

11 March 2016

Ms Kris Peach  
Chair  
Australian Accounting Standards Board  
PO Box 204  
Collins St West Victoria 8007  
AUSTRALIA

Dear Ms Peach

**Invitation to Comment (ITC 34) AASB Agenda Consultation 2017-2019**

The Australasian Council of Auditors-General (ACAG) welcomes the opportunity to contribute to the future domestic work program of the AASB. Please find attached the ACAG response to the *AASB Agenda Consultation 2017-2019* (ITC 34).

ACAG supports the AASB's current work program of standards-level projects and research projects as they are critical areas of attention for public sector financial reporting.

ACAG's suggestions for the 2017-2019 work program are based on our experiences as the auditor of public sector financial reports of not-for-profit and for-profit entities. We have suggested these projects on the basis that they either require clarification in terms of existing requirements and application guidance and/or to fill a void in existing pronouncements.

The views expressed in this submission represent those of all Australian members of ACAG.

The opportunity to comment is appreciated and I trust you will find the attached comments useful.

Yours sincerely



A T Whitfield PSM  
**Chairman**  
**ACAG Financial Reporting and Auditing Committee**

## Specific Matters for Comment

1. What topics, including external reporting topics, do you think should be added to the AASB work program (research and standard-setting)? Please outline the reasons why you think the project(s) should be addressed by the AASB.

### a) Projects for the AASB standard-setting work program

Topic	Reasons for inclusion
AASB 108 <i>Accounting Policies, Changes in Accounting Estimates and Errors</i>	<p>Current interpretation and application issues include:</p> <ul style="list-style-type: none"> <li>• whether immaterial prior year errors can be adjusted retrospectively?</li> <li>• whether a third balance sheet should be prepared for the retrospective correction of prior period errors that are not quantitatively material? AASB 101.40A(b) requires a third balance sheet for material retrospective misstatements. However, preparers may currently both make a retrospective restatement, and refuse to make suitable disclosures on the basis that it is not quantitatively material. Should retrospective restatements be considered to be qualitatively material?</li> <li>• difficulties in distinguishing between an error and change in accounting policy and between a change in a change in accounting policy and a change in estimate</li> <li>• current trends of ‘un-zipping’ prior periods. The standard requires material prior period errors to be adjusted retrospectively, but is silent on the treatment of immaterial errors. In the absence of explicit guidance, entities are posting immaterial errors retrospectively. As the standard does not deal with immaterial errors, auditors have no basis to consider the practice unacceptable</li> </ul>
AASB 101 <i>Presentation of Financial Statements – Going Concern Assumption</i>	<p>Currently, the existing requirements of AASB 101, para 25 &amp; 26, do not cater for the public sector context where material uncertainties relating to the going concern assumption are different from the private sector. There are unique public sector factors that can influence the existence of a material uncertainty, including the entity’s government funding model, changes in the enabling legislation, and machinery of government changes. The standard could prescribe the factors a public sector reporting entity should consider when assessing if there is a material uncertainty.</p>
Grant expense/liability	<p>While the AASB is working on the accounting by the grantee (income), there is currently a lack of guidance from the grantor’s perspective as to when to recognise an expense.</p>

### b) Projects for the AASB research centre work program

Topic	Reasons for inclusion
Post Implementation Review of AASB 13 <i>Fair Value Measurement</i>	<p>ACAG believes it is timely for a post-implementation review of AASB 13 and its application to the valuation of public sector assets. Since its implementation, the requirements of AASB 13 have been particularly difficult to apply to public sector assets mainly because of their nature and attributes which are not market or profit driven. ACAG has identified the following areas of concern:</p> <ul style="list-style-type: none"> <li>• which valuation approach to use for a public sector asset where there are few or no market participants and where information about the inputs to a current replacement cost model may be scarce</li> <li>• the practical issues of creating a hypothetical market transaction in a hypothetical market</li> <li>• there is a lack of guidance on current replacement cost which has led to extreme variations in the valuation industry (e.g. the use of greenfield vs brownfield rates)</li> <li>• clarification on whether the income approach method should be used if the income is derived in a rate regulated market, e.g. water and electricity services</li> <li>• inconsistency of the interpretation and disclosure of significant unobservable inputs</li> </ul>

