PRE-BALLOT DRAFT
For Board member comment at M171 (June 2019)

AASB Exposure Draft

ED XXX
[Month Year]

Amendments to Australian Accounting Standards – Removal of Special Purpose Financial Statements under Standards for For-Profit Entities

Comments to the AASB by DD MONTH YYYY

Australian Government
Australian Accounting Standards Board

Commenting on this AASB Exposure Draft

Comments on this Exposure Draft are requested by DD MONTH YYYY.

Formal Submissions

Submissions should be lodged online via the “Work in Progress – Open for Comment” page of the AASB website (www.aasb.gov.au/comment) as a PDF document and, if possible, a Word document (for internal use only).

Other Feedback

Other feedback is welcomed and may be provided via the following methods:

E-mail: standard@aasb.gov.au
Phone: (03) 9617 7600

All submissions on possible, proposed or existing financial reporting requirements, or on the standard-setting process, will be placed on the public record unless the Chair of the AASB agrees to submissions being treated as confidential. The latter will occur only if the public interest warrants such treatment.

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Introduction

Australian Accounting Standards

The Australian Accounting Standards Board (AASB) develops, issues and maintains Australian Accounting Standards.

The AASB is a Commonwealth entity under the *Australian Securities and Investments Commission Act 2001*. AASB 1053 *Application of Tiers of Australian Accounting Standards* explains the two tiers of Australian Accounting Standards.

Exposure Drafts

The publication of an Exposure Draft is part of the due process that the AASB follows before making a new Australian Accounting Standard or amending an existing one. Exposure Drafts are designed to seek public comment on the AASB's proposals for new Australian Accounting Standards or amendments to existing Standards.

Why we are making these proposals

The International Accounting Standards Board (IASB) issued a revised Conceptual Framework titled *Conceptual Framework for Financial Reporting* (RCF) in March 2018. However, the RCF definition of reporting entity is different from the reporting entity concept in Statement of Accounting Concepts SAC 1 *Definition of the Reporting Entity* and some Australian Accounting Standards (AAS). This inconsistency between the RCF and SAC 1 and AAS could result in misinterpretation, incorrect application of AAS and non-compliance with IFRS Standards.

The current Australian reporting entity concept allows entities to self-assess whether they should prepare:

(a) general purpose financial statements (GPFS), which requires compliance with all AAS, including their definition, recognition, measurement, presentation and disclosure requirements; or

(b) special purpose financial statements (SPFS), which requires compliance with only a handful of AAS, which focus more on the fundamental presentation of financial statements and certain disclosures, and permits entities to self-select other AAS requirements (such as recognition and measurement (R&M) requirements) to apply in preparing and presenting the SPFS.

The ability for entities to self-assess their reporting requirements under the Australian reporting entity concept has given rise to the more fundamental 'SPFS problem', when two similar entities might prepare very different sets of financial statements, one preparing GPFS using a robust and consistent framework, and the other preparing SPFS with self-selected requirements. This reduces comparability for entities of similar economic circumstances and undermines the fundamentals of trust and transparency in financial reporting.

The Board has been working to address the SPFS problem for over a decade. During that time, it has been made aware of a range of fundamental issues with the application of the Australian reporting entity concept, as well as the quality of SPFS. For example:

(a) research has suggested that the reporting entity concept is neither well understood nor always applied as intended, leading to entities inappropriately lodging SPFS on the public record;

(b) SPFS are not required to apply all accounting standards, which results in variability in recognition, measurement and disclosure of similar items, limiting the consistency, comparability and transparency of financial statements;

(c) users of financial statements have raised concerns that the current financial reporting framework does not provide consistent, comparable and transparent financial statements; and

(d) SPFS have been the subject of significant regulatory scrutiny, such as the Senate Economics References Committee enquiry on corporate tax avoidance.

A range of other issues relating to the SPFS problem are addressed in the Basis for Conclusions to this Exposure Draft.

In May 2018, the Board issued Invitation to Comment ITC 39 *Applying the IASB's Revised Conceptual Framework and Solving the Reporting Entity and Special Purpose Financial Statement Problems*, proposing to remove the ability of entities to prepare SPFS when required to comply with AAS. That consultation process confirmed that the 'SPFS problem' needs to be addressed.

In light of the current regulatory environment – with calls in the *Final Report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry* to remove special rules and exceptions that create regulatory complexities – it is time for the AASB to play its role in improving the consistency, comparability, transparency and enforceability of financial reporting in Australia.

What we are proposing

This ED proposes:

(a) amendments to AAS to remove the ability to prepare SPFS for the following for-profit entities when compliance with standards is required:

  (i) for-profit private sector entities that are required by legislation to comply with either Australian Accounting Standards or accounting standards;

  (ii) other for-profit private sector entities that are required only by their constituting document or another document to comply with Australian Accounting Standards, provided that the relevant document was created or amended on or after 1 July 2020; and

  (iii) other for-profit entities that elect to apply the Conceptual Framework and the consequential amendments to other pronouncements set out in Accounting Standards AASB 2019-1 *Amendments to Australian Accounting Standards – References to the Conceptual Framework* and AASB 2019-Y *Amendments to Australian Accounting Standards – Removal of Special Purpose Financial Statements under Standards for For-Profit Entities*; and

(b) to provide relief from restating and presenting comparative information in the year of transition for entities transitioning to full R&M requirements (refer to the transition requirements section below).

This ED does not change which entities are required by legislation to prepare financial statements – that is not the role of the AASB. However, the Australian Government Treasury has recently doubled the thresholds in the *Corporations Act 2001* for distinguishing large and small proprietary companies. As a consequence, the financial reporting obligations of large proprietary companies are better targeted at economically significant companies.

The AASB acknowledges that removing the ability to prepare SPFS with no other mitigating action would result in an increased reporting burden for some entities if they were to be required to transition from SPFS into the current two-tiered GPFS framework: Tier 1, which is full AAS, and Tier 2, which is AAS Reduced Disclosure Requirements (RDR). A related Exposure Draft ED 2XX *New Accounting Standard: General Purpose Financial Statements – Simplified Disclosures for Tier 2 Entities* proposes replacing the current GPFS Tier 2 (RDR) framework with a framework that would still require compliance with all recognition and measurement requirements in AAS but would have simplified disclosures.

Transition requirements

In order to facilitate an earlier effective date (reporting periods beginning on or after 1 July 2020) for the removal of the ability for many for-profit entities to prepare SPFS when compliance with AAS is required, the Board decided to propose amendments to AASB 1 *First-Time Adoption of Australian Accounting Standards*. Under these amendments, an entity preparing GPFS under Tier 2 requirements for the first time would not need to restate or present comparative information as otherwise required by AAS. The date of transition would also be changed to the beginning of the reporting period, rather than the beginning of the earliest comparative period. Instead of full comparative information, the amendments to AASB 1 would require entities adopting this approach to provide information for financial statement users on the adjustments required in transitioning from SPFS to GPFS-Tier 2.

The AASB noted that relief from the restatement of comparative information would be beneficial as it would reduce costs to preparers whilst also providing a consistent, comparable, transparent and enforceable reporting framework earlier. The AASB considered other options for transitional relief, including allowing entities that are subsidiaries to recognise amounts based on information provided in reporting packs to their parent entity for consolidation purposes, and allowing entities to immediately write off 'deemed goodwill' calculated in accordance with AASB 1, Appendix C. However, the AASB considered there were insufficient compelling reasons or evidence to warrant any other transitional relief, in addition to the relief not restate or present comparative information, as explained in paragraphs BC89-BC100.

Application date

It is proposed that this Standard would be applicable to annual reporting periods beginning on or after 1 July 2020, with earlier adoption permitted.

What happens next

The AASB will consider feedback on this Exposure Draft at future meetings and based on the information received will determine whether the proposals should form the basis of the amending Standard, with or without amendment. Depending on the nature and extent of the feedback, the AASB may publish a Fatal-Flaw Review Draft to enable further consultation with stakeholders.

We need your feedback

Comments are invited on any of the proposals in this Exposure Draft by DD MONTH YYYY. Submissions play an important role in the decisions that the AASB will make in regard to a Standard. The AASB would prefer that respondents express a clear overall opinion on whether the proposals, as a whole, are supported and that this opinion be supplemented by detailed comments, whether supportive or otherwise, on the major issues. The AASB regards supportive and non-supportive comments as essential to a balanced review of the issues and will consider all submissions, whether they address some or all specific matters, additional issues or only one issue (whether an issue specifically identified below or another issue).

Specific matters for comment

The AASB would particularly value comments on the following:

1 The proposed amendments to the *Conceptual Framework for Financial Reporting* paragraph Aus1.1 (see page 10 of this ED) identifies the for-profit entities that would be required to apply the revised Conceptual Framework and hence no longer have the ability to prepare SPFS when compliance with Standards is required. Do you agree that:

(a) the amendments set out in this ED effectively remove the ability to prepare SPFS for the for-profit entities identified in paragraph Aus1.1 of the Conceptual Framework? If not, please provide your reasons.

(b) the exception for other for-profit private sector entities that are required only by their constituting document or another document to comply with Australian Accounting Standards, provided that the relevant document was created or amended on or after 1 July 2020, is appropriate? If not, please provide your reasons (see paragraphs BC61-BC72).

(c) entities that are not explicitly required to comply with accounting standards, but are required by legislation or otherwise to provide financial statements or financial information that gives a true and fair view should not be covered by these proposals? If not, please provide your reasons (see paragraphs BC58-BC59).

2 Do you agree with the proposal to amend AASB 1 to provide relief from the restatement of comparative information in the year of transition from SPFS to GPFS Tier 2 (see paragraphs BC91-BC100)? If not, please provide reasons. If yes, do you agree with:

(a) the proposed disclosures in relation to the comparative period (see paragraph AusE8.4 for AASB 1 on page 12). If not, please provide your reasons.

(b) the additional option for quantified adjustment information where the SPFS have not applied the recognition and measurement requirements of only a few Standards (see paragraph AusE8.5 for AASB 1 on page 12)? If not, please provide your reasons.

3 Do you agree that additional transition relief is not required (see paragraphs BC91-BC100)? If not, what transitional relief should be provided and what are your reasons?

4 Do you agree with the proposed effective date of annual periods beginning on or after 1 July 2020 (see paragraphs BC101-BC104), given the proposed transition relief? If not, please provide your reasons.

Commented [BJ1]: Question 1 for Board members
Do Board Members consider there are any other Specific Matters for Comment required in addition to those proposed below?

Commented [BJ2]: Question 2 for Board members
Do Board members agree that this Specific Matter for Comment should be asked as part of this ED?

Commented [AC3]: Question 3 for Board members
Do you agree with proposing this additional option?

Please refer to staff comments at page 12.

General matters for comment

The AASB would also particularly value comments on the following general matters:

5 Whether *The AASB's For-Profit Entity Standard Setting Framework* and *The AASB's Not-for-Profit Entity Standard Setting Framework* has been applied appropriately in developing the proposals in this Exposure Draft?

6 Whether there are any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals, including Government Financial Statistics (GFS) implications?

7 Whether, overall, the proposals would result in financial statements that would be useful to users?

8 Whether the proposals are in the best interests of the Australian economy?

9 Unless already provided in response to matters for comment above, the costs and benefits of the proposals relative to the current requirements, whether quantitative (financial or non-financial) or qualitative? In relation to quantitative financial costs, the AASB is particularly seeking to know the nature(s) and estimated amount(s) of any expected incremental costs, or cost savings, of the proposals relative to the existing requirements.

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Contents

PREFACE

[DRAFT] ACCOUNTING STANDARD
AASB 2019-Y *AMENDMENTS TO AUSTRALIAN ACCOUNTING STANDARDS – REMOVAL OF SPECIAL PURPOSE FINANCIAL STATEMENTS UNDER STANDARDS FOR FOR-PROFIT ENTITIES*

[Draft] Australian Accounting Standard AASB 2019-Y *Amendments to Australian Accounting Standards – Removal of Special Purpose Financial Statements under Standards for For-Profit Entities* is set out on pages 9 – 17. All the paragraphs have equal authority.

Preface

Standards amended by AASB 2019-Y

This Standard makes amendments to the Australian Accounting Standards and other pronouncements listed on page 9 of the Standard.

These amendments extend the application of the *Conceptual Framework for Financial Reporting* (May 2019) to additional for-profit private sector entities. They build upon the consequential amendments to pronouncements previously made in Accounting Standard AASB 2019-1 *Amendments to Australian Accounting Standards – References to the Conceptual Framework*.

Main features of this Standard

Main requirements

This Standard makes amendments to the *Conceptual Framework for Financial Reporting* (*Conceptual Framework*) so that it applies to:

(a) for profit-private sector entities that are required by legislation to comply with either Australian Accounting Standards or accounting standards (with the previous limitation to entities with public accountability removed);

(b) other for-profit private sector entities that are required only by their constituting document or another document to comply with Australian Accounting Standards, provided that the relevant document was created or amended on or after 1 July 2020; and

(c) other for-profit entities (including for-profit public sector entities) that elect to apply the *Conceptual Framework* and the consequential amendments to other pronouncements set out in AASB 2019-1 and this Standard.

The *Framework for the Preparation and Presentation of Financial Statement*s and Statement of Accounting Concepts SAC 1 *Definition of the Reporting Entity* are amended so that they continue to not apply to for-profit entities that are applying the *Conceptual Framework* (subject to exceptions stated in the Standards).

