

## **Feedback from AASB Roundtable Financial Reporting Framework – Not-for-Profit Public Sector Entities**

**Melbourne, 20 January 2016**

### **About the Roundtable**

#### *Purpose*

- 1 The purpose of the AASB Roundtable was to provide a forum to discuss issues and share views in relation to the Australian financial reporting framework, particularly in terms of the requirements for not-for-profit (NFP) public sector entities. The aim included discussing the way forward (a roadmap) for progress on this aspect of the AASB project, if the Roundtable considered there was sufficient scope for improvements in the application of reporting requirements to NFP public sector entities.
- 2 The agenda for the Roundtable is included in the Appendix to this summary.

#### *Participants*

- 3 As the purpose of the Roundtable was exploratory in nature, it was organised as an invitation-only session. External participants were from:
  - State and Commonwealth Treasuries/Finance (6)
  - Auditor-General's Offices (3)
  - Audit firms (4)
  - Accounting bodies (2)
- 4 Participants did not comment on whether their input into the Roundtable discussion would similarly be extendable to local governments, which are subject to requirements established by State or Territory governments.

### **Summary**

- 5 Participants agreed that the AASB should continue with this aspect of its Australian Financial Reporting Framework project, working in conjunction with other government bodies, to produce a Consultation Paper for public comment. Participants noted that it was important for relevant stakeholders to be actively engaged from early on in the project to ensure that any proposals would be appropriate and supported by major stakeholders.
- 6 Overall, participant feedback reflected that there is an issue with the level of financial reporting by NFP public sector entities. Participants noted that Tier 2 Reduced Disclosure Regime (RDR) general purpose financial statements (GPFS) are not generally regarded as being cost-beneficial at present for eligible public sector entities. However, jurisdictions expressed some support for the possibility of certain entities preparing a different form of GPFS in the future. Participants also noted that a third GPFS Tier may be useful and appropriate.

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- 7 A relative Expenses threshold was generally supported as a potential criterion, especially for determining entities that might be permitted to apply Tier 3 GPFS requirements.
- 8 Education may be necessary to overcome some of the current hurdles to adopting a lower level of financial reporting for many individual government entities, and to communicate that fewer disclosures do not necessarily mean poorer transparency.

**Is there a Financial Reporting Problem?** (see Appendix, agenda item 2, for more detail)

- 9 Participants noted that State or Commonwealth legislation required the preparation of financial reports in accordance with Australian Accounting Standards (the wording varies). This has been generally interpreted as requiring the preparation of GPFS. Accordingly, government agencies, statutory authorities, departments, and other NFP government entities<sup>1</sup> do not generally prepare special purpose financial statements. Participants flagged that the various financial reporting Acts would most likely need to be amended as part of the outputs of this project to achieve the project aims.
- 10 Treasury participants noted that departments and agencies (and other entities within the General Government Sector (GGS)/ Whole of Government financial reports) were generally required to prepare Tier 1 GPFS, rather than Tier 2 Reduced Disclosure Regime (RDR) GPFS. Participants considered audit issues to be a significant barrier to preparation of Tier 2 GPFS, and were concerned about the ability of the State or Commonwealth to otherwise obtain the necessary information to prepare the consolidated GPFS. Conservatism and public perception were also factors in evaluating RDR adoption.
- 11 Various participants commented that RDR was not seen as being particularly attractive at present given the limited cost-benefit return, including any potential audit complications, even though participants identified note disclosures as taking a lot of time to prepare. Disclosures about financial instruments were especially noted as being of concern, as the disclosures took time to prepare (and added volume to the annual report) but were not regarded as of being much value to users. The requirement to consolidate under both Tier 1 and RDR was also noted as affecting the cost-benefit assessment.
- 12 However, State and Commonwealth Treasuries expressed some support for the possibility of departments and agencies preparing a different form of GPFS (for example, RDR GPFS) in the future, especially given the effort required to prepare Tier 1 GPFS. Some participants noted that RDR was currently permitted or being explored (as part of a de-cluttering initiative) in their jurisdictions. For example, the Queensland government currently permits entities that are not consolidated (on the grounds of immateriality) into the GGS/ Whole of Government GPFS to prepare Tier 2 GPFS.
- 13 Participants generally supported all government entities having some form of external financial reporting responsibility, to ensure that the entity remains accountable to the public. Participants noted that it was important for governance purposes to

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1 This summary generally refers to ‘departments and agencies’. However, there could be a range of other government entities within the GGS/Whole of Government such as statutory authorities. References to ‘departments and agencies’ generally should be read as including other NFP public sector entities.

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demonstrate how public monies were utilised by the entity, although it was asked whether publicly available financial statements were the best mechanism – see paragraph 25.

- 14 However, participating jurisdictions communicated that, typically, only a limited number of subsidiary entities within the GGS/ Whole of Government (e.g. fewer than 20% of the total number of entities reporting) were material to the consolidated financial statements. The audit of these subsidiary entities was generally prioritised by the auditor.