Topic	Reasons for inclusion
	<ul style="list-style-type: none"> <li>• lack of specific requirements for determining obsolescence in a public sector asset, including issues of overdesign or overcapacity and the availability of newer/cheaper technology</li> <li>• relationships between current replacement cost (CRC), useful lives and remaining service potential</li> <li>• clarification required on the links between depreciation and valuation and non-proportionate changes in accumulated depreciation</li> <li>• confusion between entity perspective v. market perspective when using the cost approach. The DRC method commonly used by valuers generally adopts an entity's perspective, i.e. "the market participant buyer steps into the shoes of the entity" (IFRS 13.BC78). On the other hand, there are instances when a valuer has adopted a market participant's perspective when determining the remaining service potential e.g. use market participant's estimate of remaining economic life rather than the entity's estimate of remaining useful life</li> <li>• need for a deprivation test in the current replacement cost approach (similar to that in the definition of value-in-use for NFP entities in AASB 136 – removed in ED 269)</li> <li>• whether to use a "gross" valuation or "net" valuation presentation approach in disclosures</li> <li>• clarification on what constitutes a unit of account and the contradiction of allowing assets to be separated into smaller units even when the highest and best use is in combination with other assets.</li> <li>• clarification on accounting for revaluation adjustments in a for-profit entity – is it necessary to allocate to all individual assets, or is it acceptable to allocate to certain classes only?</li> </ul>
Measurement of Heritage assets	The AASB could leverage off the International Public Sector Accounting Standards Board's (IPSASB's) work planned for 2016 to research the measurement of heritage assets in the public sector. ACAG's view is that the existing requirements are not sufficient to address the valuation of heritage assets.
Post Implementation Review of AASB 1049 <i>Whole of Government and General Government Sector Financial Reporting</i>	In light of the recent amendments to the System of National Accounts and the Government Finance Statistics manual, ACAG believes it is timely for a post-implementation review of AASB 1049 <i>Whole of Government and General Government Sector Financial Reporting</i> . In addition, ACAG suggests that the AASB reconsider the requirement to have all property, plant and equipment measured at fair value.
Public sector combinations	The AASB could leverage off the work being undertaken by the IPSASB as existing Australian pronouncements do not adequately prescribe the accounting treatment of public sector combinations, and in particular, the requirements for machinery of government changes.
Post Implementation Review of AASB 1055 <i>Budgetary Reporting</i>	<p>We recommend the AASB undertake a post-implementation review of AASB 1055. Given other mechanisms such as final budget outcomes are the primary source of information about how agencies have performed against budgets, the value of the information in financial reports needs to be analysed against the costs of preparing and auditing recast budgets and explanations of major variances.</p> <p>We note there has been varied application of requirements. For example, in one jurisdiction budget information for the statements of financial position and cash flows, including explanation of major variances from budget, has not been required on the basis that the budget information included in those statements is not prepared on the same basis as accounting standards. Accordingly, it was determined that the related budget information and variance analysis was unlikely to result in useful information for users.</p> <p>Other interpretation and application issues include the:</p> <ul style="list-style-type: none"> <li>• definition of "major variances"</li> <li>• quality of explanations for "major variances".</li> </ul>

Topic	Reasons for inclusion
Framework for Government budgets and forward estimates	<p>The AASB could look at a project, which is outside the conventional historical financial reporting, that researches the different accounting frameworks used by governments to prepare and report budget information and forward estimates. The government's budgets, forward estimates and final budget outcomes attract more interest from users and stakeholders than historical annual financial reports. In applying AASB 1055 <i>Budgetary Reporting</i>, it is clear that there are varying approaches in how these budgets and estimates are prepared.</p> <p>The AASB could develop a framework that includes:</p> <ul style="list-style-type: none"> <li>• references to the qualitative characteristics of key assumptions and bases for prospective financial information</li> <li>• measurement and recognition requirements of the accounting standards</li> <li>• budgets to be prepared using the accounting policies required to account for financial results so that the actual results are directly comparable to budget estimates</li> <li>• linkage of the reporting budget information and actual outcomes with reporting of service performance information.</li> </ul>
Government departments & AASB 1050 <i>Administered Items</i>	<p>The AASB has carried forward differentiation in accounting treatment of government departments from AAS 29 <i>Financial Reporting by Government Departments</i>. Government departments are defined with reference to being created pursuant to administrative arrangements or otherwise being designated as a government department. It is not clear what the conceptual basis is for the differential treatment of government departments is. For example, is the basis of differentiation that departments are core appropriation process? Contemporary government structures may not reflect this.</p> <p>Some of the differentiation for government departments may not be achieving outcomes intended. For example, in some jurisdictions, volunteer fire fighting entities are not government departments, which bring in to question the differentiation for mandatory recognition of volunteer services on the basis of whether or not an entity is a department.</p> <p>We particularly consider that review of the scope of AASB 1050 <i>Administered Items</i> is necessary. There are public sector entities, other than government departments, that manage administered items on behalf of government which are not required to disclose these transactions and balances in their financial reports. In reviewing the scope of this standard, further guidance on identifying administered items would be beneficial.</p>
Australian Reporting Framework	<p>The AASB could expand the scope of this project, beyond an examination of which entities should be in which tier, to consider whether the benefits could be achieved by other methods e.g. guidance on applying materiality and decluttering financial statements.</p>
Post Implementation Review of AASB 124 <i>Related Party Disclosures</i>	<p>ACAG suggests that a post-implementation review of the AASB 124 Related party Disclosures and its application to the not-for-profit public sector financial reports would be beneficial. A review within a year or two of the implementation of AASB 124 would identify whether the objectives of the standard have been met, measuring the costs and benefits of compliance, and whether any changes or additional guidance is required. Through this early phase of preparing for the implementation of AASB 124, some examples that may require additional guidance include:</p> <ul style="list-style-type: none"> <li>• it is not clear what constitutes a transaction (with a related party) that would potentially need to be disclosed. For example, in a local government context, does rezoning land owned by a Councillor constitute a related party transaction (RPT)? Also, would this be a material RPT that should be disclosed?</li> <li>• The definition of related party transactions includes the statement, “regardless of whether a price is charged”. Guidance on transactions within the public sector where there is no price charged would be beneficial. While it is clear in some instances that a related party transaction occurred (for example free electricity supply or forgiveness of debt), there are other circumstances (like changes of laws or zoning which provide a benefit to a KMP) that are more difficult to determine if they are a related party transaction.</li> </ul>