An entity that is required to apply the *Conceptual Framework* cannot therefore identify as a non-reporting entity under SAC 1. As a consequence, the ability of such an entity to prepare special purpose financial statements is removed and it will need to prepare general purpose financial statements that comply with Australian Accounting Standards (or accounting standards under legislative requirements). Consequential amendments are made to various Standards, including to the applicability of the reporting entity definition in AASB 1057 *Application of Australian Accounting Standards*, which is not relevant to entities applying the *Conceptual Framework*.

This Standard also makes amendments to AASB 1 *First-Time Adoption of Australian Accounting Standards* to provide relief from restating and presenting comparative information in the year of transition for entities transitioning from special purpose financial statements to general purpose financial statements (Tier 2).

Application date

This Standard applies to annual reporting periods beginning on or after 1 July 2020, with earlier application permitted.

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[Draft] Accounting Standard AASB 2019-Y

The Australian Accounting Standards Board makes Accounting Standard AASB 2019-Y *Amendments to Australian Accounting Standards – Removal of Special Purpose Financial Statements under Standards for For-Profit Entities* under section 334 of the *Corporations Act 2001*.

Kris Peach

Chair – AASB

Dated … [date]

[Draft] Accounting Standard AASB 2019-Y
Amendments to Australian Accounting Standards – Removal of Special Purpose Financial Statements under Standards for For-Profit Entities

Objective

This Standard amends:

(a) the *Conceptual Framework for Financial Reporting* (May 2019);

(b) the *Framework for the Preparation and Presentation of Financial Statements* (July 2004);

(c) Statement of Accounting Concepts SAC 1 *Definition of the Reporting Entity* (August 1990);

(d) AASB 1 *First-Time Adoption of Australian Accounting Standards* (July 2015);

(e) AASB 10 *Consolidated Financial Statements* (July 2015);

(f) AASB 1053 *Application of Tiers of Australian Accounting Standards* (June 2010); and

(g) AASB 1057 *Application of Australian Accounting Standards* (July 2015);

to update the set of for-profit entities for which the *Conceptual Framework for Financial Reporting* is relevant and the reporting entity concept in SAC 1 is no longer relevant. Such entities are therefore not able to prepare special purpose financial statements when compliance with Australian Accounting Standards is required. This Standard also makes transition and consequential amendments to other Standards and pronouncements.

Commented [AC4]: Note for Board members
This is the basic approach in this amending Standard. This means that all of the AusCF paragraphs and footnotes inserted into numerous Standards and Interpretations by AASB 2019-1 (the phase 1 amending Standard) remain in place and do not require amendment. Hence this is a much shorter amending Standard.

Application

The amendments set out in this Standard apply to entities and financial statements in accordance with the application of the other Standards and Interpretations set out in AASB 1057 *Application of Australian Accounting Standards* (as amended).

This Standard applies to annual periods beginning on or after 1 July 2020.

This Standard may be applied to annual periods beginning before 1 July 2020. When an entity applies this Standard to such an annual period, it shall disclose that fact.

This Standard uses underlining, striking out and other typographical material to identify some of the amendments to a pronouncement, in order to make the amendments more understandable. However, the amendments made by this Standard do not include that underlining, striking out or other typographical material. Amended paragraphs are shown with deleted text struck through and new text underlined. Ellipses (…) are used to help provide the context within which amendments are made and also to indicate text that is not amended.

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Amendments to the *Conceptual Framework for Financial Reporting*

Paragraphs Aus1.1 and Aus1.2 are amended.

APPLICATION

Aus1.1 This *Conceptual Framework* applies to:

(a) for-profit private sector entities that ~~have public accountability* and~~ are required by legislation to comply with either Australian Accounting Standards or accounting standards; ~~and~~

(b) other for-profit private sector entities that are required only by their constituting document or another document to comply with Australian Accounting Standards, provided that the relevant document was created or amended on or after 1 July 2020; and

(c) other for-profit entities that elect to apply the *Conceptual Framework* and the consequential amendments to other pronouncements set out in Accounting Standards AASB 2019-1 *Amendments to Australian Accounting Standards – References to the Conceptual Framework* and AASB 2019-Y *Amendments to Australian Accounting Standards – Removal of Special Purpose Financial Statements under Standards for For-Profit Entities*.

~~* The term 'public accountability' is defined in AASB 1053 *Application of Tiers of Australian Accounting Standards*.~~

Aus1.2 This *Conceptual Framework* applies to periods beginning on or after 1 January 2020. Earlier application is permitted if at the same time an entity also applies the amendments made by AASB 2019-1 and AASB 2019-Y.

Amendments to the *Framework for the Preparation and Presentation of Financial Statements*

Paragraphs Aus1.2A and Aus1.2B are amended.

Application

…

Aus1.2A This *Framework* does not apply in relation to reporting periods beginning on or after 1 July ~~January~~ 2020 to:

(a) for-profit private sector entities that ~~have public accountability* and~~ are required by legislation to comply with either Australian Accounting Standards or accounting standards; ~~and~~

(b) other for-profit private sector entities that are required only by their constituting document or another document to comply with Australian Accounting Standards, provided that the relevant document was created or amended on or after 1 July 2020; and

(c) other for-profit entities that elect to apply the *Conceptual Framework for Financial Reporting* and the consequential amendments to other pronouncements set out in Accounting Standards AASB 2019-1 *Amendments to Australian Accounting Standards – References to the Conceptual Framework* and AASB 2019-Y *Amendments to Australian Accounting Standards – Removal of Special Purpose Financial Statements under Standards for For-Profit Entities*;

except as otherwise required by Australian Accounting Standards.

~~* The term 'public accountability' is defined in AASB 1053 *Application of Tiers of Australian Accounting Standards*.~~

Aus1.2B If an entity identified in paragraph Aus1.2A elects to apply the *Conceptual Framework for Financial Reporting* to an annual reporting period prior to its mandatory application for the entity ~~beginning before 1 January 2020~~, the entity shall not apply this *Framework* to that period, except as otherwise required by Australian Accounting Standards.

Commented [AC5]: Note for Board members
The *Framework* is mandatory for periods beginning on or after 1-1-20 for phase 1 entities, but 1-7-20 for phase 2 entities. Compiled versions of the *Framework* will be required for both dates.

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Amendments to Statement of Accounting Concepts SAC 1

Paragraphs 2A and 2B are amended.

Application and Operative Date

…

2A This Statement does not apply in relation to reporting periods beginning on or after 1 July ~~January~~ 2020 to:

(a) for-profit private sector entities that ~~have public accountability* and~~ are required by legislation to comply with either Australian Accounting Standards or accounting standards; ~~and~~

(b) other for-profit private sector entities that are required only by their constituting document or another document to comply with Australian Accounting Standards, provided that the relevant document was created or amended on or after 1 July 2020; and

(c) other for-profit entities that elect to apply the *Conceptual Framework for Financial Reporting* and the consequential amendments to other pronouncements set out in Accounting Standards AASB 2019-1 *Amendments to Australian Accounting Standards – References to the Conceptual Framework* and AASB 2019-Y *Amendments to Australian Accounting Standards – Removal of Special Purpose Financial Statements under Standards for For-Profit Entities*;

~~* The term 'public accountability' is defined in AASB 1053 *Application of Tiers of Australian Accounting Standards*.~~

2B If an entity identified in paragraph 2A elects to apply the *Conceptual Framework for Financial Reporting* to an annual reporting period prior to its mandatory application for the entity ~~beginning before 1 January 2020~~, the entity shall not apply this Statement to that period.

Amendments to AASB 1

Paragraphs AusE8.1–AusE8.5, and a heading before paragraph AusE8.1, are added.

Australian short-term exemption from restating comparative information

AusE8.1 Paragraphs AusE8.1–AusE8.5 apply to a for-profit private sector entity's first Australian-Accounting-Standards reporting period beginning on or after 1 July 2020 but before 1 July 2021.

AusE8.2 Paragraphs AusE8.1–AusE8.5 apply to for-profit private sector entities that:

(a) apply Tier 2 reporting requirements (Australian Accounting Standards – Reduced Disclosure Requirements [*or* Australian Accounting Standards – Simplified Disclosures for Tier 2 Entities[1]]) in the first Australian-Accounting-Standards financial statements; and

(b) prepared its most recent previous financial statements in the form of special purpose financial statements (including consolidated financial statements) that meet either or both of the following criteria:

(i) have not applied, or only selectively applied, the recognition and measurement requirements of Australian Accounting Standards;

(ii) are not prepared in accordance with AASB 10 *Consolidated Financial Statements*, in the case of a parent entity.

AusE8.3 Notwithstanding paragraph RDR21.1 [*or* comparative information requirements in AASB 10XX *Simplified Disclosures for Tier 2 Entities*[1]], comparative information need not be restated or presented in the entity's first Australian-Accounting-Standards financial statements (Tier 2), except as specified in paragraphs AusE8.4 and AusE8.5. Under this approach, references to the 'date of transition to Australian Accounting Standards' shall mean the beginning of the first Australian-Accounting-Standards reporting period. Consequently, consistent with paragraph 11, the entity shall recognise adjustments arising from any differences between the carrying amounts in its previous special purpose financial statements and its opening carrying amounts based on the retrospective application of Australian Accounting Standards directly in retained earnings (or, if appropriate, another category of equity) at the beginning of the first Australian-Accounting-Standards reporting period.

1 The Tier 2 requirements are subject to AASB Exposure Draft ED XXX *New Accounting Standard: General Purpose Financial Statements – Simplified Disclosures for Tier 2 Entities* ([Month] 2019). AASB 2019-Y when finalised will refer to the Tier 2 requirements in place at the time for the periods of its application – which might therefore refer to both sets of Tier 2 requirements.

Commented [BJ6]: Note for Board members
See Question 9 in the Basis for Conclusions in relation to the scope of this exception.

Commented [AC7]: Note for Board members
Appendix A of AASB 1 defines terms such as 'first Australian-Accounting-Standards reporting period', 'first Australian-Accounting-Standards financial statements' and 'date of transition to Australian Accounting Standards'.

Commented [AC8]: Note for Board members
The AASB decided at the April meeting to limit this additional relief to entities preparing Tier 2 GPFS.

An entity preparing Tier 1 GPFS is not being provided with any additional relief beyond AASB 1 currently, since IFRS compliance is expected.

Commented [AC9]: Note for Board members
Paragraph (b) covers SPFS that meet (i) or (ii) or both. The drafting avoids identifying consolidation requirements as recognition and measurement requirements.

Similar wording is proposed as an amendment to paragraph 18A of AASB 1053. This makes clear that the AASB 1 relief for business combinations, for example, is available in any first-time Tier 2 case following SPFRs. The AASB 1 amendments here relate to a specific period only, when additional relief is available.

AusE8.4 Subject to paragraph AusE8.5, an entity that elects to not restate and present comparative information in its first Australian-Accounting-Standards financial statements shall:

(a) present two statements of financial position in accordance with Australian Accounting Standards as at the beginning and the end of the first Australian-Accounting-Standards reporting period;

(b) disclose the statement of financial position (not necessarily compliant with Australian Accounting Standards) for the reporting period presented in its most recent previous special purpose financial statements, with a description of the main adjustments required to prepare the statement of financial position at the beginning of the first Australian-Accounting-Standards reporting period. An entity need not quantify those adjustments;

(c) present two statements of profit or loss and other comprehensive income as follows:

(i) the statement for the first Australian-Accounting-Standards reporting period, in accordance with Australian Accounting Standards; and

(ii) the statement presented in its most recent previous special purpose financial statements (not necessarily compliant with Australian Accounting Standards);

(d) disclose a description of the main adjustments that would have been required to make the comparative statement of profit or loss and other comprehensive income required by paragraph (c)(ii) compliant with Australian Accounting Standards. An entity need not quantify those adjustments; and

(e) label the information prominently as not being prepared in accordance with Australian Accounting Standards.

AusE8.5 Where an entity's most recent previous special purpose financial statements have not applied, or only selectively applied, the recognition and measurement requirements of only a few Australian Accounting Standards, the entity may elect to not restate comparative information in its first Australian-Accounting-Standards financial statements, but instead to present comparative information consistent with its most recent previous special purpose financial statements. Where comparative information is not in accordance with Australian Accounting Standards, an entity shall:

(a) label the information prominently as not being prepared in accordance with Australian Accounting Standards; and

(b) disclose the nature and amount of the main adjustments that would make it comply with Australian Accounting Standards.

Commented [AC10]: Note for Board members
A limitation is required on the applicability of para AusE8.5 to prevent all entities just choosing this approach rather than the approach in para AusE8.4.

Question 4 for Board members
Is this reference to "a few" Standards appropriate? An alternative is to refer to "one or two" Standards, for example.

Is providing an optional approach in addition to para AusE8.4 appropriate?

Commented [AC11]: Note for Board members
Requiring disclosure of the main reconciling amounts (for the comparative profit or loss, statement of financial position, cash flow statement etc.) is intended to make this approach more onerous if there are a lot of differences with Australian Accounting Standards, to reduce the attractiveness of the option and make it most suitable for limited departures from the Standards.

The para AusE8.4 approach requires a description of the main adjustments, but not amounts.

Question 5 for Board members
Is it appropriate to require quantification of the main adjustments in this case?

Amendments to AASB 10

Paragraph Aus4.2 is amended.

