of actual and potential dependent users of financial statements of entities that do not have ‘public accountability’.

Readers of this Report will see evidence of great disparity and variety among the lodged financial statements. It is apparent that accounting standards are not being applied by a great many entities on the basis that they are asserted not to be reporting entities.

Furthermore, the AASB has introduced Reduced Disclosure Requirements in Australia and those requirements now apply. They substantially reduce the disclosures required in the GPFSs of Tier 2 reporting entities.

The AASB has indicated in the past that it is fully prepared to reconsider the clarity of the guidance used in classifying entities as reporting entities. It accepts there may have been some misunderstanding about the need to consider both actual and potential users and perhaps the need to think about the full range of users rather than a particular category (for example, shareholders).

I note that, in some countries, private companies are generally not required to lodge financial statements (e.g. in the USA). On the other hand, some other countries require all incorporated entities to lodge, even if they are very small. Australia has sensibly deregulated reporting requirements for many micro and small entities, focussing requirements on larger entities that meet certain size criteria. It is my opinion that there is scope for further deregulation regarding the types of entities that are required to lodge financial statements. Whilst I would say deregulation of all entities that do not have public accountability would be well outside community expectations, I believe a case could be made, for example, for substantially increasing the size thresholds for companies, providing that those companies meeting any new thresholds lodge Tier 1 or Tier 2 GPFSs. The AASB is concerned that, if lodging entities frequently do not lodge GPFSs, users will be deprived of the information they need. The main public policy issue is the trade-off between entities enjoying the privileges of incorporation/registration, for example limited liability, and the need for those entities to be accountable to external parties.

Expressed differently, I am very concerned about the questionable quality of the many and varied forms of SPFSs. I see no consistent financial reporting purpose being served in such reporting and worry that lodgement of financial statements has become only a matter of (costly) compliance. At best, SPFSs that materially differ from accounting standards are an imprecise and unconvincing means of engendering some meaning for requirements to keep adequate books and records. At worst, they could provide directors with a means of trying to avoid the risks inherent in holding out financial statements as being high quality (GPFSs) and a mechanism for auditors attempting to reduce audit risk. I say ‘trying to avoid’ and ‘attempting’ because, in many cases, I would not want to be defending SPFSs where the overall meaning of the financial reporting was seriously being questioned.

I know the AASB would like to see a general consensus about the need for lodged financial statements to serve the needs of users (actual and potential) by those statements being prepared in accordance with accounting standards applicable to GPFSs and the subject of meaningful audit reports. Without those clear benchmarks, users are left with uncertainty and regulators face unmanageable enforcement tasks.

I would like to thank the researchers, who have devoted considerable energy to analysing large samples of data that form the basis for the findings presented in this Report. Their work shows the value that can come from high quality empirical research that analyses data relevant to the setting of public policy for financial reporting, auditing and enforcement. Research of this type deepens and widens our knowledge of financial statements of entities that do not have public accountability – a level somewhat ignored in the literature in the past.

Hopefully the publication of this Report will stimulate a healthy public debate from which public policy can benefit.

Kevin M Stevenson
(Chairman AASB)

June 2014

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Application of the Reporting Entity Concept and Lodgement of Special Purpose Financial Statements

Executive Summary

1 This Research Report analyses the application of the reporting entity concept and the adoption of special purpose financial reporting, particularly by entities lodging financial statements with the Australian Securities and Investments Commission (ASIC) and with state-based regulators in Australia's three most populous states, namely, Consumer Affairs Victoria, NSW Fair Trading and Queensland Office of Fair Trading.

2 This Report does not cover entities that have their equity interests traded in a public market, such as listed companies, and some other entities with 'public accountability'.[1]

3 The Report's findings in relation to reporting practices are intended to inform any future discussion by public-policy makers, regulators and the Australian Accounting Standards Board (AASB) on the application of the reporting entity concept and what that concept implies for financial statements lodged with various regulatory bodies.

The information analysed

4 In examining reporting practices of companies lodging with the ASIC, a random sample of 1,546 companies is used to provide results that can be generalised, to a 95 per cent confidence level, across the following five populations of companies:

(a) Large proprietary companies;

(b) Small proprietary companies controlled by a foreign company (also referred to as 'Foreign-controlled companies');

(c) Small proprietary companies that are required to lodge reports with the ASIC (also referred to as 'Small proprietary companies');

(d) Unlisted public companies other than those limited by guarantee (also referred to as 'Unlisted public companies'); and

(e) Public companies limited by guarantee.

5 A further random sample of 1,163 was drawn from entities lodging with state-based regulators, that is, Consumer Affairs Victoria (400 entities), NSW Fair Trading (377

1 Entities with 'public accountability' are identified in AASB 1053 *Application of Tiers of Australian Accounting Standards* – in particular, refer to Appendix A *Defined Terms* and Appendix B *Public Accountability* of AASB 1053.

entities) and Queensland Office of Fair Trading (386 entities). The lodged financial statements of these entities are analysed to provide evidence of the reporting practices of various types of entities – including co-operatives and associations.

Structure of the Research Report

6 The Report is made up of two parts:

(a) Part A reports on the findings for companies lodging annual financial statements with the ASIC in two main sections:

(i) the implementation by these companies of the reporting entity concept; and

(ii) the special purpose financial reporting practices of these companies; and

(b) Part B reports on the findings for state-based entities lodging annual financial statements with Consumer Affairs Victoria, NSW Fair Trading, and Queensland Office of Fair Trading by:

(i) documenting the legislation and associated guidance that affects the financial statements lodged by these entities; and

(ii) examining the special purpose financial reporting practices of these entities.

PART A

The implementation of the reporting entity concept by companies lodging financial statements with the ASIC

7 A majority of companies lodging financial statements with the ASIC (58.7%) across the five sample groups classify themselves as non-reporting entities and lodge special purpose financial statements (SPFSs) rather than general purpose financial statements (GPFSs). For large proprietary companies, this percentage increases to nearly 80 per cent. The summary table below captures the frequency of the type of financial statements lodged by the different types of companies.

Summary of type of statements lodged with the ASIC by different types of companies

	GPFSs		**SPFSs**	
	Frequency	**%**	**Frequency**	**%**
Large proprietary companies	79	20.1	315	79.9
Foreign-controlled companies	53	15.6	287	84.4
Small proprietary companies	23	24.2	72	75.8
Unlisted public companies	242	69.7	105	30.3
Public companies limited by guarantee	239	65.5	126	34.5
Total	**636**	**41.3**	**905**	**58.7**

8 Section 3 of Part A of this Report examines measures that proxy for factors identified in Statement of Accounting Concepts SAC 1 *Definition of the Reporting Entity* as

indicative of the existence of a reporting entity (i.e., separation of management from economic interest; economic or political influence/importance; financial characteristics). The analysis suggests that those factors do not consistently and systematically explain the application of the reporting entity concept. In other words, the decision about whether a company classifies itself as a reporting entity and lodges GPFSs could be substantially driven by factors other than those identified in SAC 1. Further, throughout Part A of this Report, a number of anecdotes are provided to support the findings. Also, no significant correlation was found between the application of the reporting entity concept (lodgement of GPFSs or SPFSs) and the choice of financial statement auditor (Big 4 v non-Big 4).

9 In interpreting the findings relating to the application of the reporting entity concept, although the application of the concept is mandatory for members of the professional accounting bodies in Australia under Accounting and Professional Ethical Standard APES 205 *Conformity with Accounting Standards*, the question arises whether that Standard is effective. In addition, anecdotal evidence accumulated in preparing Part A of this Report suggests that members of the accounting profession have different views on applying the definition of the reporting entity and this might, in part, explain the findings. Specifically, it appears that accounting professionals are generally divided as to whether a reporting entity is an entity that *does have* dependent users, or whether a reporting entity is one for which it is *reasonable to expect*[2] the existence of those users. AASB Essay 2014-1 *The Critical Role of the Reporting Entity Concept in Australian Financial Reporting* (Hamidi-Ravari, AASB Research Centre, 2014) addresses this issue.

Special purpose financial reporting practices of companies lodging financial statements with the ASIC

10 Section 4 of Part A of this Report examines the financial reporting practices of the sample of companies lodging SPFSs with the ASIC.

11 The research does not discern a particular pattern of accounting policy choices among companies lodging SPFSs.

12 Special purpose financial reporting practices are analysed across three primary dimensions, to gauge the quality of the SPFSs. First, information provided in the significant accounting policies note[3] of the SPFSs of the five groups of companies is analysed in relation to the disclosure of the application of recognition and measurement in accordance with the Australian Accounting Standards (R&M). Second, the quality of accruals recognised by the sample of large proprietary companies is analysed, and third, the timeliness of lodgement of financial information is examined for the same sample.

13 Examining these dimensions of quality helps facilitate an understanding of differences that exist between the companies lodging GPFSs and those lodging SPFSs. The findings from the examination of the reporting practices of companies lodging SPFSs indicate that, while the majority of companies state that they apply the recognition, measurement and particular disclosure requirements in Australian Accounting

2 The definition of reporting entity in AASB 1053 refers to an "… entity in respect of which it is reasonable to expect the existence of users …".

3 The significant accounting policies note is usually found in Note 1 or 2 to the financial statements.

Standards, a substantial minority of companies (around 20%) state non-application, while for other companies (approximately 15%) no clear statement of application is made. For companies lodging SPFSs, the research identifies a wide variation in disclosure practices.

14 An analysis of the quality of accruals by comparing outcomes with accruals over time for the sample of large proprietary companies provides evidence that the accruals recognised in the SPFSs by the companies that stated application of R&M are of lower quality compared with those recognised by companies lodging GPFSs. It also provides evidence that SPFSs that include a statement that they have not applied R&M, or are unclear on whether they have applied R&M, are of lower quality compared with those SPFSs that stated they applied R&M. Examining accruals in this way can facilitate a better understanding of whether accrual-based profit is being 'appropriately' measured by large proprietary companies independent of disclosed practices such as those set out in the notes to the financial statements (see, for example, Dechow & Dichev, 2002; Dechow, 1994).

15 In a large body of research literature (e.g., Givoly, 1982; Abd-Elsalam & Street, 2007; Ball et al., 2008), there is a well-established relationship between the timeliness of information contained in financial statements and the value or relevance of the information reported. Prior research in this area has examined various aspects of the relationship. The body of research literature indicates that more timely financial statements have higher information content and are associated with more efficient debt and equity markets as well as stronger corporate governance for the entities preparing the statements. Drawing on aspects of this literature, Section 4.3 of Part A of this Report examines the timeliness of the lodgements for the large proprietary companies sample. It begins with the assumption that lodgements are made in accordance with the timing specified in the corporations law, which states that lodgements should be made within four months of year end. The Report uses these requirements to proxy for timeliness and identify late lodgements to the ASIC. The analysis found that 47.2 per cent of large proprietary companies lodging GPFSs lodged more than four months after year-end, and 47.9 per cent of companies lodging SPFSs made late lodgements.

Comments on the findings in relation to companies lodging financial statements with the ASIC

16 A majority of companies in the sample were not classified as reporting entities and thus lodged SPFSs. The research findings highlight the variation in the application of the reporting entity concept. This observed variation in the reporting entity classification is consistent with the differing views apparent among practitioners regarding the essence and application of the reporting entity concept. In addition, as noted in paragraph 13 above, around 20% of the SPFSs stated non-application of R&M. Further, SPFSs seem to have provided lower quality accruals compared with those companies that lodged GPFSs. The incidence of late lodgement is similar among the SPFSs and GPFSs.

17 Taken together, the findings and analysis in Part A of this Report have the potential to inform any future discussion about the use of the reporting entity concept and to inform any discussion on public policy reforms to lodgement requirements. In particular, the findings indicate a need to address the apparent inconsistent application of the reporting entity concept.

18 The findings suggest that further consideration could be given to the current lodging requirements, having regard to cost/benefit considerations.

19 The findings also suggest that if the reporting entity concept were to be retained as a key feature of the differential reporting regime in Australia, future actions may need to be taken to help ensure the concept is applied in a more consistent manner.

20 Part A of this Report notes the *Corporations Act 2001* requirements for lodging entities to apply accounting standards, and notes guidance on applying accounting standards in ASIC Regulatory Guide 85 (RG 85) *Reporting requirements for non-reporting entities*. The research findings show an apparent wide variation in the stated application of accounting standards by companies. As acknowledged in Part A of this Report, it is possible that for some companies the content of the significant accounting policies note to the financial statements does not reflect the actual application of standards in preparing the statements. However, an absence of explicit evidence of compliance, of itself, has the potential to reduce the reliance that users can place on the financial statements, especially in an environment in which SPFSs are predominant. Accordingly, public-policy makers and the AASB may need to consider ways to enhance the transparency of accounting policies disclosure by these companies.

21 More research would be needed to uncover why companies decide to lodge SPFSs rather than GPFSs, including whether choices are made on the basis of costs to be incurred, the sensitivity of disclosures, or risk avoidance (because there is a risk in holding out that financial statements comply with requirements applicable to GPFSs, which could be challenged). The large-scale nature of the research undertaken for Part A of this Report precludes a thorough analysis of possible motives. In particular, it would not be feasible as part of this research to follow up with all the relevant companies whose financial statements were analysed in a way that would yield an unbiased response overall.

PART B

Financial reporting practices of entities lodging financial statements with state-based regulators

22 Part B of this Report documents the reporting and auditing requirements that shape the lodgements made to state-based regulators and specifically analyses the reporting practices of entities lodging financial statements with Consumer Affairs Victoria, NSW Fair Trading, and Queensland Office of Fair Trading.

23 The rationale for documenting the reporting and auditing requirements affecting lodgements to state-based regulators is to provide a basis for understanding the content of the lodgements made, particularly in view of the complex array of state-based legislation and industry-specific guidance.

24 With the exception of Western Australia, which does not require periodic lodgements to be made, the reporting requirements relating to larger (incorporated) associations are broadly consistent across states. However, the specific quantitative thresholds (typically based on revenues and/or assets) used for the classification of larger associations, and which carry more extensive reporting requirements, vary widely.

Given that the classification of entities directly impacts the information required to be lodged, such variation could act as an impediment to any future effort that might be directed at improving the consistency of information lodged by entities across states. Further, the state-based legislation and associated guidance does not always explicitly require consistent application of Australian Accounting Standards.

25 The requirements for co-operatives are reasonably consistent across states for the years analysed in this Report – as the relevant legislation requires preparation of financial statements under Chapter 2M of the Corporations Act. More recently, this consistency has been enhanced by harmonising legislation on co-operatives across Australia, enabled largely by the work of the Council of Australian Governments (COAG) *Legislative and Governance Forum on Consumer Affairs*. The sample of entities examined in Part B of this Report also includes some that were focused on charitable, community purpose and fundraising activities – for which additional state-based regulations typically apply.[4]

26 The analysis of lodgements of financial statements made in Victoria, NSW and Queensland reveals great variation in the quantity and quality of information lodged. However, for larger associations and co-operatives, the variations appear less significant. A large proportion of entities examined across the three states provided no explicit indication as to whether the financial statements were GPFSs or SPFSs (i.e., 78% in Victoria, 71% in NSW and 40% in Queensland). Around 18 per cent of entities in Victoria, 24 per cent in NSW, and 53 per cent in Queensland lodged SPFSs with their state-based regulator, while only around five per cent of entities lodged statements identified as GPFSs across the three states. The summary table below outlines the frequency of the type of statements lodged by the different groups of state-based entities.

4 The *Australian Charities and Not-for-profits Commission Act 2012* (Cth) established the Australian Charities and Not-for-profits Commission (ACNC) in 2012. The ACNC does not substitute the state supervising bodies and it has stated that it will co-operate with other government agencies to oversee a simplified and streamlined regulatory framework for not-for-profit entities.

Summary of descriptions of financial statements lodged with state-based regulators by different types of entities[*]

VICTORIA				NSW				QUEENSLAND			
Type of Entity	**GPFSs %**	**SPFSs %**	**No clear statement %**	**Type of Entity**	**GPFSs %**	**SPFSs %**	**No clear statement %**	**Type of Entity**	**GPFSs %**	**SPFSs %**	**No clear statement %**
Prescribed Associations	17	60	23	Tier-One Incorporated Associations	10	67	24	Level-One Incorporated Associations	7	73	20
Non-Prescribed Associations	0	9	91	Tier-Two Incorporated Associations	2	17	82	Level-Two Incorporated Associations	2	62	36
								Level-Three Incorporated Associations	0	36	64
Co-operatives	0	50	50	Co-operatives	67	33	0	Co-operatives	33	33	33
Fundraisers	30	35	35					Charities	50	35	15
Patriotic Funds	0	18	82					Community Purpose Entities	20	50	30
Total	**4**	**18**	**78**	**Total**	**5**	**24**	**71**	**Total**	**7**	**53**	**40**

* *Some Panels do not add to 100 per cent due to rounding*

27 There was substantial variation in the information disclosed across the different types of financial statements and in some instances the quality of disclosure appeared to be extremely poor. The analysis in Part B of this Report of the transparency of reporting indicates that, with the exception of larger associations and co-operatives, entities varied as to whether they lodged balance sheets and/or income statements, and entities rarely lodged statements of cash flows. Variation in disclosure was also evident when the notes to the financial statements were examined. A significant number of entities also appear to lodge cash-based statements, rather than accrual-based statements, which may impede the usefulness of the statements for understanding the performance and accountability of those entities.

28 In summary, the majority of entities lodged financial statements that typically did not follow Australian Accounting Standards and were prepared in an inconsistent format.

29 While in Queensland the significant majority of financial statements lodged were audited, this was not the case for the smaller entities in Victoria or NSW.

30 The research findings might inform discussion among state policy makers in identifying areas for reform. Any such discussion might involve re-assessing user needs for lodged financial information and considering measures that might bring about greater consistency of financial statements across lodging entities. In particular, that discussion might involve considering clarifying whether some entities must lodge GPFSs and, for those entities permitted to lodge SPFSs, the specific information required. However, future research could be undertaken to identify who the users are and their information needs.

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List of Acronyms/Abbreviations Used in the Research Report

AASB	Australian Accounting Standards Board
AARF	Australian Accounting Research Foundation
ACC	Accruals
ACNC	Australian Charities and Not-for-profits Commission
AGM	Annual General Meeting
AICPA	American Institute of Certified Practicing Accountants
APES	Accounting Professional and Ethical Standards
ASCPA	Australian Society of Certified Practicing Accountants
ASIC	Australian Securities and Investments Commission
ASX	Australian Securities Exchange
CAV	Consumer Affairs Victoria
CFO	Cash-flows from Operations
CICA	Canadian Institute of Chartered Accountants
CPAA	CPA Australia
ED	Exposure Draft
FASB	Financial Accounting Standards Board of America
FASC	Financial Accounting Standards Committee of the American Accounting Association
FSAC	Financial Sector Advisory Council of Australia
GAAP	Generally Accepted Accounting Principles
GST	Goods and Services Tax
GPFSs	General Purpose Financial Statements
IASB	International Accounting Standards Board
IATA	International Air Transport Association
ICAA	Institute of Chartered Accountants in Australia
IFRS	International Financial Reporting Standards
IPA	Institute of Public Accountants
NAS	Non-audit services
NSWFT	NSW Fair Trading
NZASB	New Zealand Accounting Standards Board
QOFT	Queensland Office of Fair Trading
PDF	Portable Document Format
RDR	Reduced Disclosure Requirements
RG	Regulatory Guide
R&M	Recognition and Measurement in accordance with Australian Accounting Standards
SAC	Statement of Accounting Concepts
SD	Standard Deviation
SMEs	Small and Medium-sized Entities
SPFSs	Special Purpose Financial Statements

Note:

There are a number of rounding differences that affect figures reported in some of the Tables in this Report.
There are also some inconsistencies in figures reported in and between Tables due to inconsistencies in the data analysed, including, on occasions, missing values.

PART A: REPORT ON ASIC LODGEMENTS

1. Background

There were approximately 22,000 Australian companies that are the subject of Part A of this Report and lodged on the public record financial statements with the corporate regulator, the Australian Securities and Investments Commission (ASIC), under the *Corporations Act 2001* (See Table 1 below).

Part A of this Report is concerned with the companies that need to assess whether they are reporting entities for lodgement purposes and are included in one of the following five categories of companies:

(a) Large proprietary companies (private companies satisfying at least two of the three size criteria specified in the Corporations Act[5]);

(b) Small proprietary companies controlled by a foreign company;[6]

(c) Small proprietary companies lodging at the direction of the ASIC or at the request of shareholders;

(d) Unlisted public companies other than those limited by guarantee, which include a range of entities such as insurance companies and finance companies; and

(e) Public companies limited by guarantee, which mainly comprise charities, clubs, institutes and societies.

This Report does not address entities that have their equity traded in public markets, such as listed companies, and some other entities that have 'public accountability'.[7] This is because the focus of this Report is on analysing the application of the reporting entity concept and the adoption of special purpose financial reporting, while entities that have their equity traded in public markets and most other entities that have public accountability are clearly reporting entities and are therefore compelled to adopt general purpose financial reporting.

Section 3 of this Part of this Report presents descriptive data based on random samples of companies drawn from each of the five categories of companies lodging financial statements with the ASIC. A random sample of 1,546 companies was drawn from 2008-09 population counts provided by the ASIC (see Table 1 for a breakdown of the populations and respective samples by each category of company)[8]. The data analysed was hand collected from Portable

5 The size criteria are: (i) the consolidated gross operating revenue for the financial year is $25 million or more; (ii) the value of consolidated gross assets at the end of the financial year is $12.5 million or more; (iii) the company and entities it controls have 50 or more employees at the end of the financial year.

6 The substance of the various legislative provisions relating to this group of companies is that 'foreign-controlled' is the term that captures those companies that are 'controlled' by foreign companies and are registered to carry on business in Australia.

7 Among the entities that AASB 1053 *Application of Tiers of Australian Accounting Standards* deems to have public accountability are disclosing entities and registered managed investment schemes, which are required to lodge financial statements with the ASIC (paragraph B2).

8 Econometric sampling techniques were applied to achieve a 95 per cent confidence level that the resulting sample used is representative of the population of companies lodging with the ASIC, by company type. The sample may not be representative of the population across additional stratification criteria such as size

Document Format (PDF) copies of company lodgements provided by the ASIC. The data years subject to analysis were the most recently available annual report years – with most report years ending in 2009 and 2010. To enable additional analysis on aspects of financial reporting quality for large proprietary companies, additional company year observations were obtained up to and including 2010 for these companies. Further discussion of the approach taken in preparing this Part of this Report is contained in Section 3 below.

Table 1: Companies that are the subject of this Report that lodged Financial Statements with ASIC in 2010-11 and 2008-9

Type of Company	Population 2010-11	Population 2008-09	Sample 2008-09
Large proprietary companies (non-disclosing entities)	6,339	5,097	394[a]
Small proprietary companies controlled by a foreign company	2,797	2,237	340
Small proprietary companies – financial statements requested by the ASIC or shareholders	186	131	95
Unlisted public companies other than those limited by guarantee	3,985	3,884	347
Public companies limited by guarantee	8,404	9,673	370
Total:	**21,711**	**21,022**	**1,546**

[a] *The initial sample for the large proprietary companies group was 357 companies. Due to additional data provided by the ASIC to overcome errors, the sample was increased by 37 companies.*

To contextualise the issues addressed in this Part of this Report, it is relevant to note that some of those issues were also raised in 2005 by the ASIC as a result of its reviews of an unspecified sample of financial statements lodged, which identified inconsistent application of the reporting entity concept and led to the publication of Regulatory Guide 85 (RG 85) *Reporting requirements for non-reporting entities* (ASIC, 2005). In those reviews, the ASIC concluded that a number of companies that had classified themselves as non-reporting entities should have been classified as reporting entities. The implication is that some of the companies that had lodged special purpose financial statements (SPFSs) might more appropriately have lodged general purpose financial statements (GPFSs). Companies lodging GPFSs apply Australian Accounting Standards, whereas companies lodging SPFSs usually apply a limited number of requirements in the Standards and lodge financial statements with materially less financial information. Until now, the conclusions drawn by the ASIC in 2005 have not been subject to large-scale empirical analysis – Part A of this Report responds to the need to provide such analysis.

Previous research in this area suggests that members of the accounting profession in Australia adopt different approaches to implementing broad principles such as the reporting entity concept (Walker, 2007). Further, entities face complex incentives in determining the format and content of financial statements. Primarily, entities have a responsibility to produce financial statements that comply with appropriate regulation and provide information that is useful for decision-making. At the same time, the preparation of financial statements and the disclosure of additional information are costly, and while the extra costs of disclosing each additional line item can be debated, the cost of complying with recognition and measurement approaches in accounting standards may, for some entities, be considerable. Accordingly, regulations and policies that advocate the application of recognition and measurement

of company (e.g., total revenue, number of employees) and industry, as lodgements are made to the ASIC in PDF and it was not feasible for them to be organised and searched in these ways.

requirements in Australian Accounting Standards by smaller entities arguably should do so in the context of the costs and benefits involved for entities and for the users of the financial statements.

The reporting practices of small and medium-size entities (hereafter 'SMEs') also are the subject of ongoing debate internationally, with accounting regulators in different countries adopting varied approaches to regulating the reporting practices of SMEs (IASB, 2010).

These factors, taken together, provide significant motivation to develop a greater understanding of the reporting practices of these entities.

In response to these matters, the AASB released in February 2010 Exposure Draft ED 192 *Revised Differential Reporting Framework*, proposing a revised reporting framework. Following feedback from constituents, the AASB subsequently issued AASB 1053 *Application of Tiers of Australian Accounting Standards*, which introduced a second tier of reporting requirements, involving reduced disclosures for some entities producing GPFSs. The AASB then commissioned the research that forms the basis for this Report to investigate the financial reporting practices of entities in Australia with a view to informing any future discussion of regulatory developments for entities that currently need to assess whether they are reporting entities.

The analysis in Part A of this Report primarily focuses on the reporting patterns of companies between the years 2008 and 2010. It does not, therefore, include examination of the impact of changes in the reporting patterns of companies following the issue of AASB 1053 in 2010. This is noted as an area for future post-implementation work by the AASB and by the New Zealand Accounting Standards Board (NZASB), which has also adopted the Reduced Disclosure Requirements (RDR) approach.

The remainder of Part A of this Report addresses two primary issues identified by the AASB. Specifically, it examines:

(a) the implementation of the reporting entity concept by companies lodging financial statements with the ASIC (Sections 2 and 3); and

(b) the financial reporting practices of those companies across the ASIC samples, with a focus on large proprietary companies (Section 4).

2. The Reporting Entity Concept

Differential reporting has been a feature of the Australian financial reporting environment for decades, incorporated in the Australian Accounting Standards since the early 1990s. Companies currently lodge with the ASIC either GPFSs or SPFSs. Reporting entities must lodge GPFSs and are required to apply Australian Accounting Standards.[9] Reporting entities include entities that have their equity traded in public markets. However, non-reporting entities may lodge SPFSs instead of GPFSs, but the ASIC's RG 85 notes that they should apply (all applicable) recognition and measurement requirements specified in Australian Accounting Standards (referred to in this Report as R&M) and apply a number of mainly

9 Australian Accounting Standards incorporate International Financial Reporting Standards (IFRSs). Reduced Disclosure Requirements (RDR) were not available for application until 2010.

presentation and disclosure Standards in full.[10] The extent to which companies that classify themselves as non-reporting entities state application of R&M and at least three of the five mandatory presentation and disclosure standards is analysed in Section 4.1 of this Part of this Report.

According to Brailsford and Ramsay (1993), the reporting entity concept was introduced in Australia in the early 1990s in response to the 'accounting standards overload problem' and was designed to reduce the burden on some entities of preparing financial statements. Whether the reporting entity concept should continue to apply in Australia as the driver for having to prepare GPFSs is a central issue pertinent to this Report. In essence, what needs to be established is whether the application of the concept results in financial statements being produced that meet the needs of users of financial statements. Alternatively, it is also possible that there is a level of subjectivity surrounding the application of the concept that enables some entities to evade their reporting responsibilities under Australian Accounting Standards – thus not complying with the spirit of the concept or its associated reporting implications.

The remainder of this section (Section 2) explains the definition of the reporting entity concept as outlined in the Statement of Accounting Concepts SAC 1 *Definition of the Reporting Entity* and as endorsed in Professional Standard APES 205 *Conformity with Accounting Standards*.[11] This is followed by, in Section 3, an empirical analysis of the application of the reporting entity concept across the five categories of companies lodging annual financial statements identified in Section 1 above. As a basis for the analysis, proxies for indicative factors as outlined in SAC 1 (paragraphs 19-22) to suggest the existence of a reporting entity are identified and tested to understand the application of the reporting entity concept by companies in the sample.

SAC 1 – The reporting entity concept – SAC 1 states that "reporting entities shall prepare general purpose financial statements. Such reports shall be prepared in accordance with Statements of Accounting Concepts and Accounting Standards" (paragraph 41). APES 205 (2007) requires members of the professional accounting bodies who are responsible for financial statements of a reporting entity to take all reasonable steps to ensure that the reporting entity prepares GPFSs (paragraph 4.3) and that members take all reasonable steps to apply Australian Accounting Standards when they prepare such statements that purport to comply with the Australian Financial Reporting Framework (paragraph 5.1). Following SAC 1, entities not regarded as reporting entities need not prepare GPFSs.

SAC 1 sets out indicative factors for identifying a reporting entity, which is based on whether it is reasonable to expect the existence[12] of external users who are dependent on GPFSs as

10 This Report distinguishes between: (1) requirements that stipulate when and how assets, liabilities, equity items, revenues and expenses are recognised and measured in financial statements; and (2) requirements that stipulate the manner of presentation and extent of disclosure of amounts in the financial statements.

11 APES 205, issued by the Accounting Professional and Ethical Standards Board (APESB), is classified as a 'professional standard', and outlines responsibilities of members of the professional accounting bodies in Australia. This includes members of the Institute of Chartered Accountants in Australia (ICAA), CPA Australia (CPAA) and the Institute of Public Accountants (IPA). Taken together, members of these bodies comprise more than 200,000 accounting and business professionals globally.

12 In conducting this research, discussions held with senior staff at a number of accounting firms of various sizes were wide-ranging and informative and provided insights that are pertinent to the content of this Report. These discussions also indicated a variation in the understanding of the application of the reporting entity concept. Particularly, practitioners were generally divided as to whether a reporting entity is an entity

their primary source of information for making and evaluating resource allocation decisions. Examples of entities typically considered to be reporting entities are provided in various regulations, policy statements and accounting standards such as AASB 1053 and include various types of companies (e.g., companies whose securities are publicly listed); listed trusts and other trusts that raise funds from the public; government-controlled entities and government departments (see Walker, 2007).

Existence of a reporting entity – While SAC 1 states that GPFSs are prepared to provide users with information about the reporting entity that is useful for making and evaluating decisions about the allocation of scarce resources, there are no specific and quantitative measures set out in accounting pronouncements that can be used to identify the existence of a reporting entity. SAC 1 acknowledges the judgement involved in applying the concept and identifies a number of indicative factors that can assist in determining the existence of users who are dependent on GPFSs:

(a) **Separation of management from economic interest** – According to SAC 1 (paragraph 20), entities that demonstrate a greater separation of ownership and management are more likely to have users who are dependent on GPFSs;

(b) **Economic or political importance/influence** – According to SAC 1 (paragraph 21), reporting entities are also more likely to have a greater impact on the welfare of external parties. Examples of such entities include organisations with dominant positions in their respective market place, employer/employee associations and public sector entities that have regulatory power; and

(c) **Financial characteristics** – SAC 1 (paragraph 22) also identifies financial characteristics such as size (e.g., value of sales or assets, or number of employees or customers) and the entity's relative level of indebtedness to external parties.

To summarise, under SAC 1, an entity is regarded as a 'reporting entity' whenever it is reasonable to expect the existence of users who are dependent on GPFSs for information in making and evaluating decisions about the allocation of scarce resources (SAC 1, paragraph 40). Factors are outlined in SAC 1 to assist in determining the existence of a reporting entity, but these factors are indicative only. The factors identified in SAC 1 are also consistent with an established body of research literature that is often described as focussing on 'contracting' issues. According to this literature, those entities for which there is a greater demand for financial information for external monitoring of performance and accountability will make different reporting choices and produce higher quality reports (see for example, Allee and Yohn, 2009; Ball and Shivakumar, 2005; Bharath et al., 2008; Watts 2003).

The implications of classification as a non-reporting entity – RG 85 suggests that although companies lodging SPFSs under the Corporations Act are subject to limited disclosure requirements, they should prepare financial statements that apply R&M for lodgement in

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that *does have* dependent users, or whether a reporting entity is one for which it is *reasonable to expect* the existence of those users – as stated in SAC 1. An Essay published by the Research Centre of the AASB (*The Critical Role of the Reporting Entity Concept in Australian Financial Reporting*, Hamidi-Ravari, 2014) addresses this issue.

accordance with Chapter 2M of the Corporations Act (ASIC RG 85, 2005, paragraph 2). There are five accounting standards[13] that specifically apply to all entities preparing financial statements under Part 2M.3 of the Corporations Act. The application paragraphs of these standards are such that they apply to financial statements – regardless of whether they are prepared by a reporting entity. The five standards to be applied by entities preparing SPFSs contain mainly presentation and disclosure requirements, and are AASB 101 *Presentation of Financial Statements*; AASB 107 *Cash Flow Statements*; AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*; AASB 1031 *Materiality*; and AASB 1048 *Interpretation and Application of Standards*.[14]

The empirical analysis in Section 3 provides an assessment of the application of the reporting entity concept by the companies in the sample. The analysis considers proxies for indicative factors outlined in SAC 1 (paragraphs 19-22), as noted above:

(a) separation of management from economic interest;

(b) economic or political importance/influence; and

(c) financial characteristics,

to examine whether those factors appear to explain the application of the reporting entity concept.

3. Analysis of Implementation of the Reporting Entity Concept

3.1 Large Proprietary Companies

As noted in table 1 above, there were 6,339 large proprietary companies that lodged financial statements with the ASIC in 2010-11. Under the Corporations Act (Division 5A s.45A(3)), a large proprietary company is defined as one that is limited by share capital, has less than 50 non-employee shareholders and has not raised money from the public. These companies also satisfy at least two of the following three size tests: (i) the consolidated gross operating revenue for the financial year is $25 million or more; (ii) the value of consolidated gross assets at the end of the financial year is $12.5 million or more; (iii) the company and entities it controls have 50 or more employees at the end of the financial year. The Corporations Act requires all large proprietary companies, unless grandfathered,[15] to lodge a directors' report and audited financial statements with the ASIC.

To examine reporting practices of these companies, a random sample (with a 95% confidence level) of 394 was drawn based on population counts of large proprietary companies lodging financial statements with the ASIC. The original sample was drawn primarily from 2008-09

13 This Report is expressed in terms of requirements as they existed during the data years that are the subject of the analysis in this Report. At that time, there were five accounting standards of the type referred to.

14 AASB 107 is now titled *Statement of Cash Flows* and AASB 1048 is now titled *Interpretation of Standards*.

15 'Grandfathered' is a term used to describe a situation in which an old regulation continues to apply to some existing situations. In this case, a grandfathered proprietary company is a company that was formerly granted an exemption for lodging audited financial statements based on criteria in section 319(4) of the Corporations Act, that is, the company continues to meet the exempt proprietary company definition at all times since 30 June 1994; the company was deemed large at the end of its first financial year ending after 9 December 1995; the company had the financial statements audited for 1993 and each subsequent year; and the company lodged notice within four months of end of the first financial year ending after 9 December 1995.

population counts. To facilitate additional analysis relating mainly to the quality of accruals (see Section 4.2 below), additional panel data was obtained to cover the years 2006 to 2010. While this extended the data set significantly, the distribution of companies varied across the five years, with the majority coverage between 2008 and 2010.[16] Based on the most recent company-year data for each company, results in Table 2 show that around 20 per cent of large proprietary companies lodged GPFSs, while approximately 80 per cent lodged SPFSs. In the period 2006 to 2010, it was observed that six companies that had lodged GPFSs in earlier years had switched to lodging SPFSs. In contrast, one company that had lodged SPFSs switched to lodging GPFSs.

Table 2: Frequency of Type of Financial Statements in the Sample – Large Proprietary Companies

	Frequency	%
GPFSs	79	20.1
SPFSs	315	79.9
Total:	**394**	**100.0**

3.1.1 Statistical Analysis – Large Proprietary Companies

To understand reporting decisions made by companies with respect to the reporting entity concept, proxies for indicative factors outlined in SAC 1 were identified and tested. Table 3 shows results of a series of t-tests, which examine mean differences on a number of proxies for factors outlined in SAC 1 that suggest the existence of a reporting entity. These tests are conducted for large proprietary companies to examine whether there are significant differences across the proxies for factors for companies lodging GPFSs compared with entities lodging SPFSs. As data among most ‘size’ and ‘liabilities’ variables are subject to significant skewness due to extreme values (i.e., high standard deviations from the mean), various standard econometric techniques are used to enhance the generalisability of the results.[17] If the companies in the sample were indeed applying factors identified in SAC 1, there should be differences in the mean (median) values across the samples. Tests performed on financial variables that proxy for ‘size’ (such as trading revenue, total assets, and number of employees) provide some indication that larger entities are lodging GPFSs.

Variables identified to proxy for the ‘separation of management from economic interest’ are the number of members (shareholders) and ‘more than one member’ (i.e., a measure filtering out entities that only have one member). With multiple members/shareholders there is potential for agency conflict,[18] suggesting a greater demand for enhanced transparency through higher quality financial reporting, possibly leading to a higher likelihood that GPFSs will be prepared. When there is only one member/shareholder, the likelihood of agency conflict is low, suggesting *ex ante*, a possible higher incidence of SPFSs being prepared. Results do not indicate statistically significant differences between companies lodging GPFSs

16 There are various reasons why the full five-year data set was not complete for some companies. Most often this occurred when company reports were lodged with the ASIC with data missing from the lodgement.

17 For example, t-tests are adjusted for unequal variances and two-sample Wilcoxon rank-sum (Mann-Whitney) tests on median differences are also conducted. In addition, variables that proxy for ‘size’ and ‘liabilities’ were normalised by using natural logarithmic procedures (i.e., to reduce the standard deviation) and to provide corroboration of the t-test and the Wilcoxon rank-sum test results.

18 Agency conflict refers to the separation of owners’ (principals’) and managers’ (agents’) interests in an entity, that is, agents may act in their own self-interest rather than those of the principals, thus creating unnecessary costs for the entity (Jensen and Meckling, 1976).

and SPFSs for both variables that proxy for agency conflict. This suggests that the widening of separation between management and ownership/members does not impact the decision to classify as a reporting entity and lodge GPFSs. By implication, companies lodging SPFSs do not appear to have a different spread of ownership/management compared with companies lodging GPFSs.