2. What priority should be ascribed to the project(s)? Please outline the reasons why you think the project(s) should be prioritised in this manner by the AASB.

a) Projects for the AASB standard-setting work program

Topic	Priority assigned	Reasons
AASB 108 <i>Accounting Policies, Changes in Accounting Estimates and Errors</i>	High	The uncertainty and lack of clarity of the accounting requirements is creating confusion amongst preparers and auditors which is leading to a decline in the quality of financial reporting and increased costs.
AASB 101 <i>Presentation of Financial Statements – Going Concern Assumption</i>	Medium	ACAG are only requesting guidance be provided for management's going concern assessment for not-for-profit public sector entities, particularly as public sector entities often cease, but with their functions continuing elsewhere.
Grant expense/liability	High	There are tens of \$billions of grants issued by Australian Governments every year, without any direction or clear guidance from Australian Accounting Standards as to the recognition of the expense.

b) Projects for the AASB research centre work program

Topic	Priority assigned	Reasons for assignment
Post Implementation Review of AASB 13 <i>Fair Value Measurement</i>	High	The uncertainty and lack of clarity of the accounting requirements, such as measurement of public sector assets and the application of the fair value hierarchy, is creating confusion amongst preparers and auditors which is leading to a decline in the quality of financial reporting and increased costs.
Heritage assets	Medium	The lack of prescriptive materials in existing pronouncements is creating inconsistent practices and reduces the comparability of financial reports.
Post Implementation Review of AASB 1049 <i>Whole of Government and General Government Sector Financial Reporting</i>	Medium	Recent amendments to the System of National Accounts and the Government Finance Statistics manual warrant a post-implementation review of the AASB 1049.
Public sector combinations	Medium	The lack of prescriptive materials in existing pronouncements is creating inconsistent practices and reduces the comparability of financial reports.
Post Implementation Review of AASB 1055 <i>Budgetary Reporting</i>	High	ACAG believes that further clarification and guidance will improve the consistency and comparability of financial reporting and improve the information provided to the users of government financial reports.
Framework for Government budgets and forward estimates	Medium	The lack of prescriptive materials in existing pronouncements is creating inconsistent practices and reduces the comparability of Government budget documents and historical financial reports that contain budget information.

<b>Topic</b>	<b>Priority assigned</b>	<b>Reasons for assignment</b>
Government departments & AASB 1050 <i>Administered Items</i>	Medium	It is likely that clarification of the conceptual basis would assist in more relevant information in financial reports.
Australian Reporting Framework	Medium	Before the AASB invests further effort in fine-tuning tiered reporting, ACAG suggests the Board consider whether tiered reporting is the right solution.
Post Implementation Review of AASB 124 <i>Related Party Disclosures</i>	High	The uncertainty and lack of clarity of the accounting requirements is creating confusion amongst preparers and auditors which may lead to a decline in the quality of financial reporting and increased costs upon implementation.

**3. Are there any topics on the current AASB work program that you think should be removed from the work program? Please outline the reasons why you think the project(s) should be removed.**

ACAG supports the AASB's current work program of standards-level projects and research projects as they are critical areas of attention for public sector financial reporting.

ACAG does not recommend the removal of any projects from the current AASB work program as the current projects are adequate and cater for a range of constituents such as for-profits, not-for-profits and public sector agencies.