Scope

…

Aus4.2 Notwithstanding paragraphs 4(a) and Aus4.1, the ultimate Australian parent shall present consolidated financial statements that consolidate its investments in subsidiaries in accordance with this Standard when the ultimate Australian parent is required by legislation to comply with Australian Accounting Standards or accounting standards, except if the ultimate Australian parent is required, in accordance with paragraph 31 of this Standard, to measure all of its subsidiaries at fair value through profit or loss.

Commented [AC12]: Note for Board members
All references in the Standards to Australian Accounting Standards remain as such. An explicit reference to "accounting standards" is appropriate when referring to legislative requirements, as here.

Amendments to AASB 1053

Paragraphs 2, 11 and 18A are amended.

Application

2 This Standard applies to[1]:

(a) each entity that is required to prepare financial reports in accordance with Part 2M.3 of the Corporations Act;

(b) ***general purpose financial statements*** **of each** ~~***reporting entity***~~ **reporting entity;**

(c) **financial statements that are, or are held out to be, general purpose financial statements;**

(d) **financial statements of General Government Sectors (GGSs) prepared in accordance with AASB 1049 *Whole of Government and General Government Sector Financial Reporting*;** ~~**and**~~

(e) **for-profit private sector entities that** ~~**have public accountability and**~~ **are required by legislation to comply with either Australian Accounting Standards or accounting standards; and**

(f) **other for-profit private sector entities that are required only by their constituting document or another document to comply with Australian Accounting Standards, provided that the relevant document was created or amended on or after 1 July 2020.**

Commented [AC13]: Note for Board members
This group includes for-profit private sector entities that voluntarily choose to adopt the new CF and so are not covered by (e) or (f).

…

Application of Tier 1 Reporting Requirements

11 **The following types of entities shall prepare general purpose financial statements that comply with Tier 1 reporting requirements:**

(a) **for-profit private sector entities that have public accountability and are required by legislation to comply with Australian Accounting Standards or accounting standards; and**

(b) **the Australian Government and State, Territory and Local Governments.**

…

First-time Adoption of Australian Accounting Standards

…

18A **When applying Tier 2 reporting requirements for the first time, an entity that prepared its most recent previous financial statements in the form of special purpose financial statements:**

(a) **without applying, or only selectively applying, applicable recognition and measurement requirements of Australian Accounting Standards, or, in addition or separately, if a parent entity, without presenting consolidated financial statements prepared in accordance with AASB 10 *Consolidated Financial Statements* if required, shall apply either:**

(i) **all relevant requirements of AASB 1; or**

(ii) **Tier 2 reporting requirements directly using the requirements in AASB 108;**

(b) **applying all applicable recognition and measurement requirements of Australian Accounting Standards shall not apply AASB 1.**

Commented [AC14]: Note for Board members
The added text reflects paragraph AusE8.2 that is being added to AASB 1 in this amending Standard. See comments there.

Question 6 for Board members
Do members support this proposed amendment?

Amendments to AASB 1057

Paragraphs 2, 5–10, 12, 18, 20, 22–24 and 26 and the Appendix are amended.

Application of this Standard

2 **This Standard applies to:**

(a) **each entity that is required to prepare financial reports in accordance with Part 2M.3 of the Corporations Act;**

(b) ***general purpose financial statements*** **of each** ***reporting entity*;**

(c) **financial statements that are, or are held out to be, general purpose financial statements;**

(d) **financial statements of General Government Sectors (GGSs) prepared in accordance with AASB 1049 *Whole of Government and General Government Sector Financial Reporting*;** ~~**and**~~

(e) **for-profit private sector entities that** ~~**have public accountability and**~~ **are required by legislation to comply with either Australian Accounting Standards or accounting standards; and**

(f) **other for-profit private sector entities that are required only by their constituting document or another document to comply with Australian Accounting Standards, provided that the relevant document was created or amended on or after 1 July 2020.**

…

Application of Australian Accounting Standards

5 **Unless specified otherwise in paragraphs 6-21, Australian Accounting Standards apply to:**

- **(a)** **each entity that is required to prepare financial reports in accordance with Part 2M.3 of the Corporations Act and that is a reporting entity;**
- **(b)** **general purpose financial statements of each other reporting entity;**
- **(c)** **financial statements that are, or are held out to be, general purpose financial statements; ~~and~~**
- **(d)** **for-profit private sector entities that ~~have public accountability and~~ are required by legislation to comply with <u>either</u> Australian Accounting Standards<u> or accounting standards; and</u>**
- **<u>(e) other for-profit private sector entities that are required only by their constituting document or another document to comply with Australian Accounting Standards, provided that the relevant document was created or amended on or after 1 July 2020</u>.**

6 **AASB 8 *Operating Segments* applies to:**

- **(a)** **each for-profit entity that is required to prepare financial reports in accordance with Part 2M.3 of the Corporations Act and that is a reporting entity;**
- **(b)** **general purpose financial statements of each other for-profit reporting entity;**
- **(c)** **financial statements of a for-profit entity that are, or are held out to be, general purpose financial statements; ~~and~~**
- **(d)** **for-profit private sector entities that ~~have public accountability and~~ are required by legislation to comply with <u>either</u> Australian Accounting Standards<u> or accounting standards; and</u>**
- **<u>(e) other for-profit private sector entities that are required only by their constituting document or another document to comply with Australian Accounting Standards, provided that the relevant document was created or amended on or after 1 July 2020</u>.**

7 **AASB 101 *Presentation of Financial Statements*, AASB 107 *Statement of Cash Flows*, AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*, AASB 1048 *Interpretation of Standards* and AASB 1054 *Australian Additional Disclosures* apply to:**

- **(a)** **each entity that is required to prepare financial reports in accordance with Part 2M.3 of the Corporations Act;**
- **(b)** **general purpose financial statements of each reporting entity;**
- **(c)** **financial statements that are, or are held out to be, general purpose financial statements; ~~and~~**
- **(d)** **for-profit private sector entities that ~~have public accountability and~~ are required by legislation to comply with <u>either</u> Australian Accounting Standards<u> or accounting standards; and</u>**
- **<u>(e) other for-profit private sector entities that are required only by their constituting document or another document to comply with Australian Accounting Standards, provided that the relevant document was created or amended on or after 1 July 2020</u>.**

8 **AASB 120 *Accounting for Government Grants and Disclosure of Government Assistance* applies to:**

- **(a)** **each for-profit entity that is required to prepare financial reports in accordance with Part 2M.3 of the Corporations Act and that is a reporting entity;**
- **(b)** **general purpose financial statements of each other for-profit reporting entity;**
- **(c)** **financial statements of a for-profit entity that are, or are held out to be, general purpose financial statements;~~ and~~**
- **(d)** **for-profit private sector entities that ~~have public accountability and~~ are required by legislation to comply with <u>either</u> Australian Accounting Standards<u> or accounting standards; and</u>**

(e) other for-profit private sector entities that are required only by their constituting document or another document to comply with Australian Accounting Standards, provided that the relevant document was created or amended on or after 1 July 2020.

9 AASB 133 *Earnings per Share* applies to:

(a) each entity that is required to prepare financial reports in accordance with Part 2M.3 of the Corporations Act and that is a reporting entity or discloses earnings per share; and

(b) for-profit private sector entities that ~~have public accountability and~~ are required to prepare financial reports in accordance with Part 2M.3 of the Corporations Act or disclose earnings per share.

10 AASB 134 *Interim Financial Reporting* applies to:

(a) each disclosing entity required to prepare half-year financial reports in accordance with Part 2M.3 of the Corporations Act;

(b) interim financial reports that are general purpose financial statements of each other reporting entity; ~~and~~

(c) interim financial reports that are, or are held out to be, general purpose financial statements;

(d) interim financial reports of for-profit private sector entities that are required by legislation to comply with either Australian Accounting Standards or accounting standards; and

(e) interim financial reports of other for-profit private sector entities that are required only by their constituting document or another document to comply with Australian Accounting Standards, provided that the relevant document was created or amended on or after 1 July 2020.

Commented [AC15]: Note for Board members
Added paragraphs (d) and (e) now for phase 1 and 2 entities that are not disclosing entities. This application paragraph now has the same scope as the Phase 2 entities.

Question 7 for Board members
Do Board members agree with adding paragraphs (d) and (e)?

…

12 AASB 1038 *Life Insurance Contracts* applies to:

(a) a life insurer; or

(b) the parent in a group that includes a life insurer;

when the entity:

(c) is a reporting entity that is required to prepare financial reports in accordance with Part 2M.3 of the Corporations Act;

(d) is an other reporting entity and prepares general purpose financial statements;

(e) prepares financial statements that are, or are held out to be, general purpose financial statements; ~~or~~

(f) is a for-profit private sector entity that ~~has public accountability and~~ is required by legislation to comply with either Australian Accounting Standards or accounting standards; or

(g) is an other for-profit private sector entity that is required only by its constituting document or another document to comply with Australian Accounting Standards, provided that the relevant document was created or amended on or after 1 July 2020.

…

18 AASB 1053 *Application of Tiers of Australian Accounting Standards* applies to:

(a) each entity that is required to prepare financial reports in accordance with Part 2M.3 of the Corporations Act;

(b) general purpose financial statements of each reporting entity;

(c) financial statements that are, or are held out to be, general purpose financial statements;

(d) financial statements of GGSs prepared in accordance with AASB 1049; ~~and~~

(e) for-profit private sector entities that ~~have public accountability and~~ are required by legislation to comply with either Australian Accounting Standards or accounting standards; and

(f) other for-profit private sector entities that are required only by their constituting document or another document to comply with Australian Accounting Standards, provided that the relevant document was created or amended on or after 1 July 2020.

…

20 AASB 1056 *Superannuation Entities* applies to:

(a) general purpose financial statements of each superannuation entity that is a reporting entity;

(b) financial statements of a superannuation entity that are held out to be general purpose financial statements; ~~and~~

(c) for-profit private sector entities that ~~have public accountability and~~ are required by legislation to comply with either Australian Accounting Standards or accounting standards; and

(d) other for-profit private sector entities that are required only by their constituting document or another document to comply with Australian Accounting Standards, provided that the relevant document was created or amended on or after 1 July 2020.

…

Application of Australian Interpretations

22 Unless specified otherwise in paragraphs 23–26, Interpretations apply to:

(a) each entity that is required to prepare financial reports in accordance with Part 2M.3 of the Corporations Act and that is a reporting entity;

(b) general purpose financial statements of each other reporting entity;

(c) financial statements that are, or are held out to be, general purpose financial statements;~~ and~~

(d) for-profit private sector entities that ~~have public accountability and~~ are required by legislation to comply with either Australian Accounting Standards or accounting standards, and

(e) other for-profit private sector entities that are required only by their constituting document or another document to comply with Australian Accounting Standards, provided that the relevant document was created or amended on or after 1 July 2020.

23 Interpretation 110 *Government Assistance – No Specific Relation to Operating Activities* applies to:

(a) each for-profit entity that is required to prepare financial reports in accordance with Part 2M.3 of the Corporations Act and that is a reporting entity;

(b) general purpose financial statements of each other for-profit reporting entity;

(c) financial statements of a for-profit entity that are, or are held out to be, general purpose financial statements; ~~and~~

(d) for-profit private sector entities that ~~have public accountability and~~ are required by legislation to comply with either Australian Accounting Standards or accounting standards; and

(e) other for-profit private sector entities that are required only by their constituting document or another document to comply with Australian Accounting Standards, provided that the relevant document was created or amended on or after 1 July 2020.

24 Interpretation 1019 *The Superannuation Contributions Surcharge* applies to:

(a) each superannuation plan that is required to prepare financial reports in accordance with Part 2M.3 of the Corporations Act and that is a reporting entity;

(b) general purpose financial statements of each other superannuation plan that is a reporting entity;

(c) financial statements of a superannuation plan that are, or are held out to be, general purpose financial statements; ~~and~~

(d) for-profit private sector entities that ~~have public accountability and~~ are required by legislation to comply with either Australian Accounting Standards or accounting standards; and

(e) other for-profit private sector entities that are required only by their constituting document or another document to comply with Australian Accounting Standards, provided that the relevant document was created or amended on or after 1 July 2020.

…

26 Interpretation 1047 *Professional Indemnity Claims Liabilities in Medical Defence Organisations* applies to entities that are or include medical defence organisations as follows:

(a) **each entity that is required to prepare financial reports in accordance with Part 2M.3 of the Corporations Act and that is a reporting entity;**

(b) **general purpose financial statements of each other reporting entity;**

(c) **financial statements that are, or are held out to be, general purpose financial statements; ~~and~~**

(d) **for-profit private sector entities that ~~have public accountability and~~ are required by legislation to comply with either Australian Accounting Standards or accounting standards; and**

(e) **other for-profit private sector entities that are required only by their constituting document or another document to comply with Australian Accounting Standards, provided that the relevant document was created or amended on or after 1 July 2020.**

…

Appendix
Defined terms

…

reporting entity

An entity in respect of which it is reasonable to expect the existence of users who rely on the entity's general purpose financial statements for information that will be useful to them for making and evaluating decisions about the allocation of resources. A reporting entity can be a single entity or a group comprising a parent and all of its subsidiaries.