It is noteworthy that companies lodging GPFSs have significantly more directors (mean = 4.45) compared with companies lodging SPFSs (mean = 3.48), suggesting larger boards are more likely to require the preparation of GPFSs, which might reflect a greater focus on corporate governance and financial reporting procedures.

According to SAC 1, another indicator of whether users exist who are dependent on GPFSs is the level of indebtedness of the entities. In other words, greater levels of indebtedness could indicate the existence of external users who are dependent on financial information. Intuitively, creditors, financial institutions, and other debt-holders will seek reliable and understandable information about an entity to assist in making lending decisions, suggesting a greater likelihood that the entity will be a reporting entity and lodge GPFSs. Variables that proxy for 'indebtedness' such as creditors, bank debt, and total liabilities all show significant differences between the GPFSs and SPFSs groups. Taken together, these results suggest that the likelihood a company will lodge GPFSs increases with the level of indebtedness.

Table 3: Reporting Entity Test – Large Proprietary Companies

		GPFSs	**SPFSs**	**Significance of Differences**
Panel A: 'Size' Test				
Trading Revenue	Mean	$312,000,000	$125,000,000	t = 2.5497, p = .0058
	Median	$64,500,000	$43,500,000	z = 4.043 , p = .0001
*ln*Trading Revenue	Mean	$18.10	$17.51	t = 3.6535, p = .0002
	Median	$18.05	$17.61	z = 3.962 , p = .0001
Total Assets	Mean	$821,000,000	$199,000,000	t = 2.9103, p = .0020
	Median	$78,100,000	$34,100,000	z = 5.241 , p = .0000
*ln*Total Assets	Mean	$18.48	$17.57	t = 5.7141, p = .0000
	Median	$18.19	$17.36	z = 5.496 , p = .0000
No. Employees	Mean	592	243	t = 3.3924, p = .0004
	Median	146	103	z = 2.813 , p = .0049
*ln*No. Employees	Mean	5.30	4.82	t = 3.1897, p = .0008
	Median	5.20	4.85	z = 3.173 , p = .0015
Panel B: 'Separation of Management from Economic Interest' Test				
No. Members	Mean	4	3	NS
	Median	1	1	NS
More than 1 Member	%	57.9%	42.2%	NS
No. Directors	Mean	4.45	3.48	t = 5.3218, p = .0000
	Median	4	3	z = 4.632 , p = .0000

		GPFSs	SPFSs	Significance of Differences
Panel C: 'Indebtedness' Test				
Creditors	Mean	$168,000,000	$58,400,000	t = 3.4832, p = .0003
	Median	$26,800,000	$8,305,487	z = 5.026 , p = .0000
*ln*Creditors	Mean	$16.95	$15.92	t = 5.3632, p = .0000
	Median	$17.10	$15.94	z = 4.873 , p = .0000
Bank Debt	Mean	$283,000,000	$76,800,000	t = 2.9088, p = .0020
	Median	$9,604,000	$3,879,601	z = 4.052 , p = .0000
*ln*Bank Debt	Mean	$16.56	$15.44	t = 4.5353, p = .0006
	Median	$16.36	$15.71	z = 4.275 , p = .0001
Total Liabilities	Mean	$476,000,000	$143,000,000	t = 3.0497, p = .0013
	Median	$46,100,000	$19,400,000	z = 5.414 , p = .0000
*ln*Total Liabilities	Mean	$17.91	$16.88	t = 5.6175, p = .0000
	Median	$17.75	$16.84	z = 5.526 , p = .0000

Note: ln = natural logarithm. Proxies for factors identified in SAC 1 as suggesting the existence of a reporting entity were compared using independent samples t-tests (adjusted for unequal variances) and two-sample Wilcoxon rank-sum (Mann-Whitney) tests on mean and median differences. The adjustment for unequal variance was performed because of extreme mean values on the indicative factors. t-tests and Wilcoxon rank-sum are based on one-tailed significance tests. Where t, z and p values are provided, the difference for the relevant variable between the groups is statistically significant. ***The smaller the value for p, the greater the statistical difference.*** *'NS' refers to no statistical significance in the difference between the GPFSs and SPFSs groups for the variable examined.*

Multivariate analysis –Results from the univariate analyses (immediately above) should be treated with caution because of the possibility that variables, which are intercorrelated in highly complex ways, are not sensitive to this complexity. For example, if large companies also have more creditors, it is not possible to conclude whether it is size that causes the significant difference or if it is creditors causing the difference. Accordingly, additional multivariate analysis is undertaken to control for the unique contribution of each proxy for an indicative factor on the choice between GPFSs and SPFSs. To augment the univariate test results, a logistic regression[19] analysis was used to predict discrete outcomes (i.e., whether a company is more likely to lodge GPFSs) from five key variables that proxy for the reporting entity test as outlined in SAC 1.

The logistic regression analysis (see Table 4 below) assesses predictions of entities lodging GPFSs on the basis of the following variables:

(a) natural logarithm[20] of trading revenue (*lntrading*);

19 A logistic regression is a form of regression that is run to enable the prediction of a dependent variable that takes on dichotomous (i.e., binary) values. In this case, the dependent variable is whether the entity lodges GPFSs. The chi-square test fundamentally assesses how well the logistic regression model fits the data. This is achieved by comparing a logistic regression model that includes no independent variables (i.e., one which only includes the constant [_cons] value in the model) with a logistic regression model that includes a number of independent variables. A chi-square statistic that is associated with a small p-value indicates there is a difference between the two models, that is, the effect of the inclusion of at least one independent variable on the dependent variable (i.e., on whether the entity lodges GPFSs) in the model differs from zero. A higher chi-square statistic indicates that the independent variables have greater predictive ability. The degrees of freedom (df) are the minimum number of independent information points or data that can be used to estimate a test statistic. In this case, the degrees of freedom indicate the number of independent variables that are free to vary and that are used in the calculation of the chi-square statistic.

20 The analysis in this Report takes the natural logarithm of a number of variables. This is done to linearise and normalise the function being examined, enabling the estimation and interpretation of the coefficients on the variables in the model.

(b) natural logarithm of employees (*lnemployees*);

(c) more than one member (*mem_dum*);

(d) natural logarithm of creditors (*lnCREDITORS*); and

(e) natural logarithm of total liabilities (*lnTOTAL_LIABILITIES*).

An examination of the results of the logistic regression model indicates that the predictors provide some information about decisions to lodge GPFSs and SPFSs [$\chi^2 = 48.56$, df (degrees of freedom) = 5, $p < .0001$]; however, the explanatory power of the model is low (as indicated by the pseudo R^2 [refer Table 4 below] only explaining the decision to prepare GPFSs for these entities 8.08% of the time). According to the Wald criterion, *lntrading*, *lnemployee*s, and *lnCREDITORS* are not statistically significant in the model, whereas *mem_dum* and *lnTOTAL_LIABILITIES* are statistically significant in the model. Table 4 shows regression coefficients and Wald statistics for each of the predictors.

The logistic regression results suggest that lodgement of GPFSs is not dependent on size and creditors, but there is a statistical relationship with the proxy for 'separation of management from economic interest' (i.e., more than one member/shareholder) and total liabilities.

In conclusion, around 20 per cent of large proprietary companies classified themselves as reporting entities (i.e., lodged GPFSs). While univariate results show significant differences across a number of dimensions that proxy for 'size', 'separation of management from economic interest', and 'indebtedness'; multivariate logistic regression results show that only levels of members/shareholders and total liabilities are associated with the decision by large proprietary companies to classify as a reporting entity and lodge GPFSs. The existence of arguably less powerful stakeholders such as employees and creditors do not appear to have significant influence in a company's decision as to whether to classify as a reporting entity and lodge GPFSs. Differences observed between the univariate and multivariate techniques used in this Part of this Report can be explained by the fact that univariate results concentrate on individual variables without including the impacts of other data into the calculations. However, multivariate techniques examine multiple variables simultaneously by combining numerous variables to consider a broader impact from the data as well as controlling for the unique contribution of each proxy for the indicative factors on the decision to lodge either GPFSs or SPFSs.

Table 4: Logistic Regression on Key Indicative Reporting Entity Test Factors – Large Proprietary Companies

Logistic regression	Number of observations	=	567
	Wald $chi^2(5)$	=	48.56
	Prob > chi^2	=	0.0000
Log pseudolikelihood = -276.065	Pseudo R^2	=	0.0808

GP_SP	**Odds Ratio**	**Std. Err.**	**z**	**p>|z|**	**[95%**	**Conf. Level]**
lntrading	1.02970	.09927	0.29	0.768	.16529	.22383
lnemployees	.90828	.08131	-1.18	0.237	-.25557	.06317
mem_dum	.54106	.21778	-2.82	0.005	-1.04108	-.18739
lnCREDITORS	1.01977	.10401	0.19	0.851	-.18429	.22343
lnTOTAL_LIABILITIES	.65777	.11781	-3.56	0.000	-.64980	-.18799
_cons	8.51841	1.40945	6.04	0.000	5.75593	11.28088

Note: ***GP_SP*** *refers to the discrete (binary) dependent variable in the model that measures whether a company is more likely to lodge GPFSs. This discrete outcome is predicted from five key independent variables that proxy* *for the reporting entity test as outlined in SAC 1.* ***_cons*** *(constant) is used as an econometric technique to enable a clearer interpretation of the impact of variables in the model on the decision to lodge GPFSs.*

3.1.2 Anecdotes – Large Proprietary Companies

While empirical tests are helpful to shed light on drivers of the decision to implement the reporting entity concept (i.e., lodge GPFSs or SPFSs), they do not fully allow an appreciation of the variation in reporting decisions made. Thus, further insight is provided via anecdotes (below) that highlight the variation observed.

(a) A management services company stated its sole business purpose was to provide administration services and staff to the wider group. The company had $100 million in assets, $16 million in trade creditors and 55 employees who were charged out to the group. This company was not classified as a reporting entity and lodged SPFSs.

(b) In the sample there were four aged care providers, all of which collected bonds from residents living in the entities' facilities. Three of the four companies were classified as reporting entities and lodged GPFSs and one of the four indicated they were not a reporting entity and lodged SPFSs. The non-reporting entity had over $20 million in resident bonds (liabilities), employed more than 100 staff and had more than $1 million in trade creditors.

(c) One example was noted of a global financial services company lodging SPFSs, with stated activities that suggest the probable impact on the welfare of external parties – a factor mentioned in SAC 1 as indicating the existence of a reporting entity. In the large proprietary companies sample, this company reported the second largest amount of *trade and other payables*, which included almost $500 million owed to external parties. This same company reported in a note *unsecured external borrowings* (which included *client segregated funds* of more than $200 million) of more than $2 billion in total. Two other entities in the same industry and with similar financial profiles, lodged GPFSs.

(d) One company noted was a wholly-owned subsidiary of a global mining company, reporting more than 500 employees, which had classified as a non-reporting entity. The same company reported *trade payables* of almost $250 million – one of the largest amounts for companies lodging SPFSs.

(e) A global engineering company was noted that lodged SPFSs, having only one member but more than 4,000 employees. This company reported *trade payables* of almost $100 million (2009) and *amount due to customers under engineering contracts* of just under $160 million (2009). In the balance sheet, the total amount of *current trade payables* (which includes the two amounts mentioned previously) was nearly $300 million, one of the largest for companies lodging SPFSs.

3.1.3 Auditor Choice – Large Proprietary Companies

Auditor choice among the large proprietary companies was examined to give some insight into the costs and benefits of alternative regulatory approaches that might be considered for these companies. While there is ample research evidence on auditor choice for listed entities (e.g., Knechel et al., 2008), there is a paucity of evidence for private companies. Research literature suggests that Big 4 auditors[21] are associated with higher financial reporting quality among listed public companies (Francis, 2004). Further, if clients of Big 4 auditors are, on average larger, there should be a greater proportion of Big 4 clients classifying as reporting entities (lodging GPFSs) relative to the clients of non-Big 4 firms.

Auditor choice and type of financial statements (GPFSs v SPFSs) are presented in Table 5 below. For the 345 companies that were subject to an audit (n=345), it appears there is no statistically significant difference ($\chi^2 = 0.0508$, $p = 0.822$) in the proportion of clients of Big 4 auditors lodging GPFSs (20%) and the clients of non-Big 4 auditors lodging GPFSs (24%). Interestingly, 43 companies (i.e., 12.5% of the large proprietary companies sample) were granted an audit exemption by the ASIC.

Table 5: Auditor Choice – GPFSs and SPFSs – Large Proprietary Companies

		GPFSs		SPFSs	
	Total	**Freq.**	**%**	**Freq.**	**%**
Audit Exemption Granted by the ASIC	43	4	10	39	90
No Audit Opinion	4	1	25	3	75
Audit Opinion Issued (i.e., Audit Conducted)	345	74	21	273	79
Total	**392**	**79**	**20**	**315**	**80**
Big 4 Auditor	242	48	20	194	80
Non-Big 4 Auditor	103	25	24	78	76
Total	**345**	**73**	**21**	**272**	**79**

3.1.4 Audit Fees – Large Proprietary Companies

Table 6 contains results of the analysis of audit fees (and fees for non-audit services 'NAS') by type of financial statements. Since disclosure requirements for GPFSs are more detailed and complex than for SPFSs, it is predicted that the audit fees for GPFSs would be greater than the audit fees charged to companies lodging SPFSs, and initial analysis provides support for this prediction ($t = 4.6227$, $p = .0000$). This analysis, however, does not take into account the size of company. Prior research (e.g., Chow, 1982; Abdel-Khalik, 1993) finds that firm (i.e., company) size is the most significant predictor of the audit fee. Accordingly, the audit fee is scaled by total assets in order to control for company-size effects. A comparison of the audit fees (scaled by total assets) paid by companies lodging GPFSs with the audit fees paid by companies lodging SPFSs reveals no significant differences ($t = 0.3995$, $p = .6552$). This suggests that, if companies were to be required to lodge GPFSs rather than SPFSs, there would not be any discernible direct audit cost burden on companies.

Similarly, there is no statistically significant difference in the non-audit service fees (NAS) paid by clients lodging GPFSs and clients lodging SPFSs.

21 References in this Report to 'Big 4 auditors' are to: Deloitte, Ernst & Young, KPMG and PricewaterhouseCoopers.

Table 6: Audit Fees Comparison – GPFSs and SPFSs – Large Proprietary Companies

n = 333*	Mean	GPFSs	SPFSs	Significance of Differences
Audit Fees ($)	$130,224	$221,141	$97,993	t = 4.6227 p = 0.0000
Non-Audit Service Fees ($)	$85,171	$113,799	$78,443	**NS** t = 1.5059 p = 0.0666
Audit Fee scaled by total assets (%)	.0070773	.0052561	.0077602	**NS** t = 0.3995 p = 0.6552
NAS scaled by total assets (%)	.0010541	.000737	.0013171	**NS** t = 1.3884 p = 0.9169

* *Missing data for 12 companies that did not disclose audit fee data*.

While initial testing suggested statistically significant differences on audit fees[22] paid to Big 4 auditors (t = 4.4047, p = .0000 – see Table 7 below) and non-audit service fees paid to Big 4 auditors as a group (t = 2.5141, p = .0063 – see Table 7 below), this difference disappears when company-sizes are controlled for. Specifically, there is no statistically significant difference in the audit fees scaled by total assets paid to Big 4 auditors compared with the audit fees scaled by total assets paid to non-Big 4 auditors. This finding is in contrast to an audit fee premium to the Big 4 routinely found in the listed public company market segment (DeFond, 1992; Teoh & Wong, 1993; Craswell et al., 1995; Francis et al., 1999).

Table 7: Audit Fees Comparison – Big 4 versus Non-Big 4 – Large Proprietary Companies

n = 333*	Mean	Big 4	Non-Big 4	Significance of Differences
Audit Fees ($)	$130,224	$167,028	$49,907	t = 4.4047 p = 0.0000
Non-Audit Service Fees ($)	$85,171	$106,287	$50,132	t = 2.5141 p = 0.0063
Audit Fee scaled by total assets (%)	.0070773	.0104213	.0017642	NS t = 1.3687 p = 0.0858
NAS scaled by total assets (%)	.0010541	.0011407	.0012622	**NS** t = 0.2912 p = 0.6145

* *Missing data for 12 companies that did not disclose audit fee data.*

3.2 Foreign-Controlled Companies

As noted in Table 1 above, there were 2,797 small proprietary companies controlled by a foreign company registered with the ASIC in 2010-11. Sections 9 and 292(2)(b) of Part 2M of the Corporations Act, as well as the 'control definition' in AASB 127 *Consolidated and Separate Financial Statements*,[23] are used to determine whether a small proprietary company is considered to be 'controlled' by a foreign company (ASIC, 2011a).

22 Audit fee studies often find large (Big 4) audit firms earn significantly higher fees than smaller (non-Big 4) firms because of their perceived credibility and quality of service (e.g., DeFond, 1992).

23 AASB 10 *Consolidated Financial Statements* supersedes AASB 127 for periods beginning on or after 1 January 2013.

A random sample (i.e., with a 95% confidence level) of 340 foreign-controlled companies was drawn for this group. Results presented in Table 8 show that, similar to the distribution observed among large proprietary companies, a small proportion (approximately 16%) of foreign-controlled companies lodged GPFSs and around 84 per cent lodged SPFSs.

Table 8: Frequency of Type of Financial Statements in the Sample – Foreign-Controlled Companies

	Frequency	%
GPFSs	53	15.6
SPFSs	287	84.4
Total:	**340**	**100.0**

3.2.1 Statistical Analysis – Foreign-Controlled Companies

Results for univariate t-tests for differences in the mean values for the proxies for factors identified in SAC 1 as indicative of the existence of a reporting entity, for foreign-controlled companies lodging GPFSs and SPFSs respectively, are presented in Table 9.[24] It is noteworthy that foreign-controlled companies are not required (on Form 388 lodged with the ASIC) to disclose the number of employees and the number of members. However, approximately 25 per cent of foreign-controlled companies (n = 86) reported the number of members they have in the organisation.

Table 9: Reporting Entity Test – Foreign-Controlled Companies

		GPFSs	SPFSs	Significance of Differences
Panel A: 'Size' Test				
Trading Revenue	Mean	$20,900,000	$23,300,000	NS
	Median	$3,548,690	$5,784,162	NS
*ln*Trading Revenue	Mean	$15.26	$15.31	NS
	Median	$15.10	$15.59	NS
Total Assets	Mean	$36,100,000	$31,000,000	NS
	Median	$3,708,718	$4,330,752	NS
*ln*Total Assets	Mean	$14.63	$14.49	NS
	Median	$15.36	$15.32	NS
No. Employees	Mean	Too few observations	Too few observations	Too few observations
	Median	Too few observations	Too few observations	Too few observations
*ln*No. Employees	Mean	Too few observations	Too few observations	Too few observations
	Median	Too few observations	Too few observations	Too few observations
Panel B: 'Separation of Management from Economic Interest' Test				
No. Members	Mean	23	5	NS
	Median	3	0	z = 2.162, p = .0306
More than 1 Member	%	50.0%	22.6%	NS
No. Directors	Mean	3	3	NS
	Median	3	3	NS

24 Consistent with the approach taken for the large proprietary company sample in Section 3.1 above, to enhance the generalisability of the results, a number of standard econometric techniques were applied to this sample and the other samples examined in the remainder of this Part of this Report.

		GPFSs	SPFSs	Significance of Differences
Panel C: 'Indebtedness' Test				
Creditors	Mean	$10,700,000	$5,999,715	NS
	Median	$724,854	$906,227	NS
*ln*Creditors	Mean	$13.71	$13.42	NS
	Median	$13.49	$13.72	NS
Bank Debt	Mean	$11,800,000	$4,788,035	NS
	Median	$89,990	$23,845	NS
*ln*Bank Debt	Mean	$13.53	$13.05	NS
	Median	$13.42	$12.99	NS
Total Liabilities	Mean	$21,200,000	$12,400,000	NS
	Median	$2,495,045	$2,135,819	NS
*ln*Total Liabilities	Mean	$14.75	$14.50	NS
	Median	$15.05	$14.80	NS

Note: See Table 3 above for an explanation of items referred to in this Table.

None of the variables that proxy for 'size', or 'indebtedness' demonstrate significant differences between companies lodging GPFSs and SPFSs. More specifically, the decision by these companies whether to classify as a reporting entity and lodge GPFSs does not appear to be explained by the indicative factors identified in SAC 1. For companies in the sample it appears that factors other than the characteristics (that were analysed) of the company lodging the financial statements may shape the decision. For example, the characteristics of the foreign parent and the associated implications for judging materiality may be relevant for explaining the decision. This is noted as a worthwhile avenue for further research.

Multivariate analysis – Two sets of logistic regression analyses were undertaken to understand more fully the decision by foreign-controlled companies to lodge GPFSs. Variables used in the model are the natural logarithm of trading revenue (*lntrading*), natural logarithm of creditors (*lnCREDITORS*), and natural logarithm of total liabilities (*lnTOTAL_LIABILITIES*). The variable measuring number of employees is excluded because this information is not required to be lodged by the ASIC and the variable measuring number of shareholders is excluded because there are too few observations. An examination of the results of the logistic regression model indicates that the predictors do not distinguish decisions to lodge GPFSs and SPFSs [χ^2 = 0.26, df =3, p = .9667]. The results suggest the lodgement of GPFSs by these entities does not appear to depend on any of the indicative factors outlined in SAC 1.

Table 10: Logistic Regression on Key Indicative Reporting Entity Test Factors – Foreign-Controlled Companies

Logistic regression	Number of observations	=	215
	Wald chi^2(3)	=	0.26
	Prob > chi^2	=	0.9667
Log pseudolikelihood = -101.65023	Pseudo R^2	=	0.0015

GP_SP	**Odds Ratio**	**Std. Err.**	**z**	**p>|z|**	**[95%**	**Conf. Level]**
lntrading	1.07149	.15272	0.48	0.628	.81035	1.41679
lnCREDITORS	.99817	.11102	-0.02	0.987	.80266	1.24131
lnTOTAL_LIABILITIES	.97666	.14956	-0.15	0.877	.72343	1.31854
_cons	2.27659	4.27779	0.44	0.662	.05726	90.51512

Note: See Table 4 above for an explanation of GP_SP and _cons.

3.2.2 Anecdotes – Foreign-Controlled Companies

The following anecdotes highlight the variation observed.

(a) One example was noted of a company that manufactures and sells aggregate, concrete, concrete pipe and concrete precast products in Australia, which is commonly regarded as one of the few largest in its industry globally. The company classified as a non-reporting entity and lodged SPFSs, despite reporting revenues of between $1 billion and $2 billion in each of the 2008 and 2009 years.

(b) In the sample there were four financial services companies that all had revenues of less than $10 million. Two of the four companies were classified as reporting entities and lodged GPFSs and two indicated they were not reporting entities and lodged SPFSs. One of the non-reporting entities had over $6 million in revenues and over $150 million in assets.

(c) Consistent with other samples, there is a difference with how similar-sized companies are classified. In the sample, ten companies had revenues over $100 million and assets over $50 million. Four of these companies were classified as reporting entities and lodged GPFSs and six of the companies indicated they were not reporting entities and lodged SPFSs.

3.2.3 Auditor Choice – Foreign-Controlled Companies

Auditor choice and type of financial statements (GPFSs v SPFSs) is presented in Table 11 below. For the 332 foreign-controlled companies that were subject to an audit, the clients of Big 4 auditors were no more likely to lodge GPFSs (13.3%) than clients of the non-Big 4 auditors (19.9%), in the context that the difference between the percentages is not statistically significant (χ^2 = 2.1689, p = 0.141).

Table 11: Auditor Choice by – GPFSs and SPFSs – Foreign-Controlled Companies

		GPFSs		SPFSs	
	Total	**Freq.**	**%**	**Freq.**	**%**
Audit Exemption Granted by the ASIC	-	-	-	-	-
No Audit Opinion	8	1	12.5	7	87.5
Audit Opinion Issued	332	52	15.7	280	84.3
Total	**340**	**53**	**16.0**	**287**	**84.0**
Big 4 Auditor	196	26	13.3	170	86.7
Non-Big 4 Auditor	136	27	19.9	109	80.1
Total	**332**	**53**	**16.0**	**279**	**84.0**

3.3 Small Proprietary Companies (not Controlled by a Foreign Company) where Financial Statements are Specifically Sought

Some small proprietary companies lodge financial statements with the ASIC. Under the requirements of Sections 293 and 294 of the Corporations Act, the ASIC or shareholders with five per cent or more of the voting capital may direct a small proprietary company to prepare financial statements. The rationale for this requirement is to ensure that shareholders with five per cent or more of the voting capital in these small entities have "adequate access to financial information without imposing an unreasonable burden on small companies" (Australian Commonwealth Treasury, 2006, p.3). In addition, the ASIC might direct a company to lodge audited financial statements because of a dispute between shareholders or the company might have committed a ‘strict liability offence’ such as abrogation of directors’ duties.

In 2010-11, as reflected in Table 1 above, the financial statements of 186 small proprietary companies were specifically sought and lodged. A random sample (i.e., with a 95% confidence level) of 95 small proprietary companies was drawn from this group. Table 12 (below) shows that around 24 per cent of the small proprietary companies in the sample lodged GPFSs and around 76 per cent lodged SPFSs.

Table 12: Frequency of Type of Financial Statements in the Sample – Small Proprietary Companies

	Frequency	%
GPFSs	23	24.2
SPFSs	72	75.8
Total:	**95**	**100.0**

3.3.1 Statistical Analysis – Small Proprietary Companies

Further empirical analysis was conducted to understand any differences between the companies lodging GPFSs and SPFSs that might explain the application of the reporting entity concept by this group. Table 13 shows results of statistical tests examining mean and median differences on the proxies for indicative factors outlined in SAC 1, comparing small proprietary companies that lodged GPFSs and SPFSs. Table 13 shows significant differences on the variables *lnTrading Revenue*, *Total Assets*, *Bank Debt* and *Total Liabilities* for companies lodging SPFSs compared with GPFSs – but not in the predicted direction. More specifically, it appears companies lodging SPFSs are larger in size (based on assets and revenue) and appear to have both larger mean value liability amounts (Mean = $76.4 million) compared with companies lodging GPFSs (Mean = $2.73 million) and have larger median bank debts recorded in their financial statements ($52,350 for SPFSs v $0 for GPFSs). It was not feasible to conduct mean and median comparisons on number of employees because this data is not required to be reported (i.e., four companies in the GPFSs group revealed number of employees ranging from 29 to 80 employees in Form 388, the remainder did not disclose employee numbers). The remaining measures that proxy for ‘indebtedness’ such as *creditors* and *bank debt* also demonstrate non-significant differences between small proprietary companies lodging GPFSs and SPFSs.

In summary, the indicative factors identified in SAC 1 as suggesting the existence of users dependent on GPFSs do not appear to explain variation in the decision to lodge GPFSs or SPFSs by small proprietary companies. The results discussed above and presented in Table 13 suggest that lodgement of SPFSs by small proprietary companies is associated with the size of company and the size of their indebtedness, although contrary to expectations, larger companies with higher liability levels more commonly lodge SPFSs. The significant inverse association of size and total liabilities is counter-intuitive. However, when a multivariate analysis is conducted (see Table 14), these results disappear, suggesting that, overall, company characteristics analysed for the purpose of this Report do not significantly explain the reporting entity decision.

Table 13: Reporting Entity Test – Small Proprietary Companies

		GPFSs	SPFSs	Significance of Differences
Panel A: 'Size' Test				
Trading Revenue	Mean	$7,848,856	$48,100,000	NS
	Median	$1,061,551	$3,350,658	NS
*ln*Trading Revenue	Mean	$14.91	$15.63	t = -2.0255, p = .0259
	Median	$13.92	$15.39	z = -1.891 , p = .0587
Total Assets	Mean	$4,604,980	$94,400,000	t = -2.0772, p = .0207
	Median	$1,301,887	$4,804,023	NS
*ln*Total Assets	Mean	$13.64	$14.39	NS
	Median	$14.08	$15.44	NS
No. Employees	Mean	Too few observations	Too few observations	Too few observations
	Median	Too few observations	Too few observations	Too few observations
*ln*No. Employees	Mean	Too few observations	Too few observations	Too few observations
	Median	Too few observations	Too few observations	Too few observations
Panel B: 'Separation of Management from Economic Interest' Test				
No. Members	Mean	Too few observations	Too few observations	Too few observations
	Median	Too few observations	Too few observations	Too few observations
More than 1 Member	%	Too few observations	Too few observations	Too few observations
No. Directors	Mean	4	4	NS
	Median	3	3	NS
Panel C: 'Indebtedness' Test				
Creditors	Mean	$1,965,990	$34,600,000	NS
	Median	$147,486	$234,000	NS
*ln*Creditors	Mean	$12.42	$13.08	NS
	Median	$12.06	$13.37	NS
Bank Debt	Mean	$1,604,164	$41,200,000	NS
	Median	$0	$52,350	z = -1.979 , p = .0478
*ln*Bank Debt	Mean	$12.67	$13.20	NS
	Median	$12.29	$13.30	NS
Total Liabilities	Mean	$2,726,354	$76,400,000	t = -1.7827, p = .0395
	Median	$311,804	$3,090,768	z = -1.894 , p = .0582
*ln*Total Liabilities	Mean	$13.08	$14.74	t = -2.7654, p = .0041
	Median	$12.89	$15.13	z = -2.419 , p = .0156

Note: See Table 3 above for an explanation of items referred to in this Table.

Multivariate analysis – A logistic regression analysis enables predictions of the likelihood of small proprietary companies lodging GPFSs on the basis of the natural logarithm of trading revenue (*lntrading*), natural logarithm of creditors (*lnCREDITORS*), and natural logarithm of total liabilities (*lnTOTAL_LIABILITIES*). Variables measuring number of employees and number of members/shareholders are excluded because of high rates of missing values. An examination of the logistic regression model (Table 14) indicates that the predictors do not distinguish decisions to lodge GPFSs or SPFSs [χ^2 = 3.29, df = 3, p = .3495].

Table 14: Logistic Regression on Key Indicative Reporting Entity Test Factors – Small Proprietary Companies

Logistic regression	Number of observations	=	63
	Wald $chi^2(3)$	=	3.29
	Prob > chi^2	=	0.3495
Log pseudolikelihood = -32.965833	Pseudo R^2	=	0.0467

GP_SP	**Odds Ratio**	**Std. Err.**	**z**	**p>|z|**	**[95%**	**Conf. Level]**
*ln*trading	1.42220	.39615	1.26	0.206	.82388	2.45503
*ln*CREDITORS	.86417	.18530	-0.68	0.496	.56765	1.31559
*ln*TOTAL_LIABILITIES	1.02268	.22587	0.10	0.919	.66336	1.57665
_cons	.07776	.17616	-1.13	0.260	.00092	6.59288

Note: See Table 4 above for an explanation of GP_SP and _cons.

3.3.2 Auditor Choice – Small Proprietary Companies

Auditor choice and type of financial statements (GPFSs v SPFSs) is presented in Table 15. For the 90 small proprietary companies that were subject to an audit, the clients of Big 4 auditors appear less likely to lodge GPFSs (17.5%) than clients of the non-Big 4 auditors (39.4%) and the result is statistically significant (χ^2 = 5.2449, p = 0. 022) at the 5 per cent level of significance.

Table 15: Auditor Choice – GPFSs and SPFSs – Small Proprietary Companies

		GPFSs		**SPFSs**	
	Total	**Freq.**	**%**	**Freq.**	**%**
Audit Exemption Granted by the ASIC	5	0	0.0	5	100.0
No Audit Opinion	0	0	0.0	0	0.0
Audit Opinion Issued	90	23	24.4	67	75.6
Total	**95**	**23**	**24.2**	**72**	**75.8**
Big 4 Auditor	57	10	17.5	47	82.5
Non Big 4 Auditor	33	13	39.4	20	60.6
Total	**90**	**21**	**25.6**	**67**	**74.4**

3.4 Unlisted Public Companies other than those Limited by Guarantee

Unlisted public companies include companies limited only by shares, a small number of 'no-liability' (mining) public companies and public companies limited by both shares and by guarantee. They differ from proprietary companies in their capacity to have more than 50 non-employee members and to offer shares to the public. In a sense, this suggests unlisted public companies may have broadly similar legislative obligations under the Corporations Act as a listed public company. However, in contrast to a listed public company, unlisted public companies' shares are not included on the official list of a securities exchange. All unlisted public companies registered under the Corporations Act must have at least three directors, two of whom must be Australian residents. There were 3,985 (see Table 1 above) unlisted public companies required to lodge audited financial statements with the ASIC in the financial year 2010-11.

The rationale for unlisted public companies lodging audited financial statements is that these companies have the ability to offer shares and raise capital from the general public. The Corporations Act seeks to ensure that investors or shareholders with smaller holdings have access to audited financial information for decision-making purposes (Australian

Commonwealth Treasury, 2006). These companies can decide to lodge either GPFSs or SPFSs depending on their reporting entity status.

A random sample (i.e., with a 95% confidence level) of 347 small proprietary companies was drawn for this group. Table 16 shows that, in contrast to the samples discussed above, a majority (around 70%) of unlisted public companies lodged GPFSs.

Table 16: Frequency of Type of Financial Statements in the Sample – Unlisted Public Companies

	Frequency	%
GPFSs	242	69.7
SPFSs	105	30.3
Total:	**347**	**100.0**

3.4.1 Statistical Analysis – Unlisted Public Companies

Table 17 contains results of the tests on proxies for factors identified in SAC 1 as suggesting the existence of users dependent on the information contained in GPFSs. The Table indicates that, with the exception of median *lnTrading revenue*, variables that proxy for ‘size’ do not systematically explain the decision by companies in this sample to lodge GPFSs. It is not feasible to conduct a mean/median comparison on other variables in this category because these companies are not required to disclose certain information (e.g. employee numbers).

Variables that proxy for the ‘separation of management from economic interest’ such as number of directors, show that significant differences exist between companies lodging GPFSs and SPFSs, that is, companies lodging GPFSs have, on average, significantly more directors (mean = 5) compared with companies lodging SPFSs (mean = 4). It is not possible, however, to conduct comparisons on the variables ‘number of members’ and ‘more than one member’ (i.e., a measure filtering out entities that only have one member) as there were no observations for these variables for both GPFSs and SPFSs groups.

Measures that proxy for ‘indebtedness’ such as mean values for creditors, bank debt and total liabilities all show non-significant differences between the GPFSs and SPFSs groups. While creditors, bank debt, and total liabilities show significant mean differences, these differences should be regarded cautiously as some extreme values appear to be driving these results (i.e., one financial institution observation with total liabilities of around $15 billion and one insurance company with total liabilities of almost $30 billion).

Table 17: Reporting Entity Test – Unlisted Public Companies

		GPFSs	SPFSs	Significance of Differences
Panel A: ‘Size’ Test				
Trading Revenue	Mean	$231,000,000	$54,400,000	NS
	Median	$2,372,928	$361,733	z = 2.691 , p = .0071
*ln*Trading Revenue	Mean	$15.14	$14.86	NS
	Median	$15.15	$14.81	NS
Total Assets	Mean	$461,000,000	$162,000,000	NS
	Median	$3,288,152	$2,422,746	NS
*ln*Total Assets	Mean	$15.00	$14.44	NS
	Median	$15.08	$15.00	NS
No. Employees	Mean	No observations	No observations	No observations
	Median	No observations	No observations	No observations
*ln*No. Employees	Mean	No observations	No observations	No observations
	Median	No observations	No observations	No observations

		GPFSs	SPFSs	Significance of Differences
Panel B: 'Separation of Management from Economic Interest' Test				
No. Members	Mean	No observations	No observations	No observations
	Median	No observations	No observations	No observations
More than 1 Member	%	No observations	No observations	No observations
No. Directors	Mean	5	4	t = 4.9058, p = .0000
	Median	4	3	z = 2.491 , p = .0128
Panel C: 'Indebtedness' Test				
Creditors	Mean	$128,000,000	$38,200,000	t = 1.9228, p = .0277
	Median	$679,059	$281,327	NS
*ln*Creditors	Mean	$13.63	$13.13	NS
	Median	$13.65	$12.66	NS
Bank Debt	Mean	$293,000,000	$55,700,000	t = 1.7809, p = .0381
	Median	$ 77,256	$25,990	NS
*ln*Bank Debt	Mean	$14.28	$14.73	NS
	Median	$14.09	$15.16	NS
Total Liabilities	Mean	$384,000,000	$69,900,000	t = 2.1094, p = .0179
	Median	$1,09,885	$558,277	NS
*ln*Total Liabilities	Mean	$14.45	$14.12	NS
	Median	$14.32	$14.25	NS

Note: See Table 3 above for an explanation of items referred to in this Table.

Multivariate analysis – A logistic regression analysis enables predictions of companies lodging GPFSs on the basis of the natural logarithm of trading revenue (*lntrading*), directors, natural logarithm of creditors (*lnCREDITORS*), and natural logarithm of total liabilities (*lnTOTAL_LIABILITIES*). Variables measuring number of employees and number of shareholders are excluded because of a lack of observations. An examination of the logistic regression model indicates that the predictors provide some information about decisions to lodge GPFSs or SPFSs [χ^2 = 10.05, df =4, p = .0395]; however, the explanatory power of the model is low (as indicated by the pseudo R^2 [refer Table 18 below]). Specifically, the logistic regression results suggest that lodgement of GPFSs among unlisted public companies other than those limited by guarantee was not dependent on 'size' and 'liabilities' (i.e., indicative factors outlined in SAC 1), but was dependent on the number of directors. Results suggest neither the level of total liabilities nor the level of creditors influenced whether an unlisted public company was classified as a reporting entity and lodged GPFSs.

Table 18: Logistic Regression on Key Indicative Reporting Entity Test Factors – Unlisted Public Companies

Logistic regression	Number of observations	=	164
	Wald $chi^2(4)$	=	10.05
	Prob > chi^2	=	0.0395
Log pseudolikelihood = -40.984975	Pseudo R^2	=	0.0977

GP_SP	Odds Ratio	Std. Err.	z	p>|z|	[95%	Conf. Level]
lntrading	.93654	.07719	-0.80	0.426	.79683	1.10075
directors	.60535	.11042	-2.75	0.006	.42340	.86551
lnCREDITORS	.77758	.13533	-1.45	0.148	.55285	1.09367
lnTOTAL_LIABILITIES	1.24413	.23139	1.17	0.240	.86408	1.79133
_cons	2.37546	4.88839	0.42	0.674	.04208	134.0948

Note: See Table 4 above for an explanation of GP_SP and _cons.

