Australian Government
Australian Accounting Standards Board

Staff Paper

Project:	**Not-for-Profit Private Sector Financial Reporting Framework**	**Meeting:**	M188
Topic:	**Tier 3 – Approach to developing disclosure requirements**	**Agenda Item:**	12.3.1
		Date:	6 June 2022
Contact(s):	Ao Li ali@aasb.gov.au Fridrich Housa fhousa@aasb.gov.au	**Project Priority:**	High
		Decision-Making:	High
		Project Status:	Initial deliberations

The objective of this paper

1 The objective of this staff paper is for the Board to decide its preliminary views, for the purpose of the discussion paper (DP), on the approach to developing Tier 3 disclosure requirements for not-for-profit (NFP) private sector entities.

2 Agenda Paper 12.3.2 presents draft disclosure requirements for three key topics and staff preliminary consideration on the method to develop disclosure requirements for other key topics[1] to be included in the DP to illustrate the application of the staff recommended approach to developing draft disclosures for transactions covered in the Tier 3 Standard.

Background and reasons for bringing this paper to the Board

3 At its February 2021 meeting, the Board agreed to develop a further reporting Tier (Tier 3) for application by NFP private sector entities. Several staff papers have been presented, including the approach to simplification agreed by the Board at its August 2021 Board meeting,[2] as shown in Appendix A of Agenda Paper 12.1. The Board has made a number of tentative decisions to date in developing the Tier 3 accounting requirements. These decisions are summarised *in The Not-for-Profit Private Sector Financial Reporting Framework Project Summary*.

4 This staff paper discusses the approach to developing the disclosure requirements for the proposed Tier 3 general purpose financial statements (GPFS) for NFP private sector entities. Disclosure requirements play a complementary role in simplified recognition and measurement (R&M) requirements. Staff, therefore, think the Board should form preliminary views on this topic to include in the DP before further considering R&M requirements in the next stage of the project (e.g. an exposure draft (ED)). The DP would include the Board's preliminary views on key aspects of Tier 3 reporting requirements, including the disclosure requirements for key T3

1 See Agenda Paper 4.1 (M182) August 2021 for the scope of key topics, for the purpose of the DP, to be included in the Tier 3 Standard. For other possible future topics likely to be included in the Tier 3 requirements that have been not identified to date as an area of significant interest by stakeholders and beyond terminology and language where staff have not identified any specific areas for simplification, staff plan to bring suggested drafting for these topics, primarily based on the NZ PBE SFR – A (NFP), for the Board's consideration in the next stage of the project (e.g. an exposure draft (ED)).

2 Refer minutes of the 182nd AASB meeting.

topics[3], to seek stakeholders' feedback on the approach the Board intends to take when developing the ED.

5 Staff noted that presentation and disclosure requirements are combined in some Australian Accounting Standards (AAS). In some instances, the term 'disclosure' encompasses items presented in the primary financial statements (PFS).[4] In this paper, disclosure requirements refer to those requirements that permit information to be presented either in the PFS or disclosed in the notes.[5]

Structure of the paper

6 This paper is structured as follows:

(a) summary of staff recommendations (paragraphs 7 – 8);

Current accounting requirements and whether there is a reason for the Board to address

(b) current requirements under Australian Accounting Standards (paragraphs 9 – 10);

(c) Australian legislative requirements (paragraph 11);

(d) summary of approaches taken by selected other jurisdictions and reporting frameworks (paragraphs 12 – 16);

(e) feedback from Australian stakeholders (paragraphs 17 – 19);

(f) findings from academic research and other literature (paragraphs 20 – 22)

Considering options for simplifications and staff analysis and recommendation

(g) options for the approach to developing Tier 3 disclosure requirements (paragraphs 23 – 29);

(h) evaluation of options against the tier 3 development principles (paragraph 30);

(i) staff recommendations (paragraph 31)

Summary of staff recommendations

7 For transactions covered in Tier 3 requirements, staff recommend the Board, for the purpose of the DP and with reference to the approach to simplification agreed by the Board at its August 2021 Board meeting,[6] adopt the following approach (illustrated in Figure 1 below) to determine the disclosure requirements:

(a) For transactions with no R&M difference between the Tier 2 and Tier 3 reporting requirements (i.e. R&M requirements for Tier 3 are the same or similar to the corresponding R&M requirements for Tier 2), use the disclosure requirements in AASB 1060 *General Purpose Financial Statements – Simplified Disclosures for For-Profit*

3 Key topics include change in accounting policies and accounting for errors, income including revenue, financial instruments, leases, investment property, impairment of non-current assets and employee benefits. Refer to Agenda Paper 4.1 (M182) August 2021.

4 See paragraph 48 of AASB 101 *Presentation of Financial Statements*. For example, although AASB 119 *Employee Benefits* does not require specific disclosures about short-term employee benefits. AASB 101 *Presentation of Financial Statements* requires employee benefits expenses to be presented in the statement(s) of profit or loss, which is considered as a case where presentation and disclosure requirements are combined.

5 Consistent with the IASB’s approach in developing its Exposure Draft ED/2021/7 *Subsidiaries without Public Accountability: Disclosures*, presentation requirements are the requirements for information to be included in the primary financial statements (PFS) (see paragraph BC39 of ED/2021/7). Any requirements in current Australian Accounting Standards (AAS) or proposed requirements for Tier 3 to provide comparative information in an entity’s PFS would be part of the presentation requirements rather than the disclosure requirements.