**Reporting Aspects to Consider** (see Appendix, agenda item 4)

*Who are the users?*

- 15 Participants noted that users of public sector GPFS are not necessarily easily identifiable for entities within the GGS/ Whole of Government. A participant noted that users would be likely to consider the GPFS from an accountability, rather than investor, perspective.
- 16 The following parties were identified by participants as being possible potential users of the general purpose financial reports of agencies, departments and GGS/ Whole of Government:
- Ratings agencies (GGS/ Whole of Government only)
  - Lobby groups
  - Parliamentarians
  - General public
  - Academics
  - Media
- 17 Participants noted that the number of actual users, including in respect of the consolidated GGS/ Whole of Government financial statements, was unlikely to be high, and that certain users (for example, lobby groups) were likely to be interested in only particular aspects of the financial report (for example, executive remuneration). A participant observed that at the agency level, it may be that either there are no users, or the potential users refer to information sources other than the financial statements.
- 18 Participants considered that one of the ways they could help identify the number of users of an entity's financial statements was by way of the number of downloads of the financial report from the entity's website, although noting that this was only a broad measure.
- 19 Participants also suggested:
- (a) it was important for the existence of users to be reviewed regularly; and
  - (b) some entities such as museums may prepare financial statements for promotional purposes, rather than because they are a reporting entity.

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*Administered items*

- 20 Participants discussed whether the ‘administered’ versus ‘controlled’ items distinction was necessary and useful, and whether different levels of accountability were attached to such items.
- 21 A participant noted that their jurisdiction valued the distinction; another participant noted that application of the distinction may not always be clear, for example, where the State operates as an agent for another tier of Government or a private sector entity. The general (but not unanimous) view was that reporting on administered items should not be extended to public sector entities other than departments.

*Terminology*

- 22 Various participants also noted concern about the use of ‘department’ or ‘agency’ by the AASB. Participants were concerned that jurisdictions might currently either employ slightly different definitions of the terms, or establish entities performing a similar function under different legal structures, with possible different accounting consequences. This might detract from the consistent application of requirements by similar entities, reducing comparability across functions.
- 23 There was support for government business enterprises (GBE) to continue to comply with IFRS. A participant noted that this allows for comparability with the GBE’s competitors.

*Different tiers of reporting*

- 24 As noted earlier, participants generally supported all public sector entities having some form of external financial reporting responsibility, and would consider possibly requiring less reporting by certain entities.
- 25 Participants noted that entities needed to be accountable for their spending. Participants discussed whether external financial reporting was the best governance mechanism to meet accountability objectives, or whether the requirement to prepare publicly available GPFS was used more as a tool to ensure discipline over entity financial record keeping.
- 26 One participant suggested that public sector entity accountability comprised both a financial aspect and a performance aspect. Another participant noted that such a distinction may be too simplified, especially where entities engage in complex transactions such as public/private partnerships, or collect tax, fee-for-service revenue, or assume debt financing.
- 27 Participants agreed that there was scope for at least one further reporting Tier below Tier 2 to be developed. Participants considered the possibility of Tier 3 GPFS to include only limited information: for example, a statement of financial position, statement of financial performance, and disclosures about service performance. Participants also discussed whether certain entities (for example, smaller departments) could prepare financial reports that are simply an extract (or segment) of the Whole of Government consolidated financial statements, rather than GPFS.

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- 28 A participant observed that it may be useful for the Australian Accounting Standards to specify criteria to require entities to apply RDR, rather than RDR merely presenting a ‘minimum’ level of reporting.
- 29 There was some support for ‘micro’ entities not being required to comply with the recognition and measurement requirements in all Australian Accounting Standards, for example fair value measurement of property, plant and equipment not held for sale and infrastructure assets such as land under roads. However, participants rejected permitting cash-based accounting, given the acceptance of accrual accounting.

**Objective Criteria/Thresholds for Reporting Tiers?** (See Appendix, agenda item 5)

- 30 Participants generally agreed that an Expenses threshold could be a useful criterion in determining an appropriate reporting Tier, in preference to Revenue. This would be consistent with a focus on how public monies were utilised by the entity. Participants supported an Expenses threshold being determined as a relative percentage, rather than a fixed numerical figure (for example, a percentage of Whole of Government expenses). Participants noted that a fixed amount may be unsuitable for smaller jurisdictions.
- 31 Other suggestions for appropriate criteria on which to base the reporting Tier assessment included:
- (a) the ability of the entity to charge for services/ collect tariffs without cap restrictions. Participants noted that some government entities were non-budget agencies and/or were self-funding (for example, certain universities, hospitals or zoos), and accordingly, that it may be appropriate to require such entities to report more detailed information publicly;
  - (b) the nature of government services delivered. For example, it may be appropriate to require more extensive financial reporting of entities delivering frontline services such as Health and Education, compared to entities performing back office regulatory roles; and
  - (c) the nature of the entity’s liabilities, for example whether an entity is debt financed, holds leases or engages in off-balance sheet financing activity.
- 32 In addition:
- (a) a participant noted that the reporting Tier determination should not focus on the number of users, but on the importance of the users. Another participant commented that the criteria for NFP public sector entities may differ from those appropriate to GBEs;
  - (b) participants generally agreed that the State/Territory and Commonwealth Governments, and entities such as Public Financial Corporations and Public Non-Financial Corporations should be categorised as Tier 1 entities; and
  - (c) participants did not express any particular support for financial reporting being determined with regard to programs/initiatives.

