



<b>Project:</b>	<b>Conceptual Framework</b>	<b>Meeting</b>	AASB December 2017 (M161)
<b>Topic:</b>	<b>Implementation Issues</b>	<b>Agenda Item:</b>	10.1
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## Introduction and objective of this paper

- 1 The objective of this paper is to obtain Board decisions in relation to the potential impact that the forthcoming revised IASB *Conceptual Framework* may have on Australian Accounting Standards, including:
  - (a) whether to amend AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*;
  - (b) whether the effective date for the revised *Conceptual Framework* should be staggered for different sectors in Australia in relation to its implications for the nature of reporting entities; and
  - (c) amending the definition of public accountability.
- 2 This paper is structured as follows:
  - (a) summary of staff recommendations; and
  - (b) staff analysis.

## Summary of staff recommendations

- 3 Staff recommend the following:
  - (a) amendment of AASB 108 is not required until all references to the *Framework* in the Standards are updated to the revised (IASB) Conceptual Framework;
  - (b) the Board supports the proposed staggered effective dates of the revised *Conceptual Framework* for different sectors in Australia; and

- (c) amendment of the definition of public accountability when the revised *Conceptual Framework* applies to publicly accountable for-profit private sector entities.

## Staff analysis

### Background

- 4 In 2013, the IASB started its latest phase of the project to revise the *Conceptual Framework for Financial Reporting (Conceptual Framework)*. The IASB decided to revise the *Conceptual Framework* on the basis that some important issues are not covered, some guidance is unclear and some guidance is out of date.
- 5 The IASB developed proposals to provide a more complete, clear and up-to-date set of underlying concepts for IFRS Standards. After considering feedback from entities, investors and regulators, the IASB is finalising its revisions to the *Conceptual Framework*.
- 6 The *Conceptual Framework* is expected to be issued in the first quarter of 2018. On 23 February 2017, the IASB tentatively decided that the IASB and the IFRS Interpretations Committee will start using the revised *Conceptual Framework* as soon as it is revised.
- 7 The revised *Conceptual Framework* will also result in consequential updates to IFRS Standards that make references to the *Conceptual Framework*. On 18 January 2017, the IASB tentatively confirmed that a transition period of approximately 18 months will be set for the amendments to IFRS Standards. This would make the revised *Framework* applicable in late 2019.

### Concerns

- 8 The lack of a specific effective date for the revised *Conceptual Framework* might be taken as indicating that it would become effective before the relevant amendments to IFRS Standards. This would cause confusion for preparers when using IFRS Standards that make reference to the *Conceptual Framework*.
- 9 The definition of a reporting entity in the revised *Conceptual Framework* does not align with the definition in AASB 1053 *Application of Tiers of Australian Accounting Standards*, AASB 1057 *Application of Australian Accounting Standards* and Statement of Accounting Concepts SAC 1 *Definition of the Reporting Entity*. This could result in inconsistencies in whether general purpose financial statements are prepared.

### Impact of the *Conceptual Framework* Effective date on IFRS Compliance

- 10 AASB 108, para. 10 refers to the application of judgement in developing and applying accounting policies. Paragraph 11 and the related footnote 3 state that when making such judgements, management shall refer to the *Framework for the Preparation and Presentation of Financial Statements* as amended by the AASB in December 2013.
- 11 The IASB staff have confirmed that transition to the revised *Conceptual Framework* for preparers that currently apply the *Framework* will be achieved through amending

Standards that contain references to the *Framework*. Where necessary, such references will be replaced with references to the *Conceptual Framework*. These amendments are included in *References to the Conceptual Framework* that the IASB is planning to issue together with the revised *Conceptual Framework*. Until these amendments become effective, preparers will have to continue referring to the *Framework* (unless they choose to apply the amendments early – *References to the Conceptual Framework* allows early application).