This reporting entity definition is not relevant to:

(a) for-profit private sector entities that ~~have public accountability and~~ are required by legislation to comply with either Australian Accounting Standards or accounting standards~~; and~~

(b) other for-profit private sector entities that are required only by their constituting document or another document to comply with Australian Accounting Standards, provided that the relevant document was created or amended on or after 1 July 2020; and

(c) other for-profit entities that elect to apply the *Conceptual Framework for Financial Reporting* and the consequential amendments to other pronouncements set out in Accounting Standards AASB 2019-1 *Amendments to Australian Accounting Standards – References to the Conceptual Framework* and AASB 2019-Y *Amendments to Australian Accounting Standards – Removal of Special Purpose Financial Statements under Standards for For-Profit Entities.*

Commented [AC16]: Note for Board members
The reporting entity definition is not relevant to entities for which SAC 1 is not relevant. Therefore, this list is the same as the (amended) list in SAC 1 of the entities that do not apply SAC 1.

The list is repeated here so that it is stated in an Accounting Standard. The same list appears in the *Conceptual Framework*, the (old) *Framework* and SAC 1, none of which are Standards.

Commencement of the legislative instrument

10 For legal purposes, this legislative instrument commences on 30 June 2020.

PRE-BALLOT DRAFT
For Board member comment at M171 (June 2019)

Basis for Conclusions

This Basis for Conclusions accompanies, but is not part of, AASB 2019-Y Amendments to Australian Accounting Standards – Removal of Special Purpose Financial Statements under Standards for For-Profit Entities.

Commented [BJ1]: Question 8 for Board Members:
As an overarching question, does the Board agree that this Basis for Conclusions appropriately reflects the Board's deliberations and decisions in respect of this ED?

In the meeting, Staff intend to ask this question for each of the sections presented in this BC.

Introduction

BC1 This Basis for Conclusions summarises the Australian Accounting Standards Board's (AASB's) considerations in reaching the conclusions in this Exposure Draft (ED). In making decisions, individual Board members gave greater weight to some factors than to others.

BC2 For more than a decade the Board has been working towards addressing problems that arise from entities being allowed to self-assess whether to prepare special purpose financial statements (SPFS) or general purpose financial statements (GPFS) when they are required to comply with Australian Accounting Standards (AAS) (see paragraphs BC13-BC16 for details). As is evident from empirical research and feedback from stakeholders (see paragraphs BC21-BC36), there is concern that SPFS lack consistency, comparability and transparency. Within the context of the AASB's International Financial Reporting Standards (IFRS) adoption policy, the recent issue of a revised *Conceptual Framework for Financial Reporting* (referred to throughout this Basis for Conclusion as 'RCF') by the International Accounting Standards Board (IASB) provides a timely opportunity to once again consider how best to improve the quality of financial reporting in Australia by solving the so-called 'SPFS problem'. The Board is progressing this work by considering each sector separately, in the first instance for-profit private sector entities required to comply with AAS (being the subject of this ED – as explained in paragraphs BC51-BC72).

BC3 The solution to the SPFS problem proposed is to remove the ability for entities within the scope of this ED to prepare SPFS when required to comply with AAS[1]. The Board acknowledges that this solution cannot be implemented in isolation, as merely removing the ability to prepare SPFS with no other mitigating action would result in an increased reporting burden for some entities if they were to be required to transition from SPFS into the current two tiered GPFS framework. Therefore the Board is considering:

(a) through this ED, providing additional transitional relief (see paragraphs BC89-BC100); and

(b) through a separate but related ED, how the current disclosure requirements of the Tier 2 GPFS framework should be revised (see AASB ED 2XX *New Accounting Standards: General Purpose Financial Statements – Simplified Disclosures for Tier 2 Entities* (issued [MONTH] 2019));

to facilitate implementation of the solution in a way that balances costs relative to benefits.

Commented [BJ2]: Note for Board members:
Some text is highlighted in this ED. This signifies where information or references may need to be updated, for example when referring to other EDs not yet issued, or when referring to findings of as yet unpublished research.

BC4 The remainder of this Basis for Conclusions provides further background and details about the reasons for developing this ED, previous Board decisions in relation to earlier stages of the process (to provide an historical perspective, see for example paragraphs BC36-BC49) and the basis for the key decisions made, including the types of entities affected by the proposals and the technical requirements that would be required (including, for context, a summary of the basis for the proposed revised Tier 2 GPFS framework (see paragraphs BC73-BC88), which is detailed in AASB ED 2XX), transitional provisions and the effective date (see paragraphs BC101-BC104). The last two sections of this Basis for Conclusions explain how the Board applied its for-profit entity standard-setting framework when developing the proposals in this ED (see paragraphs BC105-BC107) and the amendments required to implement Phase 2 (see paragraphs BC108-**Error! Reference source not found.**), respectively.

Reasons for developing this ED

The first issue – the clash of 'reporting entity' definitions

BC5 The IASB issued the RCF in March 2018. The RCF describes the objective and concepts for general purpose financial reporting under IFRS Standards. Its purpose is to assist standard-setters to develop Standards that are based on consistent concepts, and to help preparers develop consistent accounting policies when no Standard applies to a particular transaction or event, or when a Standard allows a choice of accounting policy. It also assists anyone looking to understand and interpret the Standards. However, the RCF's concept of 'reporting entity' is different from the reporting entity concept in the AASB's Statement of Accounting Concepts SAC 1 *Definition of the Reporting Entity* and some AAS[2].

1 The Australian concept of the Reporting Entity would be retained for entities not within the scope of this ED until the Board addresses such entities.

2 The term *Reporting Entity* as defined by the revised Conceptual Framework is also inconsistent with the definitions in AASB 101 *Presentation of Financial Statements* and AASB 1053 *Application of Tiers of Australian Accounting Standards*.

BC6 Making the IASB's RCF applicable in Australia, modified where necessary for public sector and not-for-profit (NFP) specific issues, would be consistent with the Financial Reporting Council's strategic direction to the Board and the Board's strategic objectives. In accordance with those strategies, the Board should:

(a) maintain compliance with IFRS Standards for publicly accountable entities; and

(b) use IFRS Standards as a base for determining the reporting requirements for all other entities, modified as appropriate, in accordance with the AASB's standard-setting frameworks for for-profit and NFP entities.

However, if the AASB's current reporting entity concept is maintained at the same time the RCF is applied, the inconsistency with the RCF could result in misinterpretation, the wrong application of AAS and non-compliance with IFRS Standards.

BC7 This so-called 'reporting entity clash' was addressed in the AASB's Invitation to Comment ITC 39 *Applying the IASB's Revised Conceptual Framework and Solving the Reporting Entity and Special Purpose Financial Statement Problems* (ITC 39), issued in May 2018, which outlined and sought comment on the clash between the reporting entity concepts and the related SPFS problem. The proposals in this ED have been informed by the AASB's research and consultation undertaken prior to and since ITC 39 was issued. The results of that research and consultation, and how it influenced the Board's decisions, are outlined throughout this ED.

BC8 Implementation of the RCF in Australia is challenging due to this clash. The reporting entity concept in the RCF determines the boundary of what needs to be reported when an entity is required to report, e.g. consolidation. In contrast, the current Australian reporting entity concept allows entities to self-assess whether they should prepare:

(a) GPFS, which requires compliance with all AAS, including their definition, recognition, measurement, presentation and disclosure requirements; or

(b) SPFS, which only requires compliance with a handful of AAS, which focus more on the fundamental presentation of financial statements and certain disclosures, and entities self-select other AAS requirements (such as recognition and measurement (R&M)).

The ability for entities to self-assess their reporting requirements under the Australian reporting entity concept has led to the more fundamental 'SPFS problem'.

The second issue – the SPFS problem

BC9 Australia is the only jurisdiction with a 'reporting entity' concept that effectively permits entities to self-assess their type of financial reporting when they are required by legislation or otherwise (such as by a constitutional document) to prepare financial statements in accordance with accounting standards (issued by the AASB)[3]. Therefore, unlike other jurisdictions, in Australia two similar entities might prepare very different sets of financial statements, one preparing GPFS using a robust and consistent framework, and the other preparing SPFS with self-selected requirements. This reduces comparability for entities of similar economic circumstances and undermines the fundamentals of trust and transparency.

BC10 Research by the AASB indicates that many for-profit private sector non-disclosing entities (approximately 55%)[4] publicly lodge SPFS in Australia, suggesting a strong need to find a solution to improve the consistency, comparability, usefulness and credibility of financial reporting in Australia.

Commented [BJ3]: Note for Board members: Results subject to final publication of report.

BC11 It is incumbent on the AASB to resolve this SPFS problem as, legislatively, the AASB must ensure there are appropriate accounting standards for each type of entity that must comply with accounting standards (*Australian Securities and Investments Commission (ASIC) Act* S229(2)(c)) and facilitate comparability (S224). The ability to make the self-assessment that gives rise to the problem sits within AAS. Currently AAS that explicitly apply to SPFS mainly only focus on presentation and disclosure (and not R&M). Accordingly, they fall short in specifying adequate requirements. As a consequence, other regulators have attempted to fill the gap by providing additional guidance in relation to R&M. Despite these attempts, discussions with users, including lenders and insolvency practitioners, indicate their needs for information about liquidity, solvency, cash flows, commitments and contingencies are currently not being provided for in most SPFS. This indicates there is the need for minimum R&M requirements to be specified in AAS.

BC12 Therefore, it is time for the AASB to play its role in improving comparability, trust and transparency within financial reporting to meet user needs, whilst mitigating, where appropriate, the increased reporting burden for some entities that are required to prepare financial statements in accordance with AAS.

3 See AASB Research Report No. 7 *Financial Reporting Requirements Applicable to For-Profit Private Sector Companies* (May 2018) for a comparison of international financial reporting frameworks.
4 As per the forthcoming AASB Research Report XX *Financial Reporting Practices of For-Profit Entities Lodging SPFSs – 2019*

Board deliberations prior to ITC 39

BC13 As noted in paragraph BC2, the Board had been aware of problems with the application of the reporting entity concept and the consequential public lodgement of SPFS for some time prior to the issuance of this ED. Indeed, the Board has previously publicly contemplated the removal of the ability for entities to self-assess and prepare SPFS when required to comply with AAS. For example:

(a) AASB Invitiation to Comment ITC 12 *Request for Comment on a Proposed Revised Differential Reporting Regime for Australia and IASB* Exposure Draft of A Proposed IFRS for Small and Medium-sized Entities (May 2007) noted the concept of SPFS might have been misunderstood in some cases. To remove the ambiguity concerning the reporting entity concept, ITC 12 sought comment on whether all financial statements available on a public register should be required to be GPFS; and

(b) AASB Consultation Paper (CP) *Differential Financial Reporting – Reducing Disclosure Requirements* (February 2010) and ED 192 *Revised Differential Reporting Framework* (February 2010), issued in tandem, followed from ITC 12 and reaffirmed the Board's view that the reporting entity concept that allows the public lodgement of SPFS should be removed. The Board elaborated on the issues surrounding SPFS in the CP, including noting that:

(i) entities are asserted to be 'abusing' the reporting entity concept by claiming to be non-reporting entities and preparing SPFS when they should be preparing GPFS. An impetus for this is the desire to avoid the cost and exposure that would come from applying full IFRS Standards as adopted in Australia;

(ii) many of the regulators requiring the preparation and lodgement of financial statements may not have given sufficient consideration to the nature of the information they require and the needs of any external users of that information; and

(iii) preparation of SPFS by entities that are required by law to prepare financial statements in accordance with accounting standards and be lodged on a public register contradicts the legislation's objective of providing information to a wide range of users who are not in a position to command specific information to satisfy their needs.

BC14 However, the Board noted the mixed feedback from constituents in response to these due process documents in regard to removing the ability for entities to self-assess and prepare SPFS when required to comply with AAS, which suggested that (as noted in paragraphs BC10-BC17 of the Basis for Conclusions to AASB 1053 *Application of Tiers of Australian Accounting Standards*):

(a) on the one hand, the reporting entity concept involves a high degree of subjectivity, is not universally understood and hence does not provide the intended result, nor does it provide a robust criterion for differential reporting purposes; and

(b) on the other hand, the reporting entity concept works well, and there appeared to be no evidence to the contrary, particularly from users.

BC15 Consequently, the Board decided to issue AASB 1053 to introduce Tier 2 GPFS framework: Reduced Disclosure Requirements (RDR) in 2010, but delay the phase of the project addressing the reporting entity concept and SPFS until further research had been undertaken as to the impact of removing the ability for entities to self-assess and prepare SPFS when required to comply with AAS.

BC16 Paragraphs BC17-BC22 immediately below summarise the Board's findings in its research that was prompted by the views noted in paragraphs BC13 and BC14 above.

Results of research into the state of public lodgement with ASIC by non-disclosing entities

BC17 The Board commissioned academic research that resulted in the publication of AASB Research Report No. 1 *Application of the Reporting Entity Concept and Lodgement of Special Purpose Financial Statements* (June 2014). That Report analysed the application of the reporting entity concept and the adoption of special purpose financial reporting, particularly by entities lodging financial statements with ASIC and with state-based regulators in Australia's three most populous states, namely, Consumer Affairs Victoria, NSW Fair Trading and Queensland Office of Fair Trading. The Report showed that, based on lodgements as at 30 July 2011, approximately 66% of for-profit non-disclosing entities[5] publicly lodged SPFS with ASIC. The findings of the Report indicated to the Board that:

(a) in light of the high incidence of SPFS lodged with ASIC, there is doubt as to whether the reporting entity concept is being applied as intended by SAC 1;

5 For-profit non-disclosing entities are large proprietary companies, small foreign controlled companies and unlisted public companies.

