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Kevin Stevenson
Chairman
Australian Accounting Standards Board
PO Box 204
Collins Street West VIC 8007

via email: standard@aasb.gov.au

23 April 2010

Dear Kevin

Re: AASB Consultation Paper & AASB ED 192 – Revised Differential Reporting Framework

We do not support introducing the proposed reduced disclosure regime in the form currently proposed by the Board. It is not entirely clear to us what the problem is that the proposals are seeking to address and we elaborate our concerns below.

If the Board's primary objective is to reduce the disclosure requirements of a defined group of entities, we believe this could be addressed in a more effective manner. The current proposals would reduce the disclosure obligations of some entities, such as unlisted public companies that prepare full IFRS general purpose financial statements, but other entities, such as wholly-owned subsidiaries of listed companies that prepare special purpose financial statements, would have increased disclosure obligations.

In our view, reducing the disclosure obligations of some entities at the expense of increasing others is an unfortunate "side-effect" of the proposals. It does not sit well with the government's efforts to reduce the reporting burden on entities, which it has been attempting to do through the Corporate Law Reform program and Standard Business Reporting initiative. Further, implementing the current proposals would be resource-intensive for many businesses that need to expand their disclosures and we do not believe the benefits are likely to outweigh the costs. The investment required for business to understand and apply new definitions, train their staff, and modify or develop systems and processes to ensure compliance should not be underestimated.

We could support an approach that reduces the disclosure requirements for some entities that are not publicly accountable.

Alternatively, if the Board is attempting to address the quality of financial reporting by non publicly accountable entities we believe this too could be achieved in a more cost effective manner. ASIC's Regulatory Guide 85 sets out that it expects non reporting entities to reflect the recognition and measurement requirement of IFRS in their financial reports. If the Board is concerned that these entities are not meeting the recognition and measurement requirements in IFRS it is likely to be more cost effective to embed the guidance in paragraph 2.5 of the Guide within the application sections of standards, rather than introduce the proposed new disclosure framework.

We are reluctant to support the changes proposed by the Board because our perspective is that the current financial reporting approach is working reasonably well in practice. The reporting entity concept gives entities the freedom to tailor their financial reports based on the needs of their users, which we believe is an important element of best practice reporting. We are not aware of there being a systemic issue of users of special purpose financial reports being misled or having relevant information withheld from them. However, we acknowledge the current reporting framework, particularly in the area of disclosure could be improved. For instance, we believe the framework would benefit from a comprehensive and holistic review of the disclosure requirements contained within IFRS. We would support the Board working with the IASB to address the business community's concern regarding the current volume of disclosure contained in financial reports.

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Notwithstanding our concerns regarding the proposals, we believe they remain more suitable to adopt in Australia than the IASB's IFRS for SMEs standard. If the Board is convinced there is compelling evidence supporting the change they propose, we would prefer to see the current proposals adopted than the IFRS for SMEs standard. Our responses to the Board's detailed questions are set out in the attached appendices.

I would welcome the opportunity to discuss our firm's views. Please contact me on (03) 8603 3868 if you would like to discuss our comments further.

Yours sincerely,

Jan McCahey
Partner, PricewaterhouseCoopers

Specific matters for comment

a. **Do you agree with the introduction of a second Tier of reporting requirements for preparing general purpose financial statements for:**

   (i) **for-profit private sector entities that do not have public accountability;**

   (ii) **not-for-profit private sector entities; and**

   (iii) **public sector entities other than those required by the AASB to apply Tier 1.**

   If not, and you do support differential reporting, what other classifications of entities do you think would be more appropriate for differential reporting and why?

(i) For profit private sector entities that do not have public accountability

We support the concept of a non-publicly accountable entity being able to apply the proposed reduced disclosure regime where doing so will result in fewer disclosures.

However, we remain unconvinced about whether the proposals will result in an overall reduced disclosure burden on Australian entities. Under the proposals some entities will enjoy fewer disclosure obligations, whereas others will be disadvantaged and have more disclosure obligations. For example, many entities that currently prepare special purpose financial statements do not include information about related parties because it is not considered useful to the users of their accounts. However, under the proposals, these entities would be required to include detailed information about their related party transactions.

(ii) Not for profit private sector entities

We support the concept of a not-for-profit private sector entity being able to apply the proposed reduced disclosure regime.

However, we are concerned about those not-for-profit private sector entities that will have increased disclosure obligations under the proposals. These entities are typically resource-constrained and may not have access to the sophisticated systems, processes and professional development resources of larger entities. We expect these entities will find it a challenge to meet any additional financial reporting requirements imposed on them.