3.4.2 Anecdotes – Unlisted Public Companies

The following anecdotes highlight the diverse application of the reporting entity concept (lodgement of GPFSs or SPFSs). These anecdotes provide a sample of the variation observed.

(a) One example was noted of a company involved in iron ore and copper-gold mining, which had revenues of almost $2 billion and around $1.5 billion over the 2007 and 2008 years and assets values of around $3 billion in each of the 2007 and 2008 years, which was classified as a non-reporting entity and lodged SPFSs.

(b) In the sample there were five financial services companies that all had revenues of less than $1 million. Three of the five companies were classified as reporting entities and lodged GPFSs and two of the five indicated they were not reporting entities and lodged SPFSs. One of the non-reporting entities had in excess of $12 million in assets.

(c) There appears to be a discrepancy with how similar-sized companies are classified. In the sample, five companies had revenues ranging between $130 million and $200 million and assets ranging between $26 million and $600 million. Two of these companies were classified as reporting entities and lodged GPFSs and three companies indicated they were not reporting entities and lodged SPFSs. One of the non-reporting entities had revenues of more than $180 million and assets of around $600 million.

3.4.3 Auditor Choice – Unlisted Public Companies

Auditor choice and type of financial statements (GPFSs v SPFSs) is presented in Table 19. For the 347 unlisted public companies, it appears that clients of Big 4 auditors are less likely to lodge GPFSs (62.0%) compared with clients of the non-Big 4 auditors (74.0%).

Table 19: Auditor Choice – GPFSs and SPFSs – Unlisted Public Companies

		GPFSs		SPFSs	
	Total	**Freq.**	**%**	**Freq.**	**%**
Audit Exemption Granted by the ASIC	0	0	0.0	0	0.0
No Audit Opinion	0	0	0.0	0	0.0
Audit Opinion Issued	347	242	69.7	105	30.3
Total	**347**	**242**	**69.7**	**105**	**30.3**
Big 4 Auditor	135	84	62.0	51	38.0
Non-Big 4 Auditor	212	157	74.0	54	26.0
Total	**347**	**242**	**69.7**	**105**	**30.3**

3.5 Public Companies Limited by Guarantee

Public companies limited by guarantee must comply with the broader legislation that applies to all public companies. Charitable or not-for-profit organisations that register a company structure with the ASIC (i.e., create a legal entity that is separate from its members)[25] are

25 A public company is a legal entity and must abide by a number of requirements. Some of these requirements are to have at least three directors and a secretary; have at least one member; be internally managed by a constitution and replaceable rules; appoint a registered company auditor within one month of

examples of public companies limited by guarantee. These companies must include the words ‘Limited’ or ‘Ltd’ after their name, unless they are eligible for an exemption from this requirement from the ASIC. Common examples of companies in this group are sports and recreation-related organisations, community service organisations, education-related institutions, and religious organisations (Australian Commonwealth Treasury, 2007). As noted in Table 1 above, there were 8,404 public companies limited by guarantee that lodged audited financial statements with the ASIC in the financial year 2010-11.

Under the Corporations Act, public companies limited by guarantee do not have the power to issue shares to members but instead each member guarantees to pay a nominal amount specified in the company’s constitution in the event that the company goes into liquidation. In other words, the liability of the company’s members is limited to the amount (typically a nominal amount) that members have guaranteed to contribute to the company in case of liquidation. Unlisted public companies tend to be significantly larger than limited-by-guarantee companies and, because of their share capital structure, are more likely to have a profit motive compared with limited by guarantee companies (Australian Commonwealth Treasury, 2007).

The financial reporting obligations of both unlisted public companies limited by shares and of limited-by-guarantee companies are fundamentally the same. However, since July 2010 (i.e., after the years for which data was analysed), limited-by-guarantee companies are subject to a three-tier reporting framework that is based on the size of the company. Under this framework, companies that have revenue of $1 million or more must lodge both audited financial statements and a directors’ report (although the requirements for directors’ reports are less detailed than for the reports required for other companies). Companies with revenue of less than $1 million must lodge both financial statements and a directors’ report, and can have their financial statements reviewed, rather than audited. ‘Small companies limited by guarantee’, being those with revenue less than $250,000, are exempt (unless directed by the ASIC) from lodging financial statements.

Limited-by-guarantee companies are mostly not-for-profit organisations and the legal nature of these companies is more complex than in the for-profit proprietary sector.

The broader range of not-for-profit entities includes entities regulated at state and territory levels. For example, each state and territory jurisdiction has its own requirements relating to incorporated associations and not-for-profit entities, which can restrict the capacity of the organisation to operate in more than one state or territory. These entities are not regulated by the ASIC unless they take on a company structure. Part B of this Report examines the financial reporting by these entities. Researchers with an interest in this area might examine auditing practices and compare potential differences across federal and state jurisdictions.

A random sample (i.e., with a 95% confidence level) of 370 companies was drawn from the population of public companies limited by guarantee, yielding a usable sample of 365. As shown in Table 20, around 66 per cent of public companies limited by guarantee lodged GPFSs, while approximately 34 per cent lodged SPFSs. For three (0.8%) limited-by-guarantee companies, the type of financial statements lodged was not clearly stated.

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its registration; keep financial records; prepare, have audited and lodge financial statements and reports annually; and send its members a copy of its financial statements and reports (see ASIC, 2012).

Table 20: Frequency of Type of Financial Statements in the Sample – Public Companies Limited by Guarantee

	Frequency	%
GPFSs	239	65.5
SPFSs	123	33.7
Unable to Determine	3	0.8
Total:	**365**	**100.0**

3.5.1 Statistical Analysis – Public Companies Limited by Guarantee

Table 21 shows results of the tests for differences on the proxies for indicative factors identified in SAC 1. Variables that proxy for 'size', that is, *trading revenue* and *total assets* (except for mean *total assets*) demonstrate that larger companies in this group seem more likely to have lodged GPFSs than SPFSs. It was not feasible to conduct a mean/median comparison on the variable 'number of employees' because this data is not required to be reported to the ASIC. Six entities lodging GPFSs disclosed employee numbers (i.e., mean = 68 and median = 21 employees) and two entities lodging SPFSs disclosed that they had no employees.

Table 21: Reporting Entity Test – Public Companies Limited by Guarantee

		GPFSs	SPFSs	Significance of Differences
Panel A: 'Size' Test				
Trading Revenue	Mean	$4,811,991	$313,197	t = 3.0093, p = .0015
	Median	$665,533	$37,059	z = 6.412 , p = .0000
*ln*Trading Revenue	Mean	$13.28	$11.23	t = 4.3222, p = .0001
	Median	$13.57	$12.32	z = 4.826 , p = .0000
Total Assets	Mean	$8,235,319	$6,651,580	NS
	Median	$1,328,480	$113,079	z = 7.507 , p = .0000
*ln*Total Assets	Mean	$13.99	$11.85	t = 6.6326, p = .0000
	Median	$14.20	$12.02	z = 7.507 , p = .0000
No. Employees	Mean	68	0	Too few observations
	Median	21	0	Too few observations
*ln*No. Employees	Mean	Too few observations	Too few observations	Too few observations
	Median	Too few observations	Too few observations	Too few observations
Panel B: 'Separation of Management from Economic Interest' Test				
No. Members	Mean	928	102	t = 3.9264, p = .0001
	Median	68	9	NS
More than 1 Member	%	65.7%	34.3%	NS
No. Directors	Mean	8	5	t = 5.8828, p = .0000
	Median	8	5	z = 5.808 , p = .0000
Panel C: 'Indebtedness' Test				
Creditors	Mean	$953,115	$637,674	NS
	Median	$123,812	$6,961	z = 7.450 , p = .0000
*ln*Creditors	Mean	$11.91	$10.05	t = 6.1311, p = .0000
	Median	$11.91	$10.14	z = 6.163 , p = .0000
Bank Debt	Mean	$1,489,798	$1,900,900	NS
	Median	$18,000	$0	z = 4.863 , p = .0000
*ln*Bank Debt	Mean	$11.77	$10.99	NS
	Median	$11.63	$10.52	z = 2.654 , p = .0080
Total Liabilities	Mean	$3,797,478	$2,341,091	NS
	Median	$272,913	$12,849	z = 7.323 , p = .0060
*ln*Total Liabilities	Mean	$12.64	$10.75	t = 5.6590, p = .0000
	Median	$12.81	$10.61	z = 5.990 , p = .0000

Note: See Table 3 above for an explanation of items referred to in this Table.

The variables that proxy for the 'separation of management from economic interest' such as number of members and number of directors show that significant differences exist between companies lodging GPFSs and SPFSs, that is, companies lodging GPFSs have significantly more members (mean = 928) and directors (mean = 8) compared with companies lodging SPFSs (Members mean = 102, and; Directors mean = 5). The results suggest that the factors identified in SAC 1 relating to 'size' and 'separation of ownership and management' could provide some explanation of the decision by companies in this group to lodge GPFSs.

The above interpretation of the results is further corroborated by variables that proxy for 'indebtedness' such as *creditors*, *total liabilities* and *bank debt*. The three variables show significant median differences between the GPFSs and SPFSs groups in the expected direction, suggesting that entities with higher debt were more likely to lodge GPFSs.

Multivariate analysis – A logistic regression analysis enables predictions of the decisions by companies to lodge GPFSs. Variables used in the model are the natural logarithm of trading revenue (*lntrading*), number of members, number of directors, the natural logarithm of creditors (*lnCREDITORS*), and natural logarithm of total liabilities (*lnTOTAL_LIABILITIES*). The variable measuring 'bank debt' is excluded because of collinearity[26] issues with 'total liabilities'. An examination of the logistic regression model indicates that the predictors provide some information about decisions to lodge GPFSs or SPFSs [χ^2 = 15.62, df = 5, p = .0080]. While the explanatory power of the model (as indicated by the pseudo R^2 [refer Table 22 below]) is higher compared with previously reported models (e.g., Table 4 in relation to large proprietary companies), it is only *lnCREDITORS* that is a significant predictor in the model, albeit with marginal statistical significance (z = -1.82, p = .068), suggesting that creditors appear to influence whether public companies limited by guarantee were classified as reporting entities and lodge GPFSs. However, the remaining logistic regression results (Table 22) suggest that lodgement of GPFSs by these companies are not dependent on any other of the indicative factors outlined in SAC 1.

Table 22: Logistic Regression on Key Indicative Reporting Entity Test Factors – Public Companies Limited by Guarantee

Logistic regression	Number of observations	=	77
	Wald $chi^2(5)$	=	15.62
	Prob > chi^2	=	0.0080
Log pseudolikelihood = -21.922044	Pseudo R^2	=	0.2627

GP_SP	Odds Ratio	Std. Err.	z	p>|z|	[95%	Conf. Level]
lntrading	.97371	.15416	-0.17	0.866	.71395	1.32800
members	.99915	.00098	-0.86	0.387	.99724	1.00107
directors	.90172	.14214	-0.66	0.512	.66206	1.22814
lnCREDITORS	.54743	.18086	-1.82	0.068	.28650	1.04603
lnTOTAL_LIABILITIES	1.09479	.22782	0.44	0.663	.72812	1.64612
_cons	174.3637	454.0399	1.98	0.047	1.05912	28705.74

Note: See Table 4 above for an explanation of GP_SP and _cons.

26 Collinearity refers to a situation when there is a near perfect relationship between two independent variables. The regression model excludes highly correlated independent variables when calculating the model.

3.5.2 Anecdotes – Public Companies Limited by Guarantee

The following anecdotes highlight the variation observed.

(a) In the sample there were six sport and recreation clubs that all had revenues less than $500,000. Three of the six clubs were classified as reporting entities and lodged GPFSs and three indicated they were not reporting entities and lodged SPFSs. One of the non-reporting entities had more than $300,000 in revenues and over $5 million in assets.

(b) Similar to other types of companies, there is an apparent discrepancy with how similar-sized companies are classified. In the sample, nine companies had revenues of less than $1 million. Three of these companies lodged GPFSs and six companies indicated they were not reporting entities and lodged SPFSs. One of the non-reporting entities had revenues of more than $750,000 and assets of almost $20 million in comparison to one of the reporting entities that had revenues of less than $400,000 and assets of less than $400,000.

3.5.3 Auditor Choice – Public Companies Limited by Guarantee

Table 23 presents results for auditor choice and type of financial statements (GPFSs v SPFSs). For the 362 public companies limited by guarantee that were subject to an audit (n=362), it appears that clients of Big 4 auditors are almost equally likely to lodge GPFSs (69.6%) compared with clients of the non-Big 4 auditors (65.8%).

Table 23: Auditor Choice – GPFSs and SPFSs – Public Companies Limited by Guarantee

		GPFSs		SPFSs	
	Total	**Freq.**	**%**	**Freq.**	**%**
Audit Exemption Granted by the ASIC	0	0	0.0	0	0.0
No Audit Opinion	0	0	0.0	0	0.0
Audit Opinion Issued	362	239	66.1	123	33.9
Total	**362**	**239**	**66.1**	**123**	**33.9**
Big 4 Auditor	35	24	69.6	11	31.4
Non-Big 4 Auditor	327	215	65.8	112	34.2
Total	**362**	**239**	**66.1**	**123**	**33.9**

3.6 Additional Analysis of Companies Lodging SPFSs by Size and Indebtedness

The results reported in Sections 3.1 to 3.5 above suggest there is variation in the manner in which the reporting entity concept is applied by companies required to lodge financial statements.

Table 24 shows additional analyses of companies that lodged SPFSs, by size and indebtedness levels. This might assist in conducting any sensitivity analysis that might be undertaken in regard to the impact of possible changes in thresholds for the lodgement of financial statements by companies.

Table 24. Comparison of Companies Lodging SPFSs by Proxies for Size-Thresholds and Indebtedness-Thresholds [Table 24 updated on 30 June 2014 to correct errors]

	Large Proprietary		Foreign-Controlled		Unlisted Public		Limited by Guarantee	
Level Trading Revenue	**%**	**Cum%**	**%**	**Cum%**	**%**	**Cum%**	**%**	**Cum%**
<= $5m	10.6	10.6	47.0	47.0	70.3	70.3	100.0	100.0
> $5m & <= $10m	4.1	14.7	19.5	66.5	2.7	73.0		
> $10m & <= $25m	14.3	29.0	21.6	88.1	6.7	79.7		
> $25m & <= $50m	27.5	56.5	5.4	93.5	2.7	82.4		
> $50m & <= $100m	18.0	74.5	4.3	97.8	5.4	87.8		
> $100m & <= $200m	13.7	88.2	2.2	100.0	12.2	100.0		
> $200m & <= $300m	4.1	92.3						
> $300m	7.7	100.0						
	100.0		**100.0**		**100.0**		**100.0**	
Level Total Assets	**%**	**Cum%**	**%**	**Cum%**	**%**	**Cum%**	**%**	**Cum%**
<= $12.5m	15.7	15.7	72.1	72.1	67.6	67.6	95.9	95.9
> $12.5m & <= $25m	20.3	36.0	10.8	82.9	6.7	74.3	2.5	98.4
> $25m & <= $50m	25.4	61.4	6.6	89.5	3.8	78.1	1.6	100.0
> $50m & <= $100m	16.2	77.6	3.9	93.4	6.7	84.8		
> $100m & <= $250m	11.3	88.9	4.2	97.6	4.7	89.5		
> $250m	11.1	100.0	2.4	100.0	10.5	100.0		
	100.0		**100.0**		**100.0**		**100.0**	
Level Total Employees	**%**	**Cum%**	**%**	**Cum%**	**%**	**Cum%**	**%**	**Cum%**
0	11.5	11.5	-		-		-	
> 0 & <= 50	12.4	23.9	-		-		-	
> 50 & <= 100	18.5	42.4	-		-		-	
> 100 & <= 500	34.4	76.7	-		-		-	
> 500	23.3	100.0	-		-		-	
	100.0		**NA**		**NA**		**NA**	
Level Creditors	**%**	**Cum%**	**%**	**Cum%**	**%**	**Cum%**	**%**	**Cum%**
<= $5m	35.6	35.6	80.3	80.3	69.0	69.0	97.1	97.1
> $5m & <= $10m	19.4	55.0	7.8	88.1	5.8	74.8	1.9	99.0
> $10m & <= $25m	21.4	76.4	6.6	94.7	16.1	90.9	1.0	100.0
> $25m & <= $50m	21.7	98.1	5.3	100.0	6.8	97.7		
> $50m	1.9	100.0			2.3	100.0		
	100.0		**100.0**		**100.0**		**100.0**	
Level Bank Debt	**%**	**Cum%**	**%**	**Cum%**	**%**	**Cum%**	**%**	**Cum%**
<= $5m	52.9	52.9	86.6	86.6	75.0	75.0	100.0	100.0
> $5m & <= $10m	9.7	62.6	3.6	90.2	6.7	81.7		
> $10m & <= $25m	15.6	78.2	4.6	94.8	7.7	89.4		
> $25m & <= $50m	18.0	96.2	2.4	97.2	1.0	90.4		
> $50m	3.8	100.0	2.8	100.0	9.6	100.0		
	100.0		**100.0**		**100.0**		**100.0**	
Level Total Liabilities	**%**	**Cum%**	**%**	**Cum%**	**%**	**Cum%**	**%**	**Cum%**
<= $12.5m	36.8	36.8	83.3	83.3	76.9	76.9	96.8	96.8
> $12.5m & <= $25m	19.0	55.8	6.6	89.9	3.9	80.8	1.6	98.4
> $25m & <= $50m	17.0	72.8	5.2	95.1	7.7	88.5	0.8	99.2
> $50m & <= $100m	11.5	84.3	4.9	100.0	2.9	91.4	0.8	100.0
> $100m & <= $250m	8.6	92.9			8.6	100.0		
> $250m	7.1	100.0						
	100.0		**100.0**		**100.0**		**100.0**	

Note: From the data, it is not possible to compute employee levels among foreign-controlled, unlisted public and limited-by-guarantee companies as these companies are not required to disclose the number of employees on Form 388 lodged with ASIC.

In analysing the data in this Table, it is useful to have regard to the current tests specified in the Corporations Act that determine the financial statements lodgement requirements applicable to:

(a) large proprietary companies: proprietary companies (unless grandfathered) satisfying at least two of the following three size tests must lodge audited financial statements (and a directors' report): (i) the

consolidated gross operating revenue for the financial year is $25 million or more; (ii) the value of consolidated gross assets at the end of the financial year is $12.5 million or more; (iii) the company and entities it controls have 50 or more employees at the end of the financial year; and

(b) public companies limited by guarantee: (i) public companies limited by guarantee that have revenue of $1 million or more must lodge both audited financial statements (and a directors' report – although the requirements for the directors' reports are less onerous and less detailed than for the reports required for other companies); (ii) proprietary companies limited by guarantee with revenue of less than $1 million must lodge both a financial and directors' report, (but can have their financial statements reviewed, rather than audited); and (iii) proprietary companies limited by guarantee with revenue less than $250,000 are exempt (unless directed by the ASIC) from lodging audited financial statements.

In addition to an examination of the size thresholds, the companies' levels of indebtedness were categorised and assessed. It is assumed that the greater the levels of indebtedness, the more likely it is that external users exist who are dependent on financial information. For example, 45 per cent of large proprietary companies reported more than $10 million of creditors; 37.4 per cent reported more than $10 million of bank debt; and 44.2 per cent reported more than $25 million of total liabilities. Following the same pattern observed in the size-threshold analysis, a significantly smaller proportion of foreign-controlled, unlisted public, and limited by guarantee companies showed higher levels of indebtedness. For example, 11.9 per cent of foreign-controlled companies and 25.2 per cent of unlisted public companies reported more than $10 million of creditors. Some 9.8 per cent of foreign-controlled and 18.3 per cent of unlisted public companies reported more than $10 million of bank debt, while 10.1 per cent of foreign-controlled and 19.2 per cent of unlisted public companies reported more than $25 million in total liabilities. In regards to companies limited by guarantee, the overwhelming proportion of indebtedness levels appears to be equal or below the $5 million value for creditors (97.1%) and bank debt (100%), and equal or below the $12.5 million value for total liabilities (96.8%).

3.7 Concluding Comments on Section 3

This concludes the analysis of the application of the reporting entity concept to companies that are the subject of Part A of this Report. The results derived from multiple approaches and documented in this Part of this Report indicate that the variables that proxy for the factors identified in SAC 1 as suggesting the existence of a reporting entity do not consistently and systematically explain the decision by entities to classify as a reporting entity or a non-reporting entity (i.e., lodge GPFSs or SPFSs).

It is noted that the factors outlined in SAC 1 are indicative only and SAC 1 itself is not mandatory for preparers of financial statements, although members of professional accounting bodies in Australia are required to take all reasonable steps to apply the principles and guidance provided in the Statements of Accounting Concepts. The decision to classify as a reporting entity and lodge GPFSs could be substantially driven by factors other than those identified in SAC 1. These reporting decisions made by the companies that were examined in Section 3 are also not explained by choice of auditor (Big 4 v non-Big 4). Section 3 also included a number of anecdotes to enhance the understanding of the extent of variation with which the reporting entity concept was applied.

4. Financial Reporting Practices of Companies Lodging SPFSs

As noted in Sections 1 and 2 above, in 2005, the ASIC released RG 85, which documented concerns about the financial reporting practices of companies lodging financial statements. In RG 85, the ASIC noted that the recognition and measurement requirements of the accounting standards had not been complied with by a number of companies lodging SPFSs. Further, the ASIC expressed general concern about the quality of financial statements and identified some standards that were not being applied by a number of companies – those relating to depreciation of non-current assets, tax effect accounting, lease accounting, measurement of inventories, and recognition and measurement of liabilities relating to employee entitlements (ASIC, 2005, paragraphs 1.2 and 1.4).

A review of information briefings, regulatory guides and the academic literature (e.g., ASIC, 2000, 2005; ICAA, 2004; Walker, 2007) suggests there is variation in interpretations by practitioners of principles-based regulations and guidelines such as the reporting entity concept, which can result in variation in the reporting practices of companies lodging annual financial statements under the Corporations Act. In this Section, disclosures made by companies in the sample are considered across three broad dimensions in an effort to gain insights into the reporting decisions and practices of those companies lodging SPFSs.

First, in Section 4.1, analysis is conducted to examine the transparency of disclosures in relation to application of R&M and also the disclosures stipulated through RG 85. It is noted that, while AASB 101 requires companies to disclose (in a summary of significant accounting policies) the measurement basis (or bases) used in preparing the financial statements and other accounting policies used that are relevant to an understanding of the financial statements, companies are not specifically required to disclose whether they have applied R&M.[27] Nor are they specifically required to disclose their application of RG 85. It is possible companies that do not state they apply R&M or follow the disclosures stipulated through RG 85 may actually be meeting these requirements and guidelines, but simply not stating this. This is dealt with in Section 4.1 by mapping the transparency of disclosure practices observed, and making no judgement as to whether the disclosures necessarily reflect the level of application by the companies involved. In addition, Section 4.1 maps the reporting practices of companies across multiple facets. As further discussed later in this Section, the evidence provided by this multi-faceted analysis indicates consistent findings about the financial reporting practices of companies.

The second broad dimension of financial reporting, considered in Section 4.2, is the quality of accruals recognised by large proprietary companies. The quality of accruals is examined by modelling the extent to which profit reported by these companies for a period provides some explanation of the following period's operating cash flows.[28] Although the results for this

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27 Members of the professional accounting bodies in Australia who are involved in, or are responsible for, the preparation, presentation, audit, review or compilation of SPFSs are required under APES 205 to take all reasonable steps to ensure SPFSs clearly identify the significant accounting policies adopted in their preparation and presentation.

28 In doing so, models developed and used over the past two decades of financial accounting research are adopted (for further reading, refer Dechow & Dichev, 2002; Dechow, 1994). The intuition behind the models is relatively simple. If accrual-based profit/loss is to deliver the benefits expected of it (i.e., to provide a more timely measure of underlying performance than is possible from examining operating cash flows alone), then there should be a relationship between a period's profit and the following period's cash

examination of the 'quality of accruals' is not the sole indicator of the quality of the financial reporting by these companies, by examining accruals in this way, a better understanding can be gained of whether accrual-based profit is being 'accurately' measured by entities, independent of disclosure about the accounting policies applied.

The third dimension, explored in Section 4.3, is the timeliness of financial reporting lodgements by companies. The timeliness with which financial statements are lodged is often considered in the broader research literature to be associated with the quality of the content of the financial statements. Thus, timeliness of lodgement is examined in an attempt to provide an enhanced understanding of the differences that exist in the typical reporting practices by companies. The analysis is undertaken for large proprietary companies that lodged financial statements with the ASIC.

4.1 Disclosure Practices Relating to the Application of R&M

4.1.1 Disclosure Practices Relating to the Application of R&M – Large Proprietary Companies

As discussed in Section 3.1 above, 79.9 per cent of large proprietary entities lodged SPFSs. A focus on the SPFSs group shows that, of the 315 companies lodging SPFSs (see Table 25, Panel A), 209 companies (66.2%) disclosed in the significant accounting policies note to the financial statements that they had applied R&M, while 106 companies (33.8%) did not state that they had done so. In addition, Panels B and C in Table 25 show a breakdown of disclosure patterns for the latter years of the sample (i.e., 2009 and 2010)[29] for comparative purposes and to demonstrate the relative consistency of the distribution between 'State Application' and 'Do Not State Application' companies over the five-year period.

Table 25: Disclosures Relating to Application of R&M – Large Proprietary Companies

Panel A: 2006-2010	**Frequency**	**%**
State Application	209	66.2
Do Not State Application	106	33.8
Total	**315**	**100.0**
Panel B: 2009	**Frequency**	**%**
State Application	104	68.9
Do Not State Application	47	31.1
Total	**151**	**100.0**
Panel C: 2010	**Frequency**	**%**
State Application	56	65.9
Do Not State Application	29	34.1
Total	**85**	**100.0**

It should be noted that this analysis is based on an in-depth examination of the 'significant accounting policies' note reported by companies. The classification of companies into the 'State Application' group is evidence-based, primarily determined by whether the company disclosed application of R&M and at least three of the five accounting standards that were mandatory for all companies lodging under the Corporations Act (i.e., AASB 101, AASB 107, AASB 108, AASB 1031, and AASB 1048). If the company did not state in the notes to the financial statements its application of R&M and at least three of the five

from operations. The greater the relationship, the more informative (i.e., 'higher quality') the measurement of accrual-based profit/loss is considered to be.

29 The years 2009 and 2010 are the most representative years in the sample.

mandatory Australian Accounting Standards, the company was classified as 'Do Not State Application'.[30]

A three-stage process was used to determine and verify the classification of companies into either the 'State Application' (coded 0) or 'Do Not State Application' groups (coded 1). In the first stage, research assistants in close collaboration with the researchers classified and coded the companies into these two groups. In the second stage, the 'Do Not State Application' group was subjected to additional examination and these companies were further classified into either 'State Non-Application' or 'Incomplete Disclosure' groups. Companies coded 'Incomplete Disclosure' were further categorised as either 'No Clear Statement of Application' or 'Minor Non-Application' (see Table 26 for an analysis of these groups). After coding was completed by the research assistants, an independent coder, who was a former company director who had practical experience with financial statements, was employed to help verify the classification of companies into the 'State Application' and 'Do Not State Application' groups, and the sub-classification of the latter group into the 'State Non-Application' or 'Incomplete Disclosure' groups (as well as the further categorisation of the 'Incomplete Disclosure' group into 'No Clear Statement of Application' and 'Minor Non-Application'). The independent coder provided their own set of codes for the classification of companies into the above-mentioned groups.

These codes were then reviewed and subjected to an interrater reliability assessment,[31] that is, the researchers verified the extent to which the research assistants' and the independent coders' codes concurred in their codings of companies into 'State Application' and 'Do Not State Application'. The interrater reliability estimate was .89, suggesting that the rate of disagreement between the codes derived by the research assistants and the codes provided by the independent coder was approximately 11 per cent. The majority of disagreements occurred where it was difficult to tell whether companies had applied any of the recognition and measurement requirements contained in accounting standards and thus most of these disagreements were further classified into the 'No Clear Statement of Application' and 'Minor Non-Application' groups.

Below is a typical example of disclosure in the significant accounting policies note for those companies classified as 'State Application' group:

30 It is acknowledged that establishing whether an entity had applied R&M based on the information disclosed in the notes to the financial statements is difficult. The benchmark used in this Part of this Report for classifying SPFSs as 'State Application' or 'Do Not State Application' of R&M is based on the link between the requirement to present financial statements in accordance with the standards that are mandatory for all companies required to lodge financial statements with the ASIC and the application of R&M under RG 85.

31 Interrater reliability = (number of coding agreements)/(number of coding agreements + number of coding disagreements) (see Tashakkori and Teddlie, 1998)

This is a special purpose financial report that has been prepared for the sole purpose of complying with the *Corporations Act 2001* requirements to prepare and distribute a financial report to the members and must not be used for any other purpose. The directors have determined that the accounting policies adopted are appropriate to meet the needs of the members.

The financial report has been prepared in accordance with AASB 101 *Presentation of Financial Statements*, AASB 107 *Cash Flow Statements*, AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*, AASB 1031 *Materiality* and AASB 1048 *Interpretation and Application of Standards* which apply to all entities required to prepare financial reports under the *Corporations Act 2001*, and other applicable Accounting Standards and Urgent Issues Group Interpretations with the exception of the disclosure requirements in the following:

AASB 2:	*Share-based Payment*
AASB 3:	*Business Combinations*
AASB 7:	*Financial Instruments: Disclosures*
AASB 112:	*Income Taxes*
AASB 114:	*Segment Reporting*
AASB 119:	*Employee Benefits*
AASB 124:	*Related Party Disclosures*
AASB 132:	*Financial Instruments: Presentation*
AASB 139:	*Financial Instruments: Recognition and Measurement*

The financial report is prepared in accordance with the historical cost convention. Unless otherwise stated, the accounting policies adopted are consistent with those of the previous year. Comparative information is reclassified where appropriate to enhance comparability.

The 106 large proprietary companies lodging SPFSs that did not state application of R&M (33.8%) were further analysed (see Table 26 Panel A). The label 'Do Not State Application' was developed drawing on the ASIC guidance in RG 85 and it describes one of two situations – 'State Non-Application' or 'Incomplete Disclosure'. After reviewing the disclosure in the significant accounting policies note, incomplete disclosure comprises two situations: First, it is often not possible to determine whether a company applied R&M ('No Clear Statement of Application') by reviewing the significant accounting policies note, since there is no regulatory requirement to disclose this information. If a company applied R&M, it may have an incentive to disclose this fact.[32] The second situation, categorised as 'Minor Non-Application', is used where a company stated it adopted R&M of all but one or two standards. In contrast, the label 'State Non-Application' describes a situation where the company clearly indicated in the significant accounting policies note that it had not applied R&M for many of the applicable accounting standards. A typical example of 'State Non-Application' is provided on the following page.

Table 26: Frequency of the 'Do Not State Application' Group by Extent of Non-Application – Large Proprietary Companies

Panel A – Do Not State Application	**Frequency**	**%**
Incomplete Disclosure	61	57.9
State Non-Application	45	42.1
Total	**106**	**100.0**
Panel B – Additional Frequency Breakdown of the '*Incomplete Disclosure*' Group		
	Frequency	**%**
No Clear Statement of Application	40	66.6
Minor Non-Application	21	33.4
Total	**61**	**100.0**

32 That incentive could be to demonstrate compliance with RG 85 and/or to take credit for having applied those requirements.

Table 26 shows that 45 large proprietary companies were classified as 'State Non-Application' suggesting that these companies had not adhered to R&M. There were 40 instances where no clear indication was given in the significant accounting policies note – 'No Clear Statement of Application' category; and 21 instances where the non-application of R&M appears to be relatively minor – 'Minor Non-Application' (see Table 26, Panel B).

An example of a disclosure categorised as 'State Non-Application' follows.

NOTE 1 - STATEMENT OF SIGNIFICANT ACCOUNTING POLICIES

This financial report is a special purpose financial report prepared in order to satisfy the financial report preparation requirements of the Corporations Act 2001. The directors have determined that the company is not a reporting entity.

The report has been prepared in accordance with the requirements of the Corporations Act 2001, and the following applicable Australian Accounting Standards and Australian Accounting Interpretations:

AASB 101:	Presentation of Financial Statememts
AASB 107:	Cash Flow Statements
AASB 108:	Accounting Policies, Changes in Accounting
	Estimates and Errors
AASB 110:	Events after the Balance Sheet Date;
AASB 117:	Leases;
AASB 1031:	Materiality; and
AASB 1048:	Interpretation and Application of Standards.

No other Accounting Standards, Accounting Interpretations or other authoritative pronouncements of the Australian Accounting Standards Board have been applied.

The financial report has been prepared on an accruals basis and is based on historical costs.

It is possible that the notes to the financial statements do not adequately reflect the reporting decisions made by companies with respect to either disclosure or R&M. More specifically, it is possible that companies are actually applying the relevant requirements but merely not stating application in the notes to the financial statements. Accordingly, while this analysis is directed at mapping disclosure practices rather than compliance, it should be noted that it is not feasible to know whether these companies applied all relevant R&M. Notwithstanding this limitation, it could be argued that these companies were less likely to have applied R&M when it was not clear in their disclosure given that, if a company were applying R&M, it may have an incentive to disclose this fact, as noted above.

The most common examples of large proprietary companies categorised as 'Minor Non-Application' were where R&M were stated to have been applied, with the exception of one or two standards.

Non-application of R&M by some companies lodging SPFSs was highlighted by the ASIC in RG 85 and the results discussed to date in this Report arguably corroborate the ASIC's findings on this matter. While many of the companies that do not apply R&M would, in all likelihood, face higher costs if they were to follow R&M, the benefit of doing so would be an overall improvement in the quality (transparency) of financial reporting and a reduction in information asymmetry between the preparers and users of financial statements.

If companies' financial statements are prepared without applying R&M, it is unclear as to whether SPFSs are able to effectively serve the needs of users in evaluating a company's accountability and stewardship. Moreover, a range of studies have identified significant economic benefits of increasing comparability in financial statements, including for financial analysis and investment as well as for understanding and better predicting economic events (Abdel-Khalik, 1983; Botosan, 1997; Bradshaw et al., 2004; Hail et al., 2010). It is thus unclear as to whether the public interest is being served for any of the companies that do not apply R&M when preparing financial statements.

Because financial information for large proprietary companies is not as readily available to the public as is the case for listed entities, there is unlikely to be the same level of external monitoring compared with listed public companies. Transparency of financial information is fundamental to effective corporate governance and for informed decisions by interested parties (ASX, 2010). Financial information is used by stakeholders to monitor entity performance and evaluate the accountability of entities and their management. Arguably listed public companies have an incentive to produce high quality financial statements (i.e., GPFSs) because the information is publicly available and such companies are generally subject to wide external scrutiny. While the financial statements of large proprietary companies lodged with the ASIC are available to members of the public, a fee is payable, which acts as a barrier to wide external scrutiny. Accordingly, the incentive for such companies to invest in high quality financial reporting may be lower because there is generally less transparency in this market compared with the market for 'seasoned' equity.

Additional testing was undertaken in an effort to better understand the disclosures made by companies classified as 'Do Not State Application'. This analysis involved determining the frequency of disclosures that large proprietary companies provided in accordance with accounting standards on the following topics: Tax effect accounting (84.3%), Consolidation (55.0%), Financial instruments (39.2%), Share-based payment (12.1%), Related party disclosures (92.2%), and Employee benefits in respect of long service leave entitlement provisions (70.6%). An analysis of the frequency of disclosures relating to the standards mentioned is intended to help inform the analysis of whether the companies involved were likely to be applying R&M more generally. Of the disclosures examined, 55 per cent of large proprietary companies disclosed information relating to four or more of the above-mentioned accounting standards and 45 per cent disclosed information relating to three or fewer of these accounting standards. Thus, it remains an open question as to the extent to which these companies applied R&M.

Stated Application of Mandatory Standards by 'State Application' Group – Large Proprietary Companies

Additional analysis was conducted on those financial statements where large proprietary companies stated application of R&M.

As noted in Panel A of Table 25 above, 209 large proprietary companies (66.2%) lodging SPFSs stated they had applied R&M. Further analysis was performed to understand disclosure of the mandatory accounting standards applied by these companies. Table 27 (below) shows three distinct patterns of disclosure.

Table 27: Frequency of Stated Application of Mandatory Standards by 'State Application' Group – Large Proprietary Companies

	Frequency	%
Stated disclosure in accordance with 3	42	20.1
Stated disclosure in accordance with 4	15	7.2
Stated disclosure in accordance with 5	152	72.7
Total	**209**	**100.0**

Disclosed application of three standards – Table 27 shows 42 out of the 209 large proprietary companies that lodged SPFSs and stated application of R&M disclosed they had applied three of the five mandatory standards. In all instances, stated 'application' was with the following standards:

(a) AASB 101 *Presentation of Financial Statements*

(b) AASB 107 *Statement of Cash Flows*

(c) AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors.*

This group of 42 companies was predominantly audited by one particular Big 4 audit firm. It is noteworthy that AASB 1053, paragraph BC7, states that "Under ASIC's view, the only 'relief' for these entities is not having to apply the disclosure requirements contained in Standards other than AASB 101, AASB 107 and AASB 108." While this statement is true, both AASB 1048 and AASB 1031 are also applicable to all lodging entities.

Disclosed application of four standards – Table 27 shows that 15 (7.2%) out of the 209 large proprietary companies that lodged SPFSs and stated application of R&M disclosed they had applied four of the five mandatory standards. The vast majority in this group stated application of the following:

(a) AASB 101 *Presentation of Financial Statements*

(b) AASB 107 *Statement of Cash Flows*

(c) AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*

(d) AASB 1048 *Interpretation and Application of Standards.*

The four standards listed above are included in the list of standards stipulated in RG 85. It is noteworthy that there are no specific recognition, measurement or disclosure requirements in AASB 1048.[33]

33 AASB 1048 is the means by which Interpretations are made applicable under the Corporations Act. The Interpretations apply to particular types of entities only to the extent stipulated.

Disclosed application of five standards – Table 27 shows that the majority 152 (72.7%) of the 209 large proprietary companies that lodged SPFSs and stated application of R&M disclosed they had applied the following five mandatory standards:

(a) AASB 101 *Presentation of Financial Statements*

(b) AASB 107 *Statement of Cash Flows*

(c) AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*

(d) AASB 1031 *Materiality*

(e) AASB 1048 *Interpretation and Application of Standards.*

The above standards should be applied by companies lodging financial statements under the Corporations Act, although it is noted that companies are not required specifically to disclose application of the standards.