(b) the reporting entity concept appears too subjective for regulators to enforce effectively and accordingly does not create a level playing field; and

(c) 63% of SPFS lodged with ASIC stated compliance with R&M requirements of applicable AAS, suggesting that R&M was not always complied with despite regulatory guidance suggesting that SPFS should apply all R&M requirements (see paragraph BC25).

BC18 The Board also commissioned subsequent academic research to investigate how the reporting practices of non-disclosing companies publicly lodging with ASIC may have changed since the introduction of the AASB's Tier 2 GPFS framework: RDR reporting framework. The key findings of the yet to be published AASB Research Report *Financial Reporting Practices of For-Profit Entities Lodging SPFS* (2019) were that approximately 15% of for-profit non-disclosing entities lodging with ASIC had adopted the Tier 2 GPFS RDR framework and 55% were lodging SPFS, a reduction of 11 percentage points compared with the findings in Research Report No.1. Despite this drop, there is still a significant number (majority) of for-profit non-disclosing entities preparing SPFS.

Commented [BJ4]: Note for Board members: Results subject to final publication of report.

Commented [BJ5]: Note for Board members: Results subject to final publication of report.

BC19 In respect of compliance with R&M requirements of AAS, the Board noted the more detailed findings of the 2019 Report indicated that 76% of for-profit non-disclosing entities complied with R&M requirements of AAS, In particular:

(a) 66% of entities clearly stated compliance with R&M requirements (compared with the 63% found in Research Report No.1 – see paragraph BC17(c)); and

(b) 10% of entities were assessed as compliant with R&M as a result of a qualitative review by AASB staff, although there was no clear statement of compliance with R&M requirements.

BC20 Accordingly, 24% of for-profit non-disclosing entities either did not comply with R&M, or it was unclear whether they complied with R&M. In particular:

(a) 10% of entities were assessed as not complying with the R&M requirements as a result of a qualitative review by AASB staff; and

(b) for the remaining 14% of entities, it was unclear whether or not they were complying with the R&M requirements, despite efforts of both the researchers and AASB staff to determine the state of compliance.

BC21 The findings raised particular concern for the Board, which noted the difficulty faced by users to understand the level of compliance with R&M requirements in publicly lodged SPFS. This leads to fundamental issues in both the comparability of SPFS with other financial statements, as well as the transparency of information available on the public record. The Board decided , given the time it will take for SPFS problem to resolved, to propose as interim measure through a separate ED the inclusion of a requirement in AASB 1054 *Australian Additional Disclosures* for an entity to disclose information on the extent of compliance with R&M (and consolidation and equity accounting) in its SPFS[6]. The Board acknowledged that such disclosure is not a sufficient solution to the SPFS problem, but provides a practical interim means of improving the quality of information provided to users of SPFS.

BC22 In addition to the research described above, the Board conducted targeted outreach prior and subsequent to issuing ITC 39, where over 200 formal meetings were held with key stakeholders, including State, Territory and Commonwealth regulators, audit offices, large and small accounting firms, the Australian Securities Exchange (ASX), ASIC, Australian Charities And Not-For-Profits Commission (ACNC), credit rating agencies, professional bodies and users (including analysts, investors and creditors) of financial statements to help identify how implementing the RCF and removing the ability to prepare SPFS when required to comply with AAS would impact Australian entities. The Board considered the feedback received, referred to throughout this ED, when developing ITC 39 and this ED.

Regulatory views and developments on SPFS

BC23 The Board noted feedback from some constituents suggesting that it was the role of other regulators (rather than the AASB) to address any supposed issues with SPFS. In particular, some constituents argued:

(a) other regulators should specify or determine whether an entity is required to lodge GPFS[7]; and

(b) if the reporting entity concept is not being applied correctly, this is a matter of enforcement as opposed to standard-setting.

6 See ED 2XX *Amendments to Australian Accounting Standards – Disclosure of Compliance with Recognition and Measurement Requirements* issued …[date]

7 Consistent with the view that the AASB's role and expertise is in specifying what should be reported in GPFS rather than who should report GPFS.

BC24 Thus, the Board has paid particular regard to the views of other regulators, and noted the increasing regulatory interest in and concern about the public lodgement of SPFS to assess what role the Board should play in addressing the issues.

BC25 ASIC issued Regulatory Guide 85 *Reporting requirements for non-reporting entities* (RG 85) in July 2005, expressing the view that non-reporting entities required to prepare financial statements in accordance with Chapter 2M of the Corporations Act should comply with the R&M requirements of all accounting standards in order to determine the financial position and profit or loss of any entity preparing financial reports in accordance with the Corporations Act. Under RG 85, the only 'relief' for these entities is not having to apply the disclosure requirements in AAS, except for those contained in AASB 101 *Presentation of Financial Statements*, AASB 107 *Statement of Cash Flows*, AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*, AASB 1048 *Interpretation of* Standards and AASB 1054. However, as noted in paragraph BC19 above, the research into the extent of compliance with the R&M requirements in AAS by for-profit non-disclosing entities lodging SPFS with ASIC shows that at least 10% and potentially up to 24% of them do not appear to have followed the guidance outlined in RG 85.

BC26 SPFS have also been called into question in a number of other regulatory matters. As part of the *Senate Economics References Committee on Tax Avoidance*, the Board's Chair was asked to explain to the Committee the reporting entity concept and its role in facilitating the preparation of SPFS. The Board noted the subsequent Report, *Corporate tax avoidance Part III, Much heat, little light so far* (May 2018), which outlined strong concern that multinationals operating within Australia are avoiding public scrutiny through the preparation of SPFS, which are not required to disclose corporate tax and related party transactions, and also noted the Board's role in facilitating the public lodgement of SPFS through its reporting entity concept. The Report recommended the Government require all companies, trusts and other financial entities with income above a certain amount to lodge GPFS with ASIC. These comments, albeit with a focus on tax, reinforce the view that a problem exists in relation to the way in which the reporting entity concept is applied, as well as the information provided through the public lodgement of SPFS.

BC27 The Board also reflected on the recommendations in the *Final Report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry* (February 2019), particularly the recommendation to remove special rules and exceptions that can create regulatory complexities. The Final Report indicated that exceptions departing from underlying principles have consequences often resulting in exploitation and that exceptions act as barriers to simplification of regulation. The Board further considered the theme of enforceability within the Final Report, noting in particular that the subjectivity inherent in the current Australian reporting entity concept may not provide regulators an objective basis on which to enforce financial reporting obligations.

BC28 In addition, other regulatory developments indicated the growing need for GPFS instead of SPFS for entities required to prepare financial statements in accordance with AAS, for example:

(a) the requirement for Significant Global Entities (SGE)[8] to lodge GPFS with the Australian Taxation Office (ATO), which would subsequently be provided to ASIC[9] (December 2015);

(b) questions to the Board Chair and Financial Reporting Council (FRC) Chair on the AASB and FRC's approach to resolving the SPFS issue by the Parliamentary Joint Committee on Corporations and Financial Services as part of its inquiry into the oversight of ASIC and the Takeovers Panel (February 2018); and

(c) the Senate Economics References Committee report *Financial and tax practices of for-profit aged care providers* (November 2018), which supported the Board's intent to remove the ability for entities to prepare SPFS in accordance with AAS.

BC29 In light of the regulatory developments and public enquiries noted above, the Board also observed the increasing public interest and media scrutiny of the trust, transparency and accountability of publicly available financial reporting, both generally and specifically in relation to the reporting entity concept and its facilitation of publicly lodged SPFS.

BC30 In proposing to remove the ability for entities to prepare SPFS when required to comply with AAS, the Board has received support from other regulators, particularly ASIC and the ATO, who conveyed the following views to the Board:

8 An entity is an SGE for a period if it is one of the following (as defined in Subdivision 960-U of the *Income Tax Assessment Act 1997*):
(a) a 'global parent entity' whose 'annual global income' is A$1 billion or more
(b) a member of a group of entities consolidated (for accounting purposes) where the global parent entity has an annual global income of A$1 billion or more.

9 Introduced by *Tax Laws Amendment (Combating Multinational Tax Avoidance) Act 2015*.

(a) ASIC fully supports the consultation to remove SPFS for entities regulated by ASIC and remove the subjective 'reporting entity' test under SAC 1, facilitating a comparable, consistent and transparent framework for preparation of financial statements in Australia; and

(b) the ATO is supportive of the AASB's proposed approach to consulting on a series of principles or concepts for enhancing the transparency of entities currently preparing SPFS as part of adopting the RCF issued by the IASB and for inclusion in AAS by 2021.

BC31 The Board also worked in consultation with the Treasury in considering legislative requirements that specify which types of for-profit entities should be required to publicly lodge financial statements with ASIC. Accordingly, in April 2019, the Treasury announced changes to the Corporations Regulations[10] to increase (double) the thresholds used in determining whether an entity is a large proprietary company, with companies falling below the threshold no longer being required to publicly lodge financial reports with ASIC. As part of the changes, the Board supported the Treasury in providing objective criteria based on economic significance for determining thresholds for when an entity should publicly lodge financial statements and noted the commentary in the Treasury's Explanatory Statement, which is consistent with the Board's proposal to remove the ability to prepare SPFS when required to comply with AAS, in particular:

(a) the requirement for large proprietary companies to lodge financial reports was first introduced to focus regulation of reporting on the financial affairs of proprietary companies that have a significant economic influence; and

(b) the financial reports of companies that have economic significance should be publicly available because of their size and potential to affect the community and the economy. The larger the size, the more likely it is that there will exist users dependent on GPFS as a basis for making economic decisions.

BC32 In light of the above, the Board concluded that it should play its role in the regulatory environment to ensure that the current subjective reporting entity concept that leads to a lack of consistent, comparable, enforceable financial reporting, is removed from the AAS.

Feedback from constituents, including financial report users

BC33 In addition to the above, the Board noted the general agreement amongst stakeholders that there is an SPFS problem in its outreach both prior and subsequent to the issue of ITC 39. In considering submissions received on ITC 39 the Board noted that of the 33 formal respondents, 85% agreed there is a problem with SPFS that needs to be solved, with similar feedback received anecdotally in other outreach.

BC34 As part of the due process, a significant amount of feedback was provided by users of financial statements. Of particular importance was the Board's publication *Enhancing the revised* Conceptual Framework *and replacing Special Purpose Financial Statements, For-profit User and Preparer Survey Results* (December 2018), which indicated that, from the perspective of users (analysts, investors and creditors):

(a) there is a problem with SPFS that needs to be addressed – 78% of primary users expressed concern that SPFS do not consistently apply R&M requirements in AAS;

(b) 93% of primary users and over 95% of other users said that comparability, transparency, comprehensibility and consistency are all paramount[11]; and

(c) there is dissatisfaction with SPFS that needs to be addressed, particularly around the lack of related party disclosures, lack of comparability and that the extent to which entities comply with R&M is unclear to users.

BC35 In addition to the information in paragraph BC34 the Board also noted other evidence that clearly indicates the existence of users who would benefit from having access to GPFS rather than SPFS. For example:

(a) over 98,000 copies of financial statements are purchased annually from ASIC. Of those financial statements purchased, 80% were of proprietary companies, 16% were of unlisted public companies and 4% were of small foreign controlled companies;

(b) anecdotally, data aggregators[12] rely on publicly available information to assist their clients with determining the viability, capacity and credit risk associated with a company; and

(c) as noted in paragraph BC31, the Treasury has indicated in its Explanatory Statement to the revision of the large proprietary company thresholds the expectation of users dependent on GPFS of large

10 Introduced by *Corporations Amendment (Proprietary Company Thresholds) Regulators 2019*.
11 'Primary users' refers to users that meet the definition of primary users in AASB Practice Statement 2 *Making Materiality Judgements* (i.e. investors (and analysts), lenders and other creditors). All other respondents to the user survey are referred to as 'other users' throughout this document.
12 Data aggregators purchase and analyse data for the purpose of providing informed credit and risk management advice, industry profiling and other analytic products and services.

proprietary companies, given their economic significance. Further, that Explanatory Statement noted that average access rates through ASIC of the revised (smaller) population of large proprietary companies was significantly higher (on average 3.6 times) than the proprietary companies that would no longer have an obligation to lodge financial statements with ASIC (on average 1.8 times).

BC36 Despite the relatively lower access rates of small foreign controlled companies and unlisted public companies noted in paragraph BC35(a) immediately above, the Board noted its expectation that those users would benefit from having access to GPFS rather than SPFS given that:

(a) small foreign controlled companies are already provided with significant relief from financial reporting obligations if the company is included in consolidated financial statements lodged with ASIC by a registered foreign company Additionally, ASIC Corporations (Foreign-Controlled Company Reports) Instrument 2017/204 provides further relief to small foreign controlled entities – even if they are not consolidated by a registered foreign company lodging with ASIC – by requiring them to lodge financial statements with ASIC only if directed to do so by shareholders or ASIC or if they are part of a large group in Australia. The requirement for small foreign controlled companies to lodge financial statements where they are part of a large group is designed to prevent foreign-controlled companies disaggregating their Australian activities into smaller companies to avoid financial reporting obligations[13]. In light of this Australian public interest context, there appears to be no justification for small foreign controlled companies to not be required to prepare GPFS; and

(b) unlisted public companies would have at least 50 non-employee shareholders (ie external users) and have the ability to offer shares to the public. As such, the Board noted it would be difficult to justify there being no external users of such entities' financial statements – and therefore GPFS are warranted.