- 12 When the revised IASB *Conceptual Framework* is issued and applicable through IFRS Standards, there is a risk of non-compliance with IFRS Standards if AASB 108 continues to refer to the AASB *Framework for the Preparation and Presentation of Financial Statements*, which is not consistent with the revised IASB *Conceptual Framework*.
- 13 Paragraph 11 of AASB 108 states that management shall refer to, and consider the applicability of, the AASB *Framework*. Paragraph 12 permits management to also ‘consider the most recent pronouncements of other standard-setting bodies that use a similar conceptual framework...to the extent that these do not conflict with the sources in paragraph 11.’ However, the revised IASB *Conceptual Framework* would conflict with the current AASB *Framework*.

#### *Staff recommendation*

- 14 Staff recommend that AASB 108, para. 11(b) and footnote 3 be amended to refer to the revised *Conceptual Framework* along with other *Framework* references in Australian Accounting Standards when the revised *Framework* is issued in Australia.

#### **Question for Board members**

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| <p>Q1 Do Board members agree with the staff recommendation to amend AASB 108 and other Australian Accounting Standards to refer to the revised <i>Conceptual Framework</i> when it is issued in Australia?</p> |
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#### The Reporting Entity

- 15 The ‘reporting entity’ concept as defined in SAC 1 *Definition of the Reporting Entity* is unique to Australia. Internationally, the determination of which entities are reporting entities (ie who should report) is determined by legislation outside the remit of national accounting standard setters. The accounting standard setters are responsible for determining what information should be reported by reporting entities.
- 16 Accordingly, the revised IASB *Conceptual Framework* is not prescriptive as to which entities should be reporting entities. Instead, it infers a ‘boundary’ of what the reporting entity is such that the financial statements provide information that is useful to users of the entity’s financial statements.
- 17 The definition of a reporting entity per the revised IASB *Conceptual Framework* and Australian Accounting Standards can be summarised as follows:

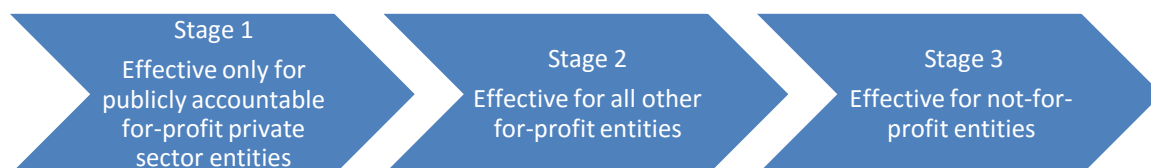
AASB 1053 and AASB 1057 (Appendix)	Revised IASB Conceptual Framework (Paragraphs 3.10 and 3.11)
Reporting entity means an entity in respect of which it is reasonable to expect the existence of users who rely on the entity's general purpose financial statements for information that will be useful to them for making and evaluating decisions about the allocation of resources. A reporting entity can be a single entity or a group comprising a parent and all of its subsidiaries.	<p>A reporting entity is an entity that is required, or chooses, to prepare financial statements*.</p> <p>A reporting entity is not necessarily a legal entity. It can comprise two or more legal entities, or a portion of a legal entity.</p> <p>* Footnote 1 in Chapter 1 of the Conceptual Framework states:</p> <p>'Throughout this <i>Conceptual Framework</i>, the terms 'financial reports' and 'financial reporting' refer to general purpose financial reports and general purpose financial reporting unless specifically indicated otherwise.'</p>

- 18 Staff are concerned that the inconsistent definition of a reporting entity per the revised *Conceptual Framework* and Australian Accounting Standards would cause confusion for preparers and users of financial statements. For example, any entity required to prepare general purpose financial statements is a reporting entity under the *Conceptual Framework*, but under Australian Accounting Standards, an entity has to satisfy the general-purpose user criterion. Furthermore, whereas the *Conceptual Framework* permits a portion of a legal entity to be a reporting entity, the Australian definition refers only to a single entity or a group.
- 19 The issue regarding reporting by a portion of a legal entity would be particularly relevant for proposals to introduce a new form of corporate collective investment vehicle. Such corporate entities may consist of numerous sub-funds, which are not legal entities in their own right but for which separate general purpose financial statements would be required. The revised reporting entity definition would facilitate this reporting.
- 20 Staff considered the following two approaches to address this:

Approach 1	Approach 2
Amend the definition of 'reporting entity' in AASB 1053 and AASB 1057 to align with the revised <i>Conceptual Framework</i> , for all entities.	Apply a staggered approach to the effective date of the revised <i>Conceptual Framework</i> for different sectors in Australia.