6 Refer to Appendix A in Agenda Paper 12.1

and Not-for-Profit Tier 2 Entities as a starting point and consider further tailoring (e.g. simplification) for Tier 3 as appropriate (e.g. via benchmarking with selected overseas jurisdictions and/or feedback on the DP consultation) **(Method 1)**;

As part of the consultation, staff recommend the Board seek stakeholders' feedback on whether amendments (e.g. simplifications) to AASB 1060 disclosure requirements are needed for Tier 3 entities on topics:

(i) covered in the DP as part of the key topics,[7] and there are no R&M differences between Tier 3 and upper tiers;

(ii) included in AASB 1060 but not covered in the DP (e.g., disclosure-only topics such as related party transactions);[8] and

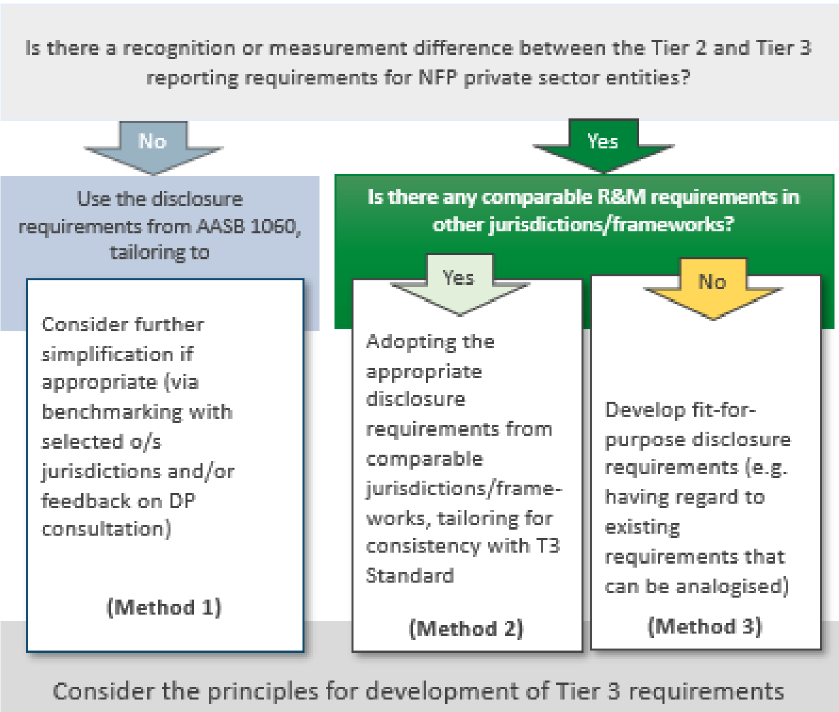
(iii) if yes to (i) and (ii) above, which specific disclosure requirements should be further amended (e.g. simplified) and why.

(b) For transactions where there is an R&M difference between Tier 3 and Tier 2 reporting requirements for NFP private sector entities:

(i) adopt appropriate disclosure requirements from comparable jurisdictions/frameworks with comparable R&M requirements **(Method 2)**; or

(ii) develop fit-for-purpose disclosure requirements (e.g. using the existing disclosure requirements for topics whose R&M requirements could be analogised to the Tier 3 topics as the base to develop fit-for-purpose Tier 3 disclosures) if there are no comparable R&M requirements in other jurisdictions/frameworks **(Method 3).**

Figure 1 Staff Recommendation - approach to develop Tier 3 disclosure requirements for topics included in Tier 3 reporting



7 See footnote 3.

8 The topic of related party transactions is not included in the draft DP as it is a disclosure-only topic with no R&M differences between Tier 3 and upper tiers. Initial feedback from targeted stakeholders has suggested broad support to align Tier 3 related party definition and disclosures with those of Tier 2. Most stakeholders agreed that related party transactions are common even among small NFP entities and broadly supported the proposal to require the same level of disclosure for Tier 3 entities as upper Tiers. See Agenda Paper 5.1 (M177) September 2020 (Key matter 9 Related Party disclosures, page 10 and 25).

8 For disclosure requirements for topics not covered by Tier 3 requirements, staff recommend the Board for the DP to adopt the same approach to applying accounting policies for topics omitted in Tier 3 requirements.[9]

Current requirements under Australian Accounting Standards

9 Under AASB 1053 *Application of Tiers of Australian Accounting* Standards, NFP private sector entities shall comply with Tier 2 reporting requirements, as a minimum, when preparing the general purpose financial statements (GPFS). Tier 2 disclosure requirements are set out in AASB 1060 and are the minimum disclosures required to be included in GPFS. Entities may include additional disclosures using Tier 1 reporting requirements as a guide if, in their judgement, such additional disclosures are consistent with the objective of GPFS.

10 AASB 1060 was developed using a bottom-up approach, starting from an established framework for similar-sized entities, in this case, the *IFRS for SMEs* Standard, and adjusted where necessary, based on the premise that: [10]

(a) the disclosure in the *IFRS for SMEs* Standard should be retained where the R&M requirements and options are the same or similar in the *IFRS for SMEs* and full IFRS Standards;

(b) where R&M requirements or options in the *IFRS for SMEs* Standard are not available in full IFRS Standards, the related disclosure will be removed; and

(c) where the R&M measurement principles in full IFRS Standards are significantly different from those in the *IFRS for SMEs* Standard or certain topics are not addressed in the *IFRS for SMEs Standard*, disclosures may be added.