Accounting Standards where Specific Disclosures are Stated as not Applied by 'State Application' Group – Large Proprietary Companies

In the following analysis the disclosure practices of the 209 large proprietary companies that lodged SPFSs and stated application of R&M is further considered. This analysis identifies the particular accounting standards that companies specifically stated as not being applied. Results presented in Table 28 below show that nearly 34 per cent of large proprietary companies indicated they applied three or more of the five mandatory standards applicable to both reporting entities and non-reporting entities, which could suggest that disclosures in other accounting standards were not made.

Turning now to the disclosure pattern by the 209 companies that lodged SPFSs and stated they had applied R&M, approximately 80 per cent stated they did not follow the disclosures in the following standards:

(a) AASB 7 *Financial Instruments: Disclosure*

(b) AASB 112 *Income Taxes*

(c) AASB 124 *Related Parties*

(d) AASB 132 *Financial Instruments: Presentation*

(e) AASB 114 *Segment Reporting.*[34]

Of the 209 companies that lodged SPFSs and stated they had applied R&M, approximately 50 per cent stated they did not apply the disclosures in the following standards:

(a) AASB 2 *Share Based Payment*

(b) AASB 3 *Business Combinations*

(c) AASB 116 *Property, Plant and Equipment*

(d) AASB 117 *Leases*

(e) AASB 119 *Employee Benefits*

(f) AASB 136 *Impairment of Assets*

34 AASB 114 is superseded from 1 January 2009 by AASB 8 *Operating Segments*.

(g) AASB 139 *Financial Instruments: Recognition and Measurement.*

It can be argued that companies may choose not to follow specific accounting standards because of their complexity and, therefore, cost. It is noteworthy that more than 80 per cent of the companies in the sample had recognised either a future income tax asset or future income tax liability, suggesting the vast majority adopted R&M income tax accounting in accordance with AASB 112, which is commonly regarded as complex.[35] However, more than 80 per cent of the companies in the sample disclosed they did not apply the disclosures in AASB 112.

Table 28: Frequency of Stated Non-Application of Disclosures of Relevant Accounting Standards by 'State Application' Group – Large Proprietary Companies

	Frequency	%
Disclosed all	9	4.40
Non-disclosure of 1	2	0.96
Non-disclosure of 2	2	0.96
Non-disclosure of 3	6	2.90
Non-disclosure of 4	8	3.80
Non-disclosure of 5	8	3.80
Non-disclosure of 6	15	7.20
Non-disclosure of 7	12	5.70
Non-disclosure of 8	12	5.70
Non-disclosure of 9	15	7.20
Non-disclosure of 10	10	4.80
Non-disclosure of 11	10	4.80
Non-disclosure of 12	7	3.35
Non-disclosure of 13	5	2.39
Non-disclosure of 14	6	2.87
Non-disclosure of 15	1	0.48
Non-disclosure of 16	2	0.96
Non-disclosure of 17	2	0.96
Non-disclosure of 18	3	1.44
Non-disclosure of 19	1	0.48
Non-disclosure of 20 or more	2	0.96
Non-disclosure of all other than the 'mandatory' disclosure standards[36]	71	33.97
Total	**209**	**100.00**

For companies in the sample that stated application of R&M, Table 28 documents stated non-application of the disclosures in relevant accounting standards.

'Do Not State Application' of R&M, by Auditor – Large Proprietary Companies

The following reviews results for large proprietary companies that did not state application of R&M, by particular types of audit firms. As shown in Table 29, 47 of 392 companies were not audited – and this is because they had been granted audit relief. A majority of companies not audited (47.1%) did not state application of R&M. Specifically, only 23.5 per cent of companies not audited stated non-application of R&M requirements.

35 Only 17.3 per cent of companies actually disclosed segment information, which could suggest that they do not disclose fully in accordance with AASB 114 *Segment Reporting*. The low rate of non-disclosure of segment information is possibly suggestive of entities wishing to protect proprietary information.

36 Disclosure in accordance with three or more of: AASB 101, AASB 107, AASB 108, AASB 1031, AASB 1048, but no other standard.

Table 29: 'Do Not State Application' of R&M – Classified by Type of Financial Statements and Auditor – Large Proprietary Companies

	Total	Do Not State Application %	State Non-Application %	Incomplete Disclosure %
No Audit	47	47.1	23.5	23.6
Audit Opinion Issued	345	31.7	15.6	16.1
Total	**392***			
GPFSs	79	0.0	0.0	0.0
SPFSs	315	33.8	14.3	19.4
Total	**394***			
Audited Entities Lodging SPFSs				
Big 4 Auditor	194	18.6	8.0	10.6
Non-Big 4 Auditor	78	31.1	7.4	23.7
Total	**272**			

* *There is a discrepancy between the Total for Audit (i.e., No Audit and Audit Opinion Issued) of 392 and Total for GPFSs and SPFSs of 394 since on two occasions it was not feasible to determine whether an audit was conducted.*

All companies lodging GPFSs (n=79) disclosed application of R&M as required under the Corporations Act (see Table 29). Among the 315 large proprietary companies lodging SPFSs, 33.8 per cent 'Do Not State Application' of R&M. Furthermore, 14.3 per cent of companies lodging SPFSs 'State Non-Application' of R&M, while for 19.4 per cent of companies 'Incomplete Disclosure' was made.

The disclosure practices of entities lodging SPFSs by type of auditor are also reported in Table 29. A proportion of the clients of the non-Big 4 (31.1%) did not state application of R&M. In contrast, 18.6 per cent of Big 4 audit clients did not state application of R&M. The proportion of companies that stated non-application of R&M is broadly consistent across auditor type.

4.1.2 Disclosure Practices Relating to the Application of R&M – Foreign-Controlled Companies

As discussed in Section 3.2 above (Table 8), 84.4 per cent of foreign-controlled companies lodged SPFSs. Further examination shows that, of the 287 foreign-controlled companies lodging SPFSs, 178 (62.2%) disclosed in the significant accounting policies note to the financial statements that they had applied R&M, while 109 companies (37.8%) did not state application of R&M.

Table 30: Disclosure Relating to Application of R&M – Foreign-Controlled Companies

	Frequency	%
State Application	178	62.2
Do Not State Application	109	37.8
Total	**287**	**100.0**

The 109 foreign-controlled companies lodging SPFSs that did not state application of R&M are further categorised as 'Incomplete Disclosure' and 'State Non-Application' (see Table 31 Panel A). The disclosure by the 16 companies classified as 'State Non-Application' indicates these companies did not apply R&M. There were 93 instances in the 'Incomplete Disclosure' category where either no clear statement was made (n = 76) to determine whether the company applied R&M from its disclosure in the significant accounting policies note ('No

Clear Statement of Application'), or where the stated non-application of R&M (n = 17) was relatively minor ('Minor Non-Application') – see Table 31 Panel B.

Table 31: Frequency of the 'Do Not State Application' Group by Extent of Non-Application – Foreign-Controlled Companies

Panel A - Do Not State Application	**Frequency**	**%**
Incomplete Disclosure	93	85.3
State Non-Application	16	14.7
Total	**109**	**100.0**
Panel B – Additional Frequency Breakdown of the '*Incomplete Disclosure*' Group		
	Frequency	**%**
No Clear Statement of Application	76	81.3
Minor Non-Application	17	18.7
Total	**93**	**100.0**

Stated Application of Mandatory Standards by 'State Application' Group – Foreign-Controlled Companies

For the 178 foreign-controlled companies that lodged SPFSs and stated application of R&M, Table 32 shows the distinct patterns of disclosure.

Table 32: Frequency of Stated Application of Mandatory Standards by 'State Application' Group – Foreign-Controlled Companies

	Frequency	**%**
Stated disclosure in accordance with 3	52	29.2
Stated disclosure in accordance with 4	23	12.9
Stated disclosure in accordance with 5	103	57.9
Total	**178**	**100.0**

Disclosed application of four standards – Table 32 shows that 23 (12.9%) out of 178 foreign-controlled companies that lodged SPFSs and stated application of R&M disclosed they had applied four of the five mandatory standards. The vast majority in this group stated application of the following:

(a) AASB 101 *Presentation of Financial Statements*

(b) AASB 107 *Statement of Cash Flows*

(c) AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*

(d) AASB 1048 *Interpretation and Application of Standards.*

The four standards listed above are included in the list of standards stipulated in RG 85.

Disclosed application of five standards – Table 32 shows that the majority 103 (57.9%) of the 178 foreign-controlled companies that lodged SPFSs and stated application of R&M disclosed they had applied all five mandatory standards:

(a) AASB 101 *Presentation of Financial Statements*

(b) AASB 107 *Statement of Cash Flows*

(c) AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*

(d) AASB 1031 *Materiality*

(e) AASB 1048 *Interpretation and Application of Standards.*

The above standards are applicable to companies lodging financial statements under the Corporations Act.

'Do Not State Application' of R&M, by Auditor – Foreign-Controlled Companies

The following reviews results for companies that did not state application of R&M, by particular types of audit firms. As shown in Table 33, eight of 340 foreign-controlled companies were not audited. A majority of companies not audited (62.5%) did not state application of R&M. Approximately 31 per cent of the audited companies did not state application of R&M.

Table 33: 'Do Not State Application' of R&M – Classified by Type of Financial Statements and Auditor – Foreign-Controlled Companies

	Total	Do Not State Application %	State Non-Application %	Incomplete Disclosure %
No Audit	8	62.5	37.5	25.0
Audit Opinion Issued	332	31.3	4.8	26.5
Total	**340**			
GPFSs	53	0.0	0.0	0.0
SPFSs	287	38.0	5.6	32.4
Total	**340**			
Audited Entities Lodging SPFSs				
Big 4 Auditor	170	6.1	2.0	4.1
Non Big 4 Auditor	109	66.2	8.1	58.1
Total	**279**			

4.1.3 Disclosure Practices Relating to the Application of R&M – Small Proprietary Companies

As noted in Section 3.3 above (Table 12), 72 small proprietary companies (75.8%) of the sample of those companies lodged SPFSs. Of those, 38 companies (52.9%) disclosed in their significant accounting policies note they had applied R&M, while 34 companies (47.1%) did not state application of R&M.

Table 34: Disclosure Relating to Application of R&M – Small Proprietary Companies

	Frequency	%
State Application	38	52.9
Do Not State Application	34	47.1
Total	**72**	**100.0**

The 34 companies lodging SPFSs that did not state application of R&M are further categorised as 'Incomplete Disclosure' and 'State Non-Application' (see Table 35 Panel A). The disclosure by the 26 companies classified as 'State Non-Application' indicates that the companies stated they had not applied R&M. There were eight instances in the 'Incomplete Disclosure' category wherein either no clear statement of application was made (n = 2), or where the stated non-application of R&M was relatively minor ('Minor Non-Application', n = 6), see Table 35 Panel B.

Table 35: Frequency of the 'Do Not State Application' Group by Extent of Non-Application – Small Proprietary Companies

Panel A – Do Not State Application	Frequency	%
Incomplete Disclosure	8	23.5
State Non-Application	26	76.5
Total	**34**	**100.0**
Panel B – Additional Frequency Breakdown of the '*Incomplete Disclosure*' Group		
	Frequency	**%**
No Clear Statement of Application	2	25.0
Minor Non-Application	6	75.0
Total	**8**	**100.0**

Stated Application of Mandatory Standards by 'State Application' Group – Small Proprietary Companies

For the 38 small proprietary companies that lodged SPFSs and stated application of R&M, Table 36 shows the distinct patterns of disclosure.

Table 36: Frequency of Stated Application of Mandatory Standards by 'State Application' Group – Small Proprietary Companies

	Frequency	%
Stated disclosure in accordance with 3	15	39.5
Stated disclosure in accordance with 4	6	15.8
Stated disclosure in accordance with 5	17	44.7
Total	**38**	**100.0**

Disclosed application of four standards – Table 36 shows that six (15.8%) out of 38 small proprietary companies that lodged SPFSs and stated application of R&M disclosed they had applied four of the five mandatory standards. The vast majority in this group stated application of the following:

(a) AASB 101 *Presentation of Financial Statements*

(b) AASB 107 *Statement of Cash Flows*

(c) AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*

(d) AASB 1048 *Interpretation and Application of Standards*.

The four standards listed above are included in the list of standards stipulated in RG 85.

Disclosed application of five standards – Table 36 shows that 17 (44.7%) of the 38 small proprietary companies that lodged SPFSs and stated application of R&M disclosed they had applied all five mandatory standards:

(a) AASB 101 *Presentation of Financial Statements*

(b) AASB 107 *Statement of Cash Flows*

(c) AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*

(d) AASB 1031 *Materiality*

(e) AASB 1048 *Interpretation and Application of Standards.*

The above standards are applicable to companies lodging financial statements under the Corporations Act.

'Do Not State Application' of R&M, by Auditor – Small Proprietary Companies

The following reviews results for companies that did not state application of R&M, by particular types of audit firms. As shown in Table 37, five of 95 small proprietary companies were not audited. All companies that were not audited did not state application of R&M. Approximately 32 per cent of the audited companies did not state application of R&M.

Table 37: 'Do Not State Application' of R&M – Classified by Type of Financial Statements and Audit Firm – Small Proprietary Companies

	Total	Do Not State Application %	State Non-Application %	Incomplete Disclosure %
No Audit	5	100.0	na	na
Audit Opinion Issued	90	32.2	23.3	8.9
Total	**95**			
GPFSs	23	0.0	0.0	0.0
SPFSs	72	47.2	36.1	11.1
Total	**95**			
Audited Companies Lodging SPFSs				
Big 4 Auditor	47	29.8	na	na
Non Big 4 Auditor	20	60.0	28.0	32.0
Total	**67**			

na = not available

4.1.4 Disclosure Practices Relating to the Application of R&M – Unlisted Public Companies other than those Limited by Guarantee

As noted in Section 3.4 above (Table 16), 105 of the sample of unlisted public companies (other than those limited by guarantee) (30.3%) lodged SPFSs. Of the companies that lodged SPFSs, 68 companies (64.8%) stated in the significant accounting policies note to the financial statements they had applied R&M, while 37 (35.2%) that lodged SPFSs did not state application of R&M.

Table 38: Disclosure Relating to Application of R&M – Unlisted Public Companies

	Frequency	%
State Application	68	64.8
Do Not State Application	37	35.2
Total	**105**	100.0

The 37 companies that lodged SPFSs that did not state application of R&M are further categorised as 'Incomplete Disclosure' and 'State Non-Application' (see Table 39 Panel A). The disclosure by the 26 companies classified as 'State Non-Application' indicates that the companies had stated they had not applied R&M. There were 11 instances in the 'Incomplete Disclosure' category wherein either no clear statement regarding application was made (n = 4), or where the non-application was relatively minor (n = 7) – see Table 39 Panel B.

Table 39: Frequency of the 'Do Not State Application' Group by Extent of Non-Application – Unlisted Public Companies

Panel A	**Frequency**	**%**
Incomplete Disclosure	11	29.7
State Non-Application	26	70.3
Total	**37**	**100.0**
Panel B - Additional Frequency Breakdown of the '*Incomplete Disclosure*' Group		
	Frequency	**%**
No Clear Statement of Application	4	36.4
Minor Non-Application	7	63.6
Total	**11**	**100.0**

Stated Application of Mandatory Standards by 'State Application' Group – Unlisted Public Companies

For the 68 sampled unlisted public companies lodging SPFSs and stating application of R&M, Table 40 shows the distinct patterns of disclosure.

Table 40: Frequency of Stated Application of Mandatory Standards by 'State Application' Group – Unlisted Public Companies

	Frequency	**%**
Stated disclosure in accordance with 3	11	16.2
Stated disclosure in accordance with 4	3	4.4
Stated disclosure in accordance with 5	54	79.4
Total	**68**	**100.0**

Disclosed Application of four Standards – Table 40 shows that three (4.4%) out of 68 unlisted public companies that lodged SPFSs and stated application of R&M disclosed they had applied four of the five mandatory standards. The three companies in this group stated they had applied the following:

(a) AASB 101 *Presentation of Financial Statements*

(b) AASB 107 *Statement of Cash Flows*

(c) AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*

(d) AASB 1048 *Interpretation and Application of Standards.*

The four standards listed above are included in the list of standards stipulated in RG 85.

Disclosed Application of five Standards – Table 40 shows that 54 of the 68 unlisted public companies that lodged SPFSs and stated application of R&M (79.4%) disclosed they had applied all five mandatory standards:

(a) AASB 101 *Presentation of Financial Statements*

(b) AASB 107 *Statement of Cash Flows*

(c) AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*

(d) AASB 1031 *Materiality*

(e) AASB 1048 *Interpretation and Application of Standards.*

The above standards are applicable to companies lodging financial statements under the Corporations Act.

Accounting Standards where Specific Disclosures are Stated as not Applied by 'State Application' Group – Unlisted Public Companies

For unlisted public companies that stated application of R&M, the following shows the frequency of stated non-application of the disclosures in relevant accounting standards (Table 41).

Table 41: Frequency of Stated Non-Application of Disclosures of Relevant Accounting Standards by 'State Application' Group – Unlisted Public Companies

	Frequency	%
Disclosed all	2	2.9
Non-disclosure of 1	0	0.0
Non-disclosure of 2	3	4.4
Non-disclosure of 3	2	2.9
Non-disclosure of 4	9	13.2
Non-disclosure of 5	2	2.9
Non-disclosure of 6	1	1.5
Non-disclosure of 7	3	4.4
Non-disclosure of 8	6	8.8
Non-disclosure of 9	1	1.5
Non-disclosure of 10	2	2.9
Non-disclosure of 11	0	0.0
Non-disclosure of 12	0	0.0
Non-disclosure of 13	1	1.5
Non-disclosure of 14	1	1.5
Non-disclosure of 15	1	1.5
Non-disclosure of 16	1	1.5
Non-disclosure of 17	0	0.0
Non-disclosure of 18	0	0.0
Non-disclosure of 19	0	0.0
Non-disclosure of 20 or more	0	0.0
Non-disclosure of all other than the mandatory disclosure standards	33	48.5
Total:	**68**	**100.0**

'Do Not State Application' of R&M, by Auditor – Unlisted Public Companies

The following reviews results for companies that did not state application of R&M, by particular types of audit firms. As shown in Table 42, 9.8 per cent of the audited companies did not disclose application of R&M.

Table 42: 'Do Not State Application' of R&M – Classified by Type of Financial Statements and Auditor – Unlisted Public Companies

	Total	Do Not State Application %	State Non-Application %	Incomplete Disclosure %
No Audit	0	0.0	0.0	0.0
Audit Opinion Issued	347	9.8	3.4	6.4
Total	**347**			
GPFSs	242	5.8	0.4	5.4
SPFSs	105	10.5	6.7	3.8
Total	**347**			
Audited Entities Lodging SPFSs				
Big 4 Auditor	51	3.9	0.0	3.9
Non-Big 4 Auditor	54	16.7	13.0	3.7
Total	**105**			

4.1.5 Disclosure Practices Relating to the Application of R&M – Public Companies Limited by Guarantee

As noted in Section 3.5 above (Table 20), 123 of the sampled unlisted public companies limited by guarantee (33.7%) lodged SPFSs. Of the companies lodging SPFSs, 44 (35.8%) disclosed in the significant accounting policies note to the financial statements they had applied R&M, while 79 (64.2%) lodging SPFSs did not state application of R&M.

Table 43: Disclosure Relating to Application of R&M – Public Companies Limited by Guarantee

	Frequency	%
State Application	44	35.8
Do Not State Application	79	64.2
Total	**123**	**100.0**

The 79 companies lodging SPFSs that did not state application of R&M are further categorised as 'Incomplete Disclosure' and 'State Non-Application' (see Table 44 Panel A). The classification of 63 companies as 'State Non-Application' is for those companies that stated they had not applied R&M. There were 13 instances in the 'Incomplete Disclosure' category wherein no clear statement regarding application was made in the significant accounting policies note ('No Clear Statement of Application'), and three instances where the non-adherence to R&M was relatively minor ('Minor Non-Application') – see Table 44 Panel B.

Table 44: Frequency of the 'Do Not State Application' Group by Extent of Non-Application – Public Companies Limited by Guarantee

Panel A	**Frequency**	**%**
Incomplete Disclosure	16	20.3
State Non-Application	63	79.7
Total	**79**	**100.0**
Panel B – Additional Frequency Breakdown of the '*Incomplete Disclosure*' Group		
	Frequency	**%**
No Clear Statement of Application	13	81.2
Minor Non-Application	3	18.8
Total	**16**	**100.0**

Stated Application of Mandatory Standards by 'State Application' Group – Public Companies Limited by Guarantee

For the 44 public companies limited by guarantee that lodged SPFSs and stated application of R&M, Table 45 shows the distinct patterns of disclosure.

Table 45: Frequency of Stated Application of Mandatory Standards by 'State Application' Group – Public Companies Limited by Guarantee

	Frequency	%
Stated disclosure in accordance with 3	11	25.3
Stated disclosure in accordance with 4	9	20.3
Stated disclosure in accordance with 5	24	54.4
Total	**44**	**100.0**

Disclosed application of four standards – Table 45 shows that nine out of 44 companies that lodged SPFSs and stated application of R&M (20.3%) disclosed they had also applied four of the five mandatory standards. The vast majority in this group applied the following:

(a) AASB 101 *Presentation of Financial Statements*

(b) AASB 107 *Statement of Cash Flows*

(c) AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*

(d) AASB 1048 *Interpretation and Application of Standards.*

The four standards listed above are included in the list of standards stipulated in RG 85.

Disclosed application of five standards – Table 46 shows that 24 of the 44 public companies limited by guarantee that lodged SPFSs and stated application of R&M (54.4%) disclosed they had applied all five mandatory standards:

(a) AASB 101 *Presentation of Financial Statements*

(b) AASB 107 *Statement of Cash Flows*

(c) AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*

(d) AASB 1031 *Materiality*

(e) AASB 1048 *Interpretation and Application of Standards.*

The above standards are applicable to companies lodging financial statements under the Corporations Act.

Accounting Standards where Specific Disclosures are Stated as not Applied by 'State Application' Group – Public Companies Limited by Guarantee

For public companies limited by guarantee that state application of R&M, the following shows the frequency of stated non-application of the disclosures in relevant accounting standards (Table 46).

Table 46: Frequency of Stated Non-Application of Disclosures of Relevant Accounting Standards by 'State Application' Group – Public Companies Limited by Guarantee

	Frequency	%
Disclosed all	16	36.4
Non-disclosure of 1	2	4.5
Non-disclosure of 2	2	4.5
Non-disclosure of 3	3	6.8
Non-disclosure of 4	1	2.3
Non-disclosure of 5	0	0.0
Non-disclosure of 6	1	2.3
Non-disclosure of 7	0	0.0
Non-disclosure of 8	1	0.0
Non-disclosure of 9	0	0.0
Non-disclosure of 10	0	0.0
Non-disclosure of 11	0	0.0
Non-disclosure of 12	0	0.0
Non-disclosure of 13	0	0.0
Non-disclosure of 14	0	0.0
Non-disclosure of 15	0	0.0
Non-disclosure of 16	0	0.0
Non-disclosure of 17	0	0.0
Non-disclosure of 18	0	0.0
Non-disclosure of 19	0	0.0
Non-disclosure of 20 or more	0	0.0
Non-disclosure of all other than the mandatory disclosure standards	18	40.9
Total:	**44**	**100.0**

'Do Not State Application' of R&M, by Auditor – Public Companies Limited by Guarantee

The following reviews results for companies that did not state application of R&M, by particular types of audit firms. As shown in Table 47, all companies in this group were audited. Approximately 22 per cent of the audited companies did not disclose application of R&M and 17.2 per cent stated non-application.

Table 47: 'Do Not State Application' of R&M – Classified by Type of Financial Statements and Auditor – Public Companies Limited by Guarantee

	Total	Do Not State Application %	State Non-Application %	Incomplete Disclosure %
No Audit	0			
Audit Opinion Issued	368	21.5	17.2	4.3
Total	**368**			
GPFSs	239	0.0	0.0	0.0
SPFSs	123	64.2	51.2	13.0
Total	**362**			
Audited Entities Lodging SPFSs				
Big 4 Auditor	11	9.1	0.0	9.1
Non Big 4 Auditor	112	79.5	15.9	63.5
Total	**123**			

4.2 Quality of Accruals – Large Proprietary Companies

To further understand the characteristics of financial statements lodged by companies, this Section (Section 4.2) focuses on the accruals recognised by companies among the large proprietary company sample. This is because five years of data was able to be analysed for large proprietary companies, which is necessary to facilitate the development of generalisable findings regarding the quality of accruals. The analysis is undertaken in two ways. First, the research examines the information contained in a period's profit (year t) for predicting cash flows from operations one period ahead (year t+1). Second, the research examines the role of accruals recognised by these companies in mitigating the 'noise' inherent in year t's cash flows. Accordingly, this Section investigates the quality of accruals between three different groups that make up the large proprietary company sample. Comparisons on the quality of accruals are conducted between the GPFSs and the SPFSs that stated application of R&M ('State Application' group); between the SPFSs 'State Application' and SPFSs 'Do Not State Application' groups; and between the SPFSs 'State Application' and SPFSs 'State Non-Application' groups. These tests and the associated implications are explained below in three separate sub-sections 4.2.1 – 4.2.3.

4.2.1 Comparing the Quality of Accruals between the GPFSs and the SPFSs 'State Application' Group – Large Proprietary Companies

Accrual accounting is typically identified as a more timely approach to recognising the effects of economic transactions and, thus, a better measure of 'true' economic performance in any particular period. This view is acknowledged in textbooks in the field and supported by large volumes of extant research (e.g., Dechow & Dichev, 2002; Dechow, 1994). An implication of accrual accounting is that if accruals provide a more timely measure of performance, there should be a clear relationship between a period's profit and cash flows from operations one-year-ahead.[37] The stronger the magnitude of the relationship, the more 'accurate' profit is said to be as a measure of economic performance for the period (year t).[38] To examine the usefulness of accrual-based earnings among large proprietary companies, the following regression equation is estimated:

$CFO_{it+1} = \alpha + \beta_1 Profit_{it} + \beta_2 CFO_{it} + \beta_3 GP\_SP_{it} + \varepsilon_{it+1}$ Equation (1)

Where:

CFO_{it+1} = the cash-flow from operations of a large proprietary company *i* in year *t* + 1 scaled by total assets at the end of year *t*;

$Profit_{it}$ = the reported profit/loss for a large proprietary company *i* in year *t* scaled by total assets at the end of year *t* – 1;

CFO_{it} = the cash-flow from operations of a large proprietary company *i* in year *t* scaled by total assets as at the end of year *t* – 1; and

GP_SP_{it} = a dummy variable where 1= a large proprietary company has lodged SPFSs that state application of R&M and 0 = a large proprietary company has lodged GPFSs.

37 For example, where credit sales are made in the current period and are accurately measured and reported, future cash flows from operations relating to those sales are able to be estimated with greater accuracy.

38 This narrative summarises the findings of decades of research in the field. For a more detailed discussion of the literature and the associated implications, refer to Pinnuck and Potter (2009).

The research utilises panel study methodology over the period 2006 to 2010 as panel data provides more robust information, more sample variability, less collinearity among variables, more degrees of freedom and more efficiency compared with a methodology that uses cross-sectional data (i.e., measurements on distinct companies) at a given point in time. The methodology also permits control of unobserved company heterogeneity. As the research examines whether past earnings contain information about future (one-year-ahead) cash-flows, a number of econometric issues arise that are addressed in standard ways.[39] The primary variable of interest in Equation (1) is $Profit_{it}$. If profit is accurately measured and thus provides information for predicting cash-flows from operations for the following period, the coefficient on this variable (β_1) should be positive and statistically significant. Further, since the research is able to compare the financial statements for those companies lodging GPFSs and those lodging SPFSs (that state application of R&M) assuming GPFSs are of higher quality, the coefficient should be higher for the GPFSs sample than for the SPFSs sample. Alternatively, if R&M is applied by all companies regardless of the type of financial statements lodged, there should be no difference in the quality of accruals recognised by these groups of companies. Examining the quality of accruals in this way also offers greater insight into whether companies are likely to be applying R&M in substance, holding constant disclosures made by companies about the application of R&M. This is intended to help address the question of whether companies are applying R&M without disclosing the extent to which they are applying R&M. The results are reported in Table 48.

Table 48: Results of Fixed Effects Regression Estimates of Accruals Usefulness between GPFSs and SPFSs 'State Application' – Large Proprietary Companies

	Model 1 $\mathbf{CFO_{it+1}}$	**Model 2** $\mathbf{CFO_{it+1}}$	**Model 3** $\mathbf{CFO_{it+1}}$
$Profit_{it}$	0.070	0.225***	-0.091
	(0.48)	(3.04)	(-0.41)
CFO_{it}	-0.271	-0.256	-0.315
	(-1.33)	(-1.30)	(-1.18)
_cons	7.229	0.066***	12.62
	(1.34)	(6.25)	(1.23)
N	258	83	175
R^2	0.109	0.143	0.165
adj. R^2	0.099	0.122	0.155

*t statistics, in parentheses, are calculated using the Huber-White sandwich estimator to correct standard errors. The b-coefficient is represented by the values that are not in parentheses. _cons is explained in Table 4 above. Model 1 = GPFSs and SPFSs 'State Application' Group; Model 2 = GPFSs Group; Model 3 = SPFSs 'State Application' Group. * p<0.10, ** p<0.05, *** p<0.01*

Model 1 above contains the data for the entire sample; model 2 contains the results run for the GPFSs sample, while model 3 shows the results for the SPFSs that included a statement of application of R&M. The results in the first row of the table refer to $Profit_{it}$, the variable of most interest in this analysis. From the above it can be seen that the coefficient for the SPFSs sample (b = -0.0905; t = -0.41, p > .05) is negative and not statistically significant, whereas results on the same variable of interest for the GPFSs sample (b = 0.225; t = 3.04, p < .01), are

39 For example, fixed effects regressions are employed to estimate Equation (1). In addition, the fixed effects model takes into account the correlation of the individual error component ε_i with one or more regressors in the model. More importantly, the fixed effects estimation technique is appropriate for most accounting research as it addresses the possibility of spurious relationships between the dependent and independent variables, due to the exclusion of unmeasured explanatory variables that nonetheless still affect company behaviour (Baltagi, 2008; De Jager, 2008).

positive and statistically significant. This provides evidence that indicates that the accruals recognised by companies lodging SPFSs that include a statement of application of R&M are of lower quality than those recognised by the GPFSs sample.

As a further measure of quality, some supporting evidence for the usefulness of accruals for predicting future cash-flows is provided. Accruals primarily mitigate operating cash-flow 'noise' that arises from variations in working-capital levels (Dechow et al., 1998). This is based on the notion that accruals temporarily shift or adjust the recognition of cash flows over time; accruals are negatively related to current cash-flows from operations and are positively related to past and future cash flows.[40] For example, if a company encounters a positive economic shock to its operations, the economic rationale behind accruals is there will be a net positive increase in accruals as revenue is accrued, but there will also be a net decrease in cash flows as cash is used to purchase raw materials and supplies. This relationship will thus result in a negative association between current-period accruals and cash-flows. This prediction is tested using the following model of accruals:

$ACC_{it} = \alpha + \beta_1 CFO_{it+1} + \beta_2 CFO_{it-1} + \beta_3 CFO_{it} + \beta_4 GP\_SP_{it} + \varepsilon_{it}$ Equation (2)

Where:

ACC_{it} = the accruals for a large proprietary company *i* in year *t* scaled by total assets at end of the year *t* – 1. The accruals are calculated as net profit in year *t* less cash-flow from operations in year *t*;

CFO_{it+1} = the cash-flow from operations of a large proprietary company *i* in year *t* + 1 scaled by total assets at the end of year *t*;

CFO_{it-1} = the cash-flow from operations of a large proprietary company *i* in year *t* – 1 scaled by total assets at the end of year *t*;

CFO_{it} = the cash-flow from operations of a large proprietary company *i* in year *t* scaled by total assets as at the end of year *t* – 1; and

GP_SP_{it} = a dummy variable where 1= a large proprietary company has lodged SPFSs that state application of R&M and 0 = a large proprietary company has lodged GPFSs.

Table 49: Results of Fixed Effects Regression Estimates of Accruals and Cash-Flows Relationship between GPFSs and SPFSs 'State Application' – Large Proprietary Companies

	Model 1 ACC_{it}	**Model 2** ACC_{it}	**Model 3** ACC_{it}
CFO_{it+1}	0.073	0.349	-0.022
	(0.54)	(0.90)	(-0.21)
CFO_{it-1}	0.111	0.137	0.083
	(1.00)	(0.42)	(0.92)
CFO_{it}	-1.021***	-0.950***	-1.031***
	(-11.21)	(-3.86)	(-12.11)
_cons	4.970**	0.008	8.463***
	(2.00)	(0.17)	(3.04)
N	258	83	175
R^2	0.673	0.421	0.831
adj. R^2	0.667	0.399	0.828

40 This property of accruals is supported by a significant body of existing literature (e.g., Dechow & Dichev, 2002). This relationship is typically found when a positive shock is experienced. When persistent negative shock is experienced, the relationship may not hold.

*t statistics, in parentheses, are calculated using the Huber-White sandwich estimator to correct standard errors. The b-coefficient is represented by the values that are not in parentheses. _cons is explained in Table 4 above. Model 1 = GPFSs and SPFSs 'State Application' Group; Model 2 = GPFSs Group; Model 3 = SPFSs 'State Application' Group. * p<0.10, ** p<0.05, *** p<0.01*

The variable (measure) of most interest in Table 49 is current cash-flows from operations (i.e., CFO_{it}). The coefficient results on current cash-flows from operations are consistent with the results reported in the previous test, that is, accrual-based profit is being significantly more accurately measured by companies lodging GPFSs (b = -0.950; t = -3.86, p < .01) than for those companies lodging SPFSs that state application of R&M (b = -1.031; t = -12.11, p < .01).

As hypothesised, the b-coefficient measuring cash flow from operations one year ahead (i.e., CFO_{it+1}) is positively related to accruals for the GPFSs group, while the coefficient is negatively related to accruals for the SPFSs 'State Application' group, suggesting lower accrual quality for the SPFSs group.

4.2.2 Comparing the Quality of Accruals between the SPFSs 'State Application' and SPFSs 'Do Not State Application' of R&M Groups – Large Proprietary Companies

This sub-section compares the quality of accruals between the SPFSs 'State Application' of R&M group and SPFSs that 'Do Not State Application' of R&M group. This analysis is based on the assumption that if application of R&M leads to a more 'accurate' measure of profit, then it is possible to gauge whether there is substance to the distinction between these two groups. If profit is accurately measured and thus provides information for predicting cash-flows from operations for the following period, it is expected that the coefficient on $Profit_{it}$ (β_1) should be positive and statistically significant for the SPFSs 'State Application' group compared with the SPFSs 'Do Not State Application' group. Alternatively, if the classification of companies as 'Do Not State Application' is merely capturing those entities that apply R&M but do not indicate this application, the predicted relationship is unlikely to hold.

Table 50: Results of Fixed Effects Regression Estimates of Accruals Usefulness between SPFSs 'State Application' and SPFSs 'Do Not State Application' of R&M Groups – Large Proprietary Companies

	Model 1 CFO_{it+1}	Model 2 CFO_{it+1}	Model 3 CFO_{it+1}
$Profit_{it}$	0.000***	0.000***	-0.096
	(14.14)	(8.66)	(-0.40)
CFO_{it}	0.097	0.160	-0.398
	(0.97)	(0.94)	(-1.44)
_cons	-1.834	0.072***	11.75
	(-0.93)	(3.50)	(1.50)
N	350	113	237
R^2	0.061	0.685	0.190
adj. R^2	0.053	0.679	0.183

*t statistics, in parentheses, are calculated using the Huber-White sandwich estimator to correct standard errors. The b-coefficient is represented by the values that are not in parentheses. _cons is explained in Table 4 above. Model 1 = SPFSs 'State Application' and SPFSs 'Do Not State Application' Groups; Model 2 = SPFSs 'State Application' Group; Model 3 = SPFSs 'Do Not State Application' Group. * p<0.10, ** p<0.05, *** p<0.01*

The primary variable (measure) of most interest in Table 50 is current period profit (i.e., $Profit_{it}$). Table 50 indicates that the coefficient for the SPFSs 'State Application' model (b = 0.000000452; t = 8.66, p < .01) is positive and statistically significant and larger than for the SPFSs 'Do Not State Application' model (b = -0.0963; t = -0.40, p > .05), which is negative and statistically non-significant. Recall that the stronger the magnitude of the relationship between current period profit and cash flow from operations one-year ahead, the more 'accurate' profit is said to be as a measure of economic performance. Accordingly, the above results suggest that the accruals recognised by companies lodging SPFSs that contain a statement of application of R&M are of higher quality than those recognised by the SPFSs that do not state application of R&M. An examination of cash-flows from operations does not reveal a significant relationship between current period cash flows from operations and cash flows one-year-ahead.

Table 51: Results of Fixed Effects Regression Estimates of the Relationship between Accruals and Cash-Flows: SPFSs 'State Application' and SPFSs 'Do Not State Application' of R&M Groups – Large Proprietary Companies

	Model 1 ACC_{it}	Model 2 ACC_{it}	Model 3 ACC_{it}
CFO_{it+1}	-0.167	-0.0226	-0.0241
	(-1.00)	(-0.21)	(-0.31)
CFO_{it-1}	-0.194***	0.0375	0.0796
	(-3.84)	(1.01)	(0.89)
CFO_{it}	-0.000***	-0.000***	-1.030***
	(-16.08)	(-40.55)	(-12.15)
_cons	3.819***	-0.0191	6.333***
	(3.85)	(-1.35)	(3.06)
N	350	113	237
R^2	0.269	0.975	0.831
adj. R^2	0.260	0.975	0.829

*t statistics, in parentheses, are calculated using the Huber-White sandwich estimator to correct standard errors. The b-coefficient is represented by the values that are not in parentheses. _cons is explained in Table 4 above. Model 1 = SPFSs 'State Application' and SPFSs 'Do Not State Application' Groups; Model 2 = SPFSs 'State Application' Group; Model 3 = SPFSs 'Do Not State Application' Group. * p<0.10, ** p<0.05, *** p<0.01*

The variable (measure) of interest in Table 51 is current cash-flows from operations (i.e., CFO_{it}). The coefficient results on current cash-flows from operations are consistent with the results reported in the previous test on the association between current period profit and cash flow from operations one-year ahead. In other words, results on current period cash-flows from operations indicate that accruals are more accurately measured by companies lodging SPFSs that state application of R&M (b = -0.000000955; t = -40.55, p < .01) than for those companies lodging SPFSs that do not state application of R&M (b = -1.030; t = -12.15, p < .01).