In our view, the financial reporting requirements of not-for-profit entities is an area that requires holistic review. Reducing the disclosure obligations of these entities is only one of the concerns shared by the Australian business community; other concerns include improving the transparency of the financial statements prepared by charities and better understanding the needs of users of these financial statements.

***(iii)* Public sector entities other than those required by the AASB to apply Tier 1**

We support the concept of certain public sector entities being able to apply the proposed reduced disclosure regime. However, consistent with our overall view, we do not believe that disclosure obligations should be reduced for some entities, at the cost of increasing the obligations of others.

b. **Do you agree that entities within the second Tier should be able to apply the proposed reduced disclosure regime, which retains the recognition and measurement requirements of full IFRS or would you prefer another approach (e.g. IFRS for SMEs)?**

We support the concept of retaining the recognition and measurement requirements of full IFRS, as opposed to adopting the IFRS for SMEs standard.

We believe introducing the IFRS for SMEs standard would add a layer of complexity to the Australian financial reporting framework for both preparers and users. The majority of Australian entities with statutory financial reporting obligations currently apply the recognition and measurement requirements of full IFRS. Requiring entities (and users) to learn another set of accounting rules and apply these to their business would result in significant implementation costs in the areas of compliance (including, monitoring and enforcement), education and professional development, and systems and processes.

c. The definition of public accountability (which is used to identify those for-profit entities that must apply Tier 1) and whether there are categories of entities in the Australian environment that should be cited as examples of publicly accountable entities other than those already identified in paragraph 26 of the Exposure Draft.

We support using the IASB's definition of "publicly accountable" as the cornerstone for determining which entities can adopt the reduced disclosure regime. However, we do not believe the Board should list examples to illustrate the meaning of the definition because doing so may undermine the principles underpinning the IASB-issued IFRS.

More generally, we remain concerned about the potential inclusion of additional "rules". In practice, understanding and applying new terminology and rules can be resource intensive; in our experience, continually adding to the "rule book" can create more issues than it solves.

Therefore, we urge the Board to exercise caution in adding to the guidance; where necessary, we encourage the Board to take a principles-based approach to any new guidance issued.

d. Would you require any other classes of public sector entities, such as Government Departments, Government Business Enterprises (GBEs) or Statutory Authorities, to be always categorised as 'Tier 1' reporting entities? If so, on what basis?

No comment.

e. The clarification of the meaning of GPFSs and modifying the way the reporting entity concept is used.

We do not support modifying the reporting entity concept. We would prefer the Board retain the reporting entity concept as the basis for determining the type of financial report an entity is required to prepare (eg, general purpose financial statements or special purpose financial statements). In our view, the reporting entity concept helps give preparers of financial statements the flexibility to tailor their financial reports to meet the needs of their users.

f. The extent and nature of the proposed disclosures under the RDR (Tier 2), including whether the RDR would be effective in reducing sufficiently the disclosure burden on entities in preparing their GPFSs.

The extent and nature of disclosure reduction will vary depending where in the spectrum of financial reporting a non-publicly accountable entity is currently placed. Under the proposals, entities currently preparing full IFRS general purpose financial reports will benefit from a reduced disclosure burden while those entities currently preparing special purpose financial reports will suffer from increased requirements. We expect many entities will be surprised to find their financial reporting burden has increased as they are expecting a "reduced" burden based on how the current proposals are being publicised. This expectation gap is something the Board needs to address.

Entities may be disappointed that some of the reduced disclosure requirements do not go far enough. For example, the Board could have taken this opportunity to perform a more holistic review of the disclosure requirements rather than benchmarking to IFRS for SMEs.

g. Any particular disclosure requirements that:

- **i) have been retained in the RDR that you consider should be excluded from the RDR, and your reasons for exclusion; or**
- **ii) have been excluded from the RDR that you consider should be retained, and your reasons for retention.**

Refer to Table 1 in the enclosed Appendix 2. We have focused on the disclosures that could be excluded from the reduced disclosure regime rather than those that could be added. We have shared our detailed comments in relation to both questions in a discussion with AASB staff.

h. Transitional provisions for entities first applying Tier 1 or 2 and moving between Tiers

The transitional provisions for entities moving between Tiers are complex. For example, consider an entity that currently prepares general purpose financial statements and therefore will have previously applied AASB 1. If the entity applies the reduced disclosure regime and then in a subsequent period transitions from Tier 2 to Tier 1, the transitional provisions would require the entity to once again apply AASB 1. It is unclear as to why the entity would need to do so since the change in Tiers would only impact the level of disclosure rather than any recognition and measurement requirements. We would welcome clarity from the AASB in this area.

i. Are there any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals?

