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Mr Kevin Stevenson
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Dear Mr ~~Stevenson~~ Kevin

ED 212- *Not-for-Profit Entities within the General Government Sector*

The Heads of Treasuries Accounting and Reporting Advisory Committee (HoTARAC) welcomes the opportunity to provide comments to the Australian Accounting Standards Board (AASB) on Exposure Draft – ED 212 *Not-for-Profit Entities within the General Government Sector.*

The majority of HoTARAC holds the view that the benefits of these proposals outweigh the costs, and will result in improved financial reporting. They argue that much of the work required to implement this standard in part has already been carried out, as most jurisdictions already choose GAAP options that align with GFS, and value assets at fair value, for consolidation purposes. A minority of HoTARAC members maintain that the costs of these proposals outweigh the benefits, and will not result in an improvement in financial reporting.

While the exposure draft makes some attempt at harmonisation of Generally Accepted Accounting Principles and Government Finance Statistics, the majority of HoTARAC members believe that requiring on-the-face presentation will provide a better result and one that is more consistent with the objective of achieving a single set of reports.

Nevertheless, the majority of HoTARAC is in favour of making this standard mandatory for all Commonwealth, state and territory jurisdictions. Due to the varying views of HoTARAC members, however, we would support a flexible approach that meets the needs of individual jurisdictions, yet provides a consistent approach by those that choose to adopt it.

HoTARAC's responses to the Specific Matters for Comment from the exposure draft as well as additional comments are attached.

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If you have any queries regarding HoTARAC's comments, please contact Peter Gibson from the Department of Finance and Deregulation on 02 6215 3551.

Yours sincerely

Grant Hehir
CHAIR
HEADS OF TREASURIES ACCOUNTING AND REPORTING ADVISORY COMMITTEE
3 November 2011
Encl

HoTARAC Response to ED 212 Not-for-Profit Entities within the General Government Sector

General Comments

The majority of HoTARAC is of the opinion that the proposals on the whole will lead to an overall improvement in financial reporting. The main points of view from within HoTARAC are included, below.

(a) whether the proposals would lead to an overall improvement in general purpose financial reporting by not-for-profit entities within the GGS.

The majority of jurisdictions are of the opinion that these proposals will lead to an overall improvement in general purpose financial reporting, subject to specific comments below. It will provide additional disclosures, enhancing transparency and accountability, and it will ensure comparability between entities within the same jurisdiction and will provide a clearer link between an entity and its whole of government. In this respect we note that the proposals include more than simply GAAP/GFS harmonisation.

A minority of jurisdictions believe that the proposals will not lead to such an improvement, citing that comparability on its own does not improve the quality of financial reporting. Further, they believe GFS is predominantly a macroeconomic tool and not relevant at entity level, and that mandating the choice of a GFS aligned GAAP option is not the role of an accounting standard setter.

Irrespective of your response to this general question, the AASB would value specific comments on:

(a)(i) the proposal to limit the entities affected by the proposals in this Exposure Draft to not-for-profit entities within the GGS. In particular, the Board seeks comment on whether the proposals should also apply to for-profit entities within the GGS (see paragraphs 2 and BC10-BC13);

HoTARAC has previously expressed the view that these proposals are appropriate to for-profit entities within the GGS. The majority of HoTARAC members note that applying these proposals to for-profit GGS entities will not lead to significant differences as the proposals are consistent with the current requirements of AASB 101 *Presentation of Financial Statements* (AASB 101) and AASB 107 *Cash Flow Statements* (AASB 107).

However, the majority of HoTARAC does not hold a strong view about this and could accept application to only not-for-profit entities. A minority feel these proposals are solely relevant to not-for-profit entities.

(a)(ii) the proposal that the version of the ABS GFS Manual to be applied is a version that was effective at the beginning of the previous annual reporting period or any version effective at a later date, rather than necessarily the latest version (see paragraphs 9 and BC14-BC15);

HoTARAC considers this to be appropriate, in line with the recent amendments to AASB 1049 *Whole of Government and General Government Sector Financial Reporting.*

(a)(iii) the proposal to limit GAAP recognition and measurement options to those that align with GFS and thereby require the same accounting policies as those adopted under AASB 1049 for whole of governments and the GGSs (see paragraphs 10-12 and BC16-BC25);

The majority of HoTARAC agrees with the proposal as this will ensure consistency between the jurisdictions, between GGS entities and their whole of government (WoG), and will fortify the benefits and relevance of harmonisation at both an entity and WoG level.

