



Department of Treasury and Finance

1 Treasury Place
 GPO Box 4379
 Melbourne Vic 3001
 Australia
 Telephone: (+61 3) 9651 5111
 Facsimile: (+61 3) 9651 5298
 DX 210759

Contact: David Laidley
 Phone: 02 9228 4759

Mr Kevin Stevenson
 The Chairman
 Australian Accounting Standards Board
 PO Box 204
 Collins Street West
 Victoria 8007

Dear Mr Stevenson

ED 238 CONSOLIDATED FINANCIAL STATEMENTS – AUSTRALIAN IMPLEMENTATION GUIDANCE FOR NOT-FOR-PROFIT ENTITIES

The Heads of Treasuries Accounting and Reporting Advisory Committee (HoTARAC) welcomes the opportunity to provide comments to the Australian Accounting Standards Board Exposure Draft 238 *Consolidated Financial Statements – Australian Implementation Guidance for Not-for-Profit Entities*.

HoTARAC is highly supportive of the AASB's efforts in developing Australian Implementation Guidance for not-for-profit (NFP) entities regarding AASB 10 *Consolidated Financial Statements*.

While HoTARAC generally agrees with the proposed Guidance, our key issues are in the following areas, where we believe that additional consideration is required:

- Delegated power – to clarify that a delegated power of itself is not sufficient to demonstrate control or preclude control.
- Removal rights – to confirm that that a Minister's power to remove a public sector entity's decision makers does not, of itself, preclude a public sector entity from controlling another body.
- Substantively enacted legislation – to reconsider whether substantively enacted legislation provides the investor the current ability to direct relevant activities.

- De facto agent – to provide additional guidance regarding the meaning of de facto agents as this is a critical issue for the public sector.
- Removal of certain Aus paragraphs – to include a table of concordance which clearly shows where previous Aus paragraphs were not retained.

Further detailed comments are attached. If you have any queries regarding HoTARAC's comments, please contact David Laidley from New South Wales Treasury on (02) 9228 4759.

Yours sincerely


Grant Hehir
CHAIR
HEADS OF TREASURIES ACCOUNTING AND REPORTING ADVISORY
COMMITTEE

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Encl

**HoTARAC Response to AASB ED 238 *Consolidated Financial Statements—
Australian Implementation Guidance for Not-for-Profit Entities***

Specific matters for comment

1. *Whether Australian implementation guidance for NFP entities should be added to AASB 10 and AASB 12 and, if so, whether it should, as proposed, be authoritative (ie “integral” to the Standard) or non-authoritative material.*

HoTARAC agrees that authoritative Australian implementation guidance should be added for NFP entities to AASB 10 and AASB 12.

2. *Whether the proposed implementation guidance appropriately explains the definition of ‘control’ in AASB 10 for application by NFP entities, including the following aspects:*
 - (a) *the broad nature of returns from a controlled NFP entity, including non-financial and indirect benefits (paragraphs IG16 and IG17); and*
 - (b) *the four detailed sets of implementation examples in the proposed Appendix E for AASB 10.*

- (a) HoTARAC agrees that the proposed implementation guidance appropriately explains the broad nature of returns from a controlled NFP entity.
- (b) HoTARAC is strongly supportive of the AASB’s decision to include implementation examples to help clarify the application of the AASB 10 requirements to NFP entities. However, HoTARAC offers the following comments on the examples, and an additional example, for further consideration.

IG21 and the legal concept of delegations

IG21 provides that “a department acts as a principal in its own right even under a delegation of power from the Minister if it is acting with its own discretion, not subject to specific direction by the Minister”.

This is not entirely consistent with HoTARAC’s understanding of the concept of “delegation” (as summarised in AASB Agenda Paper 7.3, June 2012). We understand that where there is a delegated power, the person/entity exercising that power is always acting in their own right (in relation to that power) and with their own discretion and cannot be directed by the delegator. The wording in paragraph IG21, however, implies that it is possible that a person may be acting under delegation and may not always have discretion; i.e. they may be subject to specific direction by the delegator.

We think that this paragraph confuses the concept of delegation and needs to be explained more clearly. That is, in HoTARAC’s view, a delegated power of itself is not sufficient to demonstrate control or preclude control. The issue is more whether

the delegated power is sufficiently wide to allow the delegate to control the relevant activities of the other entity.

Example IG4A

Example IG4A concludes that "...the Department has delegated power over the statutory authority and is acting as an agent on behalf of the Minister".

However, the information in Example IG4, which forms the background to Example IG4A, does not refer to there being a delegation even though the conclusion is that the Department has "delegated power". Instead, the facts refer to the Department "acting on behalf of the Minister" and requiring the Minister's approval for certain decisions. This is not consistent with HoTARAC's understanding of a delegation or "delegated power", where the delegate acts in its own right and cannot be directed by the delegator.

In addition, in assessing control, the conclusion makes no mention of the key fact included in Example IG4, that the Minister appoints the statutory authority's governing council. Further, the reference to remuneration does not seem a particularly strong argument that supports the Department acting as an agent. This is because the nature of government is such that whether or not the Department is acting as a principal or agent the Department is likely to be explicitly remunerated.

Example IG4B

This example introduces a new term "delegated control", without explanation. Again, as per Example IG4A, there are no facts given which indicate that the Minister has delegated power to the Department. Further, the example varies the facts in IG4 to support the conclusion that the Department is acting as a principal. However, there is no variation to the core fact, which states that the Department "acts as 'system manager' for the State public health system on behalf of the Minister". The phrase "on behalf of" implies the Department is acting as an agent, which is contrary to the conclusion.