When determining whether to add disclosures to AASB 1060, the AASB uses the principles[11] applied by the IASB in developing the disclosures in the *IFRS for SMEs* Standard.

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9 The Board decided to propose that entities in the scope of Tier 3 should apply the requirements of a higher tier of AAS in full for transactions not covered by the Tier 3 reporting requirements. Where transactions are also not covered in Tier 1 or Tier 2 requirements, judgement would be required to determine an accounting policy. Entity management would need to consider the applicability of the following sources, in descending order: (a) the principles and requirements in Tier 3 reporting requirements dealing with similar and related transactions or events; and (b) the definitions, recognition criteria and measurement concepts for assets, liabilities, income and expenses in the Conceptual Framework, to the extent they do not conflict with the Tier 3 reporting requirements. In making the judgement, management could also consider the most recent pronouncements of other standard-setting bodies that use a similar conceptual framework, other accounting literature and accepted industry practices, to the extent these do not conflict (see Minutes of the 183rd meeting (Sep 2021) of the AASB).

10 Paragraphs BC34 – BC55 of AASB 1060.

11 In determining what disclosures to add to AASB 1060, the following principles have been applied by the Board, which are consistent with those applied by the IASB in developing the disclosures in the *IFRS for SMEs* Standard:

(a) users of the financial statements of for-profit entities that are not publicly accountable entities are particularly interested in information about short-term cash flows and about obligations, commitments, or contingencies, whether or not recognised as liabilities. Thus, disclosures in full IFRS Standards that provide this sort of information are necessary;

(b) users of the financial statements of for-profit entities that are not publicly accountable entities are particularly interested in information about liquidity and solvency. Thus, disclosures in full IFRS Standards that provide this sort of information are necessary;

(c) information on measurement uncertainties is important;

(d) information about an entity's accounting policy choices is important;

(e) disaggregation of amounts presented in the financial statements of for-profit entities that are not publicly accountable entities are important for an understanding of those statements; and

(f) some disclosures in full IFRS Standards are more relevant to investment decisions in public capital markets than to the transactions and other events and conditions encountered by typical for-profit entities that are not publicly accountable entities.

Australian legislative requirements

11 Staff noted that some disclosure requirements in AASB 1060 are also applicable to NFP private sector entities preparing to prepare special purpose financial statements (SPFS).[12] Section 60.30 of the *Australian Charities and Not-for-profits Commission Regulation 2013* (ACNC Regulation) lists the full presentation and disclosure requirements in the compulsory standards for charities preparing SPFS. Recent changes to ACNC Regulation give charities preparing SPFS the option to apply the simplified disclosure requirements in AASB 1060.[13] From 2023 reporting periods onwards, instead of the full presentation and disclosure requirements in the compulsory standards for SPFS listed in section 60.30 of the ACNC Regulation,[14] charities can choose to apply the relevant paragraphs from AASB 1060. Charities that choose to comply with the AASB 1060 must comply with all the relevant requirements in AASB 1060 for the six compulsory standards for SPFS that entities preparing SPFS must comply with, and the additional disclosures in AASB 1054.

Summary of approaches taken by selected other jurisdictions and reporting frameworks

12 The disclosure requirements in New Zealand's PBE SFR-A (NFP) were developed using a top-down approach,[15] starting from the PBE standards and simplifying a number of disclosure requirements.[16] Disclosure requirements were developed following the general approach that PBE SFR-A (NFP) should be simplified by creating a single, short, and simple standard written in less technical language than is normally found in accounting standards.

13 The disclosure requirements in the *IFRS for SMEs* are substantially reduced from the disclosure requirements in full IFRS.[17] The requirements were developed using broadly based on principles focusing on users' needs and cost-benefit considerations.

14 IASB issued the Exposure Draft ED/2021/7 *Subsidiaries without Public Accountability: Disclosures* (ED/2021/7) in July 2021. ED/2021/7 proposed an optional IFRS Standard that would specify which disclosure requirements would apply to subsidiaries that do not have public accountability and whose parent produces consolidated financial statements available for public use that comply with the IFRS Standards. ED/2021/7 addresses the subsidiaries' needs to use the R&M requirements in the IFRS Standards for consolidation with their parents,

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12 For example, the Australian Charities and Not-for-Profits Commission (ACNC) allow medium and large charities, those with total annual revenue of AUD 250,000 or more, to prepare SPFS if they are not a 'reporting entity'.

13 Refer to *Standards and Financial Reporting, ACNC* for detail.

14 Paragraphs 1 – 6 (i.e. objective of, application of, and definitions of specific terms within AASB 1054), paragraphs 9 – 9B (i.e. disclosure about general purpose or special purpose financial statements) and paragraph 17 (i.e. IFRS Standard not yet issued in Australia) of AASB 1054.

15 The top-down approach refers to the approach that new disclosures are developed starting from the top of the range requirements and remove or simplify the requirements not applicable to the targeted entity group.