There are a number of regulatory issues which may impact the implementation of the proposals.

a) Australian business is on the precipice of significant financial reporting change. In the next three years we expect more than 50 accounting changes will need to be considered by business (including the overhaul of the financial instruments standards). Given this degree of change, we question whether the time is right for the Board to introduce more change.

b) The proposed changes to the *Corporations Act* announced by Treasury in December 2009 would require entities to complete a statement of compliance with IFRS in their directors' declaration. It is our understanding that an entity applying the reduced disclosure regime will not be able to assert compliance with IFRS. The Board will also need to consider the associated impact on Australian Auditing Standards and the wording of audit opinions issued to the members of entities preparing and lodging accounts.

c) We are unsure of the level of consultation the AASB has had with ASIC, but we would encourage joint discussion of the following issues.

- The application of the proposals to holders of Australian Financial Services Licences
- The impact on existing class orders (both issued and available for application)
- The impact on small foreign controlled proprietary companies (preparation of general purpose financial reports could be unduly burdensome for these entities).
- Many non-reporting entities rely on ASIC Regulatory Guide 85 to support their rationale to prepare separate financial statements rather than consolidated financial statements where neither the parent entity or consolidated group is a reporting entity. Therefore any consequential impacts introduced by the reduced disclosure regime should be considered for their effect on this guidance.

d) We encourage the Board to consider the alignment between the proposed framework and the core principles of the professional obligations of members of the accounting profession. Entities that report outside of the *Corporations Act* currently use the reporting entity concept to help them determine whether to prepare general purpose financial statements or special purpose financial statements. The Board should consider the effect that any modification of the reporting entity concept and financial reporting framework would have on these entities. It would be unfortunate if the Board's proposals undermined the philosophy set out in APES 205 *Conformity with Accounting Standards*, which was developed in conjunction with the AASB, to articulate the responsibilities of members in respect of the reporting entity concept and general purpose financial statements.

j. Overall, do you agree that the proposals would decrease the costs of preparing financial statements whilst not materially reducing the usefulness of those statements to users?

Overall we do not believe the reduced disclosure regime would reduce the costs associated with preparing financial statements. In fact, for entities that will have increased disclosure obligations under the proposals, we expect it to increase their financial reporting costs for questionable "added benefit" to the users of their accounts. Some smaller entities may not find it easy to absorb such cost increases.

We do not expect the proposed regime to significantly reduce the usefulness of financial statements. In any case, the proposals focus on a minimum set of requirements; we expect best practice reporters to continue to consider voluntary disclosure where that benefits users. For example, under the proposed regime some entities will not be required to include a reconciliation of operating cash flows to profit after tax. However, these entities might believe that users of their accounts benefit from this information, so they may choose to voluntarily disclose it.

k. Are the proposals in the best interests of the Australian economy?

In our view, the Board's proposed approach would serve the Australian economy better than the IFRS for SMEs standard. However, we encourage the Board to consider those entities that will have increased disclosure obligations under the proposals as we expect these entities would not view the proposals as being in their best interests. We also encourage the Board to consider the government's recent actions to reduce the reporting burden on Australian business (eg, through the Corporate Law Reform program and Standard Business Reporting initiative) and how that fits with the notion of some entities having more reporting requirements under the proposals.

We are not convinced that reducing some entities' disclosure obligations while increasing others is the best approach for the Australian business community. Further, we are yet to see compelling evidence that any increase in disclosure obligations and regulatory burden will provide substantial benefit to users of financial statements.

Question (g) - Any particular disclosure requirements that:

(i) have been retained in the RDR that you consider should be excluded from the RDR, and your reasons for exclusion.