4.2.3 Comparing the Quality of Accruals between the SPFSs 'State Application' and SPFSs 'State Non-Application' of R&M Groups – Large Proprietary Companies

This sub-section reports the quality of accruals between the SPFSs 'State Application' and SPFSs 'State Non-Application'. While earlier sub-sections report on fixed effect panel regression results, this sub-section provides results based on ordinary least squares regressions. Panel regression modelling was unable to be conducted because of the low number of observations (n=47) among the SPFSs 'State Non-Application' group. Table 52 reports there are no statistically significant differences between the 'State Application' group and 'State Non-Application' group on the relationship between current period profits ($Profit_{it}$) and cash-flows from operations one-year ahead. However, an examination of current period cash-flows from operations (CFO_{it}) in relation to cash flow from operations one-year ahead (CFO_{it+1}) shows that although the b-coefficient in the SPFSs 'State Application' group is significantly negative (b = -0.0000115, t = -8.92, p < .01), it is smaller than the coefficient for the SPFSs 'State Non-Application' group (b = 0.158, t = 0.68, p > .05). These results suggest that future cash-flows are less accurately predicted (i.e., lower accruals quality) for the SPFSs 'State Non-Application' group compared with the SPFSs 'State Application' group. The results in Table 53 on the relationship between current cash-flows from operations and accruals are consistent with the results reported in Table 52, providing corroborating evidence that the SPFSs 'State Non-Application' group demonstrates lower quality accruals.

Table 52: Results of Ordinary Least Squares Regression Estimates of Accruals Usefulness between SPFSs 'State Application' and SPFSs 'State Non-Application' of R&M Groups – Large Proprietary Companies

	Model 1 CFO_{it+1}	Model 2 CFO_{it+1}	Model 3 CFO_{it+1}
$Profit_{it}$	-0.000	-0.000	0.0324
	(-0.30)	(-0.39)	(0.76)
CFO_{it}	-0.000***	-0.000***	0.158
	(-8.91)	(-8.92)	(0.68)
_cons	0.080***	0.080***	0.080**
	(8.92)	(8.93)	(2.47)
N	222	175	47
R^2	0.003	0.003	0.027
adj. R^2	0.003	0.003	0.017

*t statistics, in parentheses, are calculated using the Huber-White sandwich estimator to correct standard errors. The b-coefficient is represented by the values that are not in parentheses. _cons is explained in Table 4 above. Model 1 = SPFSs 'State Application' and SPFSs 'State Non-Application' Groups; Model 2 = SPFSs 'State Application' Group; Model 3 = SPFSs 'State Non-Application' Group. * p<0.10, ** p<0.05, *** p<0.01*

Table 53: Results of Ordinary Least Squares Regression Estimates of the Relationship between Accruals and Cash-Flows: SPFSs 'State Application' and SPFSs 'State Non-Application' of R&M Groups – Large Proprietary Companies

	Model 1 ACC_{it}	Model 2 ACC_{it}	Model 3 ACC_{it}
CFO_{it+1}	-0.124	-0.130	-0.0308
	(-1.49)	(-1.34)	(-0.35)
CFO_{it-1}	0.000***	0.000***	0.106**
	(9.87)	(9.38)	(2.08)
CFO_{it}	-0.000***	-0.000***	-0.577***
	(-21.52)	(-21.66)	(-9.18)
_cons	-0.025**	-0.025**	0.036**
	(-2.25)	(-2.11)	(2.34)
N	222	175	47
R^2	0.034	0.036	0.645
adj. R^2	0.016	0.019	0.620

*t statistics, in parentheses, are calculated using the Huber-White sandwich estimator to correct standard errors. The b-coefficient is represented by the values that are not in parentheses. _cons is explained in Table 4 above. Model 1 = SPFSs 'State Application' and SPFSs 'State Non-Application' Groups; Model 2 = SPFSs 'State Application' Group; Model 3 = SPFSs 'State Non-Application' Group. * p<0.10, ** p<0.05, *** p<0.01*

4.3 Late Lodgement of Annual Financial Statements with the ASIC – Large Proprietary Companies

As timeliness is relevant to the usefulness of financial information, large proprietary companies are required to lodge financial statements with the ASIC within four months of the end of the annual reporting period.[41] To further understand the financial reporting practices of companies, the late lodgement of annual reports by large proprietary companies is examined by calculating the difference between the date of lodgement of the company's annual report to the ASIC and the company's reported financial year end in the lodgement. This is also followed by an analysis of the proportion of such companies making late lodgement of financial statements. This analysis is extended to late lodgement by type of audit firm. The research on late lodgement was undertaken in respect of large proprietary companies to assess whether it would provide any support for the findings on the quality of accruals analysis in Section 4.2 above – however, this research did not find a statistically significant difference between late lodgement of GPFSs and SPFSs.

The primary proxy adopted for 'late' lodgement is whether the company lodges its financial statements with the ASIC within four months of the end of the annual reporting period. The mean lodgement period from the company's reported financial year end is 165.3 days, that is, more than six weeks later than specified. The median lodgement period is 121 days. The minimum number of lodgement days observed is six, with a maximum number of days being 1,067 (i.e., two years and nine months). Table 54 demonstrates that the rate of late lodgement is 47.2 per cent. Interestingly the rate of late lodgement is consistent between companies lodging GPFSs (44.3%) and companies lodging SPFSs (47.9%), and the chi-square test ($\chi^2 = 1.1235$, p = 0.289) suggests that companies lodging SPFSs do not have a statistically significant higher rate of late lodgement compared with companies lodging GPFSs. Table 54 demonstrates that the rate of late lodgement is 34.7 per cent for the Big 4 clients and 85.4 per cent for the non-Big 4 clients, and these differences are statistically significant ($\chi^2 = 13.8346$, p = 0.000). One Big 4 firm stands out as the firm whose clients are significantly less likely to lodge late, with only 24.5 per cent of its clients lodging their financial statements with the ASIC more than 4 months after year end ($\chi^2 = 4.113$ $p = .042$, *2 tailed test*).

Table 54: Late Lodgement of Annual Report to the ASIC for Large Proprietary Companies Subject to an Audit

	Frequency	Late Lodgement to the ASIC	
		No.	%
Full Sample	394	186	47.2[a]
GPFSs	79	35	44.3
SPFSs	315	151	47.9[b]
Total	**394**	**186**	
Entities Subject to an Audit	345	172	49.9
Big 4 Auditor	242	84	34.7
Non-Big 4 Auditor	103	88	85.4[c]
Total	**345**	**172**	

[a] *Based on the proportion of lodgements later than 120 days.*

[b] *Chi-square tests do not show statistically significant differences between GPFSs and SPFSs, that is, companies lodging SPFSs do not have a higher rate of late lodgements compared with the GPFSs group.*

[c] *Chi-square tests show statistically significant differences between Big 4 and Non-Big 4 Audit firms.*

41 Section 319(3)(b) of the Corporations Act. Financial statements lodged after this time are subject to nominal late fees.

4.4 Concluding Comments on Section 4

This concludes the analysis of the examination of the financial reporting practices by companies in the sample lodging financial statements with the ASIC. Financial reporting practices are analysed across three primary dimensions to gauge the quality of lodged financial statements. First, information provided in the significant accounting policies note to the financial statements of the five categories of companies is analysed in the context of the disclosure of the application of R&M. Second, the quality of accruals recognised by large proprietary companies is analysed, and third, the timeliness of lodgement of financial statements for the sample of large proprietary companies is examined.

The results of the examination of the reporting practices of companies lodging SPFSs indicate that the majority of companies stated they apply R&M, around 20 per cent of the SPFSs appear not to have applied R&M, and approximately 15 per cent of companies were found to provide no indication of whether they applied R&M.

The accruals recognised by companies among the large proprietary company sample is examined. This analysis shows that the SPFSs group seems to have provided lower quality accruals compared with those companies that lodged GPFSs. The analysis also provides evidence to indicate that the accruals recognised by companies that lodged SPFSs that did not state application or stated non-application of R&M are of lower quality than those recognised by companies that lodged SPFSs and stated application of R&M.

A large body of research literature (e.g., Givoly, 1982; Abd-Elsalam & Street, 2007; Ball et al., 2008) reports a significant statistical association between the timeliness of information contained in financial statements and the value or relevance of the information reported. This research suggests that more timely financial statements have higher information content and are associated with more efficient debt and equity markets as well as stronger corporate governance for the entities preparing the financial statements. Drawing on aspects of this research, the timeliness of lodgement of financial information for the sample of large proprietary companies is examined. Companies required to lodge financial statements are required to do so within four months of the end of the annual reporting period. These requirements are used to proxy for timeliness and identify late submission of company lodgements to the ASIC. The analysis indicates that 47 per cent of large proprietary companies preparing GPFSs lodged more than four months after year-end, and 48 per cent of large proprietary companies lodged SPFSs late (which is not significantly different).

The large-scale nature of the research underpinning the findings summarised here precludes a thorough analysis of the possible motives behind decisions to lodge GPFSs or SPFSs. In particular, it would not be feasible as part of this research to follow up with all the relevant companies whose financial statements were analysed in a way that would yield an unbiased response overall.

PART B: REPORT ON STATE-BASED LODGEMENTS

1. Introduction

Requirements relating to financial reporting by entities lodging with state-based regulators are primarily found in disparate state-based legislation. In each state, requirements by class of entity are provided in relation to the following aspects: the classes of entity for reporting purposes; the content of financial statements; audit requirements; and lodgement (including timing). While in most instances the legislation and associated guidance is consistent with definitions such as current assets and revenue in Australian Accounting Standards, in other instances this is not the case.[42]

This Part (Part B) of this Report seeks to achieve the following two primary objectives:

(a) document the legislation and associated guidance that affects financial statements of incorporated associations, co-operatives and other entities lodged with state-based regulators; and

(b) examine the financial reporting practices of entities lodging with Consumer Affairs Victoria, NSW Fair Trading and Queensland Office of Fair Trading.

Data from Victoria, NSW and Queensland was more readily available relative to the other jurisdictions. Accordingly, this Report examines the data in relation to Victoria, NSW and Queensland and only provides an overview of the relevant regulation in Tasmania, South Australia and Western Australia. This Report does not address entities regulated by the Northern Territory and Australian Capital Territory governments.

In Section 2 below, an overview is provided of the regulation that applies to financial reporting of the entities that are the subject of the research.

2. Overview – Regulatory Guidance on Financial Reporting

Incorporated Associations: Broadly, with the exception of Western Australia, the structure of the financial reporting and audit requirements for incorporated associations is consistent across states in that quantitative tests, based on amounts for revenues and assets, typically determine the levels of reporting and disclosure required by these entities. In most states, additional requirements, primarily relating to audit, apply when the entity is involved in gaming and/or charitable activities.[43]

Co-operatives: The requirements for co-operatives are reasonably consistent across states for the years analysed in this Report – as the relevant legislation requires preparation of financial statements under Chapter 2M of the Corporations Act. More recently, this consistency has been enhanced by harmonising legislation on co-operatives across Australia, enabled in large

42 For example, as Section 4 of this Part of this Report shows, in NSW the current classification of associations for reporting and audit purposes depends on the levels of current assets and revenue. In this instance, current assets and revenue are defined in a manner that is not necessarily consistent with Australian Accounting Standards.

43 Some industry-based regulations are relevant to the financial reporting by incorporated associations across Australia. For example, the *Travel Agents Handbook* (IATA, 2012) requires travel agents in Australia to prepare financial reports in accordance with Australian Accounting Standards and have those reports audited.

part by the work of the Council of Australian Governments (COAG) *Legislative and Governance Forum on Consumer Affairs*. The legislation is very similar across jurisdictions and is based on a set of standard provisions developed in 1996 by the Standing Committee of Attorneys-General, which signed the *Consistent Co-operative Laws Agreement*.

Charities and Fundraisers: Entities undertaking charitable and/or fundraising activities must register within their state and lodge audited financial statements with the state regulator. Some states provide exemption from these requirements for smaller charities.

2.1 Recent Nation-Wide Legislative Amendments – Charities and Not-for-Profit Entities

The *Australian Charities and Not-for-profits Commission Act 2012* and *Australian Charities and Not-for-profits Commission Regulation 2013* (ACNC Regulations) require uniform financial reporting for medium and large registered charities for financial years ending on or after 30 June 2014, subject to the following exceptions:

(a) The Australian Charities and Not-for Profits Commission (ACNC) Commissioner announced on 18 February 2014 that she will exercise her discretion under the *Australian Charities and Not-for-profits Commission (Consequential and Transitional) Act 2012* to accept financial reports lodged with state and territory regulators in place of ACNC financial reports for the 2014 reporting period.

(b) Also for the 2014 reporting period, there is a transitional arrangement (pursuant to the ACNC Regulations) for registered charities that were not required under an Australian law to prepare a financial report in accordance with Australian Accounting Standards for the 2013 reporting period. Under this transitional arrangement, eligible charities are only required to lodge a statement including the financial components as set out in the ACNC Regulations.

For the 2015 reporting period onwards, unincorporated charities such as unincorporated associations, societies, clubs and trusts will have to lodge the same financial statements and be subject to the same audit/review requirements as charities operating through incorporated entities such as companies limited by guarantee, incorporated associations and co-operatives.

Sections 3, 4 and 5 below outline the research undertaken on samples of financial statements lodged by entities with regulators in Victoria, New South Wales and Queensland respectively.

Sections 6, 7 and 8 below outline the regulations applying to entities that lodge financial statements with regulators in Tasmania, South Australia and Western Australia respectively.

3. Victorian Entities

Table 1 below shows the Victorian entity groups and their respective population numbers as of 2010 and the relevant reporting legislation.

Table 1: Victorian Data

Victorian Entity Group	Population n	Population %	Relevant reporting legislation
Incorporated Associations	35,991	90.72	*Associations Incorporation Act 1981* *Associations Incorporation Regulations 2009* *Co-operatives Act 1996* *Fundraising Act 1998* *Gambling Regulation Act 2003* *Travel Agents Act 1986* *Veterans Act 2005* *Veterans (Patriotic Funds) Regulations 2008* *Retirement Villages Act 1986* *Funerals Act 2006*
Co-operatives	707	1.78	
Patriotic Funds	613	1.55	
Fundraisers	1,415	3.57	
Retirement Villages	400	1.01	
Funeral Services	380	0.96	
Limited Partnerships	167	0.42	
Total	**39,673**	**100.00**	

3.1 Reporting and Auditing Regulation – Victoria

3.1.1 Incorporated Associations – Victoria

Incorporated associations primarily comprise not-for-profit clubs or community groups that are given formal legal structure (i.e., an incorporated association is a legal entity whereby members are protected from liabilities of the association) by way of their incorporation under the Associations Incorporation Act (and, effective from November 2012, the *Associations Incorporation Reform Act 2012*).

Relevant authority: The financial reporting requirements for incorporated associations in Victoria, for the period covered by this Part of this Report are primarily found in the Associations Incorporation Act.

Classes of entity for reporting: The Associations Incorporation Act establishes differential content of reports according to whether an entity is a prescribed or non-prescribed Association.

According to section 3, a prescribed association is an incorporated association with:

(a) gross receipts in excess of $200,000; or

(b) gross assets in excess of $500,000.

A non-prescribed association is, by default, not a prescribed association.

Reporting requirements: The Associations Incorporation Act specifies: “An Incorporated Association must maintain adequate and accurate accounting records of the financial transactions of the Incorporated Association” (s.30A). The Act specifies that, at the annual general meeting (AGM), an incorporated association shall submit to its members a statement containing:

(a) the income and expenditure of the association during its last financial year; and

(b) the assets and liabilities of the association at the end of its last financial year.

The Act specifies that the statements submitted to the AGM must:

(a) give a true and fair view of the financial position of the association during and at the end of its last financial year (s.30(3A)); and

(b) in the case of a prescribed association, be accompanied by the accounts audited in accordance with section 30B.

Section 30B states the audit of a prescribed association must be performed by:

(a) a registered company auditor; or

(b) a firm of registered company auditors; or

(c) a person who is a member of CPA Australia or the Institute of Chartered Accountants in Australia; or

(d) any other person who is approved by the Registrar as an auditor of the accounts of the incorporated association.

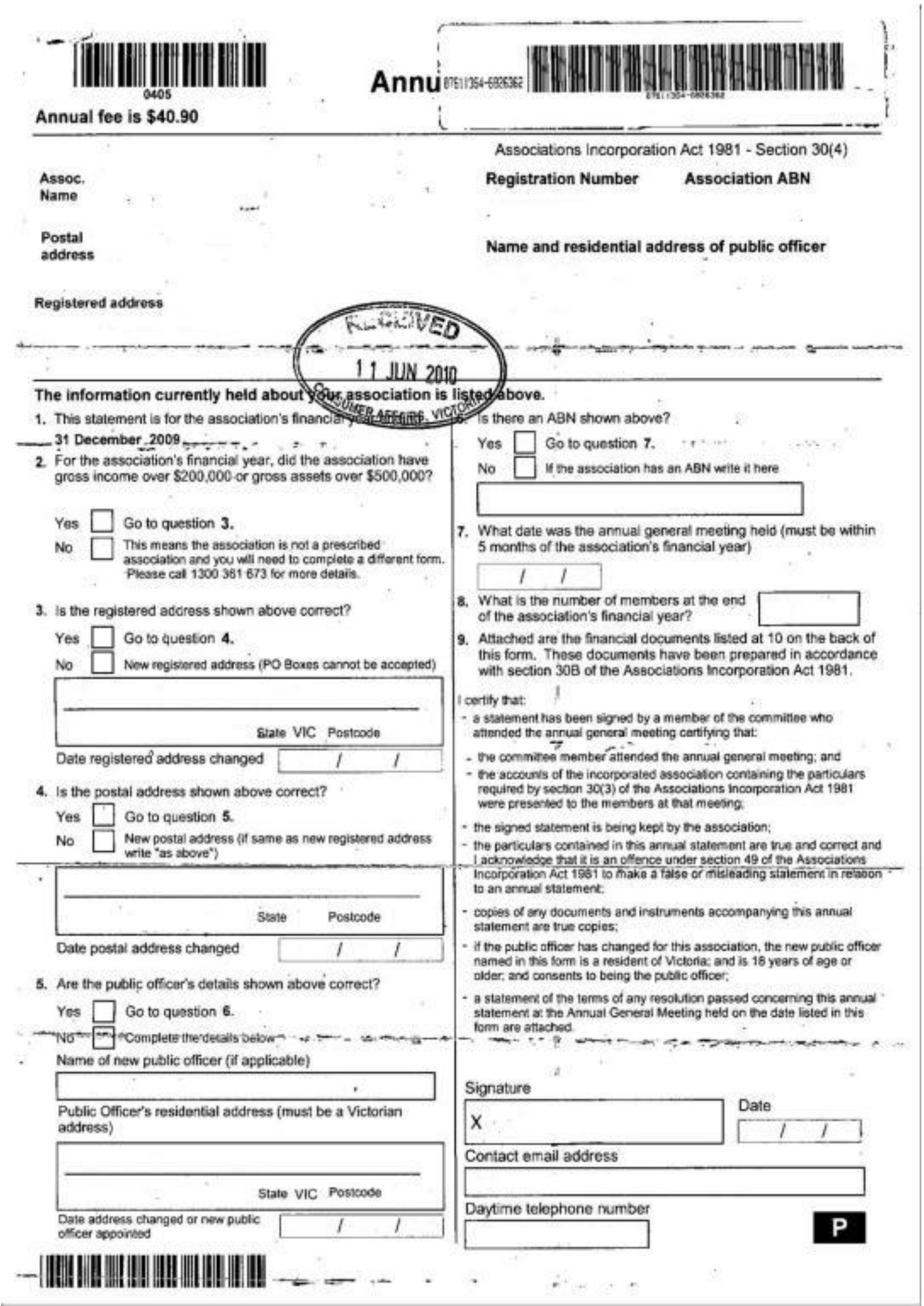
The Incorporated Associations Act makes provision for a prescribed association to apply to Consumer Affairs Victoria (CAV) for an audit exemption (s.38B(4)).

While the Act specifies the nature of the financial statements to be tabled at the AGM and lodged with the registrar (statement of income and expenditure, statement of assets and liabilities), the Act does not specify the standards governing the content of the financial statements for either prescribed or non-prescribed associations. The Act states that the information submitted at the AGM must be given to the Registrar in the form approved by the Registrar (s.30(4)).

The Registrar specifies the reporting requirements on the annual lodgement form.[44] Requirements specified on the annual lodgement form are explained further below. Sample lodgement forms for prescribed and non-prescribed associations are re-produced as Figures 1 and 2 immediately below.

44 Each year the association's public officer receives a form that has been partially completed by CAV. The form comes completed with information regarding the association name, postal address, registered address, name and residential address of public officer, registration number, and association ABN.

Figure 1: Sample Form Lodged in Victoria by Prescribed Associations



0405

Annual fee is $40.90

Annu

Associations Incorporation Act 1981 - Section 30(4)

Assoc. Name

Registration Number | Association ABN

Postal address

Name and residential address of public officer

Registered address

RECEIVED 11 JUN 2010 CONSUMER AFFAIRS VICTORIA

The information currently held about your association is listed above.

1. This statement is for the association's financial year ending 31 December 2009
2. For the association's financial year, did the association have gross income over $200,000 or gross assets over $500,000?
   Yes ☐ Go to question 3.
   No ☐ This means the association is not a prescribed association and you will need to complete a different form. Please call 1300 361 673 for more details.
3. Is the registered address shown above correct?
   Yes ☐ Go to question 4.
   No ☐ New registered address (PO Boxes cannot be accepted)
   State VIC Postcode
   Date registered address changed / /
4. Is the postal address shown above correct?
   Yes ☐ Go to question 5.
   No ☐ New postal address (if same as new registered address write "as above")
   State Postcode
   Date postal address changed / /
5. Are the public officer's details shown above correct?
   Yes ☐ Go to question 6.
   No ☐ Complete the details below
   Name of new public officer (if applicable)
   Public Officer's residential address (must be a Victorian address)
   State VIC Postcode
   Date address changed or new public officer appointed / /
6. Is there an ABN shown above?
   Yes ☐ Go to question 7.
   No ☐ If the association has an ABN write it here
7. What date was the annual general meeting held (must be within 5 months of the association's financial year)
   / /
8. What is the number of members at the end of the association's financial year?
9. Attached are the financial documents listed at 10 on the back of this form. These documents have been prepared in accordance with section 30B of the Associations Incorporation Act 1981.

I certify that:

- a statement has been signed by a member of the committee who attended the annual general meeting certifying that:
- the committee member attended the annual general meeting; and
- the accounts of the incorporated association containing the particulars required by section 30(3) of the Associations Incorporation Act 1981 were presented to the members at that meeting;
- the signed statement is being kept by the association;
- the particulars contained in this annual statement are true and correct and I acknowledge that it is an offence under section 49 of the Associations Incorporation Act 1981 to make a false or misleading statement in relation to an annual statement;
- copies of any documents and instruments accompanying this annual statement are true copies;
- if the public officer has changed for this association, the new public officer named in this form is a resident of Victoria; and is 18 years of age or older; and consents to being the public officer;
- a statement of the terms of any resolution passed concerning this annual statement at the Annual General Meeting held on the date listed in this form are attached.

Signature X

Date / /

Contact email address

Daytime telephone number

P

Figure 1 cont.: Sample Form Lodged in Victoria by Prescribed Associations

10. Financial requirements

You must attach the financial accounts of the prescribed association that have been prepared in accordance with the prescribed Australian Accounting Standards (listed below). The financial statements must be audited and consist of the following documents:

- Statement of Financial Performance AAS1 (Income & Expenditure Statement);
- Statement of Financial Position - AAS36 (Balance Sheet);
- Statement of Cashflows - AAS28;
- Notes to the Accounts (Explanation for accounts disclosure, accounting policies etc.);

The financial statement must be accompanied by the signed auditor's report and must give a true and fair view of the association's financial position

More information about financial requirements for prescribed associations

Who can conduct audits

- a registered company auditor; or
- a firm of registered company auditors; or
- a person who is a member of CPA Australia or the Institute of Charted Accountants in Australia; or
- any other person who is approved by the registrar as an auditor of the accounts of the incorporated association for the purposes of section 30B.

Who cannot conduct audits

- a member of the committee of the incorporated association; or
- an employer or employee of a member of that committee; or
- a member of the same partnership as a member of that committee; or
- an employee of the incorporated association.

Keeping accounting records

A prescribed association must keep all accounting records of the incorporated association for a period of 7 years after the completion of the transactions to which they relate.

Australian Accounting Standards

Australian Accounting Standard Number	Name of Australian Accounting Standard	Issued
AASB 1018 (replaces AAS1)	Statement of Financial Performance	June 2002
AAS 4	Depreciation	August 1997
AAS 5	Materiality	September 1995
AAS 6	Accounting Policies	March 1999
AAS 8	Events Occuring After Reporting Date	October 1997
AAS 15	Revenue	June 1998
AAS 17	Leases	October 1998
AAS 28	Statement of Cash Flows	October 1997
AAS 36	Statement of Financial Position	October 1999
AASB 1041 (replaces AAS38)	Revaluation of Non-Current Assets	July 2001

How to lodge and pay

Make sure the public officer has signed on the front page of this form.

The fee of $40.90 can be paid by cheque, money order or credit card. Do not send cash through the mail. Cash will be accepted if paying in person. Cheques and money orders are to be made payable to: "Consumer Affairs Victoria". Please attach financial statements, cheques or money orders and other documents by paperclip. Do not staple.

Deliver in person to:
Victorian Consumer & Business Centre
113 Exhibition Street, Melbourne
Counter area (cnr Little Collins St) is open 8.30am - 5.00pm Monday to Friday (closed on public holidays)

Send by post to:
Consumer Affairs Victoria
GPO Box 4567, Melbourne VIC 3001
(please use a large envelope and fold this form as little as possible)

If paying by credit card, fill in your credit card details below

Name of cardholder

Visa ☐ Mastercard ☐ Amex ☐

Card number

Card expiry date ☐☐ / ☐☐ Amount $40.90 CCV number* ☐☐☐ *(see note below)

Signature of cardholder X Date / /

Daytime telephone number

* Note on CCV numbers: Credit card cards are now issued with a CCV number. This is the last three numbers located on the signature strip on the back of the card. If your credit card has been allocated this number enter the 3 numbers in the space provided.

Privacy
CAV is committed to responsible and fair handling of your personal information, consistent with the laws we administer and the Information Privacy Act 2000. The information on this form will be placed on the public register in accordance with the Incorporated Associations Act 1981. We may be unable to process this form if you do not provide the required information. You can contact us at any time to request access to the personal information we hold about you. In exceptional circumstances, you may apply to have public access to your personal information restricted. Our privacy statement, and other privacy information, is available at www.consumer.vic.gov.au or on request.

Consumer Affairs Victoria,
121 Exhibition Street, Melbourne
GPO Box 4567, Melbourne 3001
Telephone: 1300 361 673
www.consumer.vic.gov.au

Victoria The Place To Be

IA Form 3A (21/05/2002)

Figure 2: Sample Form Lodged in Victoria by Non-Prescribed Associations

Annual 87649930-6996999

0410

Annual fee is $41.80

Associations Incorporation Act 1981 - Section 30(4)

Assoc. Name

Registration Number **Association ABN**

Postal address

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CONSUMER AFFAIRS, VICTORIA

Name and residential address of public officer

Registered address

The information currently held about your association is listed above.

1. This statement is for the association's financial year ending
   30 June 2010
2. For the association's financial year, did the association have gross income over $200,000 or gross assets over $500,000?
   No ☐ Go to question **3.**
   Yes ☐ This means the association is a prescribed association and you will need to complete a different form. Please call 1300 361 673 for more details.
3. Is the registered address shown above correct?
   Yes ☐ Go to question **4.**
   No ☐ New registered address (PO Boxes cannot be accepted)
   State VIC Postcode
   Date registered address changed / /
4. Is the postal address shown above correct?
   Yes ☐ Go to question **5.**
   No ☐ New postal address (if same as new registered address write "as above")
   State Postcode
   Date postal address changed / /
5. Are the public officer's details shown above correct?
   Yes ☐ Go to question **6.**
   No ☐ Complete the details below
   Name of new public officer (if applicable)
   Public Officer's residential address (must be a Victorian address)
   State VIC Postcode
   Date address changed or new public officer appointed / /
6. Is there an ABN shown above?
   Yes ☐ Go to question **7.**
   No ☐ If the association has an ABN write it here
7. What date was the annual general meeting held (must be within 5 months of the association's financial year)
   / /
8. What is the number of members at the end of the association's financial year?
9. Go to question 10 on the back of this page and complete the financial statement section.

I certify that:

- a statement has been signed by a member of the committee who attended the annual general meeting certifying that:
  - the committee member attended the annual general meeting; and
  - the accounts of the incorporated association containing the particulars required by section 30(3) of the Associations Incorporation Act 1981 were presented to the members at that meeting;
- the signed statement is being kept by the association;
- the particulars contained in this annual statement are true and correct and I acknowledge that it is an offence under section 49 of the Associations Incorporation Act 1981 to make a false or misleading statement in relation to an annual statement;
- copies of any documents and instruments accompanying this annual statement are true copies;
- if the public officer has changed for this association, the new public officer named in this form is a resident of Victoria; and is 18 years of age or older; and consents to being the public officer;
- a statement of the terms of any resolution passed concerning this annual statement at the Annual General Meeting held on the date listed in this form are attached.

Signature
X

Date / /

Contact email address

Daytime telephone number

Figure 2 cont. Sample Form Lodged in Victoria by Non-Prescribed Associations

10. Financial requirements

You must either:
- fill in the financial statement below; or
- use your own format for the financial statement as set out in section 30 of the Associations Incorporation Act 1981 and attach it to this form.

Financial Statement

For end of financial year: 30 June 2010

Income	Amount $
Trading receipts (bar sales, merchandise etc.)	
Fees/Subscription from members	
Fundraising receipts	
Grants (Government/Corporate)	
Donations	
Sponsorships	
Bank interest received	
Other (specify)	
Total income (A)	
Expenditure	**Amount $**
Trading costs (eg. bar stock, merchandise etc.)	
Rent/hire (hall, meeting room, equipment etc.)	
Water, gas, electricity, insurance etc.	
Salaries and wages	
Office expenses (stationery, postage, phone etc.)	
Fundraising costs	
Bank fees and charges	
Other (specify)	
Total expenditure (B)	
Surplus (A - B)	
Assets	**Amount $**
Cash in hand or in the bank	
Value of stock on hand	
Amount owed to association	
Property, equipment, furnishings	
Investments	
Other (specify)	
Total assets (C)	
Liabilities	**Amount $**
Secured loans (outstanding balance)	
Unsecured loans (outstanding balance)	
Other (specify)	
Total liabilities (D)	
Association's equity (C - D)	

You must also list all mortgages, charges and securities affecting property here (or attach a separate sheet if needed)

During its financial year, did the association hold any trusts?

No ☐

Yes ☐ You must also attach for each trust:
- the income and expenditure of the trust
- the assets and liabilities of the trust
- the mortgages, charges and securities affecting any property of the trust.

How to lodge and pay

Make sure the public officer has signed on the front page of this form.

The fee of $41.80 can be paid by cheque, money order or credit card. Do not send cash through the mail. Cash will be accepted if paying in person. Cheques and money orders are to be made payable to: "Consumer Affairs Victoria". Please attach financial statements, cheques or money orders and other documents by paperclip. Do not staple.

Deliver in person to:
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Counter area (cnr Little Collins St) is open 8.30am - 5.00pm Monday to Friday (closed on public holidays)

Send by post to:
Consumer Affairs Victoria
GPO Box 4567, Melbourne 3001
(please use a large envelope and fold this form as little as possible)

If paying by credit card, fill in your credit card details below

Name of cardholder

Visa ☐ Mastercard ☐ Amex ☐

Card number

Card expiry date / Amount **$41.80** CCV number *(see note below)

Signature of cardholder X Date / /

Daytime telephone number

* Note on CCV numbers: Credit card cards are now issued with a CCV number. This is the last three numbers located on the signature strip on the back of the card. If your credit card has been allocated this number enter the 3 numbers in the space provided.

Privacy
CAV is committed to responsible and fair handling of your personal information, consistent with the laws we administer and the Information Privacy Act 2000. The information on this form will be placed on the public register in accordance with the Incorporated Associations Act 1981. We may be unable to process this form if you do not provide the required information. You can contact us at any time to request access to the personal information we hold about you. In exceptional circumstances, you may apply to have public access to your personal information restricted. Our privacy statement, and other privacy information, is available at www.consumer.vic.gov.au or on request.

Consumer Affairs Victoria
Consumer Affairs Victoria,
121 Exhibition Street, Melbourne
GPO box 4567, Melbourne 3001
Telephone: 1300 361 673
www.consumer.vic.gov.au

Victoria The Place To Be

IA Form 3A (10/05/2010)

Prescribed Associations: Question 10 on the lodgement form (see Figure 1 above) instructs the prescribed association to attach audited financial statements prepared in accordance with the following Accounting Standards:

(a) Statement of Financial Performance AAS1018 (Income & Expenditure Statement);

(b) Depreciation AAS4;

(c) Materiality AAS5;

(d) Accounting Policies AAS6;

(e) Events Occurring After Reporting Date AAS8;

(f) Revenue AAS15;

(g) Leases AAS17;

(h) Statement of Cash flows AAS28;

(i) Statement of Financial Position·AAS36 (Balance Sheet); and

(j) Revaluation of Non-Current Assets AAS1041.

It is noted that each of the ‘AAS’ standards referred to in the lodgement forms were superseded for annual reporting periods beginning on or after 1 January 2005. Updating the lodgement forms to require application of the corresponding current Australian Accounting Standards would be expected to assist in enabling greater consistency in the information lodged by different categories of entities nationally or, indeed, prescribed associations in Victoria.

Question 9 on the lodgement form requires the association’s public officer to certify that the financial statements, including the attached financial statements specified in question 10, are (among other things) true and correct.

Non-Prescribed Associations: Question 10 on the lodgement form instructs the non-prescribed association to either complete the financial statement template provided or use the association’s own format for the financial statement (see sample form – Figure 2). Thus there is no specific requirement under the Act for non-prescribed associations to comply with Accounting Standards.[45]

As with prescribed associations, Question 9 on the lodgement form requires the non-prescribed association’s public officer to certify that the information provided in response to question 10 is true and correct.

3.1.2 Co-operatives – Victoria

A Co-operative is a democratic organisation owned and controlled by its members for a common benefit.[46] Co-operatives are usually formed because members perceive benefits to be gained through combined purchasing, distribution or marketing power or influence of the group. Examples of entities in Victoria that commonly operate as co-operatives include schools and organisations providing social housing or services to rural communities.

45 Non-prescribed associations must list all mortgages, charges and securities affecting property.

46 http://www.consumer.vic.gov.au/businesses/registered-businesses/co-operatives/what-is-a-co-operative – accessed April 2014.

Relevant authority: Co-operatives in Victoria are administered under the Corporations Act and the Co-operatives Act.[47] CAV administers and enforces the Co-operatives Act.

Reporting requirements: The financial reporting and audit requirements of a co-operative are the same as those that apply to public companies under the Corporations Act, by virtue of section 238 of the Co-operatives Act.[48] However, the Co-operatives Act states that a co-operative must lodge an annual report with CAV, attaching the audited financial statements presented at the AGM, within 28 days of the AGM (s.249(2)(a)). As a part of annual lodgement, co-operatives in Victoria are required to complete a standardised lodgement form, a sample of which is re-produced in Figure 3 immediately below.

47 Legislative reform for Victorian co-operatives was recently introduced through the *Co-operatives (Adoption of National Law) Act 2012*; resulting in the reporting requirements for small co-operatives being reduced.

48 The significance of this is that, by virtue of section 238, reference in relevant provisions of Corporations Act to a 'company' or 'public company', is to be read as a reference to a 'co-operative'.

Figure 3: Sample Form Lodged in Victoria by Co-operatives

0701

87649891-7880868

Annual report for your co-operative

This is the annual report for:

1. Co-op Name

2. Registered Address

3. Financial Year ending:

4. At the end of your Financial Year:

No. full-time employees: __________

No. part-time employees: __________

No. active members: __________

No. memberships cancelled: __________

No. shares forfeited: __________

5. Your annual general meeting

The meeting was held

☐ No ☐ Yes, when __________

The financial accounts were presented at the AGM

☐ Yes ☐ No

Please attach the financial accounts, including those of any subsidiaries of your co-operative

The auditor's report was presented at the AGM

☐ Yes ☐ No

Please attach the auditor's report, including reports about any subsidiaries of your co-operative

6. At the beginning of your new reporting period

The current secretary is

Name __________

Home address __________

Occupation __________

Date of Birth __________ Place of Birth __________

Telephone No __________

Please attach a list of the names and addresses of all other secretaries of subsidiaries of your co-operative

7. And if applicable, the current principal executive officer is

Name __________

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14 SEP 2010
CONSUMER AFFAIRS VICTORIA

Home address __________

Occupation __________

Date of Birth __________ Place of Birth __________

Telephone No __________

8. Auditor Details

Name __________

Firm Name __________

Address __________

Phone no. __________ Fax no. __________

Signature of Secretary **Date**

Note The fee payable is $47.80

Cheques or money orders should be made payable to "Consumer Affairs Victoria".

Credit card payments Visa/Mastercard/American Express can be made by inserting details in the area provided over the page.

Make sure you attach to this form

The financial accounts ☐ The auditor's report ☐ Directors Report ☐ Directors Declaration ☐ List of Directors ☐

Registrar of Co-Operatives, Consumer Affairs Victoria

GPO Box 4567, Melbourne VIC 3001 **Phone 1300 361 673** **Fax 03 8684 6210**

CO 0005 (10/05/2010)

Figure 3 cont.: Sample Form Lodged in Victoria by Co-operatives

Financial Summary

Financial Year ending: 30-06-2010

Total revenue (gross)		$
Net surplus/(deficit) after tax for the year		$
Total C'wealth/State government grants received during the year (gross)		$
Total amount of Government Guarantee loans outstanding at the end of financial year		$
Issued capital (where applicable)	A	$
Uncalled capital/Call in arrears	B	$
Paid up capital/Members' benefits	C=A-B	$
Reserves	D	$
Retained earnings	E	$
Shareholders' funds	F=C+D+E	$
Current liabilities (including government guarantee loans)	G	$
Non-current liabilities (including government guarantee loans)	H	$
Total equity & liabilities	X=F+G+H	$
Current assets	J	$
Non-current assets	K	$
Total assets	Y=J+K	$

Credit Card Payment Slip

Type of Card

Visa ☐ MasterCard ☐ Amex ☐

Card number ☐☐☐☐ ☐☐☐☐ ☐☐☐☐ ☐☐☐☐

Card expiry date ☐☐ / ☐☐

Amount $47.80

Name of cardholder

CCV number *(see note at right)

Signature of cardholder

Date / /

*Note on new CCV numbers: Credit card cards are now issued with a CCV number. This is the last three numbers located on the signature strips on the back of the card. If your credit card has been allocated this number enter the 3 numbers in the space provided.