16 Paragraphs 12 – 14 of the NZXRB Invitation to Comment *Exposure Draft Public Benefit Entity Simple Format Reporting (Accrual) for Not-for-Profit Entities*.

17 The reduced disclosure includes:

(a) some disclosures are not included because they relate to topics covered in IFRS Standards that are omitted from the *IFRS for SMEs* Standard (as per paragraph BC88 of *IFRS for SMEs* Standard 2015 – Part B);

(b) some disclosures are not included because they relate to R&M principles in full IFRSs that have been replaced by simplifications in the *IFRS for SMEs* Standard (as per paragraphs BC98–BC136 of the *IFRS for SMEs* Standard 2015 – Part B);

(c) some disclosures are not included because they relate to options in full IFRS Standards that are not included in the *IFRS for SMEs* Standard (as per paragraphs BC84–BC86 of the *IFRS for SMEs* Standard 2015 – Part B); and

(d) some disclosures are not included on the basis of users’ needs or cost-benefit considerations (as per paragraphs BC44–BC47, BC157 and BC158 of the *IFRS for SMEs* Standard 2015 – Part B).

but with reduced disclosure requirements. Depending on whether recognition or measurement differences exist between IFRS Standards and the *IFRS for SMEs* Standard, proposed disclosure requirements in the ED either:

(a) use the disclosure requirements from the *IFRS for SMEs* Standard when there is no difference in R&M requirements between IFRS Standards and the *IFRS for SMEs* Standard; or

(b) tailor IFRS Standards' disclosure requirements when there is a difference in R&M between IFRS Accounting Standards and the *IFRS for SMEs* Standard. To tailor the disclosure requirements, IASB applied the same principles used for the development of disclosure requirements in the *IFRS for SMEs* Standard. [18]

15 As part of the second comprehensive review, the IASB tentatively decided in its April 2022 meeting to propose amendments to update disclosure requirements in sixteen sections of the current *IFRS for SMEs* Standard. For the development of the disclosure requirements proposals, the IASB tentatively decided to align the disclosure requirements in the *IFRS for SMEs* Standard with ED/2021/7 for certain sections in the *IFRS for SMEs* Standard. These sections are those where the IASB tentatively decided to align the R&M requirements in *IFRS for SMEs* Standard with the IFRS Accounting Standards.[19]

16 Staff have not identified any specific approaches taken by selected other jurisdictions in developing the relevant disclosure requirements for their proportionated reporting framework for NFP private sector entities.[20]

Feedback from Australian stakeholders

17 In the AASB NFP Project Advisory Panel (NFP PAP) meeting held on 17 May 2021[21], many NFP PAP members supported the proposed approach to develop Tier 3 disclosure requirements and considered it appropriate. Two panel members commented that the draft disclosure for changes in accounting policies (Example A) could be further simplified. These panel members suggested simplification be achieved by not requiring entities to disclose the amount of the adjustment for each financial statement line item affected for the current period and in the aggregate for all affected prior periods, to the extent practicable.[22] These panel members questioned the benefit of this draft disclosure requirement. They considered that if the intent

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18 See footnote 11.

19 Agenda paper 30A, *Towards an exposure draft – align disclosure requirements with IFRS Accounting Standards*

20 For the purposes of this staff paper, the disclosure requirements from the following jurisdictions (reporting framework) were reviewed and considered:

(a) International Financial Reporting Standard for Small and Medium-sized Entities (*IFRS for SMEs*).

(b) IFRS Standards Exposure Draft ED/2021/7 *Subsidiaries without Public Accountability: Disclosures* (ED/2021/7)

(c) New Zealand Public Benefit Entity Simple Format Reporting – Accrual (Not-For-Profit) (NZ PBE SFR – A (NFP)).

(d) Financial Reporting Standard 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland (UK FRS 102).

(e) Financial Reporting Standard 105 The Financial Reporting Standard applicable to the Micro-entities Regime (UK FRS 105).

(f) Accounting and Reporting by Charities: Statement of Recommended Practice applicable to charities preparing their accounts in accordance with the Financial Reporting Standard applicable in the UK and Republic of Ireland (UK Charities SORP).

(g) Singapore Charities Accounting Standard (Singapore CAS).

(h) Hong Kong Small and Medium-sized Entity Financial Reporting Framework and Financial Reporting Standard (HK SME-FRF & SME-FRS).

21 Refer Agenda Paper 12.4 *Not-for*-Profit *Project Advisory Panel minutes from 17 May 2022 meeting*.

22 See Example C in Agenda Paper 12.3.2 – draft disclosure requirements paragraph 1(c) for change in accounting policy.

for the disclosure is to provide information comparing the application of the new accounting policy to the previous accounting policy applied, then the information is not relevant and only adds to the cost of preparation for smaller NFP entities.

18 A stakeholder (regulator) provided additional comments after the NFP PAP meeting. This stakeholder suggested further simplifying the draft disclosure requirements for lessees and lessors by streamlining the disclosure of future lease payments by not requiring disclosure of future lease payments for three periods, namely a period not later than one year, later than one year and not later than five years, and later than five years).[23] Staff have not recommended any further simplification for these disclosures at this stage and recommended the Board, as part of the consultation, to seek stakeholders' feedback on whether further simplifications should be considered.