**Roadmap – Where to from Here?** (see Appendix, agenda item 3)

- 33 There was strong support from participants for the AASB to continue developing this aspect of its Australian Financial Reporting Framework project, working in conjunction with the relevant other government bodies. Participants generally supported some change via the accounting standards (in addition to legislation). Participants considered this would provide a stronger basis for decisions about the content and structure of the financial reports, since the AASB does not have a vested interest in a jurisdiction's financial statements. For the same reason, participants also considered that AASB involvement would give weight to justifying any change to reduce the public reporting obligations of some public sector entities.
- 34 Participants generally agreed that the AASB should help develop a Consultation Paper as a starting point, working in conjunction with relevant government stakeholders, to promote change in this area. The AASB Chair (Kris Peach) suggested that the Consultation Paper might not be badged as an AASB Consultation Paper, since the AASB's intended role is as a lead resource in the process. For example, the Heads of Treasuries Accounting and Reporting Advisory Committee (HoTARAC) and the Australasian Council of Auditors-General (ACAG) potentially could be sponsors of the Consultation Paper. To be considered as the Paper is developed.
- 35 Participants observed that identification of appropriate stakeholders needs to be driven by the various jurisdictions (Treasuries and Audit Offices) so as to develop suitable proposals that would be supported by major stakeholders. In this regard, participants noted that it is necessary for jurisdictions to each commit a representative to providing input on the project, and on communicating any outputs (to ensure a Consultation Paper is considered by a wide audience), to improve the likelihood of the project being able to drive change. Suitable representatives should be identified by each jurisdiction in the near future.
- 36 In addition, participants considered it was important to engage with the various Public Accounts Committees to gain their support for the Consultation Paper before its issue.
- 37 **Timing.** Participants suggested that it would be useful if the Consultation Paper could be developed for comment after 2016 audited financial statements have been finalised for public sector entities.

## **Appendix: AASB Roundtable Agenda**

<b>Item</b>	<b>Topic</b>
<b>1</b>	<p><b>Welcome and Introduction</b> – Kris Peach, Chair, AASB</p> <p>AASB Australian financial reporting framework project</p> <ul style="list-style-type: none"> <li>– work with government policymakers and other regulators</li> <li>– potential reforms re who should report and what should be reported</li> <li>– ensure benefits of financial reporting exceed the costs</li> </ul>
<b>2</b>	<p><b>Is there a Financial Reporting Problem?</b></p> <p>General purpose and special purpose financial statements</p> <p>Variations across jurisdictions and regulators (benchmarking results)</p> <p>Benefits and costs of financial reporting</p> <ul style="list-style-type: none"> <li>– too much or too little information?</li> <li>– consolidated versus entity reporting?</li> <li>– audit scope issues re controlled entities?</li> </ul>
<b>3</b>	<p><b>Roadmap – Where to from Here?</b></p> <p>Who will take action?</p> <ul style="list-style-type: none"> <li>– joint or individual action?</li> <li>– roles of HoTs, HoTARAC, ACAG, AASB, others?</li> </ul> <p>What needs to be done?</p> <ul style="list-style-type: none"> <li>– focus areas?</li> <li>– public consultation on proposals?</li> </ul> <p>When should action be taken?</p>
<b>4</b>	<p><b>Reporting Aspects to Consider?</b></p> <p>Users of NFP public sector financial information?</p> <ul style="list-style-type: none"> <li>– who are the users?</li> <li>– are they interested in group or entity information?</li> </ul> <p>What information do they need?</p> <ul style="list-style-type: none"> <li>– report from governing body/directors/management?</li> <li>– primary financial statements?</li> <li>– notes to financial statements?</li> <li>– selected financial information only ... and if so, what?</li> </ul> <p>Departments and administered items</p> <ul style="list-style-type: none"> <li>– need for financial reports, statements or just information?</li> <li>– same approach for all departments?</li> <li>– Ministerial portfolio reporting?</li> <li>– administered items confuse re scope of entities?</li> </ul> <p>Tiers of financial reporting?</p> <ul style="list-style-type: none"> <li>– Tiers 1 and 2 (RDR)</li> <li>– Tier 3 – simplified financial statements or selected financial information?</li> <li>– exemption from public reporting?</li> </ul>
<b>5</b>	<p><b>Objective Criteria/Thresholds for Reporting Tiers?</b></p> <p>Economic significance</p> <ul style="list-style-type: none"> <li>– how to determine?</li> </ul> <p>Public accountability</p> <ul style="list-style-type: none"> <li>– different levels of accountability?</li> </ul> <p>Organisational characteristics</p> <ul style="list-style-type: none"> <li>– own financial resources v. appropriations?</li> <li>– operational independence (autonomy from Ministerial direction)?</li> <li>– nature of programs?</li> </ul>
<b>6</b>	<b>Summary and Concluding Remarks</b>