HoTARAC notes that any proposal to limit GAAP recognition and measurement options would have minimal implementation impact as most HoTARAC jurisdictions already require individual agencies to adopt options that align with GFS.

Additionally, we note in particular that most entities within the GGS will already have completed the significant task of determining market value for their assets in order for consolidated statements to be prepared under AASB 1049, so this will not be an issue for most entities.

A minority of jurisdictions hold the view that it is not the role of an accounting standard setter to restrict GAAP options to ensure consistency, as in the approach adopted by AASB 127 *Consolidated and Separate Financial Statements*. Further, they express the view that comparability on its own does not improve the quality of financial reporting.

(a)(iv) the proposal to require disclosure, under both Tier 1 and Tier 2 requirements, either in the financial statements or in the notes, of information based on GAAP/GFS harmonised classification and presentation principles for controlled items and, separately, administered items (including classification of income and expenses as transactions and other economic flows, and classification and presentation of cash flows from investing activities for policy purposes and liquidity management purposes) (see paragraphs 13-18, 22 and BC26-BC35).

The majority of jurisdictions support the proposal overall because it provides useful information to users of financial statements on the contribution that the GGS entity has made to the WoG and provides consistency when comparing GGS entities (within jurisdictions), subject to the specific comments outlined below.

A minority of HoTARAC feels that the information will not be useful, believing that GFS is a macroeconomic tool, will not show the contribution to the WoG or GGS, and will be costly and confusing.

(a)(iv)A. whether the on-the-face or in-the-notes presentation option should be allowed and, if not, whether on-the-face presentation of GAAP/GFS harmonised information should be prohibited given the potential for complexity; and

The majority of HoTARAC believe that the presentation of GAAP/GFS harmonised information on the face will result in more meaningful and less confusing information being conveyed to users and would be consistent with the objective of obtaining a single set of government reports as stated on page six of the exposure draft. Relegating the harmonised information to the notes does not provide uniformity of presentation and a clear read between an entity and its whole of government.

These jurisdictions believe that GAAP/GFS presentation in its own right is not inherently complex and has already been largely adopted by one jurisdiction. They argue that any potential for complexity arises as a result of the proposal to require multiple columns to be presented side by side in the one statement. The simultaneous presentation of administered items, controlled items, and their comparatives results in a minimum of four columns in each financial statement (assuming that the budgets are shown elsewhere in the notes). If a third statement of financial position is required under AASB 101 *Presentation of Financial Statements* then this increases to five columns in the statement of financial position. This is what will give rise to complexity, and this particular presentation is not supported as a mandatory principle by HoTARAC. Additionally, one jurisdiction has raised concern that the number of columns required to be disclosed, may discriminate against the visually impaired, particularly if side by side presentation is required, along with budgets and a third balance sheet.

As a result, a majority of HoTARAC feels that the disclosure of GAAP/GFS harmonised information should not be inhibited by being tied to the side by side disclosure of administered and controlled items. It is not necessary for controlled and administered items to be included side by side in the same statement. If there are concerns about complexity, we propose that this requirement be removed.

A minority of jurisdictions believe that GAAP / GFS harmonised information is not relevant at the entity level, as GFS is a macroeconomic tool only. However, if the AASB proceeds with the Standard, these jurisdictions would prefer that on the face presentation is prohibited, on the basis that it is not sufficiently relevant to be disclosed on-the-face, disclosure in the notes would be sufficient.

Given the various views of HoTARAC members, we would support a flexible approach that meets the needs of individual jurisdictions, yet provides for consistency in application whether an entity chooses to present on a harmonised basis in the face statements or in the notes.

(a)(iv)B. the proposal to require disclosure of GAAP/GFS harmonised classification information at line item level, where it is presented in the notes; and whether information at the line item level would be more beneficial than at the GFS category level;

HoTARAC agrees with the proposal to require disclosure of GAAP/GFS harmonised classification information at line item level, where it is presented in the notes. This facilitates the reconciliation to the GAAP primary financial statements and will result in information that is more meaningful and useful to users.

One jurisdiction is unclear on what 'line item level' means, and seeks clarification on this as well as 'GFS category level'.

(a)(v) the proposal to require AASB 1050 to continue to apply to government departments, to the extent its requirements are not satisfied by the proposals in this Exposure Draft (see paragraphs 19 and BC29-BC31);

The majority of HoTARAC jurisdictions agree with the proposal.

A minority of jurisdictions do not support extending GAAP/GFS disclosure requirements to administered items, until AASB 1050 is more fundamentally reviewed. In particular, these jurisdictions do not support extending disclosures to administered cash flows (as proposed in ED 212), until AASB 1050 is reviewed.