19 This stakeholder also suggested amending the draft disclosure requirements for prior period errors by specifying how the error occurred. The stakeholder suggested this approach would help users understand what the error is and how it took place (e.g. it can be due to any fraudulent activities discovered by the charity later).

Findings from academic research

20 AASB Research Report 16 *Financial Reporting by Non-corporate or Small Entities* reviews a number of academic studies examining the current practice of financial reporting of NFP entities. These studies highlighted the importance and deficiencies in NFP reporting regarding consistency, efficiency and transparency. For example, Hudack and Tyler (2004) suggest that an effective financial report for NFP entities should communicate useful information about the entity to facilitate rational decisions by its important constituents regarding economic issues.[24] Parsons (2007) and Yetman & Yetman (2012) suggest stakeholders rely on the financial disclosures of an organisation to make economic decisions in terms of whether to provide funds to an organisation or to withdraw their support from the organisation. The extent to which an organisation is considered financially accountable is directly influenced by how its financial disclosure facilitates decision-making (Hyndman et al. 2004).[25] This academic research confirms the importance of understanding the stakeholders' needs when developing the disclosure requirements for Tier 3 entities.

21 A more recent study by Ghoorah (2019) suggests that the public perceives financial disclosures related to the source of fund inflows, mission-related expenses and financial sustainability to be relatively important disclosures for NFP entities.[26] The study also found that respondents interested in financial disclosures may not necessarily have sufficient financial knowledge to understand a majority of the disclosure provided within financial statements. The author suggested that entities could use more user-friendly presentations, such as graphs, charts and pictures, to supplement financial statement information and facilitate users' information needs.

22 Staff have not identified any specific study evaluating the approaches to developing disclosure requirements for the NFP sector. However, a study examining the association between IFRS disclosure requirements and the cost of capital for Australian for-profit entities suggests that more choices or greater flexibility in disclosure requirements would reduce the amount of

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23 See Example B in agenda paper 12.3.2 – draft disclosure requirements paragraph 1(a) for lessees and lessors.

24 Hudack, LR and Tyler, ML (2004) 'A Survey of Accounting and Finance Faculty about Financial Reporting at a NFP University', *Journal of Accounting & Finance Research*, 12(6): 94-105

25 Hyndman, N, McKillop, D, Ferguson, C, and Wall, T (2004) 'The financial accountability of Irish Credit Unions: An initial empirical study', *Financial Accountability & Management*, 20(3), 253–279. doi:10.1111/j.0267-4424.2004.00385.x

26 Ghoorah, U. (2019) 'Chapter 2 Accountability via Financial Disclosures: An Exploration of the Public's Perceptions', *Modernization and Accountability in the Social Economy Sector, A volume in the Advance in Finance*, Accounting and Economics (AFAE) Book Series, Hershey, PA.

important information in the financial statements. Greater flexibility in disclosure requirements would require higher levels of judgement, which could be difficult to apply by preparers, assure by auditors and enforce by regulators.[27]

Options for the approach to developing Tier 3 disclosure requirements

23 In its April 2021 meeting, the Board decided that, for Tier 3 disclosure requirements, consistency with the accounting principles specified by AASB 1060 is desirable but might not always be warranted. Tier 3 requirements are being developed as a proportionate response to the costs incurred by certain entities whilst still meeting users' needs of the financial statements for this cohort of entities. For example, opportunities for deviation from Tier 2 accounting principles that could give a similar outcome to users while reflecting an appropriate cost/benefit balance could include disclosure requirements instead of a Tier 2 measurement requirement or an approach of specifying minimum 'prescriptive' disclosures.[28]

24 With reference to the 'Approach to simplification' flowchart in Appendix A of Agenda Paper 12.1, the principle in paragraph 23 above, the staff analysis considers current practice in Australia and international jurisdictions, feedback received from stakeholders, and the findings summarised in paragraphs 9 to 22 above. Staff have presented the options for approach to developing Tier 3 disclosure requirements in Figure 2 – *Options for approach to developing Tier 3 disclosure requirements*, regarding:

(a) which is the appropriate approach to developing Tier 3 disclosure requirements for topics to be included in Tier 3 requirements – considered in this staff paper (Table 1). This information is represented by the **red box** in the flowchart. Staff recommendations are shaded in **yellow**;

(b) the draft disclosure requirements for key topics to be included in the DP – considered in Agenda Paper 12.3.2.

25 Agenda Paper 12.3.2 presents draft disclosure requirements for three key topics and staff preliminary consideration on the method to develop disclosure requirements for other key topics to be included in the DP to illustrate the application of the staff recommended approach to developing draft disclosures for transactions covered in the Tier 3 Standard.