Standard number	Paragraph reference	(i) disclosure requirements that the AASB have retained which we believe should be excluded	(i) PwC reasons for suggesting to exclude the disclosure requirements identified in the RDR
AASB 7	27	Determining how fair value was measured for financial instruments which are carried at fair value (eg. methods and assumptions).	It is not clear which financial instruments this relates to: all or only those that are recognised at fair value? Since there is no longer a need to disclose FV for those financial instruments that are not carried at FV, we question the appropriateness of disclosing how the FV (that is not disclosed) is measured. Clarity is needed to specify that the disclosure only needs to be made for financial instruments that are carried at FV.
	29	Identification of situations where disclosures of fair value are not required (eg. when the carrying amount is a reasonable approximation of the fair value, such as short-term trade receivables).	There is no requirement to disclose FV for entities eligible to apply the RDR. This paragraph can therefore also be deleted.
AASB 110	22(a)	Examples of non-adjusting events after the end of the reporting period that would generally result in disclosure (eg. business combinations occurring after the reporting period end).	Refers to AASB 3 for specific disclosure, yet the relevant disclosures in AASB 3 do not apply to Tier 2 entities. Consistency required between the 2 standards.
	22(c)	Examples of non-adjusting events after the end of the reporting period that would generally result in disclosure (eg. classification of assets as held for sale in accordance with AASB 5)	The relevant disclosures in paragraph 12 of AASB 5 are currently shaded as not being applicable under the RDR. Consistency required between the 2 standards.
AASB 116	73(e)(viii)	A reconciliation of the carrying amount of property, plant and equipment at the beginning and end of the period, including showing the net exchange differences arising on the translation of the financial statements from the functional currency into a different presentation currency.	To be consistent with IFRS for SME this disclosure should be excluded. The proposed AASB 138 disclosure requirements under the RDR have excluded this same requirement.
AASB 119	120A(c)	Information to be disclosed in relation to defined benefit plans, including a reconciliation of opening and closing balances of the present value of the obligation, showing separately the sub-points listed in the standard.	Appears to be inappropriately shaded, for example "showing separately ...", however all of the separate sub-points are shaded which implies that an entity applying the RDR would not be required to disclose any information.
AASB 127	42(c) and 43(c)	A description of the methods used to account for investments in consolidated and separate financial statements.	Paragraphs 42(b) and 43(b) are both shaded to be removed. As a result, paragraphs 42(c) and 43(c) should also be removed as they provide a description of the information in paragraph (b).
AASB 136	129	Information required to be disclosed for each reportable segment in respect of impairment losses and reversals.	As AASB 8 is not applicable to an entity applying the RDR, this paragraph should be removed. The disclosure requirement has been retained in case an entity elects to report segment information and is thereby required to adopt AASB 8 in full. However, this is inconsistent with paragraph 130(c)(ii) and paragraph 130(d)(ii) which proposes to exclude AASB 8 related disclosures.
AASB 137	RDR84.1	Reconciliation information required for each class of provision	The original wording in paragraph 84 seems to be sufficient in stating the requirements for the reconciliation; we do not believe the additional RDR paragraph is necessary.
AASB 141	50	Reconciliation of changes in the carrying amount of biological assets between the beginning and end of the current period.	Retaining the requirement to disclose the prior year reconciliation is inconsistent with other standards where prior year reconciliations are exempt. Request AASB to re-consider and clarify the requirements, for example, by adding an RDR specific paragraph such as in AASB 116 paragraph RDR73.1.

Appendix 3

Application issues – general

Issue	Practical implication
Timeline prior to 30 June 2010	• Entities considering early adoption are concerned they may not have sufficient time to gain a detailed understanding of the changes and how they would impact their business. • Given the degree of change proposed, coupled with the Treasury's proposals to remove parent entity reporting, moving too quickly through the consultation period creates potential for error and a risk that entities will not meet the minimum requirements as prescribed in the standards.

Application issues – standard-specific

Standard	Issue
AASB 1 First time adoption of Australian equivalents to International Financial Reporting Standards	• Should explanations be included within the standard about how AASB 1 will apply in the context of the RDR? In particular, we encourage the AASB to clearly explain that "transition from previous GAAP to Australian Accounting Standards" will also include transition from RDR or the move from preparing special purpose financial reports to reporting under full IFRS (that is, moving from Tier 2 to Tier 1).
AASB 101 Presentation of financial statements	• Paragraph RDR16.1 should specifically state that entities complying with the RDR regime cannot state compliance with IASB-issued IFRS.
AASB 133 Earnings per share	• AASB 133 is not mandatory for entities that are eligible to apply the RDR. The standard should acknowledge that disclosures are only required for entities that provide EPS information voluntarily, rather than needing to meet all of the disclosure requirements of the standard.
AASB 8 Operating segments	• AASB 8 is not mandatory for entities that are eligible to apply the RDR. • This point should be clarified in Appendix B so that it is clear that the disclosures required by the standard are only required when an entity elects to voluntarily disclose segment information.
AASB 3 Business combinations	• IFRS for SMEs uses the July 2004 (amended as at December 2007) version of AASB 3, not the revised AASB 3, which the RDR has been based on. • As a result, the additional disclosures contained in AASB 3R should be analysed using the same principles applied to standards where recognition and measurement differences exist.