- 21 Amending the definition for all entities would create difficulties where legislation requires entities to comply with Australian Accounting Standards, as it would suggest that such entities thereby had to prepare general purpose financial statements. The reporting entity concept is part of a more complex issue in Australia that is currently being addressed under the Financial Reporting Framework Project. Removing the concept in one fell swoop would undercut that project.

- 22 Regarding Approach 2, staff propose the following stages:



- 23 Under Approach 2, the revised *Conceptual Framework* could first be made applicable to publicly accountable for-profit private sector entities. Such entities are required by AASB 1053 to prepare Tier 1 (full) general purpose financial statements. Accordingly, the Australian reporting entity concept is not relevant to them, and the revised reporting entity definition does not affect their general purpose financial statements preparation requirements.
- 24 Initially deferring the application of the revised *Conceptual Framework* to other for-profit entities and to not-for-profit entities would provide the Board with sufficient time to properly investigate the impact of the revised *Conceptual Framework* and address the issues with stakeholders.

*Staff recommendation*

- 25 Staff recommend that Approach 2 be followed, so that the revised *Conceptual Framework* is applied initially to publicly accountable for-profit private sector entities, with later application to other for-profit entities and then to not-for-profit entities.

**Question for Board members**

- Q2 Do Board members agree with the staff recommendation to stagger the effective date of the revised *Conceptual Framework* per Approach 2?

Definition of Public Accountability

- 26 AASB 1053 refers to ‘public accountability’ when determining the tiers for reporting requirements. This definition is referenced from the *IFRS for SMEs* Standard. In 2015, the definition of public accountability was revised in IFRS for SMEs, effective in 2017. However the definition of public accountability in AASB 1053 was not amended to align with the revised definition in IFRS for SMEs.
- 27 The table below presents the difference between the definition of public accountability per AASB 1053 and the revised definition in IFRS for SMEs.

Definition of ‘public accountability’ per AASB 1053	Revised IFRS for SMEs definition of ‘public accountability’ (2015 – applying 2017)
<p>Public accountability means accountability to those existing and potential resource providers and others external to the entity who make economic decisions but are not in a position to demand reports tailored to meet their particular information needs. A for-profit private sector entity has public accountability if:</p> <p>(a) its debt or equity instruments are traded in a public market or it is in the process of issuing such instruments for trading in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets); or</p> <p>(b) it holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses. This is typically the case for banks, credit unions, insurance companies, securities brokers/dealers, mutual funds and investment banks.</p>	<p><del>Accountability to those existing and potential resource providers and others external to the entity who make economic decisions but are not in a position to demand reports tailored to meet their particular information needs.</del> An entity has public accountability if:</p> <p>(a) its debt or equity instruments are traded in a public market or it is in the process of issuing such instruments for trading in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets), or</p> <p>(b) it holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses. <del>This is typically the case for banks, credit unions, insurance companies, securities brokers/dealers, mutual funds and investment banks.</del></p>

#### *Staff recommendation*

- 28 Staff recommend that the definition of public accountability in AASB 1053 be amended to align with the revised definition in IFRS for SMEs alongside the reporting entity change for publicly accountable for-profit private sector entities.

#### **Question for Board members**

- Q3 Do Board members agree with the staff recommendation to amend the definition of public accountability to align with the revised definition in IFRS for SMEs when the revised *Conceptual Framework* is issued in Australia for publicly accountable for-profit private sector entities?