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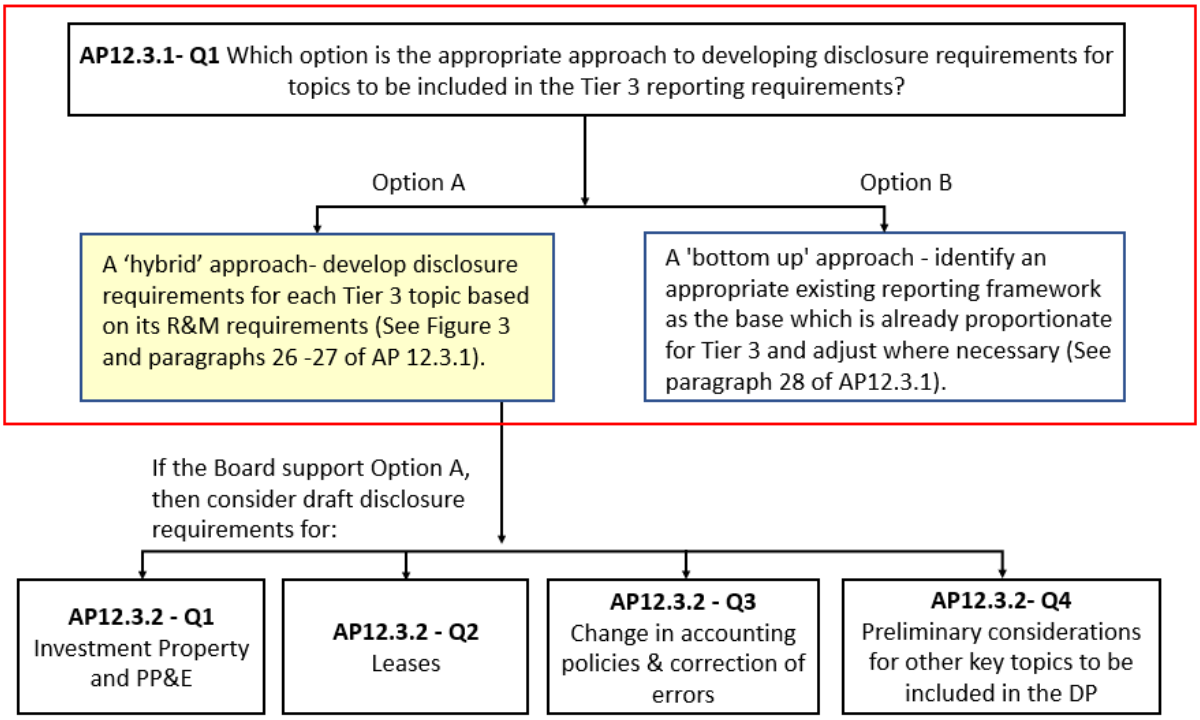
27 Saha, and Bose, S. (2021) 'Do IFRS disclosure requirements reduce the cost of capital? Evidence from Australia', *Accounting and Finance*, doi: 10.1111/acfi.12744. Stakeholder feedback on the IASB Exposure Draft ED/2021/3 *Disclosure Requirements in IFRS Standards A Pilot Approach* agrees with this study finding that greater flexibility in disclosure requirements may lead to loss of detailed information required by users and reduce the comparability of financial statements.

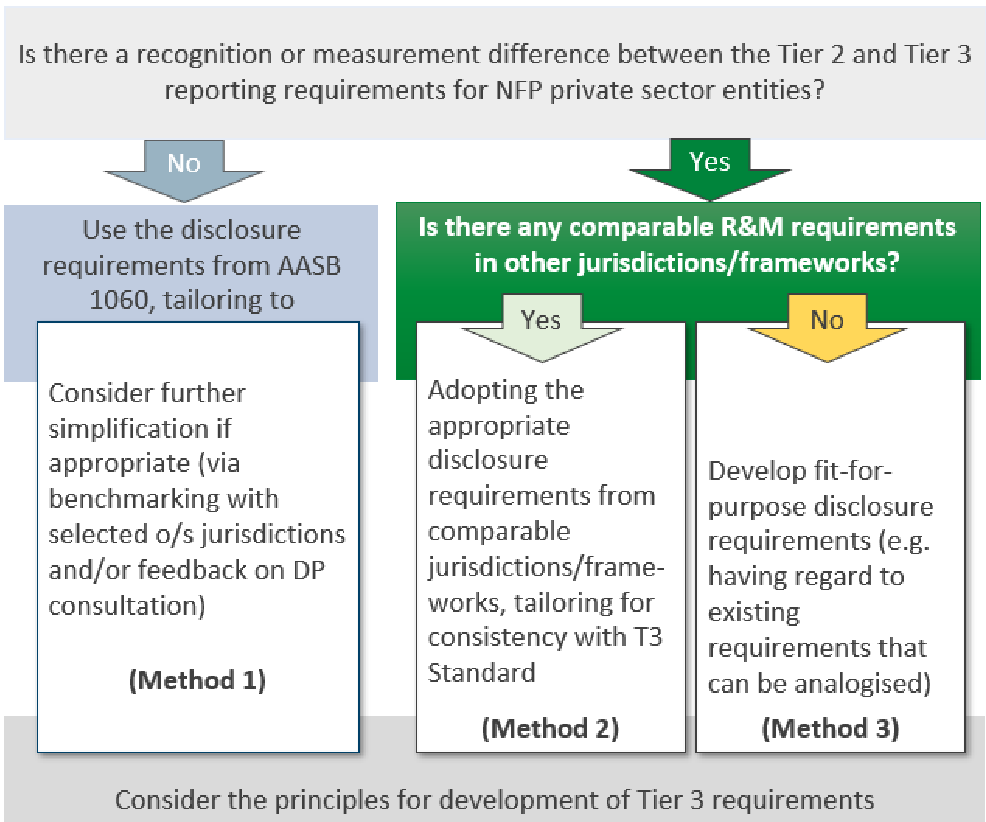
28 Minutes of the 180th meeting of the AASB, April 2021.