(a)(vi) the proposal to require disclosure, under both Tier 1 and Tier 2 requirements, of any original budgeted financial statements reflecting controlled or administered items presented to parliament, recast to align with the presentation and classification adopted in the primary financial statements and accompanying information about administered items or the GAAP/GFS harmonisation note (whichever is judged to be the more useful) and an explanation of variances (see paragraphs 23-29 and BC40-BC42);

HoTARAC members believe that the inclusion of budgeted figures could mislead users of financial statements as this information is unaudited and would potentially 'clutter' the financial statements. This could diminish a user's ability to understand the information being communicated. HoTARAC members believe it is premature to require disclosure of budgeted information, pending the AASB's separate project on budget reporting.

However, if these requirements are introduced, and there is a choice to disclose GAAP/GFS information in the primary financial statements or the notes, HoTARAC members support giving entities the discretion to exercise their judgement as to where they disclose budget information.

HoTARAC does not support the inclusion of a mandatory requirement for explanation of variances between actual and budget outcomes, as this is considered to be management information, which does not generally form part of general purpose financial reports.

(a)(vii) the proposals relating to other disclosures, from both a Tier 1 and Tier 2 perspective (see paragraphs 30-32), in particular relating to:

A requiring information to be disclosed in the accounting policy note (paragraph BC36), including disclosures about the version of the ABS GFS Manual adopted and, where relevant, a later version (paragraph BC15); and

HoTARAC agrees with the proposal.

(a)(vii)B not requiring disclosure of disaggregated information, except to the extent it continues to be required by AASB 1052 for government departments (paragraphs BC37-BC39);

The majority of HoTARAC agrees with the proposal.

(a)(viii) the proposal to provide no specific transitional requirements, except to require an entity to change the elections it previously made under AASB 1 to the extent necessary to comply with the ABS GFS Manual (see paragraphs 33-35 and BC44-BC47);

HoTARAC agrees with the proposal.

(a)(ix) unless already provided in response to other specific matters for comment relating to disclosures, the proposal to exempt entities adopting Tier 2 requirements from certain disclosures (shown as shaded text in this Exposure Draft);

HoTARAC agrees with the proposed exemption of Tier 2 entities from certain disclosures in ED 212. These exemptions are consistent with the principles of the reduced disclosure requirements.

(a)(x) the illustrative examples, and whether they provide guidance that is appropriate/helpful in implementing the proposals (see Illustrative Examples A and B and paragraphs BC49-BC50); and

HoTARAC feels that the illustrative examples are appropriate and helpful as guidance in implementing the proposals.

The net cost of services format in Illustrative Example B might be improved by showing the operating result line before splitting it between continuing and discontinued operations to maintain the flow in arriving at the operating result.

A minority of HoTARAC jurisdictions believe that the 'net cost of services' should be based on the 'net cost of services from transactions' as this is the aggregate that it is most analogous to the net operating balance at the GGS level.

(a)(xi) the proposed operative date (see paragraphs 3-4 and BC48);

HoTARAC agrees with the proposal, as it will allow adequate time for agencies to implement the new requirements and processes.

(b) unless already provided in response to specific matter for comment (a) above, whether overall, from both a Tier 1 and Tier 2 perspective, the proposals would result in financial statements that would be useful to users;

Overall, the majority of HoTARAC jurisdictions consider the proposals would result in financial statements that would be useful to users. The proposals will provide consistency when comparing results with other GGS entities within the same jurisdiction and will show the entity's contribution to the WoG.

A minority of members maintain the view that the cost of implementing this standard will outweigh the benefit. It is their view that the nature of the proposed standard is inherently complex, providing difficulty for both preparers and users and it will not be relevant to a broad range of users as GFS is predominately a macroeconomic tool. Further, they express that increasing comparability, on its own, does not improve financial reporting.

(c) whether the proposals, from both a Tier 1 and Tier 2 perspective, are in the best interests of the Australian economy; and

No comment.

(d) unless already provided in response to the specific matters for comment above, the costs and benefits of the proposals relating to both Tier 1 and Tier 2 requirements relative to the current requirements, whether quantitative (financial or non-financial) or qualitative.

The majority of HoTARAC holds the view that while experiences may vary between jurisdictions, on the whole the costs are relatively minor when compared to other standards that have been implemented (particularly the adoption of AEIFRS), and are justified by the benefits, which include providing useful information to users of financial statements on the contribution that the GGS entity has made to the whole of government and provides consistency when comparing GGS entities.