Resolving the issues

BC37 The Board decided that to play its part in resolving the clash between the reporting entity concepts, as well as to improve the consistency, comparability, transparency and enforceability of the for-profit private sector financial reporting framework, it had to remove the Australian reporting entity concept (by making the consequential amendments to AAS set out in this ED). This would also remove the ability of an entity to self-assess that it is not a reporting entity as currently defined, and so prevent it from preparing SPFS if it is required to prepare financial statements in accordance with AAS.

BC38 The Board concluded the removal of the self-assessment of the reporting entity concept and disallowance of the preparation of SPFS would simplify the reporting framework by providing a single set of minimum requirements in financial statement preparation, facilitating an objective of a consistent, comparable, transparent and enforceable Australian financial reporting framework.

BC39 In arriving at this solution the Board considered a range of alternatives through ITC 39, as noted in the next section.

ITC 39

Preferred option in ITC 39

BC40 As noted in paragraph BC7, ITC 39 was a precursor due process document to this ED. It helped the Board refine its thinking and narrow down possible courses of action. In ITC 39 the Board considered five different options for implementing the RCF in Australia and their benefits and barriers. After considering the comments on ITC 39, the Board decided to adopt Option 1 in ITC 39, a two-phased approach to applying the RCF:

(a) in the short term maintaining compliance with IFRS Standards for publicly accountable entities and entities voluntarily claiming compliance with IFRS Standards (Phase 1) – ie Tier 1 GPFS; and

(b) in the medium term maintaining IFRS Standards as a base by removing the Australian reporting entity concept from AAS and providing a revised Tier 2 GPFS framework (Phase 2)[14]. This would remove the ability of an entity to prepare SPFS as a non-reporting entity where they are required to comply with AAS.

BC41 The Board decided in favour of this two-phased approach because it:

13 See the Explanatory Statement to *ASIC Corporations (Foreign-Controlled Company Reports) Instrument 2017/204*

14 To complement and support the proposals in this ED, as noted in paragraph BC3 above, the Board has also proposed to simplify the current GPFS-Tier 2 framework in a separate ED 2XX– a summary of which is provided in paragraph BC73-BC88 below, to provide context to the proposals in this ED

(a) allows for-profit private sector entities with public accountability and entities that voluntarily report compliance with IFRS Standards to continue to do so;

(b) allows all other entities to continue preparing SPFS in the short term while the Board undertakes consultation and outreach activities and determines the appropriate Tier 2 GPFS framework to replace SPFS;

(c) maintains IFRS Standards as a base for all entities in the medium term;

(d) solves the reporting entity problem in the medium term;

(e) solves the SPFS problem in the medium term;

(f) allows time for the Board to consult and determine any NFP modifications that may be necessary to the RCF in accordance with *The AASB's Not-for-Profit Entity Standard-Setting Framework*; and

(g) facilitates comparability and ensures there are appropriate accounting standards for each type of entity required to comply with AAS.

BC42 The two phased approach option put forward in ITC 39 contemplated that during Phase 2 the Tier 2 GPFS framework in AASB 1053 would be revised to include one of the following alternatives:

(a) Reduced Disclosure Requirements (RDR) – The existing Tier 2 GPFS framework as is in AASB 1053, consisting of consolidation and equity accounting (where applicable) with adoption of full R&M with reduced disclosures from each AAS; or

(b) Specified Disclosure Requirements (SDR) – A new Tier 2 GPFS framework that would still consist of consolidation and equity accounting (where applicable) with adoption of full R&M, however with specified disclosures from AAS.

The Board subsequently decided to propose neither of the RDR or SDR frameworks, instead developing another alternative *Simplified Disclosure Requirements*, as explained further in paragraph BC73.

BC43 Phase 1 implements the RCF for publicly accountable for-profit private sector entities and other entities voluntarily reporting compliance with IFRS Standards so that they can continue to maintain IFRS compliance when the RCF takes effect internationally on 1 January 2020. Entities in Australia with public accountability must apply the full IFRS Standards as AAS incorporate IFRS Standards and therefore, the Board reconfirmed its view that for-profit private sector entities in Australia with public accountability should be required to prepare Tier 1 GPFS. The Board completed Phase 1 in June 2019 (see AASB 2019-1 *Amendments to Australian Accounting Standards – References to the Conceptual Framework*).

BC44 Subsequent to the issue of ITC 39, after hearing concerns from NFP entities about the AASB's two-phase approach as proposed in ITC 39 and considering the discussions with ACNC and other State and Territory regulators regarding recommendations in the ACNC's Legislative Review report 2018: *Strengthening for Purpose: Australian Charities And Not-For-Profits Commission*, the Board decided that the proposals in ITC 39 should only apply to for-profit entities (see paragraphs BC51-BC72 on the scope of this ED's proposals for more details).

Other options considered in ITC 39

BC45 ITC 39 considered four other options for implementing the RCF in Australia. However, after considering constituent comments, the Board decided not to pursue them, as explained in the following:

(c) Option 2 – Operate with two conceptual frameworks. This option would implement the RCF for publicly accountable for-profit entities and other entities voluntarily reporting compliance with IFRS Standards. It would also retain the *Framework for the Preparation and Presentation of Financial Statements* (the existing Conceptual Framework) for all other entities. The Board decided not to pursue this option as it requires two conceptual frameworks, which would likely lead to the development of inconsistent accounting policies between entities preparing financial statements under the existing Conceptual Framework and entities preparing financial statements under the RCF. Also this option does not solve either the clash of the reporting entity concepts or the SPFS problem.

(d) Option 3 – Implement the RCF for all entities when it first becomes applicable. This option would result in a single conceptual framework for all entities in the short term, remove the Australian reporting entity concept and the ability of an entity to prepare SPFS when they are required to comply with AAS from 1 January 2020. Option 3 would see an increase in regulatory burden as there would be a considerable step up for many entities transitioning to Tier 2 GPFS (RDR) framework given the number of entities preparing SPFS and the short timeframe for transition to GPFS. The Board was concerned that this option would not provide entities with enough time for transition.

(e) Option 4 – Retain the existing Conceptual Framework, the Australian reporting entity concept and the ability of an entity to prepare SPFS when they are required to comply with AAS. This option would mean there is no change for affected entities, however the compliance of AAS with IFRS Standards would be lost after 1 January 2020.

(f) Option 5 – Implement the RCF from 1 January 2020 when it first becomes applicable to maintain compliance with IFRS Standards and keep IFRS Standards as a base for AAS, change the name of the Australian reporting entity concept (to avoid terminology confusion) and prescribe minimum requirements for SPFS, which would mean retaining the self-assessment mechanism. Under Option 5, the Australian reporting entity concept would be retained but the name amended and minimum requirements for SPFS would be prescribed by the Board. The Board decided not to proceed with Option 5 as it did not consider this option to be much different from Option 1 (except for the phased approach) or Option 3, as the AASB would still need to prescribe minimum reporting requirements for SPFS preparers to resolve the SPFS problem.

AASB's deliberations on proceeding with Phase 2

BC46 The Board received 36 formal comment letters in response to ITC 39 from professional service firms, regulators, professional bodies, academics, preparers, users of financial statements and other respondents on specific and general matters for comment regarding Phase 2. The Board considered every comment from each respondent and set up meetings to further discuss any consequential comments raised in their responses. The responses to ITC 39 confirmed and identified the following significant issues:

(a) there is a SPFS problem that needs to be solved;

(b) the Tier 2 GPFS framework should require compliance with consolidation and equity accounting (where applicable) and all R&M requirements in AAS;

(c) neither GPFS-RDR nor GPFS-SDR is a preferable disclosure Tier 2 framework for the reasons consistent with the feedback noted in paragraph BC47(c) below;

(d) only one Tier 2 GPFS framework is necessary for for-profit entities, given the entities required to publicly lodge financial statements is such a small proportion of actively trading entities; and

(e) whether there is a need to consider transition relief in addition to what is in AASB 1 *First time Adoption of Australian Accounting Standards.*

BC47 The Board presented the Phase 2 proposals (targeted to only for-profit entities) to obtain feedback at various forums, workshops and discussion groups, including roundtable sessions held in May and September 2018, where 263 stakeholders[15] including regulators, professional bodies, users, preparers, auditors and academics across all sectors attended. Furthermore, the Board conducted user and preparer targeted surveys in 2018, which received a total of 37 user and 49 preparer responses. The surveys were focussed on specific matters in ITC 39, and were used to get a better understanding of which Tier 2 GPFS framework users preferred (and why), and what transitional relief would be helpful to preparers. The feedback received from the roundtables and surveys were consistent, indicating that:

(a) there is a SPFS problem that needs to be addressed if R&M requirements have not been consistently applied;

(b) comparability, transparency, comprehensibility and consistency are what users need most in financial statements;

(c) a revised Tier 2 GPFS framework was preferred as GPFS-SDR seemed to be missing some key disclosures, while GPFS-RDR had too many, so respondents suggested a balanced approach to disclosure; and

(d) there is widespread uncertainty on whether AASB 1 provides enough transitional relief to facilitate moving from SPFS to the Tier 2 GPFS framework (whatever form that takes).

BC48 Subsequent to receiving comments on ITC 39, the Board released all formal comment letters to the public and uploaded them to the AASB website[16]. This was also done with the various outreach events conducted by the Board, where summaries of feedback, results from user and preparer surveys, and agenda papers for AASB Board meetings were also uploaded to the AASB website for public viewing.

BC49 Based on the above, the Board decided it is imperative to proceed with Phase 2 and resolve the issue with SPFS.

15 157 attendees in May 2018 and 106 attendees in September 2018.
16 See https://www.aasb.gov.au/DirectLink.aspx?id=2155

BC50 The next section details the Board's deliberations in deciding which types of entities should be within the scope of the proposals in this ED and which should be subject to further due process before removing the current SPFS self-assessment approach.

Scope

BC51 For-profit non-disclosing entities affected by the Phase 2 proposals in this ED are large proprietary companies, unlisted public companies not limited by guarantee and small proprietary companies controlled by a foreign company, all of which have been identified by the Board as being likely to have users dependent on their GPFS(see paragraph BC34). The Board conducted research into non-disclosing entities lodging with ASIC and concluded there were approximately 12,816 for-profit non-disclosing entities lodging financial reports (based on latest lodgements by all filing entities as at 30 July 2018 – which was before the thresholds for large proprietary companies were doubled), 6,783 of which were large proprietary companies[17], 3,109 were unlisted public companies and 2,924 were small proprietary companies controlled by a foreign company. Subsequent to the revision of the large proprietary thresholds, the Board expects there are approximately 10,000 non-disclosing entities that would be required to publicly lodge financial statements with ASIC.

BC52 Anecdotally, the Board is aware that some entities preparing SPFS are parent entities but do not prepare consolidated financial statements, and some of those are not providing an explanation as to why they have not consolidated.

BC53 Despite ITC 39 proposing to include NFP and public sector entities in its scope, the Board subsequently decided, based on feedback from stakeholders, to limit the application of the Phase 2 proposals to all for-profit private sector entities (other than those in Phase 1) that are required to comply with AAS, with the exception of entities with a non-legislative requirement to comply with AAS (in certain circumstances – see paragraphs BC61-BC72). The Board concluded it would be more appropriate to address the implementation of the RCF for NFP and public sector entities via separate targeted consultations undertaken as part of the broader Financial Reporting Framework project.

BC54 In making this decision the Board noted it still aimed to achieve a simple, comparable, proportionate and transparent financial reporting framework for NFP entities (in both the private and public sectors) in due course.

Private sector entities that are required to comply with AAS, except for trusts

BC55 As noted in paragraph BC53 above, the Board decided this ED should focus only on for-profit private sector entities and that separate later consideration of the NFP private sector was needed for the following reasons:

(a) the removal of SPFS would have a significantly greater impact on the NFP private sector compared with the for-profit private sector. Of those NFP private sector entities that are required to prepare financial reports and lodge with ACNC, preliminary research indicates that only a small portion of charities state compliance with R&M requirements in AAS as opposed to approximately 76% of non-disclosing for-profit private sector entities that comply with R&M requirements in AAS (see paragraph BC19). The substantially lower level of compliance in the NFP private sector would result in a much larger proportion of the reporting population being impacted by the proposals compared with the for-profit private sector;

(b) for-profit private sector non-disclosing entities that would be required to lodge financial statements in accordance with AAS have greater levels of economic significance, size and resources than NFP private sector entities. Proportionately they are a significantly smaller number (less than 1.2% of the population of trading entities are required to prepare financial statements in accordance with AAS – see paragraph BC77 for more details), whereas approximately 33% of charities (16,170 large and medium charities out of a total of 48,782 registered with ACNC) are required to prepare financial statements in accordance with AAS. Due to the differences in characteristics, the Board consider it more appropriate to consider the merits of a third tier of GPFS for the NFP sector, as part of a separate project; and

(c) the unknown Government response to the ACNC legislative review *Strengthening for purpose: Australian Charities and Not-for-profit Commission Legislation Review* (2018), which outlined the potential for change in reporting thresholds and obligations for entities. To proceed with NFP private sector financial reporting reform could be burdensome for certain NFP entities if the AASB were to require them to comply with R&M requirements, but ACNC subsequently relieves them of any financial reporting obligations once the ACNC legislative review is finalised.