Example IG2, IG3A Alternative outcomes

A majority of HoTARAC respondents consider that the "alternative outcome" paragraphs may be unnecessary, as all examples are based on judgements and will be impacted by alternative facts. It seems particularly unnecessary in IG3A, given that IG3B illustrates the alternative scenario of where a State government does control a university.

Additional example of protective rights

HoTARAC proposes an additional example to be added to paragraph IG15 to further illustrate protective rights, as follows:

Use of a regulator's intervention powers where a regulated entity is non-compliant with performance standards or due to failure to comply with a requirement or direction issued under an Act.

Such powers include appointment of additional members to the governing body under certain restricted circumstances. For example, a State housing regulator may recommend the appointment of one or more appropriately qualified persons to the governing board of a regulated entity, when the entity has failed to comply with performance standards. The regulator must first consult with the governing body of the entity about a proposed recommendation and must consider any nominations put forward by the governing body. The regulator-appointed members will become part of the governing body of the regulated entity. The appointed members do not report to the regulator nor does the regulator direct them on how to govern. Their duties and responsibilities are exactly the same as other members of the governing body.

3. *Whether the proposed implementation guidance appropriately explains the definition of 'structured entity' in AASB 12 for application by NFP entities.*

HoTARAC agrees that the draft implementation guidance appropriately explains the definition of "structured entity" in AASB 12 for application by NFP entities. However, it is noted that a similar clarification is also relevant to FP public sector entities, which are often established under statutory provisions.

4. *Whether it is appropriate to exclude all disclosure requirements in AASB 12 in respect of GGS financial statements (see the proposed amendments to AASB 1049 set out in the ED).*

HoTARAC agrees that it is appropriate to exclude all disclosure requirements in AASB 12 in respect of GGS financial statements.

5. *Whether there are any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals, including GFS harmonisation issues.*

HoTARAC is not aware of any regulatory issues that may affect the implementation of the proposals.

6. *Whether, overall, the proposals would result in financial statements that would be useful to users.*

Subject to the above comments, overall, HoTARAC believes that the proposals would result in financial statements that would be useful to users.

7. *Whether the proposals are in the best interests of the Australian economy.*

No comments.

8. *Unless already provided in response to the above specific matters for comment, the costs and benefits of the proposals relative to the current requirements, whether quantitative (financial or non-financial) or qualitative.*

No comments.

Other comments

Removal rights

HoTARAC believes that additional guidance should be provided regarding the concept of removal rights within government. Paragraph B65 provides that when a single party holds substantive removal rights and can remove the decision maker without cause, this, in isolation, is sufficient to conclude that the decision maker is an agent.

A government Minister will often have the power to remove a decision maker. For example, the relevant Minister can always remove the Head of a Department and legislation often gives the Minister power to remove directors of statutory authorities. This seems to imply that a Department can never, and statutory authorities can only rarely, control another entity and that those other entities are acting as agents. This was previously addressed in the Basis for Conclusions to IASB ED 10 (paragraphs BC96-97), the precursor to IFRS 10, where it was explicitly stated that the IASB did not believe the guidance on agency relationships would prevent an intermediate parent from preparing consolidated financial statements. However, when IFRS 10 was issued, these paragraphs were omitted from the Basis for Conclusions.

In HoTARAC's view, a Minister's power of removal discussed above arises from a control relationship rather than a principal/agent relationship. That is, a Minister can dismiss a public sector entity's key personnel irrespective of any relationship that the entity has with other entities. Given that this is a particular issue in the public sector, where individual entities are controlled as part of the Total State Sector/Whole of Government, HoTARAC believes that this view should be confirmed by the AASB.

Substantively enacted legislation

Paragraph IG12 explains that sometimes rights can be substantive even though they are not currently exercisable. However, it then provides that rights in substantively enacted legislation cannot give the investor the current ability to direct the relevant activities.

HoTARAC understands that the clarification in paragraph IG12 is based on paragraph 30 of IPSAS 6 *Consolidated and Separate Financial Statements*. However, given that IPSAS 6 has not yet been updated for the new IFRS 10, it is not clear that the principle in IPSAS 6 is consistent with IFRS 10. Instead it may be argued that the effect of paragraph IG12 is actually to amend IFRS 10. HoTARAC believes that this needs to be further considered by the AASB.

Paragraph IG12, as it is written, is confusing and difficult to understand. HoTARAC recommends that the whole paragraph be reworded to improve clarity.

De facto agent

HoTARAC notes that the AASB has not proposed implementation guidance in respect of some topics, such as de facto agents, due to its assessment that the issue arises for both FP and NFP entities. However, HoTARAC recommends that further consideration should be given to the issue of de facto agents and what it means in the public sector context, where all public sector entities are related parties to all other public sector entities. Additional guidance on this matter is critical for the application of the AASB 10 concept in the public sector context. It would be preferable for the AASB to apply its NFP deliberations and decision on this matter to FP entities as well.

Removal of certain Aus paragraphs

The previous AASB 127 Aus paragraphs have not been fully carried forward. For example, the following paragraphs on indicators of control have been omitted:

- Para Aus17.3(e) where an entity is required to submit to Parliament reports on operations that include audited financial statements
- Aus 17.4 on the government's rights to residual assets.

It is important that the main differences for the public sector are made transparent and the reasons explained. Accordingly, HoTARAC recommends including a more detailed explanation in the Basis for Conclusions.

A table of concordance would also be useful.