For preparers at entity level, the major change is a presentational one, not a change to recognition and measurement. The majority of HoTARAC believes that for most jurisdictions this will be as simple as switching from one financial statement template to another. For at least one jurisdiction, the new format is already substantially mandated for use by entities.

One jurisdiction has already undertaken some detailed planning for implementing entity level harmonisation, and has found that there is relatively little to be completed because of the few practical recognition and measurement differences that impact individual entities – certainly by comparison with say the introduction of accrual accounting or the implementation of IFRS, or some recent accounting standard changes such as the fair value standard.

We have confidence that agencies will be able to adapt in the same way as central agencies have done in preparing budgets and note they will have the added benefit of assistance from those central agencies.

A HoTARAC minority believe that the costs of the proposal would be extensive and the benefits limited. These jurisdictions believe that the benefits of the proposals are limited because GFS is not relevant to individual entities and the benefits to a broad range of users have not been demonstrated. More specifically, the costs involved in changing systems and providing training would not bring any benefit, as this information is not used by management or general users in those jurisdictions. They believe that the costs of the current proposal are no different from those in ED 174 (per AV3), whether the GFS presentation and classification is disclosed on–the-face of the statements or in-the-notes. Both would include high system, training, ongoing maintenance and audit costs.

One jurisdiction recommends that if these proposals are issued as a standard, that not-for-profit entities that are not consolidated into the WoG and GGS financial statements are exempted from complying with this standard due to limited resources.

Additional comments:

The majority of HoTARAC feel that while the proposed approach would result in an overall improvement in general purpose financial reporting, giving entities the option of presenting on a GAAP basis in the primary statements and on a GAAP/GFS harmonised basis in the notes potentially creates two sets of financial statements in the one document, reporting on the same operations in different ways. This could lead to confusion for users of the financial statements.

A better result would be achieved if GAAP/GFS harmonised presentation is required in the primary financial statements. This would result in more meaningful and less confusing information being conveyed to users and would be consistent with the objective of obtaining a single set of government reports as stated on page six of the exposure draft.

A minority of HoTARAC agree with the AASB at BC 3, that ED 174 was not justified on the basis of GAAP/GFS harmonisation, hence the FRC's direction must be viewed in that context. Additionally, they maintain it is not necessary for GAAP/GFS information to be in the primary financial statements, to give effect to the FRC direction.

Recognition and measurement

HoTARAC suggests the Board redraft paragraph 10 of the ED. This states that 'only those options aligned with the ABS GFS Manual shall be applied' where Australian Accounting Standards allow for optional recognition and measurement. This raises a problem, as situations where no GAAP option aligns with GFS are not considered in the ED. For example, in paragraph 25 of AASB 102 *Inventories*, where a choice is allowed between the first-in, first-out and weighted average cost formula. HoTARAC suggests aligning para.10 of the ED with the language used in para.13 of AASB 1049, which states:

"In satisfying paragraph 9 of this Standard, where compliance with the ABS GFS Manual would not conflict with Australian Accounting Standards, the principles and rules in the ABS GFS Manual shall be applied. In particular, certain Australian Accounting Standards allow optional treatments within their scope. Those optional treatments in Australian Accounting Standards aligned with the principles or rules in the ABS GFS Manual shall be applied."

Reasons for not proceeding with ED 174 also apply to ED 212

A minority of jurisdictions believe that, consistent with BC3 (and AV2), the following reasons not to proceed are equally applicable to both ED212 and ED 174. That is:

- GFS is largely a macroeconomic tool and is not relevant at an entity level
- It is inconsistent with the AASB policy of transaction neutrality.
- Information for consolidation purposes can be derived through special purpose financial reports.
- GAAP/GFS is not being pursued internationally and would be inconsistent with the objective of Australia / NZ convergence.

GAAP/ GFS note - Statement of Cash flows and Statement of Financial Position

A minority of jurisdictions believe that if this Standard is to proceed then in the GAAP/GFS note, only the Statement of Comprehensive Income should be required, as it is the only financial statement that includes any of the GFS key fiscal aggregates (i.e. net operating balance).

Additional guidance

Some jurisdictions believe that additional guidance may be required regarding AASB 1 elections that are not available (refer paragraph 34). This is necessary to reduce the costs of implementation.

One jurisdiction requests clarification from the Board on the proposal to consolidate on a line by line basis, as it still supports the partial consolidation basis as adopted by AASB 1049.

One jurisdiction seeks clarification on whether it will be allowable to disclose administered and controlled items in separate statements of comprehensive income. This was discussed in (a)(iv)A.