17 This research was performed prior to Treasury doubling the thresholds used to determine large proprietary companies. Subsequently the Board noted that Treasury's increasing of the thresholds would reduce the number of large proprietary companies to 3,986.

BC56 Some respondents to ITC 39 were concerned about the NFP private sector being delayed and felt that the AASB should either prioritise the NFP private sector financial reporting framework reform, or should continue to work on it concurrently with the for-profit private sector financial reporting framework reform. The basis of those respondents' concerns were mixed. Some were concerned in relation to transaction neutrality and that the AASB would develop different reporting requirements compared with the for-profit private sector, which would decrease comparability and consistency of financial reports. Others were concerned the NFP private sector has specific needs that should be considered up front or else a framework may be imposed that is fit for purpose in the for-profit private sector but not in the NFP private sector.

BC57 The Board considered this feedback and noted that *The AASB's Not-for-Profit Entity Standard Setting Framework* (NFP Standard Setting Framework) provides for NFP sector specific modifications where justifiable. For this reason, notwithstanding the outcomes in the for-profit private sector, a thorough consideration of their appropriateness in accordance with the NFP Standard-Setting Framework would be required, and if determined not to be suitable for NFP entities, the for-profit proposals would be modified as needed. This assessment would be required, even if the for-profit and NFP reforms were undertaken concurrently.

BC58 The Board also conducted research (AASB Research Report No. 10 *Legislative and Regulatory Financial Reporting Requirements* (March 2019)) into legislation to determine which categories of for-profit private sector entities should be within the scope of this ED. In particular, the Board considered whether entities that are required by legislation to prepare financial statements that give a true and fair view without reference to compliance with AAS at the same time (for example small co-operatives and entities reporting under state and territory gaming legislation) should be affected by Phase 2. The Board noted the Corporations Act envisages compliance with the accounting standards might not necessarily result in financial statements that provide a true and fair view. In addition, the UK FRC paper *True and Fair* from June 2014 confirmed the primacy of the true and fair requirement above compliance with accounting standards. Following consultation with other regulators responsible for the the legislation referring to true and fair, the Board considered that it should be a matter for each regulator to decide as to how to interpret the relevant legislation in relation to 'true and fair view' and noted that to require compliance with AAS whenever legislation required entities to give a true and fair view could possibly have significant unforeseen consequences. Accordingly, the Board decided the application paragraphs for AAS implementing Phase 2 should not explicitly refer to true and fair, and should only refer to 'where an entity is required to prepare financial statements in accordance with AAS'.

BC59 The Board decided it was imperative to proceed with its proposal to disallow SPFS for for-profit private sector entities required to comply with AAS, especially in light of the findings of the academic research on compliance with R&M requirements and the feedback from regulatory bodies (see paragraphs BC23-BC32) and the other issues noted above.

Public sector entities

BC60 The Board decided that separate consideration of the public sector was needed because, unlike in the for-profit private sector and NFP private sector, public sector financial reporting is arguably too extensive and not targeted enough to enable public sector entities to be held sufficiently to account. For example, government departments are effectively administrative constructs, and requiring Tier 1 GPFS financial reports for all such departments when they are also included in Whole of Government (WoG) GPFS means users might not be directed to the key budget versus actual and service performance reporting that would enable genuine accountability. Therefore, the Board decided it would pursue financial reporting reform in the public sector via consultation based on the AASB Discussion Paper *Improving Financial Reporting for Australian Public Sector*, which was issued in June 2018, rather than as part of Phase 2 of ITC 39.

Trusts and other entities with a non-legislative obligation to comply with AAS.

BC61 When deciding on the scope of Phase 1 of ITC 39 the Board's intention was to allow entities to maintain compliance with IFRS Standards, not to extend requirements for entities to prepare GPFS if they were not currently required by legislation to prepare financial statements. Respondents to ITC 39 identified some entities that may be affected by the amendments proposed in Phase 1, such as trusts required by their constitutional document (rather than legislation) to prepare financial statements that comply with AAS. They do not have any legislative requirement to prepare such financial statements and may be currently preparing SPFS. Therefore, transitioning to GPFS could be burdensome for those trusts.

BC62 Consequently, the Board decided to limit Phase 1 to for-profit private sector entities that have public accountability and are required by legislation to comply with AAS, however it noted that the appropriateness of this limitation would be reconsidered as part of Phase 2 after additional research and outreach is performed.

BC63 When reconsidering the appropriateness of this limitation the Board considered entities with a non-legislative requirement to prepare financial statements that comply with AAS more broadly than just those affected by Phase 1, noting there were likely to be a significant number of additional trusts possibly affected by Phase 2.

Commented [BJ6]: Question 9 for Board Members:
At the April 2019 AASB meeting, the Board directed staff to proceed with providing an exemption for trusts in certain circumstances.

However, staff recommend extending this exemption be extended to all entities that have a non-legislative requirement to comply with AAS, as those entities also have specific users who would be able to demand the specific information that they need (see paragraph BC69 below)

Does the Board agree to provide this exemption to all all entities that have a non-legislative requirement to comply with AAS, rather than only trusts?

BC64 Based on discussions with legal advisors and additional targeted outreach, it is expected that the constituting documents of most trusts contain a requirement for them to prepare financial statements in compliance with AAS (albeit they might refer to 'accounting standards'). These financial statements are prepared for a specific purpose and a specific user (e.g. the beneficiary/ies of a trust). It is also understood that many such entities, particularly 'non-corporate' trusts, prepare SPFS.

BC65 The Board noted that:

(a) as the financial statements are prepared for specific users, those users have the ability to command whatever information they require from the entity;

(b) there is no external regulator of financial reporting for trusts; and

(c) the financial statements of trusts are not lodged on public record.

BC66 For these reasons, the Board considered whether it was appropriate to provide some form of relief to these, as the Board noted that while changing constitutional documents to remove the requirement to comply with AAS is possible, it can be onerous and if not done correctly can have tax consequences.

BC67 Targeted outreach was undertaken to understand the number of trusts that may be affected by the proposals in this ED, including their size (with reference to income and assets). This was to determine whether it was possible to develop objective criteria related to economic significance for distinguishing between those trusts that should be required to comply with the proposals contained in this ED and those that should be exempted or granted transitional relief. The Board considered whether the thresholds for determining a large proprietary company could be an appropriate benchmark for this purpose.

BC68 While there are a large number of trusts undertaking business activities and therefore lodging tax returns with the ATO, a small minority of them would meet the new income and assets thresholds used to determine a large proprietary company.

BC69 The Board also noted there are entities other than trusts that currently have a requirement to prepare financial statements in accordance with AAS in their compliance documents but are not required to do so by legislation, such as partnerships, certain joint arrangements, self-managed super funds and other operating structures, as well as requirements circumstances such as lending agreements. As these entities also have specific users, the Board decided that the issues identified above would be equally relevant to such entities.

BC70 The Board therefore decided that existing for-profit entities should be provided with an exemption from the requirement to prepare GPFS where they do not have a legislative requirement to prepare financial statements that comply with AAS. However, the Board decided this exemption should only apply whether their constituting document (or another document) requiring them to comply with Australian Accounting Standards was created or amended before after 1 July 2020 – ie any amendments or creation of such documents after 1 July 2020 would require the entity to prepare GPFS.

BC71 The Board decided the exemption should be limited as if an entity were required to make an amendment to the constituting document for any reason after the effective date of the amendments, then the trustee could at the same time amend the financial reporting requirements, subject to the agreement of the beneficiaries. Further, the relief should not be available to a constituting document created or amended after the effective date of the amendments as when drafting the constituting document, the beneficiaries should have determined their information needs including whether or not they required GPFS.

BC72 Having decided the types of for-profit private sector entities that should be preparing GPFS, the Board considered what revisions to the Tier 2 GPFS framework would appropriately weigh up the costs and benefits of the proposals in this ED. Accordingly, to provide a context to the proposals in this ED, the following section summarises the Board's deliberations on revising the Tier 2 GPFS framework (that is detailed in the related ED 2XX).

Tier 2 GPFS Framework

BC73 As noted in paragraph BC40 above, the Board acknowledges that it would be inappropriate to remove the ability to prepare SPFS without replacing it with a suitable GPFS framework, because the current Tier 2 GPFS framework would be too onerous. The Phase 2 approach in ITC 39 contemplated revising the Tier 2 GPFS framework in AASB 1053 to include one of two alternatives. As noted in paragraph BC42 above, there were two alternatives contemplated in ITC 39:

(a) alternative 1 was the existing Tier 2 GPFS – RDR under AASB 1053 established in Australia, which requires full R&M requirements of IFRS Standards (as amended for NFP specific issues) and with minimum disclosures specified in each Standard. The feedback from the roundtables, surveys and submissions on ITC 39 indicated that RDR has too many disclosure requirements; and

(b) the second proposed alternative, the SDR, was a revised disclosure framework. It required full R&M of IFRS Standards (as amended for NFP specific issues) and included the disclosure of those Standards that are currently mandatory for entities required to prepare financial statements in accordance with Chapter 2M of the *Corporations Act 2001*, being AASB 101, AASB 107, AASB 108, AASB 1048 and AASB 1054, and disclosures required by AASB 124 *Related Party Disclosures*, AASB 136 *Impairment of Assets*, AASB 15 *Revenue from Contracts with Customers* and AASB 112 *Income Taxes*.

BC74 As noted in paragraph BC47, the feedback on the proposed SDR GPFS framework was that the SDR is too much in some ways but falls short in many other ways. For example, the feedback received from roundtables, surveys and submissions on ITC 39 Phase 2 was that whilst the disclosures in SDR are important, requiring full disclosure of those nine Standards was too much. Most participants further suggested that SDR might not be appropriate for all industry sectors and is missing some critical disclosures to help predict the viability of an entity such as liquidity, contingent liabilities, subsequent events and commitment disclosures. At the same time, as noted in paragraph BC47, respondents also noted that the current RDR GPFS framework is too onerous. The Board further noted that given the small number of for-profit entities required to publicly lodge financial statements with ASIC, which will be even less once the increase of the reporting thresholds for large proprietary companies becomes applicable, the development and maintenance of more than two GPFS disclosure frameworks was not warranted. As a consequence, the Board agreed to develop a third alternative as replacement of the current Tier 2 GPFS RDR framework, being a new and separate disclosure Standard for entities reporting under Tier 2 GPFS framework, termed as 'Simplified Disclosure' that would be based on the *IFRS for SMEs* disclosures.

BC75 The disclosure to be required by the Simplified Disclosure framework are being proposed in a separate Exposure Draft, ED 2XX *New Accounting Standard: General Purpose Financial Statements – Simplified Disclosures for Tier 2 Entities*, and have been developed via a 'bottom-up' approach based on the *IFRS for SMEs* disclosures, without reference to the full IFRS disclosures (ie no shading).

One Tier 2 GPFS Framework

BC76 Some respondents to ITC 39 suggested that more than one Tier 2 GPFS framework was necessary, as having only one Tier 2 GPFS framework is too limited.

BC77 The Board noted that of the 2.5 million companies registered with ASIC in 2016-2017, only approximately 840,000 were actively trading, and of those there were only approximately 12,816 for-profit non-disclosing entities that were required to prepare financial statements. This represents approximately only 1.5 of the population of trading entities. The Board further noted that Treasury's increase of the large proprietary company thresholds would further reduce this number to 1.2% of the population of trading entities. The Board noted that this would be a very small population of the total number of trading entities and having one Tier 2 GPFS framework was sufficient for this population.

BC78 Some respondents felt that additional GPFS tiers of reporting with varying degrees of disclosure may be useful as lodging entities range in size and complexity. However the Board emphasised that entities without a statutory requirement to comply with AAS, such as those below the now doubled large proprietary company thresholds in the *Corporations Act 2001*, would be able to continue to tailor their financial statements to the needs of their specific users and therefore additional Tiers were not required.

R&M requirements of Tier 2

BC79 The Board noted the strong preference expressed by respondents of ITC 39 for a framework that includes full R&M requirements in AAS on the grounds that it would enhance the comparability, consistency and transparency of the financial statements. Feedback from targeted outreach emphasised that users agreed the usefulness of information within financial statements for decision making is adversely affected where entities have not consistently applied R&M requirements.

BC80 Findings from yet to be published AASB Research Report XX *Financial Reporting Practices of For-Profit Entities Lodging SPFS - 2019* indicate 76% of non-disclosing entities that need to publicly lodge financial statements in accordance with AAS with ASIC are complying with R&M requirements of AAS (see paragraph BC19). Therefore, the Board found moving to a Tier 2 GPFS framework that moves away from full R&M to be counter-intuitive when trying to improve the consistency, comparability, usefulness and credibility of financial reporting in Australia.

BC81 Some respondents to ITC 39 suggested having a Tier 2 GPFS framework with differential R&M, such as *IFRS for SMEs*. However, the Board felt that this might result in increased transition costs as most ASIC regulated entities preparing SPFS are complying with full R&M in AAS (see paragraph BC19). The Board also noted that any reduction in on-going compliance costs would not be significant enough to outweigh the loss of benefit to users, especially because *IFRS for SMEs* still requires consolidated financial statements, deferred tax accounting, financial instruments accounting and related party disclosures that are not substantively different from full R&M requirements. The Board noted that 65% of respondents did not agree with this option.