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Registrar of Co-Operatives, Consumer Affairs Victoria

GPO Box 4567, Melbourne VIC 3001 Phone 1300 361 673 Fax 03 8684 6210

CO 0005 (10/05/2010)

Figure 3 cont.: Sample Form Lodged in Victoria by Co-operatives

LIST OF DIRECTORS, SECRETARY AND PRINCIPAL EXECUTIVE OFFICER

Name of Co-operative: ______________________________

The undermentioned persons: *(Strike out whichever statement does not apply)*

(1) were elected as officers of the Co-operative at its formation meeting held on ______________

(2) are the officers of the Co-operative for the financial year that commenced on ______________

SURNAME Director(s):	OTHER NAME(s)	ADDRESS	OCCUPATION	DATE OF BIRTH	PLACE OF BIRTH	MEMBER/ NON-MEMBER	DATE OF APPOINTMENT
Principal Exec. Officer: (If applicable)							
Secretary:							

DATED: ______________

SECRETARY: ______________

(Strike out whichever statement is not applicable:)

(1) ***In capacity as secretary for purposes of formation meeting, or***

(2) ***As elected secretary of Co-operative***

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Consumer Affairs Victoria

3.1.3 Fundraisers – Victoria

A fundraiser is an entity that raises money and other resources from the public and applies those resources to non-commercial purposes. Examples of fundraisers are entities that raise money and resources via doorknock appeals, telephone appeals, highway collections, and sale of goods at opportunity shops. These entities are subject to the Fundraising Act. Fundraisers usually take on the structure of an incorporated association or a company limited by guarantee and will therefore be subject to the reporting provisions of the legislation applicable to this category of entity.[49]

Relevant authority: Fundraisers are regulated under the Fundraising Act. CAV is responsible for the oversight of fundraisers (s.17A).

Reporting requirements: The Fundraising Act specifies that adequate financial information is available to enable members of the public (or inspectors) to check that the proceeds of fundraising appeals have been used for the purpose for which they were solicited or received (s.28). The entity conducting a fundraising appeal must keep records sufficient to enable a true and fair view of the income and expenditure relating to the appeal (s.29(1)). The Act specifies that an entity must keep detailed records on any expenditure on assets; any expenditure on wages, salaries, commissions and other remuneration; administrative expenses; and other expenditure related to the appeal (s.29(1)). The entity conducting the appeal must ensure that accounts are finalised within three months of the date the appeal ends (s.29(4)).

The Director (of CAV) may require fundraisers to provide, among other things, the following financial information in their annual return:[50]

(a) gross proceeds during the last 12 months;

(b) names of beneficiaries and the amounts each received;

(c) an estimate of gross proceeds for the next 12 months;

(d) an estimate of the percentage of these gross proceeds that will go to beneficiaries in the next 12 months; and

(e) a copy of its most recent financial statements.

The Director may require the financial statements of fundraisers to be audited (depending on their size) under the Fundraising Act (s.32).

3.1.4 Patriotic Funds – Victoria

A patriotic fund is an entity established to collect funds, receive subscriptions, or request donations for any purpose related to any military service or duty.[51] A patriotic fund provides welfare services and clubrooms for returned service personnel and their dependents. Patriotic funds in Victoria are administered by legally appointed trustees such as the Returned and

49 There are numerous types of organisations that may be engaged in fundraising but which are exempted from registration and reporting to CAV under section 71(b). Examples include state government schools, school councils, registered non-government schools and kindergartens, universities, TAFE colleges, public and denominational hospitals, public health services, state-funded residential care services, religious bodies that have authority to marry people, political parties registered under the Victorian or Commonwealth Electoral Acts, trade unions registered in Victoria and federally-registered associations of employees, associations of employers or enterprise associations. Organisations that receive less than $10,000 gross in a financial year from fundraising, are not paid for conducting the fundraising and use only unpaid volunteers and patriotic funds within the meaning of the Veterans Act are also exempt. (For further information, refer: www.consumer.vic.gov.au).

50 Information obtained from CAV website (http://www.consumer.vic.gov.au/clubs-and-not-for-profits/fundraisers/responsibilities) – accessed April 2014.

51 http://www.consumer.vic.gov.au/clubs-and-not-for-profits/patriotic-funds/what-are-patriotic-funds – accessed April 2014.

Services League (RSL), branches of Legacy, and the Vietnam Veterans' Association of Australia (Victorian branch).

Relevant authority: Patriotic funds are regulated under the Veterans Act. The Veterans Act confers the regulatory powers in relation to patriotic funds on the Director of CAV (s.1(1)(b)(ii)).

Reporting requirements: The Veterans Act specifies that a patriotic fund must lodge with CAV:

(a) a duly audited statement of receipts and disbursements (s.42(2)(a)); and

(b) a duly audited balance sheet (s.42(2)(b)).

According to the Act, the above information is required to be lodged on a date specified in the Act or set by the Director of CAV (s.42(5)).

The term 'duly audited' referred to above is defined in the Act as audited in accordance with recognised auditing practice by a person (not being a trustee or administrative officer of the patriotic fund) who is a registered company auditor within the meaning of the Corporations Act; or a person or a member of a class of persons approved by the Director for the purposes of the audit of the statement of receipts and disbursements and balance sheet of the patriotic fund (s.42(6)).

The audit requirement for patriotic funds is subject to exemption by CAV. The Veterans (Patriotic Funds) Regulations specify that patriotic funds with annual receipts of less than $10,000 are exempted from the audit requirement.

Lodgements made by patriotic funds are required to be accompanied by a standard lodgement form. A sample of the lodgement form is shown in Figure 4 immediately below.

Figure 4: Sample Form Lodged in Victoria by Patriotic Funds

0955

SECTION 42 67753649-7472632

67753649-7472632

ANNUAL STATEMENT BY TRUSTEE/S

STATEMENT OF RECEIPTS AND DISBURSEMENTS

Year Ended 31 December 2010

Fund Name

Postal Address

CAV Reference Number

Historic Fund Number

Statement Due Date

RECEIVED
15 MAR 2011
CONSUMER AFFAIRS VICTORIA

RECEIPTS	Amounts $
Bank and investment interest received	
Fundraising activities	
Donations	
Transfers into fund approved by Director, CAV	
Other (please specify) #	
Total Receipts (A)	

DISBURSEMENTS	Amounts $
Welfare and relief payments	
Transfers out of fund approved by Director, CAV	
Admin. costs (stationery, postage, phone, bank fees and charges etc.)	
Fundraising costs	
Other (please specify) #	
Total Disbursements (B)	
Balance (A - B)	

Further details can be supplied on a separate attached schedule

BANK RECONCILIATION STATEMENT	Amounts $
Bank account balance at the start of the year	
Add total receipts	
Less total disbursements	
Less unpresented cheques and deposits not banked	
Bank account balance at end of year	

RECEIVED
ASSESSMENT TEAM
15 MAR 2011
CONSUMER AFFAIRS VICTORIA

Please remember to turn over, complete and then have this form signed where indicated.

7305061

Figure 4 cont.: Sample Form Lodged in Victoria by Patriotic Funds

BALANCE SHEET AS AT 31 DECEMBER 2010

ASSETS	Amounts $
Bank balance	
Investments (includes shares, debentures, term deposits etc)	
Loans to others	
Land value	
Building/s value	
Equipment, furnishings	
Other (specify) #	
Total Assets (C)	

LIABILITIES	Amounts $
Secured loans (outstanding balance)	
Unsecured loans (outstanding balance)	
Creditors	
Other (specify) #	
Total Liabilities (D)	
Fund Equity (C - D)	

Further details can be supplied on a separate attached schedule

OFFICER DECLARATION

I certify that the particulars contained in this annual statement and any accompanying schedules are true and correct, all items of receipts and disbursements appropriate to this fund have been included and disbursements made from the fund meet the objectives of the fund.

X

Signature of Trustee (or Treasurer of the incorporated association if that is the trustee of the fund)

Name of Trustee (or Treasurer)

Date

AUDITOR DECLARATION *(only if no certified copy of the audit report is attached)*

I have audited the books, vouchers, bank records and other records of the patriotic fund for the period covered by this annual statement and certify that in my opinion the books and records are kept in a satisfactory manner and that the above statements give a true and fair view of the funds' activities for the period and of its assets and liabilities at the end of the year.

X

Signature of Auditor

/ /

Date

Address of Auditor

Name of Auditor

Audit Qualification

How to lodge

Deliver in person to:

Victorian Consumer & Business Centre
113 Exhibition Street, Melbourne
Counter area (cnr Little Collins St) is open 8.30am - 5.00pm Monday to Friday (closed on public holidays)

Send by post to:

Consumer Affairs Victoria
GPO Box 4567, Melbourne VIC 3001
(please use a large envelope and fold this form as little as possible)

Privacy

CAV is committed to responsible and fair handling of your personal information, consistent with the laws we administer and the Information Privacy Act 2000. We may be unable to process this form if you do not provide the required information. You can contact us at any time to request access to the personal information we hold about you. In exceptional circumstances, you may apply to have public access to your personal information restricted. Our privacy statement, and other privacy information, is available at www.consumer.vic.gov.au or on request.

Consumer Affairs Victoria,
121 Exhibition Street, Melbourne
GPO Box 4567, Melbourne VIC 3001
Telephone: (03) 8684 6203

Victoria
The Place To Be

3.1.5 Other Categories of Entities Lodging with CAV – Victoria

Funeral Services: Where an entity trades as a funeral provider, the Funerals Act contains relevant requirements relating to ongoing financial management as well as dealings with clients. The Act is not explicit with respect to financial reporting or audit requirements, with such activities governed instead by the legislation applicable to the relevant category of entity.

For example, if the funeral service is also an incorporated association, the relevant accounting and audit requirements relating to incorporated associations apply.

Retirement Villages: Where an entity trades as a retirement village, its activities are governed primarily by the Retirement Villages Act. A retirement village must lodge at the AGM financial statements showing the source of income received and details of expenditure (s.34(3)). The financial statements must also be audited by a registered company auditor (within the meaning of the Corporations Act) (s.34(4)).[52] The Retirement Villages Act is not explicit with respect to the content of financial statements lodged with CAV. Since retirement villages in Victoria tend to operate as incorporated associations or companies, the financial reporting is generally governed by the relevant accounting and audit requirements applying to these categories of entities.

Gaming: The Gambling Regulation Act requires an operator to keep accounting records/information so as to explain the transactions and financial position of the operations of the operator to enable true and fair financial statements to be prepared from time to time (s.3.7.4). The Act also requires that an operator prepare a cash flow statement, profit and loss account and a balance sheet that give a true and fair view of the financial operations of the operator and that they should be 'conveniently and properly audited' (s.3.7.4).

3.2 Recent Legislative Amendments – Incorporated Associations – Victoria

In 2012, the regulation concerning incorporated associations was changed with the issuing of Associations Incorporation Reform Act.[53] That Act sets out a three-tier reporting framework for financial reporting. The tiers are defined based on the association's annual total revenue. There is no test based on the entity's assets. The tiers are defined as follows:

(a) Tier one: total revenue less than $250,000;

(b) Tier two: total revenue of $250,000 – $1 million; and

(c) Tier three: total revenue greater than $1 million (s.90).

The implications of the new framework are that:

(a) **Tier-one Associations** will continue to report to CAV on the same annual basis as previously applied to 'non-prescribed' associations in the Associations Incorporation Act;[54]

(b) **Tier-two Associations** must prepare financial statements in accordance with Australian Accounting Standards (s.95(2)(a)). Tier-two associations are required to have their accounts reviewed by a member of the accounting profession with a current audit practice certificate (CPAA, ICAA, IPA), or any other person approved by the Registrar (s.96(1)(a),(b)). The Act states that the 'review' should be conducted in accordance with auditing standards governing 'Review Engagements' (s.96(2)(a) and s.96(3)(a)); and

52 Alternatively, residents present at the annual meeting may decide by special resolution to dispense with the auditing requirement.

53 For further reading, see http://www.consumer.vic.gov.au/clubs-and-not-for-profits/incorporated-associations/running-an-incorporated-association – accessed April 2014.

54 There is no audit (review) requirement for tier-one associations unless it is requested by a majority vote of members at a general meeting or by the Registrar (s.93(1)(a),(b)).

(c) **Tier-three Associations** will continue to report to CAV consistent with requirements that previously applied to 'prescribed' associations in the Associations Incorporation Act. Tier-three associations must prepare financial statements in accordance with Australian Accounting Standards (s.98(2)(a)) and the statements must be audited by a member of the accounting profession with a current audit practice certificate (CPAA, ICAA, IPA).[55] The audit must be undertaken in accordance with Australian Auditing Standards (s.99(3)(a) and s.99(4)(a)).

3.3 Analysis of Reporting and Auditing Practices – Victorian Sample

CAV provided population data relating to 2008-2011. The most recent lodgement for the random sample of 400 not-for-profit entities reflecting the population proportions was obtained.[56]

Table 2: Victorian Data Sample

Type of Entity	Sample (n)	Sample Proportions (%)	Population Counts	Population Proportions (%)
Prescribed Associations	51	13	36,938[57]	92
Non-Prescribed Associations	307	77		
Co-operatives	6	2	707	2
Fundraisers	25	6	1,415	4
Patriotic Funds	11	2	613	2
TOTAL	**400**	**100**	**39,673**	**100**

Table 2 shows the random sample subject to analysis is consistent with the population proportions. Incorporated associations are the predominant organisational form lodging financial statements with CAV, the majority of which are non-prescribed associations. Population data on the split between 'prescribed' and 'non-prescribed' associations was not available when random sampling was conducted, however the proportion of associations in the sample (13% + 77% = 90%) approximates the population total proportion of 92 per cent. Each observation in the sample drawn relates to a unique entity with the data comprising lodgements over several years, i.e. 2011 (7%), 2010 (79%), 2009 (12%) and 2008 (2%).

55 The new Act allows any association to apply for an exemption from any or all of the reporting requirements for a particular year or longer.

56 Econometric sampling techniques were applied to achieve a 95 per cent confidence level that the resulting sample used to examine financial statements of entities lodging with state-based regulators is representative of the population proportions of entities (i.e., by entity type) provided by regulators. The sample may not be representative of the population across additional stratification criteria such as size of entity (e.g., total revenue, number of employees) and industry as lodgements are filed in PDF and thus could not be organised and searched by additional stratification criteria.

57 Comprises incorporated associations, retirement villages, funeral services and limited partnerships from Table 1 above.

Table 3: Descriptive Financial Data – Victoria

TYPE OF ENTITY	TOTAL ASSETS Mean (Median) [SD]*	LIABILITIES Mean (Median) [SD]*	REVENUE Mean (Median) [SD]*	PROFIT (LOSS) Mean (Median) [SD]*
Prescribed Associations	4,569,480 (765,929) [17,827,284]	1,613,517 (77,835) [7,716,916]	1,989,474 (377,370) [4,689,920]	160,892 (19,608) [613,467]
Non-Prescribed Associations	56,892 (29,430) [81,553]	6,279 (0) [19,747]	41,542 (21,405) [47,625]	1,917 (660) [8,870]
Co-operatives	208,595 (198,881) [211,074]	50,978 (10,557) [76,928]	120,245 (9,365) [195,090]	-2,016 (50) [41,055]
Fundraisers	4,466,529 (536,924) [10,182,226]	1,938,919 (53,234) [4,899,430]	4,793,235 (443,526) [12,517,744]	250,543 (29,000) [542,586]
Patriotic Funds	1,037,878 (41,391) [2,157,321]	81,505 (0) [175,274]	42,026 (24,989) [45,449]	-3,914 (-611) [16,845]

* [SD] refers to standard deviation.

Table 3 presents descriptive financial information. It should be noted that a large proportion (approximately 32%) of non-prescribed associations did not lodge a balance sheet, and this is discussed in more detail in later Sections of this Part of this Report (see also Table 7). Accordingly, data in Table 3, which summarises assets, liabilities, revenue and profit/loss, is only from entities disclosing financial data and as such it may not be generalisable to the population of non-prescribed associations. Prescribed associations are significantly larger than non-prescribed associations, co-operatives and patriotic funds across all dimensions, but are closer in size measured by total assets to fundraisers (see Table 3).

Table 4: Use of Templates versus Stand-alone Financial Statements by Entity Group – Victoria

Type of Entity	Templates		Financial Statements		Both Template and Financial Statements		Missing Data	Total	
	n	(%)	n	(%)	n	(%)		n	(%)
Prescribed Associations	-	(0)	51	(100)	-	(0)		51	(100)
Non-Prescribed Associations	78	(26)	210	(70)	17	(4)		305	(100)
Co-operatives	1	(17)	2	(33)	3	(50)		6	(100)
Fundraisers	-	(0)	23	(100)	-	(0)		23	(100)
Patriotic Funds	9	(82)	1	(9)	1	(9)		11	(100)
Missing Data							4	4	
TOTAL	**88**	**(22)**	**287**	**(72)**	**21**	**(6)**	**4**	**400**	**(100)**

Results presented in Table 4 indicate that the majority of entities (72%) lodged separate financial statements rather than use the template where it is provided by CAV. Prescribed associations are not given the option to complete a template and must lodge audited financial statements. However, the lodgement form provides a choice for non-prescribed associations to complete a template or lodge financial statements. A majority (70%) of non-prescribed associations in the sample chose to lodge separate financial statements rather than complete the CAV template.[58] All fundraisers and a majority of co-operatives lodged financial

58 In Section 3.4 'Additional Anecdotal Evidence …' below, further discussion is provided as to why non-prescribed associations tend not to complete the standardised financial statements template provided as part of the lodgement form.

statements, while most patriotic funds lodged financial data on the template contained within the annual lodgement form.

Table 5: Type of Financial Statements Lodged – Victoria

Type of Entity	GPFSs %	SPFSs %	No clear statement %	Total %
Prescribed Associations	17	60	23	100
Non-Prescribed Associations	0	9	91	100
Co-operatives	0	50	50	100
Fundraisers	30	35	35	100
Patriotic Funds	0	18	82	100

Table 5 shows the type of financial statements lodged for each category of entity. Specifically, the Table shows whether entities lodged GPFSs or SPFSs, or whether the type of financial statements was not clearly stated. Approximately 17 per cent of prescribed associations stated they lodged GPFSs. While the majority of prescribed associations (60%) stated they lodged SPFSs, for around 23 per cent of prescribed associations there was no explicit indication as to whether the statements were general purpose or special purpose. In each instance, the financial statements for this 23 per cent of prescribed associations were clearly SPFSs. Only nine per cent of non-prescribed associations stated they had lodged SPFSs and for the remaining 91 per cent of non-prescribed associations, there was no explicit disclosure as to the type of financial statements. On each occasion of no clear disclosure of type of statements, the statements appeared to be special purpose. For co-operatives and patriotic funds, similar to non-prescribed associations, all financial statements appear to be special purpose, although a majority of those types of entities did not explicitly disclose they lodged SPFSs. For fundraisers, 30 per cent lodged GPFSs, while around 35 per cent of entities from this group did not clearly disclose the nature of the financial statements lodged.

Table 6: Disclosed Application of Accounting Standards – Victoria

Type of Entity	Disclosed application of accounting standards %
Prescribed Associations	55
Non-Prescribed Associations	5
Co-operatives	33
Fundraisers	48
Patriotic Funds	9

Results presented in Table 6 show the proportion of entities that disclosed in their financial statements, regardless of type of financial statements (i.e., GPFSs or SPFSs), whether they had applied accounting standards. This disclosure is conventionally made in the significant accounting policies note to the financial statements. It is noteworthy that this analysis does not indicate the extent to which specific accounting standards were applied nor does it evaluate the accounting policies adopted by entities. Rather, Table 6 simply identifies whether an entity made any reference to applying accounting standards in its financial statements.

Around 55 per cent of prescribed associations and approximately 48 per cent of fundraisers made reference to applying accounting standards in the notes to their financial statements.

Any non-prescribed association, co-operative or patriotic fund that completed only the template in the form supplied by CAV is coded as not disclosing application of accounting standards since there is no provision in the template for entities to disclose such application. However, the majority of entities lodging with CAV submitted ‘stand-alone’ financial statements (see Table 4). Notwithstanding this limitation with interpreting these results, a substantial majority of non-prescribed associations, co-operatives and patriotic funds did not make reference to the accounting standards. Since it is possible that some entities may be following accounting standards without stating as such in their financial statements, it is not feasible to determine the influence of Australian Accounting Standards in the preparation of financial statements among these entities.

For prescribed associations, the lodgement form provided by CAV (refer Figure 1 above) requires that financial statements be prepared in accordance with a list of accounting standards that are specified on the form (e.g., AASB 1018 *Statement of Financial Performance*, AAS 36 *Statement of Financial Position*). Despite this, and given that all prescribed associations in the sample lodged stand-alone financial statements, only 55% disclosed the application of accounting standards. It may be that these entities are applying relevant accounting standards and not disclosing this in their financial statements. Alternatively, it is also possible that some or all of these entities are not complying with CAV lodgement requirements regarding financial reporting.

Table 7: Primary Indicators of the Level of Financial Reporting Transparency – Victoria

Type of Entity	Balance Sheet %	Income Statement %	Statement of Cash Flows %	Notes %	Financial Statements Audited %
Prescribed Associations	100	98	81	81	100
Non-Prescribed Associations	68	98	3	11	37
Co-operatives	100	100	67	83	100
Fundraisers	74	100	48	70	75
Patriotic Funds	100	91	9	18	64

An analysis of primary indicators of the level of reporting transparency in the financial statements is examined next. Results presented in Table 7 show the proportion of entities that lodged a Balance Sheet, Income Statement (either a Statement of Comprehensive Income or a simple Income Statement), Statement of Cash Flows, Notes to Financial Statements, and a signed audit report. By documenting the total information lodged by different categories of entity, it is possible to develop a broad sense of the transparency of the financial reporting of the entities in the sample.

The income statement is the most commonly lodged item and is almost always lodged with CAV. The balance sheet is lodged by all prescribed associations, co-operatives and patriotic funds but is less commonly lodged among non-prescribed associations (68%) and fundraisers (74%). Under the Associations Incorporation Act, non-prescribed associations are required to lodge a statement showing income and expenditure, and assets and liabilities (s.30(4)(a)). However, 32 per cent of non-prescribed associations do not lodge a balance sheet. Similarly, fundraisers are required to lodge financial statements but 26 per cent did not lodge a balance sheet.

Approximately 19 per cent of prescribed associations did not lodge a statement of cash flows or notes to the financial statements, despite CAV making specific reference in the lodgement form to the accounting standards relating to statement of cash flows and notes to the financial statements. The vast majority of non-prescribed associations and patriotic funds did not lodge a statement of cash flows (97% and 91%, respectively) or notes to the financial statements (89% and 82%, respectively).

All financial statements lodged by prescribed associations and co-operatives were audited, consistent with legislative requirements. While non-prescribed associations are not required by the Associations Incorporation Act to engage an auditor, around 37 per cent of non-prescribed associations appear to have voluntarily engaged an auditor. CAV can direct patriotic funds and fundraisers to be audited and the results in Table 7 indicate that the majority were audited.

Table 8: Proxy Measure of the Indicators of the Level of Financial Reporting Transparency – Victoria

Type of Entity (5 point scale)	Mean	Median	SD*	Min	Max
Prescribed Associations	4.66	5	0.60	3	5
Non-Prescribed Associations	2.16	2	0.86	1	5
Co-operatives	4.50	5	0.84	3	5
Fundraisers	3.65	4	1.47	1	5
Patriotic Funds	2.80	3	1.08	1	5

* SD refers to standard deviation.

To provide an overall sense of the level of reporting by entities, the five primary indicators of financial reporting transparency summarised in Table 7 were combined into a single measure. Each of the five indicators was equally weighted and assigned a value of 0 or 1, which can add to a maximum financial reporting transparency score of 5. For example, if the entity lodged a balance sheet, an income statement and statement of cash flows, included one or more notes, and the financial statements were audited, the entity would receive a score of 5. Data summarising the proxy measure of the level of financial reporting is presented by type of entity in Table 8. The proxy measure for financial reporting transparency is highest for prescribed associations and co-operatives with scores well above the mean (2.5). The reporting by fundraisers (3.65) is also above the mean of 2.5, while non-prescribed associations and patriotic funds displayed relatively lower financial reporting transparency as evidenced by mean scores of 2.16 and 2.8 respectively.

Table 9: Further Indicators of the Level of Reporting Transparency by Prescribed Associations – Victoria

	Line Item Comprehensive Income %	Statement of Changes in Equity %	Movements in PPE reconciled %	Non-Current Provisions %	Reserves Disclosed %	Signed Directors' Report %
Prescribed Associations	19	23	27	40	33	25

Based on the sample of prescribed associations only, a more sophisticated measure of financial reporting transparency was also developed. In addition to the basic financial statement items disclosed in Table 7 (i.e., a Balance Sheet, Income Statement, Statement of Cash Flows, Notes, and Audit Report), six additional items were identified and coded to develop an enhanced understanding of financial reporting transparency. These items are (1) reporting of the line item comprehensive income; (2) a separate statement of changes in equity; (3) property plant and equipment (PPE) > 0 and the movements in PPE over the year reconciled; (4) reporting of non-current provisions; (5) reporting of any reserves; (6) a report signed by directors (or their equivalent).[59] This measure is adapted from the measures of financial disclosure in Van Overfelt et al. (2010). In each case, the items identified arguably provide an indication of the sophistication of the information systems and reporting practices of entities.

Results presented in Table 9 indicate a low level of reporting of the items involved – significantly below the level that would typically be expected to be reported by entities lodging GPFSs. Given the disparate nature of the entities in this group it is difficult to generalise this finding. It is noteworthy that the number of members reported by the entities in the sample of prescribed associations ranges from a minimum of 6 to a maximum of 230,691 (mean 4,794; median 107). The level of members for many of these entities is arguably high enough to suggest the existence of users who would rely on the content of the financial statements for information about the entities involved and that, therefore, GPFSs should be prepared.

Table 10: Reporting of Notes to the Financial Statements by Prescribed Associations – Victoria

Notes to the Accounts	Entities %	Mean	Median	SD*	Min	Max
		7.52	6.5	6.99	0	26
No notes reported	19					
1 Note	17					
2 Notes	4					
3 Notes	4					
4 Notes	-					
5 Notes	4					
6 Notes	2					
7 Notes	2					
8 Notes	2					
9 Notes	8					
10 Notes	-					
11 Notes	2					
12 Notes	6					
13 Notes	4					
14 Notes	8					
15 Notes	4					
16 Notes	2					
17 Notes	2					
18 Notes	4					
19 Notes	4					
20+ Notes	2					
TOTAL	**100**					

* SD refers to standard deviation.

For the sample of prescribed associations only, Table 10 presents data on the reporting by entities of notes to the financial statements. As previously indicated, 81 per cent of prescribed associations included notes to their financial statements (see Table 7). As is evident from Table 10, 50 per cent of prescribed associations reported six notes or fewer (or none) and there is considerable variation in the number of notes disclosed by entities in the sample. In interpreting the information provided in Table 10, it is noteworthy that 89 per cent of non-prescribed associations did not disclose notes (Table 7). Similarly, less than one per cent of

59 This measure was applied to prescribed associations only since it is this category of entity that is most likely to report any or all of the information required.

non-prescribed associations disclosed any of the items (i.e., comprehensive income, changes in equity, movements in property, plant and equipment, etc.) identified in Table 9 – highlighting, at least to some extent, the great variation in reporting across the sample of associations.

Table 11: Reporting of Property, Plant and Equipment and Adoption of Accrual Accounting – Victoria

Type of Entity	Accrual Accounting %	Property, Plant & Equipment Disclosed %
Prescribed Associations	92	85
Non-Prescribed Associations	31	45
Co-operatives	67	50
Fundraisers	83	65
Patriotic Funds	42	46

Table 11 presents results related to two further indicators of financial reporting transparency developed for this Part of this Report. First, lodgements were examined for evidence that accrual accounting was applied (as opposed to cash accounting), which is widely assumed to lead to a superior measure of periodic performance and period-end financial position (Dechow et al., 1998; Neill et al., 1991). It was concluded that an entity had applied accrual accounting if items such as debtors, creditors or depreciation were identified in the financial statements. The purpose of doing so was not to determine whether the entity was adopting Australian Accounting Standards, but rather to assist in enhancing understanding of the extent of adoption of accrual accounting principles. Second, the disclosures made by each entity were reviewed to determine if the entity disclosed dollar values for property, plant and equipment on the assumption that asset disclosure represents decision-useful information and is indicative of greater financial reporting transparency (Dechow et al., 1998; Neill et al., 1991). It should be noted that property, plant and equipment was identified only in entities that lodged a balance sheet. Where an entity did not lodge a balance sheet (i.e., 32% of non-prescribed associations – Table 7), the observation was coded as missing and, consequently excluded. Results therefore reflect the extent of measurement of property, plant and equipment by entities that lodged a balance sheet.

Results presented in Table 11 indicate that, while most prescribed associations lodge accrual-based financial statements (92%), the majority of non-prescribed associations report on a cash basis (i.e., 69%).

Accrual accounting is adopted more commonly than cash accounting by co-operatives and fundraisers, but is less common in patriotic funds with only 42 per cent of entities adopting accrual accounting. For entities that lodge a balance sheet, a low proportion disclose property, plant and equipment. Many entities in the sample would be expected to own/control property, plant and equipment, but a substantial proportion did not disclose this in their balance sheet. In particular, 55 per cent of non-prescribed associations that lodged a balance sheet did not disclose property, plant and equipment. There are similarly higher proportions among co-operatives (50%) and patriotic funds (54%). It is noteworthy that 15 per cent of prescribed associations do not recognise property, plant and equipment, suggesting that further work is needed to fully understand the level of transparency of the financial reporting by these entities.

Table 12: Modified Audit Opinions – Victoria

Type of Entity	Financial Statements Audited %	Modified Audit Opinions %
Prescribed Associations	100	27
Non-Prescribed Associations	37	23
Co-operatives	100	-
Fundraisers	75	13
Patriotic Funds	64	14

Results in Table 12 summarise the audit opinions issued for Victorian entities. The results indicate that 27 per cent of prescribed associations receiving an audit report received a modified opinion and 23 per cent of non-prescribed associations similarly received a modified opinion. A review of the audit reports of associations indicates that the major sources of modification were ‘except for’ or ‘subject to’ opinions due to a scope limitation – most often because of not being able to substantiate whether there was effective internal control over physical cash receipts. The modification rates for fundraisers and patriotic funds were slightly lower at 13 per cent and 14 per cent, respectively. It is noteworthy that the proportion of opinion modification for these Victoria state-based entities differs from the average modification rate of 19 per cent reported among listed public companies in Australia for the period 2005-2009 (Xu et al., 2013; Xu et al., 2011). In contrast to the results for associations lodging in Victoria, most modifications to audit opinions for listed public companies are due to ‘emphasis of matter’ concerns.

Table 13: Auditors’ Professional Affiliation – Victoria

Type of Entity	Big 4 %	CA %	CPA %	IPA %	Other %
Prescribed Associations	2	45	25	-	28
Non-Prescribed Associations	-	13	36	1	50
Co-operatives	-	50	17	-	33
Fundraisers	19	56	13	-	12
Patriotic Funds	-	57	43	-	-

Results presented in Table 13 demonstrate that Chartered Accountants are the most common professional designation of auditors for Victorian entities, followed closely by CPAs. For non-prescribed associations, a majority of audits are conducted by individuals who have neither a CA nor CPA affiliation. These auditors are typically members, or connected to members, of the organisation who have some level of financial expertise and undertake the audit on a voluntary basis. This is allowed under the Associations Incorporation Act (s.30B(1)(d)).

3.4 Additional Anecdotal Evidence Concerning Financial Reporting Practices of Associations, Co-operatives and Fundraisers – Victoria

To augment the analyses of entities in Sections 3.1 to 3.3 above, this Section provides anecdotes to assist with understanding the diversity in financial reporting practices of entities lodging in Victoria.

3.4.1 Lodgement of a Statement of Receipts and Payments – Victoria

Approximately one third of non-prescribed associations lodged only a Statement of Receipts and Payments.

When a non-prescribed association lodges a 'Statement of Receipts and Payments' it is typically in the following format:

(a) Opening account balance;

(b) Receipts during the reporting period;

(c) Payments during the reporting period;

(d) Closing account balance; and

(e) Reconciliation of movements in account (bank) balance during the reporting period.

The receipts and payments reported by entities are often stated in aggregate, making it difficult to identify further detail regarding receipts and payments. When entities lodge only a Statement of Receipts and Payments, key information such as debtors, inventory, creditors and assets is not reported.

An entity can choose to lodge standardised financial information in the CAV template (Form 0410 – see Figure 2 above) or attach separate/stand-alone financial statements. Most of the stand-alone financial statements are brief (limited to Statements of Receipts and Payments) and these statements disclose less information than could potentially be provided in Form 0410.

3.4.2 Not Lodging a Balance Sheet – Victoria

As previously discussed (see Table 11), for the 68 per cent of non-prescribed associations that lodge a balance sheet, 55 per cent of them do not disclose property, plant and equipment in their balance sheet. Non-prescribed associations can (in Form 0410 – see Figure 2 above) provide the information that resembles the information typically found in a standard balance sheet (i.e., Total Assets [cash; stock; debtors; property, plant and equipment; investments; other], Total Liabilities [secured loans; unsecured loans; other], and Equity).

Non-prescribed associations that did not lodge a balance sheet commonly lodged a Statement of Receipts and Payments (in the format described in Section 3.4.1 immediately above). This limited form of reporting may be a consequence of resource constraints faced by entities. Alternatively, it is difficult to determine the extent to which such practices result from entities seeking to avoid any additional reporting burden resulting from being classified as a prescribed association; since classification was, at the time the data was collected, based on the assets of the entity.

Consideration could be given to requiring entities to complete all fields in the standard template (Form 0410 – Figure 2 above). This would help ensure more complete reporting of balance sheet items and thus enhance the quantity and transparency of the information lodged by entities.

As outlined earlier (Section 3.2 of this Part of this Report), recent reform to regulations for associations as set out in the Associations Incorporation Reform Act, uses revenue as the sole basis for classifying entities for reporting and lodgement purposes. Whereas previously the classification was prescribed/non-prescribed, the reforms introduce a three-tier system.

3.4.3 Significant Variation in Financial Reporting by Non-Prescribed Associations – Victoria

Arguably, due to the absence of definitive reporting requirements in the Associations Incorporation Act for non-prescribed associations, there was significant variation in the financial reporting by entities. Quantitative results presented in Table 4 above show that 74 per cent of non-prescribed associations did not complete the template and instead attached financial statements. There is no systematic pattern to the presentation of these attached statements. The variation is consistent with other findings reported, including the findings that 32 per cent of non-prescribed associations did not lodge a balance sheet and 11 per cent of non-prescribed associations disclosed notes to the financial statements (Table 7).

Other noteworthy issues were that many statements contained calculative errors. There were multiple examples of incomplete financial statements (e.g., financial statements disclosing income and expenditure figures, but no profit or loss/result; some financial statements disclosing total assets, although not disclosing either liabilities or equity).

A number of lodgements that included a balance sheet contained only current assets and current liabilities. There is evidence that reporting of non-current assets and liabilities was incomplete. For example, in one lodgement the auditor noted: "Please note that an asset register, cost of buildings/equipment and depreciation are not included in these reports." On occasion, income statements were incorrectly labelled as balance sheets. There are numerous examples of hand-written financial statements. Further variation in the financial statements disclosures is evidenced by the number of line items for revenue and expenses disclosed in the income statement. While the income statements in some lodgements contained few lines, one income statement was sighted that contained more than 80 line items.

3.4.4 Classification as Non-Prescribed Association – Victoria

Some variation was noted in the classification of entities as non-prescribed associations. Several financial statements were noted where entities self-classified as non-prescribed that perhaps should have been classified as prescribed associations.

3.4.5 Prescribed Associations – Victoria

Quantitative results above highlight the significant variation in reporting practices of prescribed associations. Results in Table 5 above reveal 17 per cent of prescribed associations lodged GPFSs, 60 per cent lodged SPFSs and 23 per cent did not clearly state the type of financial statements they lodged. Results in Table 9 show the considerable variation in the level of financial reporting. The variation in reporting is further highlighted by results in Table 10, which show significant variation in the number of notes to the financial statements.

3.4.6 Fundraisers – Victoria

Fundraisers seem to favour providing information via the standard CAV lodgement template. In the financial statements lodged by these entities, there is also considerable variation in the volume and quality of financial reporting.

4. New South Wales Entities

Table 14 below shows the New South Wales entity groups and their respective population number as of 2010 and the relevant reporting legislation.

Table 14: NSW Data

NSW Entity Group	Population n	Population %	Relevant reporting authority
Incorporated Associations	34,273	98.18	*Associations Incorporation Act 2009*
Co-operatives	637	1.82	*Associations Incorporation Regulation 2010*
			Charitable Fundraising Act 1991
			Co-operatives Act 1992
			Travel Agents Act 1987
Total	**34,910**	**100.00**	

The sample used for analysis in this Section of the Report was drawn randomly from a list of 19,413 incorporated associations that NSW Fair Trading has identified as being representative of the total population of NSW incorporated associations of 34,273 as at 30 June 2010.

4.1 Reporting and Auditing Regulation – NSW

4.1.1 Incorporated Associations – NSW

Incorporated Associations are generally small non-commercial community groups that are given a formal legal structure by way of their incorporation under the Associations Incorporation Act. Incorporated associations can be identified by the word 'Incorporated' or the abbreviation 'Inc.' in the entity name. Typical examples of incorporated associations include sporting groups, arts and crafts groups, and musical societies.

Relevant authority: The financial reporting requirements for incorporated associations in NSW for the period covered by Part B of this Report are primarily found in the Associations Incorporation Act.[60] NSW Fair Trading administers and enforces the Associations Incorporation Act.