Figure 2 Options for approach to developing Tier 3 disclosure requirements



Option A

Figure 3 Summary of Option A – a 'hybrid' approach to develop disclosure requirements for topics to be in the Tier 3 reporting requirements



26 As shown in Figure 3 above, Option A[29] proposes a hybrid approach to develop disclosure requirements for topics included in the Tier 3 Standard based on their R&M requirements, with the following principle:

(a) For transactions with no R&M difference between the Tier 2 and Tier 3 reporting requirements (i.e. R&M requirements for Tier 3 are the same or similar to the corresponding R&M requirements for Tier 2), use the disclosure requirements in AASB 1060 as a starting point and consider further tailoring (e.g. simplification) for Tier 3 as appropriate (e.g. via benchmarking with selected overseas jurisdictions and/or feedback on the DP consultation) (**Method 1**).

As part of the consultation, staff recommend the Board seek stakeholders' feedback on whether amendments (e.g. simplification) to AASB 1060 disclosure requirements are needed for Tier 3 entities on topics:

(i) covered in the DP as part of the key topics,[30] and there are no R&M differences between Tier 3 and upper tiers;

(ii) included in AASB 1060 but not covered in the DP (e.g. disclosure-only topics such as related party transactions);[31] and

(iii) if yes to (i) and (ii) above, which specific disclosure requirements should be further simplified and why;

(b) for transactions where there is an R&M difference between Tier 3 and Tier 2 reporting requirements for NFP private sector entities:

(i) adopting appropriate disclosure requirements from comparable jurisdictions/frameworks if there is comparable R&M requirement in other jurisdictions/frameworks (**Method 2**); or

(ii) developing fit-for-purpose disclosure requirements (e.g. using the existing disclosure requirements for topics whose R&M requirements could be analogised to the Tier 3 topics as the base for developing fit-for-purpose Tier 3 disclosures) if there is no comparable R&M requirement in other jurisdictions/frameworks (**Method 3**).

27 As summarised in Figure 3 above, method 1 – 3 under Option A will be applied in line with the principles for developing Tier 3 requirements (see Appendix A in Agenda Paper 12.1).

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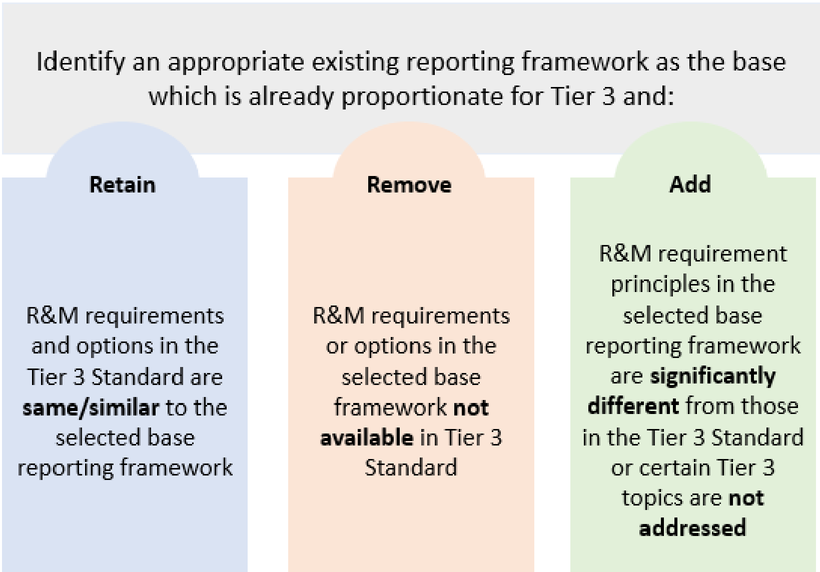
29 Both Option A and Option B are subject to aligning the terms and language with Tier 3 reporting requirements.

30 See footnote 3.

31 The topic of related party transactions is not included in the draft DP as it is a disclosure-only topic with no R&M differences between Tier 3 and upper tiers. Initial feedback from stakeholders has suggested there is broad support to align Tier 3 related party definition and disclosures with those of Tier 2. Most stakeholders agreed that related party transactions are common even among small NFP entities and broadly support for the proposal to require the same level of disclosure for Tier 3 entities as upper Tiers. See Agenda Paper 5.1 (M177) September 2020 (Key Matter 9 Related Party Disclosures, page 10 and 25).

Option B

Figure 4 Summary of Option B – a 'bottom-up' approach to develop disclosure requirements for topics to be in the Tier 3 reporting requirements



28 As an alternative to the approach proposed by staff in paragraph 26, the Board could instead adopt the 'bottom up' approach used in developing AASB 1060 (see paragraph 10), as summarised in Figure 4. This approach requires identifying an appropriate existing reporting framework as the base which is already proportionate for Tier 3 (e.g. a reporting framework developed for entities that are similar in size and nature with Tier 3) and adjust where necessary, based on the premise that:

(a) the disclosures in the selected base reporting framework should be **retained** where the R&M requirements and options are the same or similar in the Tier 3 Standard and the selected base reporting framework;

(b) the related disclosure should be **removed** where R&M requirements or options in the selected base reporting framework are not available in Tier 3 Standard; and

(c) disclosures should be **added** where the R&M requirement principles in the selected base reporting framework are significantly different from those in the Tier 3 Standard or certain Tier 3 topics are not addressed in the selected base reporting framework.