Classes of entity for reporting: The Associations Incorporation Act establishes differential content of financial statements based on a two-tier system. This is explained further below:

(a) ***Tier-one*** Associations are those for which total revenue as recorded in the income and expenditure statement for a financial year exceeds $250,000 (excluding GST) or current assets (defined as assets other than real property and capable of depreciation) exceed $500,000 (these thresholds are set out in clause 7(3) of the Associations Incorporation Regulation);[61] and

60 The Associations Incorporation Act was subject to minor amendment in 2010.

61 'Gross receipts' are defined as total revenue recorded in the income and expenditure statement for the year, and 'current assets' are considered to include all assets other than real property or assets capable of depreciation. As a consequence, it appears that both 'gross receipts' and 'current assets' are defined in a manner different from recent amendments to the Corporations Act for companies limited by guarantee (KPMG, 2010) and also with recent amendments to the Victorian Incorporated Associations Act. The definition of current assets particularly includes some assets that may not be considered current assets under Australian Accounting Standards.

(b) ***Tier-two*** Associations are those whose total revenue and current assets do not satisfy either of the above tests.

Reporting requirements: The reporting requirements set out above are described in Part 5 of the Associations Incorporation Act.

Tier-one associations

According to Section 45 of the Act, within one month of the AGM, tier-one associations must lodge the following documents with the Director-General of NSW Fair Trading:

(a) an annual summary of financial affairs (Form A12) for the financial year;

(b) the financial statements for the financial year, presented at the AGM; and

(c) the auditor's report for the statements.

The Associations Incorporation Act requires tier-one associations to prepare financial statements in accordance with Australian Accounting Standards (s.43(2)) and these financial statements must be audited (s.43(1)(b)). The auditor's report must be prepared in accordance with the Australian Auditing Standards and state whether the association has kept the necessary financial records to enable financial statements to be prepared in accordance with Australian Accounting Standards (s.43(3)).

With the enactment in May 2011 of Class Order 11/01 by the NSW Department of Fair Trading, tier-one associations whose revenue is less than $2 million are relieved from full financial reporting under section 43(2). Associations in this group have the option of lesser requirements, including lodgement of an appropriately classified statement of income and expenditure and balance sheet; a statement of movements in equity and a statement of accounting policies. These entities need not lodge a statement of cash flows, but are required to apply AASB 1048 *Interpretation of Standards* and AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*. These entities are required to apply R&M and, where appropriate, prepare consolidated financial statements in accordance with AASB 127 *Consolidated and Separate Financial Statements*. The Class Order is operative for financial years ending on or after 30 June 2010.[62]

Section 52 of the Associations Incorporation Act sets out the audit provisions relating to the audit of the financial statements of tier-one associations. The implications are that audits may be carried out by any of the following: a registered company auditor; or a member who holds a public practice certificate of the ICAA, CPAA or IPA. Unless approved by the Director-General in writing, an audit may not be carried out by any person who, within the last 2 years, has been:

(a) a member of the association;

(b) an employee or provider of professional services to the association, a committee member or its public officer.[63]

62 For further reading, refer Reporting update: 11RU-001 *NSW Associations Incorporation Act 1984 Amendments*, KPMG, 2011.

63 It is noteworthy that Class Order 10/01 (issued in 2010) states that an auditor need not be a registered company auditor provided that they are a member of ICAA, CPAA, or IPA. Class Order 10/02 (issued in 2010) exempts auditors from the independence requirements of section 52(2) provided the audit is carried

The Director-General may exempt an association from an audit (s.53).

Tier-two associations

The financial reporting requirements for tier-two associations are defined in section 47 of the Act and are less onerous than those applying to tier-one associations. Specifically, tier-two associations must ensure the financial statements for the association are prepared as soon as possible after the association's financial year end.

According to the Act, the financial statements must give a true and fair view of the association's affairs (s.47) and must include:

(a) an income and expenditure statement that sets out detailed income and expenses;

(b) a balance sheet that sets out assets and liabilities;

(c) details of any mortgages, charges and other securities affecting any property owned by the association; and

(d) a separate income and expenditure statement and balance sheet for each trust for which the association is the trustee (s.9 of the Associations Incorporation Regulation).

There is no explicit requirement that the financial statements of tier-two associations are prepared in accordance with Australian Accounting Standards, nor that they are subject to audit. Where associations are also involved with fundraising, an audit is required under section 24 of the Charitable Fundraising Act.

Incorporated associations lodging financial statements with NSW Fair Trading are also required to complete a standard Form A12 as part of their lodgement (see sample in Figure 5 immediately below).

out in accordance with the code of conduct relating to independence in APES 110 *Code of Ethics for Professional Accountants* and the auditor's report includes an auditor's independence declaration.

Figure 5: Sample Form Lodged by NSW Incorporated Associations

NSW GOVERNMENT Fair Trading
ABN 81 913 830 179

Form A12

Office use only
AFFIX DOCUMENT BARCODE LABEL HERE
v. 01a/2013

Received at:
Date:
Receipt no.:

Annual summary of financial affairs
Associations Incorporation Act 2009
(sections 45 & 49)

Please read the information provided before completing this form.
This form should be completed in BLACK or BLUE ink and in BLOCK LETTERS.

Fee must accompany form
See information sheet

Association details

Incorporation number INC / Y

Name Incorporated

The principal activity of the association is [X] *(cross 1 box only)*

1. Aged care/respite care/home care	5. Education/employment/training/research	9. Religious
2. Arts/culture/literary/heritage	6. Environment/horticulture/animal protection	10. Social services/community association
3. Business & professional association	7. Legal/civic/advocacy services	11. Sporting
4. Child care services	8. Personal interest/hobby group/social group	12. Other

ABN (if any)

Details of current public officer

Name

Has the public officer changed? Yes No

Has the official address changed? Yes No

If you answered 'Yes' to either or both questions, you are required to lodge a Form A9, 'Notice of appointment of public officer & Notice of change of association address'.

Financial summary

The association's financial year ended on: / / (DD MM YYYY)

The annual general meeting was held on: / /

Details of income, expenditure, assets & liabilities of the association & of any trust to which the association is a trustee	Association	Trust
Gross receipts*/total income	$	$
Expenditure	$	$
Current assets*	$	$
Total assets (includes current assets)	$	$
Liabilities	$	$

***See attached notes for the definition of gross receipts/total income and current assets.** **Amounts must be entered above.**

Were the accounts audited? Yes No

Number of members at end of financial year

Number of employees at end of financial year

Contact details of the person lodging this document **PLEASE TURN OVER**

Surname

Given name (s)

Title (Mr/Mrs/Ms)

Daytime telephone

Address

Town/suburb

State

Postcode

Email

FORM BM3AC

Figure 5 cont.: Sample Form Lodged by NSW Incorporated Associations

Particulars of mortages, charges and other securities affecting the property of the incorporated association

State if mortgage, charge or other security	Property affected	Amount of indebtedness at financial year end	Name and address of holder of security, etc

Are details of other mortages, charges or securities attached? ☐ Yes ☐ No

Grant funding and fundraising *(this section is optional)*

Please indicate the total grant funding received by the association from all Commonwealth, State or local government agencies during the financial year

TOTAL GRANT FUNDING
$

Please indicate which agency/ies provided the funding by placing a ' X ' in the box/es below

☐ 1. Arts NSW	☐ 5. Department of Education & Training	☐ 9. Local Council
☐ 2. Dept of Ageing, Disability & Home Care	☐ 6. Department of Planning - Heritage Office	☐ 10. Other
☐ 3. Department of Community Services	☐ 7. NSW Sport & Recreation	
☐ 4. Department of Education, Employment & Workplace Relations	☐ 8. Department of Families, Housing, Community Services & Indigenous Affairs	

If the association is registered as a charity under the *Charitable Fundraising Act 1991* please provide charitable registration number

The following information is optional and is used for statistical purposes only

Is the association specifically established for the benefit of *(tick one or more)*

☐ Aboriginal and Torres Strait Islanders
☐ People with a disability
☐ People from cultural and linguistically diverse backgrounds
☐ Women

Tier 1 associations only *(tick boxes and ensure the documents are attached)*

☐ The association's financial statements for the relevant financial year (including a separate income and expenditure statement and balance sheet for each trust for which for which the association is trustee).

☐ The auditor's report for those financial statements.

☐ If a resolution was passed at the annual general meeting in connection with the above documents, tick box and attach a copy of the resolution.

Declaration as to the financial affairs of the association and privacy acknowledgement

I declare that

- I am authorised by the committee to make the following statements,
  - the association's financial statements for the last financial year were presented to the members of the association at the annual general meeting,
  - the particulars set out in this document are correct and give a true and fair view of the financial matters to which they relate and are not misleading, and
  - there are reasonable grounds to believe, at the date of this statement that the association will be able to pay its debts as and when they fall due, and

I acknowledge that

- NSW Fair Trading is collecting and holding information (including personal information) supplied in this form for the purposes of the *Associations Incorporation Act 2009* and in particular, inclusion in a register maintained under that Act which is open to public inspection,
- NSW Fair Trading may disclose personal information to persons or bodies and to receive information from them in respect of purpose(s) related to the association's incorporation and activities, and
- I have a right to seek access to and correction of the personal information supplied/collected from me.

Signature

Date / /
DD MM YYYY

Full name

Address

Town/suburb

State

Postcode

4.1.2 Co-operatives – NSW

Co-operatives are people-centred organisations that are owned, controlled and used by their members. A co-operative's main purpose is to benefit its members.[64] Co-operatives are usually formed because members perceive benefits to be gained through combined purchasing, distribution or marketing power or influence of the group. Examples of co-operatives in NSW include entities providing social housing and sports and community clubs.

Relevant authority: Co-operatives in NSW are administered under the Corporations Act and the Co-operatives Act.[65] NSW Fair Trading administers and enforces the Co-operatives Act.

Reporting requirements: By virtue of section 243 of the Co-operatives Act, the financial reporting and audit for co-operatives is governed by Part 2M of the Corporations Act. As a consequence, the financial reporting obligations of co-operatives are consistent with those of companies incorporated under the Corporations Act.

It is noteworthy that reporting relief is available for 'small' co-operatives that satisfy the following conditions:

(a) assets do not exceed $700,000;[66] and

(b) expenses, including costs of goods sold, do not exceed $300,000.

Reporting relief includes exemption from preparing a statement of cash flows (Co-operative Circular 2008/1, Attachment 1, NSW Fair Trading 2008). Also, co-operatives with revenue of less than $250,000 may elect to have their financial statements 'reviewed' instead of 'audited' (Co-operative Circular 2011/1, NSW Fair Trading 2011).

Co-operatives lodging financial statements with NSW Fair Trading are also required to complete a standard Form 1 as part of their lodgement (a sample form is shown in Figure 6 immediately below).

64 http://www.fairtrading.nsw.gov.au/ftw/Cooperatives_and_associations/About_cooperatives.page? – accessed April 2014

65 Legislative reform for NSW co-operatives was recently introduced through the *Co-operatives (Adoption of National Law) Act 2012*; resulting in the reporting requirements for small co-operatives being reduced.

66 There is some apparent discrepancy in the guidance. The Fact Sheet *Co-operatives financial reporting requirements* (January 2013) on the NSW Fair Trading website states that assets not exceed $700,000, but Co-operative Circular 2008/1, Attachment 1, states that relief is available for entities whose assets do not exceed $750,000.

Figure 6: Sample Form Lodged by NSW Co-operatives

Form 1 **Annual report** GST FREE - ABN 81 913 830 179

PART A (Clause 17)

Co-operatives Act 1992
(Sec. 252(1)(e))

CO-OPERATIVE NAME:

A.R.B.N. (if applicable): TELEPHONE:

ADDRESS OF REGISTERED OFFICE:

CO-OPERATIVE NO:

Signature of Director, Secretary or Principal Executive Officer Date

Financial Year Ended 31/12/2009		Last Year 31/12/2008	
ANZSIC	%	ANZSIC	%

Financial Year Ended 31/12/2009		Last Year 31/12/2008	
LGA	%	LGA	%

		Financial Year Ended 31/12/2009	Last Year 31/12/2008
NUMBER OF DIRECTORS:	Active Member Directors		
	Employee Directors		
	Other independent Directors		
EXPORTS:	Value of Exports		
	% of Total Sales		

Total Turnover (including ancillary income)		
Cost of Goods Sold		
Total Interest Paid or Provided		
Number of Members		
Number of Employees		
Does the Co-operative have an exemption from any of the provisions of Clause 13 of the Co-operatives Regulation 2005. If yes, please specify details.	Yes/No	

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Figure 6 cont.: Sample Form Lodged by NSW Co-operatives

CO-OPERATIVE NAME:

FINANCIAL YEAR ENDED:

ANNUAL REPORT - MOVEMENT - SHARE VALUES (WHOLE DOLLARS)

	SHARES					
Section of Act		Section 151	Sections 151(4)(a), 156 & 282(1)(b)	Section 154	Section 155	
Narration	Shares $	Issue of shares at a premium $	Bonus shares issue $	Issue of shares to active members in exchange for property $	Members may be required to take additional shares $	Total $
BALANCE AT BEGINNING OF YEAR						
Additions						
Transfers In						
Sub-total						
					Forfeiture	
					Re-purchase non-active	
					Repurchase Active	
					Transfers Out	
					Sub-total Out	
			This figure must agree with the Total Share Capital in the Balance Sheet		**BALANCE END OF YEAR**	

ANNUAL REPORT - MOVEMENT - LOANS & CCUs (WHOLE DOLLARS)

	DEPOSITS & DEBENTURES			LOANS	CCUs	
Section of Act	Section 263A	Section 266	Section 266A	Section 268	Part 10 Division 2	
Narration	Deposits $	Debentures $	Debentures $	Loans $	CCUs to members $	CCUs to non members $
BALANCE AT BEGINNING OF YEAR						
Additions						
Transfers In						
Sub-total In						
Repayment						
Transfers Out						
Sub-total Out						
BALANCE END OF YEAR						

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Figure 6 cont.: Sample Form Lodged by NSW Co-operatives

CO-OPERATIVE NAME:

BALANCE SHEET	Financial Year Ended 31/12/2009 $	Last Year 31/12/2008 $
CURRENT ASSETS		
Cash and cash equivalents		
Trade and other receivables		
Inventories		
Financial assets		
Other current assets		
Total Current Assets		
NON-CURRENT ASSETS		
Trade and other receivables		
Assets held for sale		
Financial assets		
Property, plant & equipment		
Deferred tax assets		
Intangible assets		
Other non-current assets		
Total Non-Current Assets		
TOTAL ASSETS		
CURRENT LIABILITIES		
Trade and other payables		
Short-term borrowings		
Current tax liabilities		
Short-term provisions		
Other current liabilities		
Total Current Liabilities		
NON-CURRENT LIABILITIES		
Trade and other payables		
Long-term borrowings		
Deferred tax liabilities		
Long-term provisions		
Other non-current liabilities		
Share capital		
Co-operative capital units		
Total Non-Current Liabilities		
TOTAL LIABILITIES		
NET ASSETS		

Continued over page

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Figure 6 cont.: Sample Form Lodged by NSW Co-operatives

CO-OPERATIVE NAME:

BALANCE SHEET (Continued)	Financial Year Ended 31/12/2009 $	Last Year 31/12/2008 $
EQUITY		
Co-operative Capital Units		
Other reserves		
Retained earnings		
Parent entity interest		
Outside equity interest		
TOTAL EQUITY		

STATEMENT OF CHANGES IN EQUITY

Reserves		
Balance at start of year		
Adjustment on change in accounting policy and correction of errors (net of tax)		
Revaluation of land and buildings (net of tax)		
Available for sale financial assets (net of tax)		
Transfers to retained earnings		
Transfers from retained earnings		
Other (net of tax)		
Balance at end of year		

Retained Earnings		
Balance at start of year		
Adjustment on change in accounting policy and correction of errors (net of tax)		
Net profit (loss) for the year		
Transfers to reserves		
Transfers from reserves		
Dividends		
Rebates and bonuses provided or paid		
Balance at end of year		

Net income recognised directly in equity		
Profit (loss) for the year		
Total recognised income and expense for the year		
Attributable to:		
Equity holders of parent		
Minority interest		

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Figure 6 cont.: Sample Form Lodged by NSW Co-operatives

CO-OPERATIVE NAME:

INCOME STATEMENT

	Financial Year Ended 31/12/2009 $	Last Year 31/12/2008 $
Revenues		
Expenses excluding finance costs		
Finance costs		
Share of net profits (losses) of associates		
Profit (loss) before income tax		
Income tax		
Profit (loss) from continuing operations		
Profit (loss) from discontinued operations		
Profit (loss) for the year		
Profit (loss) attributable to minority equity interest		
Profit (loss) attributable to members of the parent entity		

Notes to and forming part of the financial statements are attached Yes ☐ No ☐

Subject to any exemption granted by the Registrar, the following documents should be attached at the time of lodgement of this form:

(1) Auditors' Report (section 252(1)(d))
(2) Directors' Report (section 252(1)(d))
(3) Directors' Declaration (section 252(1)(d))
(4) Accounts as submitted to the members (section 252(1)(b))
(5) List of Directors, Principal Executive Officer and Secretary - (section 252(1)(a) and Part B of this Form)
(6) Declarations of Interest (section 234(1) and Part C of this Form)
(7) Notice of Appointment or Cessation of Appointment of Directors and Officers (section 251B and Form AF11, supplied with this Form) if appropriate

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15 FEB 2010
REGISTRY OF CO-OPERATIVES & ASSOCIATIONS

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4.1.3 Charities – NSW

The general theme of the relevant provisions of the Charitable Fundraising Act is to ensure that adequate records/information are available to enable inspectors and members of the public to check that the proceeds of fundraising appeals have been used for the purpose for which they were solicited or received (see for example, Charitable Fundraising Act (s.24)).

4.2 Analysis of Reporting and Auditing Practices – NSW Sample

NSW Fair Trading provided population data relating to 2009-2011. The most recent lodgements for the random sample of 377 not-for-profit entities were obtained.

Table 15: NSW Data

Type of Entity	Sample (n)	Proportions (%)	Population Counts[67]	Proportions (%)
Tier-one Incorporated Associations	51	14	19,413	97
Tier-two Incorporated Associations	314	83		
Co-operatives	12	3	637	3
TOTAL	**377**	**100**	**20,050**	**100**

Table 15 shows the random sample subject to analysis is consistent with the proportions noted in the last column of the Table. Incorporated Associations [divided between 'Tier-one' (revenue > $250,000 or current assets > $500,000) and 'Tier-two' (all other associations)] are the predominant organisational form lodging financial statements with NSW Fair Trading. The majority of Associations (83%) lodging with NSW Fair Trading are tier-two associations. Each observation in the sample of 377 relates to a unique association (or co-operative) with data comprising lodgements over several years, i.e. 2009 (27%, 102 entities), 2010 (70%, 264 entities) and 2011 (3%, 11 entities).

Table 16: Descriptive Financial Data – NSW

TYPE OF ENTITY	TOTAL ASSETS Mean (Median) [SD]*	LIABILITIES Mean (Median) [SD]*	REVENUE Mean (Median) [SD]*	PROFIT Mean (Median) [SD]*
Tier-one Incorporated Associations	918,835 (375,655) [1,376,418]	320,601 (113,841) [549,898]	1,199,138 (530,383) [1,800,603]	150,429 (35,725) [490,974]
Tier-two Incorporated Associations	70,738 (16,787) [185,269]	10,745 (55,134) [55,134]	41,471 (18,934) [53,484]	2,265 (311) [22,959]
Co-operatives	1,247,382 (298,659) [1,904,901]	393,044 (97,408) [520,338]	1,155,406 (121,585) [1,677,824]	80,664 (23,722) [137,466]

* [SD] refers to standard deviation.

Table 16 presents descriptive financial information reported on assets, liabilities, revenue and profit by incorporated associations and co-operatives. All associations and co-operatives are required to complete summary financial data including assets, liabilities, revenue and profit on the annual statement lodged with NSW Fair Trading (see sample lodgement forms in Figures 5 and 6 above). Tier-one associations are significantly larger than tier-two associations (both assets and revenue), have higher levels of debt and are more profitable (i.e., reporting, on average, a surplus result).

67 Although, as noted immediately below Table 14, the total population of NSW incorporated associations was 34,273 at 30 June 2010. There is little difference between the sample size needed for a 95 per cent confidence level on 34,273 entities (380 observations) and the sample size needed for a 95 per cent confidence level on 19,413 entities (377 observations).

Table 17: Use of Templates versus Stand-alone Financial Statements, by Entity Group – NSW

Type of Entity	Summary Financial data in Annual Statements		Financial Statements		Summary Data and Financial Statements		Total	
	n	(%)	n	(%)	n	(%)	n	(%)
Tier-one Incorporated Associations	0	(0)	0	(0)	51	(100)	51	(100)
Tier-two Incorporated Associations	52	(17)	0	(0)	262	(83)	314	(100)
Co-operatives	0	(0)	0	(0)	12	(100)	12	(100)
TOTAL	**52**	**(14)**	**0**	**(0)**	**325**	**(86)**	**377**	**(100)**

Only tier-one associations are required to lodge a set of financial statements as part of their annual lodgement (Associations Incorporation Act, s.45(1)). Results presented in Table 17 indicate that 100 per cent of tier-one associations and co-operatives attached financial statements to the summary information provided at lodgement. Tier-two associations are required to complete summary information on the form lodged, but are not required to also attach financial statements (s.49(1)). However, 83 per cent of tier-two associations lodging in NSW voluntarily attached financial statements in addition to the summary financial information provided on the form.

Tier-two associations lodging in NSW are required to prepare financial statements that give a true and fair view of the association's affairs (s.47(2)) and submit the financial statements to an AGM (s.48). However as indicated above, these entities are only required to complete summary information on the form lodged with NSW Fair Trading (s.49(1)).

Table 18: Type of Financial Statements Lodged – NSW

Type of Entity	GPFSs %	SPFSs %	No clear statement %	Total %
Tier-one Incorporated Associations	10	67	24	100
Tier-two Incorporated Associations	2	17	82	100
Co-operatives	67	33	0	100

Table 18 presents data by category of entity on the type of financial statements lodged. Specifically, the results show whether the entities lodged GPFSs or SPFSs, or whether the type of statements was not clearly stated. Tier-one incorporated associations most commonly lodged SPFSs (67%), while co-operatives most commonly lodged GPFSs (67%). Of the 262 tier-two incorporated associations that lodged financial statements, 2 per cent indicated they had lodged GPFSs and 17 per cent SPFSs. 82 per cent of tier-two incorporated associations did not disclose the basis for the preparation of their financial statements.

Table 19: Disclosed Application of Accounting Standards – NSW

Type of Entity	Disclosed application of accounting standards %
Tier-one Incorporated Associations	51
Tier-two Incorporated Associations	12
Co-operatives	92

Results presented in Table 19 show the proportion of entities disclosing in their financial statements, regardless of type of financial statements (i.e., GPFSs or SPFSs), whether they had applied accounting standards. This disclosure is conventionally made in the significant accounting policies note to the financial statements. It is noteworthy that this analysis does not indicate the extent to which specific accounting standards were applied nor does it evaluate the accounting policies adopted by entities. Rather, Table 19 simply identifies whether an entity made any reference to applying accounting standards in its financial statements.

While 92 per cent of co-operatives made reference to accounting standards in the notes to their financial statements, only 51 per cent of tier-one associations did the same. Of the 262 tier-two incorporated associations that also lodged separate financial statements, 12 per cent made reference to accounting standards.

The Associations Incorporation Act states that tier-one associations must prepare financial statements in accordance with Australian Accounting Standards (s.43(2)). As previously noted, entities may be exempted from this obligation (s.53). Under Class Order 11/01, NSW Fair Trading allows tier-one associations with total revenue of less than $2 million some exemptions from the Australian Accounting Standards. The vast majority (86%) of tier-one associations disclosed revenue that was less than $2 million, and it appears they would qualify for consideration for exemption under Class Order 11/01. However, most of the financial statements analysed related to earlier periods. This probably explains why an analysis of the tier-one associations with revenue of more than $2 million revealed that only two entities did not disclose the application of accounting standards.

Table 20: Primary Indicators of the Level of Financial Reporting Transparency – NSW

Type of Entity	Balance Sheet %	Income Statement %	Statement of Cash Flows %	Notes %	Financial Statements Audited %
Tier-one Incorporated Associations	98	100	22	72	88
Tier-two Incorporated Associations	66	94	2	18	42
Co-operatives	100	100	75	100	100

An analysis of primary indicators of the level of reporting transparency in the financial statements is examined next. Results presented in Table 20 show the proportion of entities that lodged a Balance Sheet, Income Statement (either a Statement of Comprehensive Income or a simple Income Statement), Statement of Cash Flows, Notes to Financial Statements, and whether the entity was audited. By documenting the total information lodged by different categories of entity, it is possible to develop a sense of the transparency of the financial reporting of the entities in the sample.

All tier-one associations and co-operatives are required to lodge audited financial statements. With one exception, these entities complied by lodging an income statement and balance sheet – it was noted that one tier-one association did not lodge a balance sheet. Furthermore, apparently contrary to regulation, 12 per cent of tier-one associations (six entities) stated on the form lodged with NSW Fair Trading that they did not engage the services of an auditor nor did they attach an audit report. However, one of these entities attached a compilation report[68] instead of an audit report. It is noteworthy that only 22 per cent of tier-one associations lodged a statement of cash flows and 72 per cent presented notes to the financial statements.

68 A compilation report does not provide assurance or verify the accuracy or completeness of the financial information provided by management for the compilation. Nor does it express an audit opinion or a review conclusion on the preparation of the financial information.

Class Order 11/01 exempts tier-one associations with revenue of less than $2 million from the obligation to lodge a statement of cash flows. Of the 78 per cent of tier-one associations not lodging a statement of cash flows, 93 per cent had revenue below $2 million.[69] The remaining three tier-one associations that did not lodge a statement of cash flows would now seem to be in contravention of the legislation.

Tier-two associations are not required to lodge financial statements with NSW Fair Trading. Of the 262 tier-two associations that lodged financial statements (voluntarily), most lodged an income statement (94%) and a balance sheet (66%), but only a small number of entities lodged a statement of cash flows (2%) or lodged notes to the financial statements (18%). Approximately 42 per cent of tier-two associations in the sample indicated on the form lodged with NSW Fair Trading that their financial statements were audited, however, only 30 per cent of the 262 tier-two incorporated associations (78 entities) lodged an audit report. It is noteworthy that 13 associations lodged a compilation report; four of which included an audit report.

Table 21: Proxy Measure of the Indicators of the Level of Financial Reporting Transparency – NSW

Type of Entity (5 point scale)	Mean	Median	SD*	Min	Max
Tier-one Incorporated Associations	3.76	4.00	1.01	1.00	5.00
Tier-two Incorporated Associations	2.24	2.00	1.11	-	5.00
Co-operatives	4.75	5.00	0.45	4.00	5.00

* SD refers to standard deviation.

To provide an overall sense of the level of reporting by entities, the five primary indicators of financial reporting transparency summarised in Table 20 were combined into a single measure and reported in Table 21. Each of the five indicators was equally weighted and assigned a value of 0 or 1, which can add to a maximum financial reporting transparency score of 5. For example, if the entity lodged a balance sheet, an income statement and statement of cash flows, included one or more notes, and the financial statements were audited, the entity would receive a score of 5.

Data summarising the proxy measure of the level of financial reporting is presented by type of entity in Table 21. The proxy measure for financial reporting transparency is highest for co-operatives and tier-one incorporated associations with scores well above the mean of 2.5 (4.75 and 3.76 respectively). In comparison, tier-two incorporated associations that lodged financial statements displayed lower financial reporting transparency evidenced by mean scores of 2.24.

Table 22: Further Indicators of the Level of Reporting Transparency in Tier-one Incorporated Associations and Co-operatives – NSW

	Line Item Comprehensive Income	Statement of Changes in Equity	Movements in PPE reconciled	Non-Current Provisions	Reserves Disclosed	Signed Directors' Report
	%	%	%	%	%	%
Tier-one Incorporated Associations	2	6	10	27	10	73
Co-operatives	33	75	33	42	58	100

69 It is unclear whether the meaning of 'revenue' in the Class Order is the same as 'revenue' in the lodgements that were analysed.

For tier-one incorporated associations and co-operatives, a more sophisticated measure of financial reporting transparency has also been developed. In addition to the basic financial disclosures reported in Table 20 (i.e., a Balance Sheet, Income Statement, Statement of Cash Flows, Notes, and Audit Report), six additional items were identified and coded to develop an understanding of financial reporting transparency. These items are (1) reporting of comprehensive income; (2) a separate statement of changes in equity; (3) property, plant and equipment (PPE) > 0 and the movements in PPE over the year reconciled; (4) reporting of non-current provisions;[70] (5) reporting of any reserves; (6) a report signed by directors (or their equivalent). This measure is adapted from the measures of financial disclosure in Van Overfelt et al. (2010). In each case the items identified provide an additional indication of the sophistication of the information systems and reporting practices of entities.

Results presented in Table 22 indicate a low level of reporting of the specific items by tier-one associations and a moderate level of reporting by co-operatives. For tier-one associations, the only two items reported by more than 10 per cent of entities were non-current provisions (27%) and a signed directors' report (73%).

Table 23: Reporting of Notes to the Financial Statements by Tier-one Incorporated Associations – NSW

Notes to the Accounts	**Entities %**	**Mean**	**Median**	**SD***	**Min**	**Max**
		3.80	**2.000**	**4.36**	**0.0**	**15.0**
No Notes reported	28					
1 Note	20					
2 Notes	8					
3 Notes	6					
4 Notes	7					
5 Notes	4					
6 Notes	2					
7 Notes	4					
8 Notes	2					
9 Notes	6					
10 Notes	3					
11 Notes	2					
12 Notes	2					
13 Notes	0					
14 Notes	4					
15 Notes	2					
16 Notes	0					
17 Notes	0					
18 Notes	0					
19 Notes	0					
20+ Notes	0					
TOTAL	**100**					

* SD refers to standard deviation.

Table 23 presents data on the number of notes to the financial statements included in lodged financial statements by tier-one incorporated associations. As previously indicated in Table 20, 72 per cent of tier-one associations presented notes. As indicated in Table 23, there is considerable variation in the number of notes disclosed in the financial statements lodged by these entities. About half of the entities (48%) lodged either no notes, or one note only.

70 Non-current provisions disclosed were usually related to employee entitlements.

Table 24: Reporting of Property, Plant and Equipment and Adoption of Accrual Accounting – NSW

Type of Entity	Accrual Accounting %	Property, Plant & Equipment Disclosed %
Tier-one Incorporated Associations	94	75
Tier-two Incorporated Associations	29	36
Co-operatives	92	92

Table 24 presents results relating to two further indicators of financial reporting transparency developed for this Part of this Report. First, lodgements were examined for evidence that accrual accounting was applied (as opposed to cash accounting), which is widely assumed to lead to a superior measure of periodic performance and period-end financial position (Dechow et al., 1998; Neill et al., 1991). It was concluded that an entity had applied accrual accounting if items such as debtors, creditors or depreciation were identified in the financial statements. The purpose of doing so was not to determine whether the entity was adopting Australian Accounting Standards, but rather to assist in enhancing understanding of the extent of adoption of accrual accounting principles. Second, the disclosures made by each entity were reviewed to determine if the entity disclosed dollar values for property, plant and equipment, on the assumption that asset disclosure represents decision-useful information and is indicative of greater financial reporting transparency (Dechow et al., 1998; Neill et al., 1991). It should be noted that property, plant and equipment was identified only for entities that lodged a balance sheet. (i.e., 201 [66%] of the 314 tier-two associations, see Table 20).

Results presented in Table 24 show that while most tier-one incorporated associations adopted accrual accounting (94%) the majority of tier-two incorporated associations used cash accounting (i.e., 71%). Accrual accounting is adopted more commonly than cash accounting by co-operatives (92%).

Table 25: Issuing Modified Audit Opinions – NSW

Type of Entity	Financial Statements Audited %	Modified Audit Opinion %
Tier-one Incorporated Associations	88	29
Tier-two Incorporated Associations	42	23
Co-operatives	100	33

As previously noted (see Table 20), 88 per cent of tier-one associations stated on the form lodged with NSW Fair Trading that they had engaged the services of an auditor. About 42 per cent of tier-two associations indicated that their financial statements were audited.

Where an audit report was lodged with NSW Fair Trading, the type of audit report issued is summarised in Table 25. Around 29 per cent of tier-one associations lodging an audit report received a modified audit opinion and about 23 per cent of tier-two associations lodging an audit report similarly received a modified audit opinion. All co-operatives (12 entities) lodged an audit report, with 33 per cent (4 audit reports) showing modified audit opinions. It is noteworthy that the proportion of opinion modifications is higher among the state-based entities than the average modification rate of 19 per cent reported among listed public companies in Australia for the period 2005-2009 (Xu et al., 2013; Xu et al., 2011). An additional review of the audit opinions indicates that the major source of modification was an 'except for' opinion because of a scope limitation, due usually to ineffective internal control over physical cash receipts.

Table 26: Auditors' Professional Affiliation – NSW

Type of Entity	Big 4 %	CA %	CPA %	IPA %	Other %
Tier-one Incorporated Associations	2	48	20	7	23
Tier-two Incorporated Associations	1	39	20	5	35
Co-operatives	0	67	8	0	25

The professional designation of the auditor was determined from the audit report attached to the lodgements made by entities. Results presented in Table 26 demonstrate that Chartered Accountants are the most common professional designation followed by the 'Other' category, which comprises mainly individuals who signed as 'honorary auditor' without indicating their professional designation. It is also clear from the results reported in Table 26 that the financial statements of incorporated associations and co-operatives were rarely audited by Big 4 auditors.

4.3 Additional Anecdotal Evidence Concerning Financial Reporting Practices – NSW

4.3.1 Completion of Standard Form A12 – NSW

Tier-two incorporated associations are required to provide only summary financial data within the lodgement form (i.e., total assets, total liabilities, income) and are not required to attach financial statements. As such the level of reporting is limited.

4.3.2 Variation in the quality of information provided in Form A12 and in the quality of lodged financial statements – NSW

There is apparently significant variation in the quality of information provided by entities – both through the Form A12 (see Figure 5 above) and also through the financial statements lodged. Examples are provided below:

(a) The most striking discrepancy is that, for approximately 30 per cent of tier-two associations, the summary information completed on the lodgement form does not match the information provided in the financial statements attached to the lodgement. Common examples of items where discrepancies were identified included assets, income, liabilities and profit.

(b) For tier-two associations, data are missing in an estimated 25 per cent of forms lodged. The frequency of omission is greater in entities that do not attach financial statements. Examples of missing data include: financial data, indicating Yes/No to the question whether figures were audited, providing the number of employees, name of entity, year-end date, entity contact details such as address, registration code, and the existence of grants and mortgages.

(c) In one instance a tier-two association lodged financial statements labelled as GPFSs; however the financial statements were missing a statement of cash flows, and did not disclose the line item 'comprehensive income', and did not have an accompanying audit report.

(d) The financial statements attached to Form A12 completed by a number of tier-two incorporated associations were handwritten and difficult to understand.

(e) In approximately three per cent of lodgements, mainly among tier-two associations, there were arithmetic errors in the financial statements lodged.

The most common errors were income statements or balance sheets that did not add up.

4.3.3 Issues around non-disclosure – NSW

There is evidence that some entities, which should have been classified as tier-one associations (and thus lodged audited financial statements), classified themselves as tier-two associations. For example, on the assumption that the number of members is indicative of the likely size of the entity as measured by total revenue or current assets, one association with over 2,000 members had classified itself as tier-two and thus did not lodge separate audited financial statements. Another association with 4,600 members had classified itself as tier-two.

4.3.4 Issues relating to the audit report for associations and co-operatives – NSW

A proportion of audit reports issued for tier-one and tier-two associations did not resemble the standard audit report as outlined in the auditing standards. For tier-one associations, approximately 10 per cent of audit reports did not resemble the standard audit report and for tier-two associations, approximately 40 per cent of audit reports did not resemble the standard audit report.

For tier-two associations, non-standard audit reports typically contained only a few lines where the auditor would make a statement such as ‘I hereby certify that to the best of my knowledge the financial statements present a true and fair view’. In many of these instances the auditors’ qualifications and/or affiliations are not disclosed and the auditor appears to be a member of the organisation.

Not all tier-two associations that indicated they were audited by checking the box on Form A12 as ‘YES’, attached an audit opinion with their lodgement. Approximately 28 per cent of tier-two associations did not attach an audit report despite indicating that they were audited.

When an audit report was qualified due to a scope limitation, around 20 per cent of auditors incorrectly used the redundant ‘subject to’ qualification rather than an ‘except for’ qualification.

In one of the 12 co-operatives examined, the audit report referred to the 1995 co-operative regulations rather than the 2005 regulations.

5. Queensland Entities

Table 27 below shows the Queensland entity groups and their respective population numbers as of 2010 as well as the relevant reporting legislation.

Table 27: Queensland Data

Queensland Entity Group	Population n	Population %	Relevant reporting regulations
Incorporated Associations	16,570	81	*Collections Act 1966*
Charities	1,080	5	*Gaming Machine Act 1991*
Community Purpose Entities	2,569	13	*Co-operatives Act 1997*
Co-operatives	138	1	*Associations Incorporation Act 1981* *Associations Incorporation Regulation 1999*
Total	**20,357**	**100**	

5.1 Reporting and Auditing Regulation – Queensland

5.1.1 Incorporated Associations – Queensland

Incorporated associations are not-for-profit clubs or community groups that are given a formal legal structure by way of their incorporation under the Associations Incorporation Act. Incorporated associations must have the word ‘Incorporated’ or the abbreviation ‘Inc.’ in the entity name. Typical examples of incorporated associations in Queensland include sporting groups and musical societies.

Relevant authority: The relevant regulations for shaping the reporting by incorporated associations are: The Associations Incorporation Act and The Associations Incorporation Regulation.[71]

Classes of entity for reporting: As defined in Division 2 of the Associations Incorporation Act, incorporated associations are classified based on their current assets or total revenue.

(a) **Level-one** entities have current assets of more than $100,000 or total revenue of more than $100,000;

(b) **Level-two** entities have current assets between $20,000 and $100,000 and/or total revenue between $20,000 and $100,000; and

(c) **Level-three** entities have current assets of less than $20,000 and total revenue of less than $20,000.

Reporting requirements: All incorporated associations must lodge financial statements with the Queensland Government Office of Fair Trading (QOFT). Therefore, irrespective of class of entity, all level-one associations (s.59(3)(a)), level-two associations (s.59A(3)(a)), and level-three associations (s.59B(3)(a)) must lodge financial statements. The Queensland regulation does not explicitly require financial statements to be prepared in accordance with Australian Accounting Standards.

Since all entities must lodge financial statements, the primary difference between reporting requirements for different levels of incorporated associations is in relation to the audit requirements. Audit requirements are based on whether an entity is defined as level-one, two or three, although associations classified as level-two and three may be required to adhere to

71 Incorporated associations may also be registered under the Collections Act and/or Gaming Machine Act.

level-one associations' audit requirements if they are subject to specific legislation such as the Collections Act or Gaming Machine Act (s.59(1) of the Associations Incorporation Act).