29 Table 1 below summarises staff analysis of the options on the approach to developing Tier 3 disclosure requirements.

Table 1 Possible Options for Tier 3 - Approach to develop Tier 3 Disclosure Requirements

Possible options for Tier 3 – approach to developing disclosure requirements	**Support for the approach**	**Arguments against this approach**
Option A: **A hybrid approach – develop disclosure requirements for each topic to be included in Tier 3 reporting requirements based on its R&M requirements.** (Similar to the approach adopted by IASB Exposure Draft ED/2021/7).	• Aligns with the overall approach to simplification agreed by the Board to develop Tier 3 Standards. • Maintains consistency and comparability with Tier 1/Tier 2 reporting requirements where relevant. Using AASB 1060 as the base to develop Tier 3 disclosure requirements would not create significant divergence from current reporting practices and would make the transition to Tier 3 Standard more smooth. • Recognises the differences in R&M requirements between Tier 3 and upper tiers, and allows the development of appropriate disclosure requirements to accompany the simplified R&M requirements for Tier 3 entities. • Allows more flexibility in identifying disclosures for Tier 3 circumstances compared to Option B.	• It can be challenging to identify users and users' needs in the NFP private sector. • May depart from Tier1/2 reporting requirements, particularly if disclosure requirements are developed based on overseas jurisdictions' requirements. • Practitioners may be unfamiliar with disclosure requirements originated from other international pronouncements, which would introduce unnecessary complexity for preparers and additional transition/education costs, which is not desired.
Option B: **'Bottom-up' approach – using an existing reporting framework and adjusting disclosures for Tier 3, where relevant.** (Approach adopted by AASB 1060).	• Maintains consistency with the approach used to develop proportionated disclosure requirements in AAS. • Arguably, it would be easier to specify disclosures that are already required by existing reporting requirements than to develop fit-for-purpose disclosure requirements based on users' needs (where needed), particularly noting the challenges in identifying users and users' needs in the NFP private sector.	• It can be challenging to identify an appropriate base from which to build up Tier 3 requirements. Based on the AASB research conducted to date, a limited number of accounting pronouncements are targeted at smaller entities. Identified pronouncements that could be potentially used as the base framework include NZ PBE SFR – A (NFP), UK FRS 102, UK FRS 105, Singapore CAS, and HK SME-FRF & SME-FRS.[32] However, staff think it would not be appropriate to start with any of these as a base to the extent the Board is not basing its Tier 3 reporting requirements on any of these pronouncements in their entirety. • May significantly depart from Tier1/2 reporting requirements if a non-IFRS-based framework is adopted. • Practitioners may be unfamiliar with other international pronouncements, which would introduce unnecessary complexity for preparers and additional transition/education costs, which is not desired.

32 Staff consider that AASB 1060 would not be an appropriate base framework for Option B. Under Option B, as discussed in paragraph 0, an appropriate base under Option B should be an existing reporting framework that is already proportionate for Tier 3 (e.g. a reporting framework developed for entities that are similar in size and nature with Tier 3).

Evaluation of options against the Tier 3 develop principles

30 With reference to the 'Approach to simplification' flowchart in Appendix A of Agenda Paper 12.1 and the analysis in Table 1 above, staff also analysed each of the proposed options against the tentative Tier 3 principles previously agreed to by the Board members. Staff consider that Option A does broadly align with the Tier 3 principles, but Option B does not, as listed below:

Principle	Staff assessment
Consistency with the accounting principles specified in Tier 2: Australian Accounting Standards – Simplified Disclosures is desirable but might not always be warranted since Tier 3 requirements are being developed as a proportionate response.	Option B does not align with Tier 2 accounting principles if a non-IFRS-based framework is adopted as the base to develop Tier 3 disclosure requirements.

Staff recommendation

31 Based on the analysis above, staff recommend the Board adopt Option A as detailed in paragraph 26 to develop disclosure requirements for Tier 3 entities. This would:

- align with the approach to simplification agreed by the Board to develop Tier 3 Standards;
- allow the development of appropriate disclosure requirements to accompany the simplified R&M requirements for Tier 3. Staff consider that, when R&M differences exist, it would be inappropriate to use the disclosure requirements in AASB 1060 without tailoring;
- maintain consistency and comparability with Tier 1/Tier 2 reporting requirements, where relevant. Accounting professionals in the NFP sector are familiar with the existing reporting framework. Staff acknowledge that disclosure requirements may depart from upper tiers for some topics.[33] However, staff think departure may be justified regarding less well-resourced Tier 3 entities that demand simplified disclosures to save preparation costs; and
- maintain the usefulness of financial statements to users as simplifications to the disclosures will be determined by common users' needs.

Question to the Board:

Do Board members agree with staff recommendation for the DP to adopt the approach detailed in paragraph 26 (Option A) to develop disclosure requirements for Tier 3 NFP private sector entities?

If not, do Board members prefer Option B? If not, which approach do Board members prefer?

33 For example, for topics where disclosure requirements are further simplified even when there is no R&M difference between Tier 3 and upper tiers.