***Lodged financial statements must be audited*:** Level-one associations must lodge audited financial statements with the QOFT within one month after the AGM (s.59(3)). Level-one associations must be audited by an auditor or an accountant (s.59(2)(b)(i), while level-two and three associations that are required to be audited (e.g., under the Collections Act or Gaming Machine Act) may be audited by an auditor, an accountant, or a person approved by the Commissioner for Fair Trading (s.59(2)(b)(ii)).

Section 58 of the Queensland Associations Incorporation Act defines an auditor as a person registered as an auditor under the Corporations Act. An accountant is defined as a member of CPAA, the ICAA or the IPA.

***Adequacy of financial records*:** An auditor, an accountant or a person approved by the Commissioner for Fair Trading must 'attest' to the adequacy of the financial records of a level-two association. The financial statements and a statement relating to the adequacy of the financial records must be lodged with QOFT within one month after the AGM (s.59A(3)). The attestation must state 'I have sighted the association's financial records and the financial records show that the association has bookkeeping processes in place to adequately record the association's income and expenditure and dealings with its assets and liabilities' (s.59A(2)(b)(ii)).[72]

***Adequacy of financial records*:** The president of the association or its treasurer must 'attest' to the adequacy of the financial records of a level-three association. The attestation must state 'The Association keeps financial records in a way which properly records the Association's income and expenditure and dealings with its assets and liabilities' (s.59B(2)(b)(ii)). The financial statements must be lodged with QOFT within one month after the AGM (s.59B(3)).

5.1.2 Charities and Community Purpose Entities – Queensland

In Queensland, entities that undertake fundraising activities must be registered with QOFT as a charity or a community purpose entity.

Relevant authority: Charities and community purpose entities are subject to the Collections Act. Organisations need to register with QOFT if they wish to raise funds for charitable or community purposes and any organisation that fundraises in Queensland without registration or other authorisation is committing an offence under the Collections Act.

Reporting requirements: A charity or community purpose entity registered under the Collections Act must lodge audited financial statements with the QOFT each year (s.31). The audit can be undertaken by a person registered as an auditor under the Corporations Act or members of CPAA, ICAA, IPA, or someone approved by QOFT (s.31(1)(f)).

The Collections Act does not specify whether the financial statements have to follow accounting standards. Part 1 of the Act defines 'financial statements' as 'statements of receipts and expenditure, balance sheets, and such other financial statements as prescribed either generally or in the particular case.'

72 In this Section, for the purpose of this Report, an examination of the adequacy of the financial records is treated as the equivalent of an audit.

5.1.3 Co-operatives – Queensland

A co-operative is an autonomous association owned and controlled by its members to meet common economic, social and cultural needs and goals.[73] Examples of entities in Queensland that operate as co-operatives include groups of businesses involved in agriculture and farming.

Relevant authority: By virtue of section 232 of the Co-operatives Act, the financial reporting and audit for co-operatives is governed by Part 2M of the Corporations Act. As a consequence, the financial reporting requirements applicable to co-operatives is consistent with those of companies.

Reporting requirements: The financial reporting and audit requirements for co-operatives are the same as those that apply to public companies under the Corporations Act. The Co-operatives Act states that within 28 days of the AGM the co-operative must lodge an annual report with QOFT, attaching the audited financial accounts presented at the AGM (s.242(2)(a)). The content of the financial statements is governed by Part 2M of the Corporations Act.

5.2 Analysis of Reporting and Auditing Practices – Queensland Sample

QOFT provided population data relating to 2009-2011. The most recent lodging for the random sample of 386 not-for-profit entities reflecting the population proportions of incorporated associations (IA), charities, community purpose entities, and co-operatives was obtained.

Table 28: Queensland Data Sample

<table>
<tr><th>Type of Entity</th><th>Sample n</th><th>Sample Proportions %</th><th>Population Counts</th><th>Population Proportions %</th></tr>
<tr><td>IA Level-one</td><td>67</td><td>17</td><td rowspan="3">16,570</td><td rowspan="3">81</td></tr>
<tr><td>IA Level-two</td><td>126</td><td>33</td></tr>
<tr><td>IA Level-three</td><td>124</td><td>32</td></tr>
<tr><td>Charities</td><td>20</td><td>5</td><td>1,080</td><td>5</td></tr>
<tr><td>Community Purpose Entities</td><td>46</td><td>12</td><td>2,569</td><td>13</td></tr>
<tr><td>Co-operatives</td><td>3</td><td>1</td><td>138</td><td>1</td></tr>
<tr><td>TOTAL</td><td>386</td><td>100</td><td>20,357</td><td>100</td></tr>
</table>

Table 28 shows the random sample subject to analysis is consistent with the population proportions. Incorporated associations are the predominant organisational form lodging financial statements with QOFT. The incorporated associations were divided among ‘Level-one’ (current assets or revenue > $100,000), ‘Level-two’ (current assets and/or revenue between $20,000 and $100,000), and ‘Level-three’ (current assets or revenue < $20,000) entities. The sample of 386 entities comprises data from years ending 2009 (5%, 19 entities), 2010 (85%, 328 entities) and 2011 (10%, 39 entities).

Table 29 presents descriptive financial information for incorporated associations, charities, community purpose entities and co-operatives. It is to be expected that level-one incorporated associations are larger than level-two incorporated associations, and level-two incorporated

73 http://www.fairtrading.qld.gov.au/what-is-cooperative.htm – accessed April 2014

associations are larger than level-three incorporated associations (F = 36.950, p = .000).[74] While the three types of incorporated associations statistically differ by size, there is no statistically significant difference (F = 2.636, p = .074) in the levels of profitability between the three types of incorporated associations.[75]

Table 29: Descriptive Financial Data – Queensland

TYPE OF ENTITY	TOTAL ASSETS Mean (Median) [SD]*	LIABILITIES Mean (Median) [SD]*	REVENUE Mean (Median) [SD]*	PROFIT Mean (Median) [SD]*
IA Level-one	807,017 (318,028) [1,347,292]	187,614 (23,088) [432,820]	764,495 (258,883) [2,267,646]	29,414 (7,054) [153,337]
IA Level-two	80,316 (41,006) [108,289]	3,122 (0) [11,290]	40,082 (36,190) [24,662]	2,402 (1,382) [17,472]
IA Level-three	13,824 (8,496) [20,426]	505 (0) [2,083]	7,994 (7,688) [5,787]	186 (167) [3,988]
Charities	5,519,772 (359,802) [14,197,122]	1,643,501 (47,892) [5,099,765]	3,693,360 (707,488) [6,905,229]	563,309 (83,266) [2,640,430]
Community Purpose Entities	3,776,562 (105,083) [15,560,089]	681,315 (570) [2,155,775]	1,423,178 (52,000) [4,200,558]	91,310 (1,997) [397,262]
Co-operatives	2,075,974 (1,502,370) [1,573,744]	385,929 (308,465) [380,973]	3,273,709 (2,388,523) [3,293,083]	30,222 (29,373) [1,847]

* [SD] refers to standard deviation.

Table 30: Type of Financial Statements Lodged – Queensland

Type of Entity	GPFSs %	SPFSs %	No clear statement
IA Level-one	7	73	20
IA Level-two	2	62	36
IA Level-three	0	36	64
Charities	50	35	15
Community Purpose Entities	20	50	30
Co-operatives	33	33	33

Table 30 shows the type of financial statements lodged for each category of entity. Specifically, the Table shows whether entities lodged GPFSs or SPFSs, or whether the type of financial statements was not clearly stated. Level-one and level-two incorporated associations most commonly lodged SPFSs (73% and 62%, respectively), whilst a majority of level-three incorporated associations (64%) made no clear statement as to the type of financial statements lodged.

74 The F-test and its associated *p*-value is used to assess the hypothesis that no differences exist between the three levels of incorporated associations on total assets, liabilities, revenue and profit. If a difference is observed, the associated *p*-value (i.e., the probability value) will be small, indicating that the chance of obtaining such a mean (median) value is very small.

75 Oneway ANOVA (analysis of variance) results and related post hoc Scheffe tests as well as Kruskal-Wallis H nonparametric tests (χ^2 = 5.684, df = 2, p = .058) show no significant differences at the .05 level.

Approximately 50 per cent of charities in the sample lodged GPFSs, while 50 per cent of the community purpose entities lodged SPFSs. The sample of co-operatives comprised only three entities; one lodged GPFSs, one lodged SPFSs, while for one entity there was no clear statement as to the type of financial statements lodged.

Table 31: Disclosed Application of Accounting Standards – Queensland

Type of Entity	Disclosed application of accounting standards %
IA Level-one	49
IA Level-two	21
IA Level-three	14
Charities	85
Community Purpose Entities	49
Co-operatives	100

Results presented in Table 31 show the proportion of entities that disclosed in their financial statements, regardless of type of financial statements (i.e., GPFSs or SPFSs), whether they had applied accounting standards. This disclosure is conventionally made in the significant accounting policies note to the financial statements. It is noteworthy that this analysis does not indicate the extent to which specific accounting standards are being applied nor does it evaluate the accounting policies adopted by entities. Rather, Table 31 simply identifies whether an entity made any reference to application of the accounting standards in its financial statements. Table 31 shows that all co-operatives and the majority of charities (85%) made reference to applying accounting standards, as well as almost half of community purpose entities (49%) and level-one incorporated associations (49%).

Table 32: Primary Indicators of the Level of Financial Reporting Transparency – Queensland

Type of Entity	Balance Sheet %	Income Statement %	Statement of Cash Flows %	Notes %	Financial Statements Audited %
IA Level-one	93	100	9	78	100
IA Level-two	88	98	5	44	89
IA Level-three	77	91	1	33	49
Charities	95	100	65	85	100
Community Purpose Entities	85	98	22	57	100
Co-operatives	100	100	67	100	100

An analysis of primary indicators of the level of reporting transparency in the financial statements is examined next. Results presented in Table 32 show the proportion of entities that lodged a Balance Sheet, Income Statement (either a Statement of Comprehensive Income or a simple Income Statement), Statement of Cash Flows, Notes to Financial Statements, and a signed audit opinion. By documenting the total information lodged by different categories of entity, it is possible to develop a sense of the transparency of the financial reporting of the entities in the sample. The income statement is the most commonly lodged statement. Similarly, the balance sheet is lodged by most entities.

Results in Table 32 show that all level-one incorporated associations, charities, community purpose entities, and co-operatives had their financial statements audited, closely followed by level-two incorporated associations (89%). A smaller number (49%) of level-three incorporated associations had their financial statements audited. It is noteworthy that level-three incorporated associations not operating under the Collections Act or the Gaming Machine Act, are not required to lodge audited financial statements. However, consistent with the Associations Incorporation Act, 49 per cent of these associations attached a statement where the president or treasurer made an attestation in relation to the financial statements. A total of 22 entities lodged compilation reports (ten of these compilation reports were unaudited). Three compilation reports were lodged by level-one incorporated associations, ten were lodged by level-two incorporated associations (five of which were unaudited), and eight compilation reports were lodged by level-three incorporated associations (five of which were unaudited). One audited compilation report was lodged by a community purpose entity.

Table 33: Proxy Measure of the Indicators of the Level of Financial Reporting Transparency – Queensland

Type of Entity (5 point scale)	Mean	Median	SD*	Min	Max
IA Level-one	3.78	4.00	0.65	2.00	5.00
IA Level-two	3.22	3.00	0.82	1.00	5.00
IA Level-three	2.52	2.50	1.08	-	4.00
Charities	4.45	5.00	0.89	2.00	5.00
Community Purpose Entities	3.61	3.50	0.58	4.00	5.00
Co-operatives	4.67	5.00	0.58	4.00	5.00

* [SD] refers to standard deviation.

To provide an overall sense of the level of reporting transparency by entities, the five primary indicators of financial reporting transparency summarised in Table 32 were combined into a single measure and reported in Table 33. Each of the five indicators was equally weighted and assigned a value of 0 or 1, which can add to a maximum financial reporting transparency score of 5. For example, if the entity lodged a balance sheet, an income statement and statement of cash flows, included one or more notes to the financial statements, and the financial statements were audited, the entity would receive a maximum score of 5. Data summarising the proxy measure of the level of financial reporting is presented by type of entity in Table 33.

The proxy measure of financial reporting transparency is highest for co-operatives and charities, with mean reporting transparency scores of 4.67 and 4.45, respectively. Incorporated associations levels-one and two, as well as community purpose entities, have scores above the mean of 2.5 (3.78, 3.22, and 3.61, respectively). It is noteworthy that despite level-two associations being relatively small (current assets and/or revenue between $20,000 and $100,000) they achieved a proxy measure of financial reporting transparency score above the mid-point. The proxy measure for level-three incorporated associations of financial reporting transparency score was only slightly above the mean at 2.52, indicating that these entities had lodged financial statements with relatively lower levels of financial reporting transparency compared with co-operatives, charities, and level-one incorporated associations.

Table 34: Further Indicators of the Level of Reporting Transparency by All Entities – Queensland

	Line Item Comprehensive Income %	Statement of Changes in Equity %	Movements in PPE reconciled %	Non-Current Provisions %	Reserves Disclosed %	Signed Directors' Report %
IA Level-one	4	7	31	12	15	73
IA Level-two	0	0	14	0	7	51
IA Level-three	0	0	7	0	2	47
Charities	50	50	35	40	45	85
Community Purpose Entities	28	28	39	14	27	52
Co-operatives	33	67	67	33	100	100

Table 34 summarises results from a more sophisticated measure of reporting transparency. In addition to the basic financial reporting items shown in Table 32 (i.e., a Balance Sheet, Income Statement, Statement of Cash Flows, Notes, and Audit Report), six additional items were identified and coded to further develop an understanding of financial reporting transparency. These items are (1) reporting of the line item 'comprehensive income';[76] (2) a separate statement of changes in equity; (3) movements in property, plant and equipment (PPE) over the year reconciled (in entities where PPE > 0); (4) reporting of non-current provisions[77]; (5) reporting of any reserves; (6) a report signed by directors (or their equivalent). This measure is adapted from the measures of financial disclosure in Van Overfelt et al. (2010). In each case, the items identified provide an indication of the sophistication of the information systems and reporting practices of entities.

For level-one incorporated associations, the only specific items where the proxy measure of reporting transparency was above 25 per cent were movements in property, plant and equipment reconciled (31%) and signed directors' reports (73%). It is noteworthy that charities, community purpose entities, and co-operatives generally have a higher proxy measure of the level of reporting transparency than incorporated associations.

76 Where this item was no different from net profit (i.e., there were no adjusting items), the entity was coded as having 'disclosed' this item.
77 Most often, non-current provisions disclosed related to employee entitlements.

Table 35: Reporting of Notes to the Financial Statements by Level-one (and Level-two) Incorporated Associations – Queensland

Notes to the Accounts	Entities		Mean	Median	SD*	Min	Max
	Level-one %	(Level-two) %					
Level-one (Level-two)			**4.36 (1.15)**	**1.00 (0.00)**	**5.16 (2.41)**	**0.00 (0.00)**	**21.00 (16.00)**
No Notes reported	22	(56)					
1 Note	28	(25)					
2 Notes	0	(7)					
3 Notes	6	(2)					
4 Notes	7	(2)					
5 Notes	4	(2)					
6 Notes	6	(3)					
7 Notes	3	(0)					
8 Notes	3	(1)					
9 Notes	1	(0)					
10 Notes	4	(0)					
11 Notes	3	(0)					
12 Notes	1	(0)					
13 Notes	1	(0)					
14 Notes	1	(0)					
15 Notes	1	(1)					
16 Notes	0	(1)					
17 Notes	1	(0)					
18 Notes	0	(0)					
19 Notes	1	(0)					
20+ Notes	1	(0)					
TOTAL	**100**	**(100)**					

* SD refers to standard deviation.

Table 35 presents data on the numbers of notes reported in the financial statements by the 67 level-one associations and the 126 level-two associations. Approximately 78 per cent of level-one associations disclosed one or more notes and 44 per cent of level-two associations disclosed one or more notes. 50 per cent of the level-one associations disclosed less than two notes. The majority of level-two associations (81%) disclosed less than two notes. At the opposite extreme, there are entities making a considerable amount of note disclosure.

Results presented in Table 35 indicate a relatively low level of reporting of notes to the financial statements by incorporated associations.

Table 36: Reporting of Notes to the Financial Statements by Charities and Community Purpose – Queensland

Notes to the Accounts	Entities		Mean	Median	SD*	Min	Max
	Charities %	(Community Purpose) %					
Charities (Community Purpose)			**12.35 (5.52)**	**14.50 (1.00)**	**9.24 (9.22)**	**0.00 (0.00)**	**27.00 (39.00)**
No Notes reported	15	(43)					
1 Note	10	(22)					
2 Notes	0	(4)					
3 Notes	0	(0)					
4 Notes	0	(2)					
5 Notes	10	(0)					
6 Notes	0	(0)					
7 Notes	0	(0)					
8 Notes	5	(2)					
9 Notes	0	(0)					
10 Notes	0	(2)					
11 Notes	5	(4)					
12 Notes	0	(0)					
13 Notes	0	(2)					
14 Notes	5	(0)					
15 Notes	10	(0)					
16 Notes	0	(0)					
17 Notes	5	(4)					
18 Notes	5	(4)					
19 Notes	0	(0)					
20+ Notes	30	(9)					
TOTAL	**100**	**(100)**					

* SD refers to standard deviation.

Table 36 presents data on the numbers of notes reported in the financial statements lodged by the 20 charities and 46 community purpose entities. Approximately 85 per cent of charities disclosed one or more notes and 57 per cent of community purpose entities disclosed one or more notes. Only 25 per cent of the charities in the sample disclosed fewer than two notes. In contrast, the majority of community purpose entities (65%) disclosed fewer than two notes. It is noteworthy that 30 per cent of charities and 9 per cent of community purpose entities made extensive note disclosures with 20+ notes. Results also suggest considerable variation in the number of notes to the financial statements of charities and community purpose entities.

Table 37: Reporting of Property, Plant and Equipment and Adoption of Accrual Accounting – Queensland

Type of Entity	Accrual Accounting %	Property, Plant & Equipment Disclosed %
IA Level-one	79	81
IA Level-two	60	64
IA Level-three	33	41
Charities	95	50
Community Purpose Entities	59	59
Co-operatives	100	100

Table 37 presents results relating to two further indicators of financial reporting transparency developed for this Part of this Report. First, lodgements were examined for evidence that accrual accounting was applied (as opposed to cash accounting), which is widely assumed to lead to a superior measure of periodic performance and period-end financial position

(Dechow et al., 1998; Neill et al., 1991). It was concluded that an entity had applied accrual accounting if items such as debtors, creditors or depreciation were identified in the financial statements. The purpose of doing so was not to determine whether the entity was adopting Australian Accounting Standards, but rather to assist in enhancing understanding of the extent of adoption of accrual accounting principles. Second, disclosures made by each entity were reviewed to determine if the entity disclosed dollar values for property, plant and equipment on the assumption that asset disclosure represents decision-useful information and is indicative of greater financial reporting transparency (Dechow et al., 1998; Neill et al., 1991). It should be noted that property, plant and equipment was identified only in entities that lodged a balance sheet. Where an entity did not lodge a balance sheet, the observation was coded as missing. Results therefore reflect measurement of property, plant and equipment by entities that lodged a balance sheet. Property, plant and equipment was recorded as disclosed when there was a line item identifying any item of property, plant or equipment (even if its balance was disclosed as zero).

Results presented in Table 37 show the majority of entities adopt accrual accounting. All Co-operatives (100%) and most charities (95%) and level-one associations (79%) adopt accrual accounting. The majority of level-three incorporated associations used cash accounting (i.e., 67%) and a substantial minority of community purpose entities (41%) and level-two associations (40%) do the same. While accrual accounting is the most popular approach, many entities adopt cash accounting.

Table 38: Modified Audit Opinions – Queensland

Type of Entity	Financial Statements Audited %	Modified Audit Opinion %
IA Level-one	100	62
IA Level-two	89	62
IA Level-three	49	55
Charities	100	50
Community Purpose Entities	100	41
Co-operatives	100	0

Results in Table 38 summarise the auditing opinions issued for Queensland associations, charities, community purpose entities, and co-operatives. All level-one associations were audited. Analysis of the audit reports available reveals that 62 per cent had a modified audit opinion. The predominant reason for modification was an ‘except for’ qualified opinion because of a scope limitation regarding the system of control around revenue.

The financial records of 89 per cent of level-two associations were examined (as previously noted, when a statement about their adequacy is issued by a third party [i.e., auditor, accountant or approved person] – this is classified as an audit for the purpose of the research). Despite the examination of financial records being a requirement, there was no evidence of this having been done in 11 per cent of level-two associations. Similar to the results for level-one associations, more than half of the level-two statements were modified.

The financial records of 49 per cent of the level-three associations were subject to third party examination. 55 per cent of the statements about financial records were modified. All charities were audited and lodged audit opinions. Half of the audit opinions for charities were modified; predominantly qualified opinions due to scope limitations. Regarding community purpose entities, all three were audited, lodged an audit opinion, and none were modified.

Results in Table 38 suggest, as for Victoria and NSW, that the proportion of modified audit opinions is higher than the proportion observed among listed public companies in Australia (Xu et al., 2013; Xu et al., 2011).

Table 39: Auditors' Professional Affiliation – Queensland

Type of Entity	Big 4 %	CA %	CPA %	IPA %	Other %
IA Level-one	0	34	25	9	32
IA Level-two	0	24	33	18	25
IA Level-three	2	20	36	11	31
Charities	25	55	5	0	15
Community Purpose	4	39	17	7	33
Co-operatives	0	33	67	0	0

The professional designation of the auditor (or preparer of the compilation report) was determined from the audit report attached to the lodgements by these entities. Results presented in Table 39 indicate that Chartered Accountants were the most common professional designation of auditors of charities. Further, Chartered Accountants and CPAs are frequent among the auditors of incorporated associations and co-operatives. Entities in the sample were also frequently audited by a professional classified as 'Other', comprising mainly individuals who signed as 'honorary auditor' without indicating their professional designation. It is also evident from the results in Table 39 that, with the exception of charities, the financial statements of entities were rarely audited by Big 4 auditors.

6. Tasmanian Entities

Table 40: Tasmania Data

Tasmanian Entity Group	Population n	Population %	Relevant Reporting legislation
Incorporated Associations	5,762	99.60	*Associations Incorporation Act 1964*
Co-operatives	23	0.40	*Associations Incorporation Regulations 2007*
			Associations Incorporation (Model Rules) Regulations 2007
			Associations Incorporation Direction 1999
			Co-operatives Act 1999
			Travel Agents Act 1987
Total	**5,785**	**100.00**	

6.1 Reporting and Auditing Regulation – Tasmania

6.1.1 Incorporated Associations – Tasmania

Relevant authority: The financial reporting requirements for incorporated associations are found in the Associations Incorporation Act.

Requirements: Under the Tasmanian Associations Incorporation Act, unless exempted, as soon as practicable after the end of its financial year, an incorporated association is required to cause the financial affairs of the association to be audited. The Tasmanian Office of Consumer Affairs and Fair Trading has issued a publication entitled *A Guide to Audit Exemption under the Associations Incorporation Act 1964*, which indicates that associations with total revenue in any financial year of $40,000 or less and total assets (other than real property) of $40,000 or less can seek exemption. Where such an audit exemption is granted, under section 24B(1A), the financial statements, in the form of an income and expenditure statement, still need to be lodged.

6.1.2 Co-operatives – Tasmania

By virtue of section 238 of the Co-operatives Act, the financial reporting and audit for co-operatives lodging reports in Tasmania is governed by Part 2M of the Corporations Act. As a consequence, consistent with other states, the financial reporting requirements of co-operatives in Tasmania are consistent with those of companies incorporated under the Corporations Act.

7. South Australian Entities

7.1 Reporting and Auditing Regulation – South Australia

7.1.1 Incorporated Associations – South Australia

The following regulation shapes financial reporting by South Australian incorporated associations:

(a) *Associations Incorporation Act 1985*; and

(b) *Associations Incorporation Regulations 2008*.

Classes of entity for reporting: According to section 35 of the Associations Incorporation Act, the differential content of financial reports is based on whether an entity is a prescribed or non-prescribed association. Under section 35, a prescribed association means an incorporated association:

(a) that had gross receipts in that association's previous financial year in excess of:

  (i) $200,000; or

  (ii) such greater amount as is prescribed by regulation; or

(b) that is prescribed or of a class prescribed by regulation.

A prescribed association must keep its accounting records in such a manner that will enable the preparation from time to time of accounts that present fairly the results of the operations of the association; and the accounts of the association to be conveniently and properly audited.

Under section 3 of the Associations Incorporation Act, 'accounts' are taken to mean:

(a) A combination of:

  (i) an account of receipts and payments recording the total receipts and payments based on the cash method of accounting.

  (ii) a statement of assets and liabilities.

(b) A combination of:

  (i) an account of income and expenditure recording the total income and expenditure based on the accrual method of accounting.

  (ii) a balance sheet, together with such statements, reports and notes, other than auditors' reports, as are attached to and intended to be read with the account, statement or balance sheet, as the case may be.

There is no explicit indication that the accounts must be prepared in accordance with accounting standards.

7.1.2 Co-operatives – South Australia

By virtue of section 233 of the *Co-operatives Act 1997* the financial reporting and audit for these entities is governed by Part 2M of the Corporations Act. As a consequence, consistent with other states, the financial reporting requirements of co-operatives in South Australia is consistent with those of companies incorporated under the Corporations Act.

8. Western Australian Entities

8.1 Reporting and Auditing Regulation – Western Australia

8.1.1 Incorporated Associations – Western Australia

The following regulation shapes financial reporting by incorporated associations and co-operatives in Western Australia:

(a) *Associations Incorporation Act 1987*;

(b) *Associations Incorporation Regulations 1988*;

(c) *Co-operatives Act 2009*;

(d) *Charitable Collections Act 1946*; and

(e) *Travel Agents Act 1985*.

Unlike incorporated associations legislation in most other Australian states, there is no requirement in Western Australia for associations to lodge financial statements on a regular basis. The Commissioner for Consumer Protection can require financial statements to be lodged in individual cases.

There are only two things incorporated associations must do to comply with the accounting requirements of the Act: (i) keep true and accurate accounting records that explain the financial transactions and the financial position of the association in a manner that can be conveniently and properly audited; and (ii) submit accounts at each AGM, showing the financial position of the association at the end of the immediately preceding financial year.

Taxation and industrial legislation may also require financial records to be kept. In addition to these legal obligations, an association's management committee would usually need clear, accurate and up-to-date financial information to ensure the association is viable and operating efficiently (Associations Incorporation Act, s.25 to s.37).

The Act does not require accounts to be audited, but the association itself may require an audit to be carried out. This requirement would normally be specified in the rules of the association. It would be within the power of the members to pass a resolution that the accounts for a particular financial year be audited, especially if they had any reason to be concerned. Funding body agreements might also require the association's accounts to be audited to ensure that the funds provided are used according to the funding agreement and for the purpose stated in the agreement.

8.1.2 Co-operatives – Western Australia

By virtue of section 225 of the Co-operatives Act the financial reporting and audit for these entities is governed by Part 2M of the Corporations Act. As a consequence, the financial reporting requirements of co-operatives in Western Australia is consistent with those of companies incorporated under the Corporations Act.

Other specific regulations that are related to financial reporting and audit of charitable organisations and travel agents can be found in the Charitable Collections Act (s.15), and the Travel Agents Act (s.41). The common theme of these requirements is that adequate financial records must be kept that enable financial statements reporting a true and fair view to be prepared and for them to be audited.

9. Concluding Comments on Part B

This concludes the analysis of the financial reporting by entities lodging with state-based regulators. The analysis shows that requirements relating to financial reporting by these entities is primarily found in disparate state-based legislation. These disparities make the requirements difficult to synthesise and follow as a set, thus a summary of the legislation for the different classes of entities by state is provided in Appendices A to D to assist the reader.

States and territories have their own laws with different thresholds for defining tiers and different financial reporting requirements for each tier. As such, the content of the financial statements for these entities differs greatly across states. For example, Queensland thresholds are lower than those in NSW or Victoria for incorporated associations, and the proportion of incorporated associations lodging SPFSs is higher in Queensland than in NSW or Victoria. These disparities impede the comparability of the information reported across locations.

Whether these state-based entities should be required to lodge financial statements that are comparable across jurisdictions is a complex issue. On the one hand, the notion of comparability is embedded in textbooks on accounting generally and, more specifically, on financial statement analysis (White et al., 2003). Such resources invariably assert that the results of any analysis of financial statements must be interpreted in the context of some appropriate benchmark, such as previous years, similar entities or industry averages. Underpinning this is the assumption of comparable accounting and measurement of similar transactions and events across time (White et al., 2003). This, along with the established framework of accounting standards and generally accepted accounting principles (GAAP) that guide the preparation of those financial statements, explains why the financial reporting function has retained its place as a widely accepted crucial mechanism by which accountability is discharged by myriad entities.

At the same time, the entities examined in this Part of this Report, such as incorporated associations, are incorporated under specific state law. These entities are typically restricted to operating primarily within their state of incorporation. Also, given that many of these entities have little or no debt and have no publicly traded equity, conventional arguments for comparable financial reporting across jurisdictions seem more difficult to apply.

It is clear from this Part of this Report that considerable variation exists in the bases for classifying state-based entities and also in the content of the financial statements required to be lodged by these entities. Given this variation, it remains an open question as to whether the financial statements lodged by these state-based entities are enhancing the accountability of the entities within jurisdictions to the extent desired by state regulators. Further, benchmarking of reporting by entities across jurisdictions remains an elusive challenge.

The analysis provided in Part B of this Report is intended to help inform any future deliberations on which state-based entities should be required to lodge financial statements and the nature of those financial statements.

Appendix A – Web Sites

Victoria

http://www.consumer.vic.gov.au/

NSW

http://www.fairtrading.nsw.gov.au/

Queensland

http://www.fairtrading.qld.gov.au/

Tasmania

http://www.consumer.tas.gov.au/

South Australia

http://www.cbs.sa.gov.au/

Western Australia

http://www.commerce.wa.gov.au/

Appendix B – Summary of Legislation for Incorporated Associations by State

NSW	QLD	SA	TAS	VIC	WA
Tier-one Associations**:** total revenue as recorded in the income and expenditure statement for a financial year exceeds $250,000 or current assets exceed $500,000. **Reporting Implications:** Prepare financial statements in accordance with Australian Accounting Standards and these financial statements must be audited ***Tier-two Associations*****:** total revenue and current assets do not satisfy the above tests. **Reporting Implications:** Must ensure the financial statements give a true and fair view of the entity's affairs. There is no explicit requirement that the financial statements are in accordance with Australian Accounting	***Level-one Associations:*** current assets of more than $100,000 or total revenue of more than $100,000. A certified accountant or auditor must audit the financial statements. ***Level-two Associations:*** current assets between $20,000 and $100,000 and/or total revenue between $20,000 and $100,000. A certified accountant or auditor, or a person approved by the Commissioner for Fair Trading, must *verify* the financial statements. ***Level-three Associations:*** current assets of less than $20,000 and total revenue of less than	***Prescribed Associations:*** gross receipts in previous financial year in excess of $200,000; or such greater amount as is prescribed by regulation; or that is prescribed or is of a class prescribed by regulation. **Reporting Implications**: Maintain records sufficient to enable the preparation from accounts that present fairly the results of operations and have those accounts properly audited. There is no explicit requirement that the accounts need to be prepared in accordance with	An association must keep proper accounts and records of its transactions and financial affairs and shall, as soon as practical after year end, cause the reports to be audited. An exemption from this requirement is available for entities where total revenue and total assets do not exceed $40,000. **Relevant authority:** *Associations Incorporation Act 1964*	***Prescribed Associations:*** (i) gross receipts greater than $200,000; or (ii) gross assets of $500,000 or more. **Reporting Implications**: Table audited financial statements at the AGM. Specific disclosures required in line with particular accounting standards. No general requirement that financial statements be prepared in accordance with Australian Accounting Standards. ***Non-Prescribed Associations*****:** do not satisfy the above tests.	There is no requirement for associations to lodge financial statements on a regular basis. There are only two things incorporated associations must do to comply with the accounting requirements of the Act: (i) keep true and accurate accounting records that explain the financial transactions and the financial position in a manner that can be conveniently and properly audited; and (ii) submit accounts at each AGM, showing the financial position of the association at the end of the immediately

NSW	QLD	SA	TAS	VIC	WA
Standards nor that they are subject to audit. **Relevant authority:** *Associations Incorporation Act* 2009, section 43. Where Associations are also involved with Fundraising, an audit is required under section 24 of the *Charitable Fundraising Act 1991*. **FROM 2011:** With the enactment in May 2011 of Class Order 11/01, Tier-one Associations with revenues less than $2 million are relieved from full financial reporting under section 43(2). Associations in this group have the option of lesser disclosure requirements, including appropriately classified statement of income and expenditure and balance sheet; statement of movements in equity and a statement of accounting policies.	$20,000. Incorporated Associations required under the *Collections Act 1966*, *Gaming Machine Act 1991* or under any law for any other purpose must have their financial statements *audited* by a certified accountant or auditor, or person approved by the Commissioner for Fair Trading. **Reporting Implications**: The regulations do not explicitly require financial statements to be prepared in accordance with Australian Accounting Standards. **Relevant authority:** *Associations Incorporation Act 1981*	Australian Accounting Standards, ***Non-Prescribed Associations:*** do not satisfy the above test. **Relevant authority:** *Associations Incorporation Act 1985*		**Reporting Implications**: Maintain adequate accounting records. **Relevant authority:** *Associations Incorporation Regulations 2009*. **2012 ONWARDS:** Three tiers of entities: ***Tier one:*** total revenue less than $250,000; **Reporting Implications:** (refer 'Non-Prescribed Associations' above) ***Tier two:*** total revenue between $250,000 and $1,000,000. **Reporting Implications**: Prepare financial statements in accordance with Australian Accounting Standards and have them	preceding financial year. The Act does not require accounts to be audited, but the association itself may require an audit to be carried out. **Relevant authority:** *Associations Incorporation Act 1987*

NSW	QLD	SA	TAS	VIC	WA
				‘reviewed’ where required. ***Tier three***: total revenue greater than $1,000,000 (s.90). **Reporting Implications**: (refer ‘Prescribed Associations’ above) **Relevant authority:** *Associations Incorporation Reform Act 2012*	

Appendix C – Summary of Legislation for Gaming, Charitable Organisations, Patriotic Funds, Travel Agents, Funeral Services and Retirement Villages by State

NSW	QLD	SA	TAS	VIC	WA
Charitable Fundraising Act 1991 *Travel Agents Act 1986* *Retirement Villages Act 1999* *Funeral Funds Act 1996 (Amended 2003)* Acts contain additional record-keeping and audit requirements	*Collections Act 1966* *Gaming Machine Act 1991* *Retirement Villages Act 1999* *Funeral Benefit Business Act 1982* Acts contain additional record-keeping and audit requirements	*Travel Agents Act 1986* *Retirement Villages Act 1987*	*Travel Agents Act 1987* *Retirement Villages Act 2004* *Prepaid Funerals Act 2004*	*Fundraising Act 1998* *Gambling Regulation Act 2003* *Travel Agents Act 1986* *Retirement Villages Act 1986* *Veterans Act 2005* *Funerals Act 2006* Acts contain additional record-keeping and audit requirements	*Charitable Collections Act 1946* *Travel Agents Act 1985* *Retirement Villages Act 1992*

Where associations are also involved in charitable activities, gaming operations, or are patriotic funds or travel agents, additional state-based regulations are likely to apply.
One of the objectives of the *Australian Charities and Not-for-profits Commission Act 2012* (ACNC Act) has been to create uniform reporting by charities from 2014. Medium (annual revenue between $250,000 and $1,000,000) and large (revenue exceeding $1,000,000) entities are required to produce financial statements. The financial statements for medium entities may be 'reviewed' or 'audited', but financial statements for large entities must be audited.

Appendix D – Summary of Legislation for Co-operatives by State

NSW	QLD	SA	TAS	VIC	WA
As a general principle, by virtue of s.243 of the *Co-operatives Act 1992*, the financial reporting and audit for co-operatives is governed by Part 2M of the *Corporations Act 2001*. As a consequence, the financial reporting requirements applicable to co-operatives is consistent with those of companies incorporated under *The Corporations Act*. Reporting relief is available for 'small' co-operatives that satisfy the following conditions: -Assets do not exceed $700,000 and -Expenses, including costs of goods sold, do not exceed $300,000 Where such tests are met, the disclosure obligations imposed on the entity are reduced. Such entities, for	By virtue of s.232 of the *Co-operatives Act 1997*, the financial reporting and audit for co-operatives is governed by Part 2M of the *Corporations Act 2001*. As a consequence, the financial reporting requirements applicable to co-operatives is consistent with those of companies incorporated under the Act. **Relevant Authority:** *Co-operatives Act 1997*	As a general principle, by virtue of s.233 of the *Co-operatives Act 1997* the financial reporting and audit for co-operatives is governed by Part 2M of the *Corporations Act 2001*. As a consequence, the financial reporting requirements applicable to co-operatives is consistent with those of companies incorporated under the Act. **Relevant Authority:** *Co-operatives Act 1997*	As a general principle, by virtue of s.238 of the *Co-operatives Act 1999*, the financial reporting and audit for co-operatives is governed by Part 2M of the *Corporations Act 2001*. As a consequence, the financial reporting requirements applicable to co-operatives is consistent with those of companies incorporated under the Act. **Relevant Authority:** *Co-operatives Act 1999*	As a general principle, by virtue of s.238 of the *Co-operatives Act 1996*, the financial reporting and audit for co-operatives is governed by Part 2M of the *Corporations Act 2001*. As a consequence, the financial reporting requirements applicable to co-operatives is consistent with those of companies incorporated under the Act. **Relevant Authority:** *Co-operatives Act 1996*	As a general principle, by virtue of s.225 of the *Co-operatives Act 2009* the financial reporting and audit for co-operatives is governed by Part 2M of the *Corporations Act 2001*. As a consequence, the financial reporting requirements applicable to co-operatives is consistent with those of companies incorporated under the Act. **Relevant Authority:** *Co-operatives Act 2009*

NSW	QLD	SA	TAS	VIC	WA
example, need not prepare a statement of cash flows. Small co-operatives with revenue less than $250,000 may have their financial statements reviewed instead of audited. **Relevant Authority:** *Co-operatives Act 1992*					

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