BC82 The Board re-evaluated the suitability of *IFRS for SMEs* as Tier 2 GPFS framework requirements in Australia and reconfirmed that *IFRS for SMEs* is not presently suitable in Australia due to the following concerns:

(a) *IFRS for SMEs* has different R&M requirements compared with IFRS Standards, which is not consistent with ASIC and other regulators' views that the full R&M requirements of accounting standards should be applied in order to give a 'true and fair view' of the financial position and performance of an entity;

(b) *IFRS for SMEs* would result in reduced comparability between entities preparing full IFRS Standards compliant financial statements because of different accounting policy alternatives and different R&M requirements;

(c) in the event an entity moves to, or from, full IFRS Standards, there would be costs involved in migrating from the R&M requirements of one Tier of reporting to another;

(d) the feedback to ITC 39 suggested that consolidation and equity accounting for the first time would be the most difficult aspect of transitioning from SPFS to GPFS, however consolidated financial statements are required under the *IFRS for SMEs* framework anyway. As such, it does not appear that adopting the *IFRS for SMEs* would be any more cost effective in that area of concern; and

(e) additional transitional costs would be expected to arise because:

(i) based on the data in paragraph BC19, most ASIC regulated entities are already complying with R&M in AAS, therefore a larger population of preparers would see an increase in the costs associated with the transition from SPFS to the Tier 2 GPFS framework if there were to be different R&M requirements; and

(ii) subsidiaries would need to provide additional information to be compliant with IFRS Standards for the purpose of consolidating into their parent's consolidated financial statements where the parent applies Tier 1 AAS or IFRS Standards.

BC83 In light of the above, as noted in paragraph BC74, the Board decided to develop a separate *IFRS for SMEs*-based disclosure Standard. This would be a new Tier 2 GPFS framework disclosure Standard for entities that are not publicly accountable, while retaining the full R&M requirements of AAS. This Standard will replace the existing Tier 2 GPFS RDR framework.

Consolidation requirements of Tier 2 GPFS framework

BC84 While considering the new Tier 2 GPFS disclosure Standard, the Board also contemplated whether the financial information about subsidiaries could be provided in a more cost effective way, such as by providing summary financial information in the consolidated financial statements of the parent instead of a complete set of financial statements for the subsidiary. The Board undertook research (not yet published) to assess the suitability of current reporting requirements where the views of different lending institutions were sought. The feedback received showed there is a need for both a full set of subsidiary financial statements and the consolidated financial statements of the group. Feedback received from users in response the AASB's user survey and submissions to ITC 39 also highlighted the need for consolidated financial statements.

BC85 The majority of the banks interviewed mentioned that in the case of group structures, they need consolidated financial statements of the group to make their lending decisions and that these are particularly important when:

(a) there is structural subordination within group structures;

(b) there is a deed of cross guarantee;

(c) banks have legal recourse to the assets of the consolidated group;

(d) lending to a subsidiary is in the form of a credit enhancement to the whole group; and

(e) lending is to a subsidiary that does not have substantial operations and it is a financing vehicle.

BC86 Similarly, feedback from users mentioned that in order to make decisions they require:

(a) consolidated financial statements including note disclosures (which include all assets, liabilities, revenues and expenses of the parent and all subsidiaries); and / or

(b) consolidated financial statements including note disclosures plus some parent entity information to understand their dividend paying capacity.

BC87 The above provided further support to the Board's view that consolidated financial statements are essential to provide users with transparent and complete information about the financial position and financial performance of the group and the entities in the group.

BC88 Although the Board decided that a revised Tier 2 GPFS framework would help facilitate the removal of SPFS, it also decided that transitional relief was warranted to further help entities transition from SPFS to revised Tier 2 GPFS, as noted in the next section.

Transition

Feedback from ITC 39

BC89 In developing ITC 39, the Board acknowledged that some entities might incur additional costs, particularly on transition from SPFS to Tier 2 GPFS. As such, the Board included specific matters for comment in ITC 39 seeking feedback on what transitional relief should be provided, in addition to that already available in AASB 1. Feedback on transitional relief was also sought by the Board in its roundtable discussions, surveys, webinar and individual meetings with constituents.

BC90 Feedback from the consultation activities related to ITC 39 and specifically on transitional matters was mixed. Whilst some constituents agreed that AASB 1 would be sufficient to facilitate transition, others were either unclear on whether AASB 1 would be sufficient, or argued that more transitional relief was necessary. The Board noted two common areas of suggestion for transitional relief:

(a) relief from consolidation and equity accounting, particularly in relation to the retrospective application of AASB 3 *Business Combinations*; and

(b) relief from the requirement to restate a comparative period on transition from SPFS to Tier 2 GPFS.

However, the Board noted that despite requesting more information, constituents had not articulated the specific aspects of the above-mentioned transitional issues that would be particularly costly or onerous.

Options considered

BC91 In deliberating the options for transitional relief, the Board noted AASB 1053, which requires an entity to either apply all the relevant requirements in AASB 1 or instead apply the requirements in AASB 108, to transition from its most recent SPFS to Tier 2 GPFS, if that entity had not applied or had only selectively applied the R&M requirements in AAS in those SPFS. The Board noted that entities already complying with the R&M requirements of AAS would not need transitional relief, given that such entities are required to merely continue applying the applicable R&M requirements in accordance with AASB 1053.

BC92 In light of constituent feedback that consolidation and equity accounting would be the most challenging aspect of transition, the Board specifically considered the relief provided by AASB 1 from the need to retrospectively account for past business combinations (a specific challenge noted for consolidation and equity accounting). The Board concluded that the application of AASB 1 already provides significant and sufficient relief to address the constituents' concerns noted in paragraph BC90(a).

BC93 The Board also noted:

(a) **Doubling of thresholds for large proprietary companies:** As noted in paragraph BC31 above the Treasury doubled the thresholds for what constitutes a large proprietary company. Based on the data available from a data aggregator for latest lodgements by all filing entities as at 30 July 2018 (being before the doubling), as noted in paragraph BC51, there were a total of 6,783 large proprietary companies that had lodged financial statements with ASIC, out of which 4,283 entities filed SPFS. The doubling of the thresholds reduced the total population of large proprietary companies by approximately 2,797 companies, leaving approximately 3,986 economically significant companies as large proprietary companies. Based on the revised thresholds, the same data from a data aggregator indicates that only approximately 2,631 large proprietary companies would be required under the proposals in this ED to transition to Tier 2 GPFS for the first time.

In addition, the Board noted the Explanatory Statement accompanying the revision of the thresholds that had outlined the expectation that larger entities are more likely to have users that are dependent on the entity's GPFS. Further, the Explanatory Statement also noted that the average access rates for financial reports through ASIC for the remaining population of large proprietary companies is significantly higher than for those entities that would now be small proprietary companies (see paragraph BC35).

The Board considered that such economically significant companies are expected to have sufficient skills and resources to cope with any transitional challenges within the current requirements.

(b) **Findings from yet to be published AASB Research Report XX *Financial Reporting Practices of For-Profit Entities Lodging SPFS – 2019*:** One of the key findings of this research is that overall 76% of for-profit non-disclosing companies lodging SPFS with ASIC comply with the R&M requirements of AAS; 10% did not comply with the R&M requirements of AAS while for the remaining 14% it was unclear whether or not they complied with the R&M requirements of AAS. As noted in paragraph BC91, entities already applying all of the R&M requirements of AAS would not require transitional relief.

While the Board noted that these results focused only on compliance with R&M requirements in their lodged SPFS and therefore did not identify whether entities prepared consolidated financial statements, the results show that out of approximately 5,371[18] for-profit entities lodging SPFS with ASIC following the revision of the large proprietary company thresholds , only 24% (approximately 1,300 entities) are expected to be affected by the proposals to remove the ability to prepare SPFS in accordance with AAS. The Board also noted that this number may be further reduced as the research showed a clear correlation between entity size and compliance, with the level of compliance increasing with company size.

Further, the Board noted that the primary reason for 6% of entities that did not comply with the R&M requirements was due to not applying AASB 112 fully, but constituents have not raised AASB 112 as being problematic for the purpose of transition.

(c) **Insufficient compelling evidence from extensive outreach:** The Board performed extensive outreach and asked for specific information on transitional relief that might be needed through formal comments on ITC 39, roundtables in capital cities and over 200 meetings with individual entities, and did not receive compelling evidence or suggestions identifying specific issues that need transitional relief. Further, no specific feedback was received from small foreign-controlled proprietary companies or unlisted public companies not limited by guarantee.

(d) **The AASB's For-Profit Entity Standard Setting Framework:** The Board noted the presumption that IFRS Standards are appropriate as a base for all entities, with particular regard to the fact that AASB 1, which incorporates IFRS 1 *First-Time Adoption of Australian Accounting Standards* had been developed by the IASB to reduce the cost of first-time adoption of IFRS Standards so that it does not outweigh the benefits of adoption. The Board also observed that the application of AASB 1 has been an appropriate base for entities transitioning to AAS since 2005, including a large number of entities who transitioned due to the requirement for Significant Global Entities that were required to transition for reporting periods ending on 30 June 2017 (Paragraphs BC106-BC108 provide a further discussion of how the Board has application its for-profit entity standard setting framework in arriving at the proposals in this ED.)

BC94 Nevertheless the Board considered three possible options that could be considered as a basis for providing transitional relief in addition to what is available under AASB 1, as follows:

18 2,631 large proprietary companies, 954 unlisted public companies not limited by guarantee and 1,786 small foreign controlled proprietary companies

Option	Nature of the relief considered	Key factors considered
'Push-down accounting' for entities that are subsidiaries of an IFRS Standards and/or AAS compliant parent	To allow subsidiaries that are consolidating into an AAS or IFRS Standards compliant parent to recognise amounts reported in their reporting/consolidation pack (which would have been derived from acquisition date fair values) to be deemed cost in their individual financial statements (subject to requiring them to recognise only those assets and liabilities that qualify for recognition under AAS in the subsidiary's own financial statements).	The Board noted that advantages of this relief would include: (a) no need to keep two sets of parallel accounting records (ie one set for group reporting purposes and another set for its own mandatory Tier 2 GPFS). (b) opening balances would still be based on AAS principles, albeit measurement at a different point in time. However, the Board decided not to propose this relief due to: (a) the reasons noted in paragraph BC93; (b) this relief would have been inconsistent with the Standard-Setting Framework's presumption that IFRS Standards are an appropriate base; (c) anecdotally, adjusting balances to be consistent with AAS is not the most difficult area of transition, rather it is more difficult to restate prior periods (d) the relief would only be available for a limited number of entities, which would likely often be foreign-controlled and hence subject to public interest. It was not clear to the Board the number of entities that would be able to utilise this relief in any case; and (e) such an amendment would reduce comparability with other entities that are transitioning from SPFS to GPFS.
Relief from recognising 'deferred goodwill' if applying paragraph C4(j) of AASB 1.	Provide a parent entity applying the relief in AASB 1 Appendix C in relation to previously unconsolidated subsidiaries with an option to write off 'deemed goodwill' immediately in retained earnings, rather than recognise it and subject it to day 1 and annual impairment testing.	The Board noted that advantages of this relief would include: (a) potential to reduce the cost of undertaking an impairment test at the date of transition and ongoing annually; and (b) it would provide relief for entities consolidating for the first time, a key concern of respondents to ITC 39. However, the Board decided not to propose this relief due to: (a) the reasons noted in paragraph BC93; (b) this relief would have been inconsistent with the Standard-Setting Framework's presumption that IFRS Standards are an appropriate base. In particular, the Board noted that this amendment would fundamentally change the R&M requirements of AASB 1; and (c) this relief could cause significant loss of information about impairment for users and regulators.

Option	Nature of the relief considered	Key factors considered
Relief from restating comparative information as per AAS	To amend AASB 1 to specify that entities need not restate or present comparative information as per AAS. This would mean the date of transition is the beginning of the reporting period (rather than the beginning of the comparative period).	The Board decided to propose this relief (see the amendments proposed to AASB 1 in this ED), noting the advantages include: (a) the relief would facilitate transition to GPFS in a more timely manner – for periods beginning on or after 1 July 2020 (on the assumption the requirement is issued before 30 June 2020). This would also mean that, effectively, the revised Conceptual Framework and the removal of the ability to prepare SPFS would become effective for the first time in the same reporting period; (b) the relief was not expected to have implications for the R&M requirements of AAS, except to the extent that the change in the date of transition would lead to differences in opening balances based on a different date of transition; and (c) would reduce costs to all entities required to transition from SPFS to GPFS. However, the Board did note some disadvantages included: (a) reduced information for users – particularly in making trend analyses; and (b) the approach would require divergence from the presumption that IFRS Standards are appropriate as a base, albeit it would not a major deviation.

BC95 For the reasons noted in the table above, the Board decided against providing additional transitional relief in the form of 'push-down accounting' or immediate write-off of deemed goodwill against retained earnings. Instead, the Board decided it would utilise the ED process to gather any additional feedback on the need for, and nature of, any additional transitional relief that may be necessary, other than that relating to the presentation of comparative information.

Relief from restating and presenting comparative information

BC96 As noted in the table above, the Board concluded that relief from the restatement and presentation of comparative information in accordance with current AAS would be particularly beneficial as it could reduce preparation costs whilst providing a consistent, enforceable and transparent reporting framework (despite a lack of internal comparability in the first year of GPFS), and thus decided that entities should not be required to provide restated comparative information as per current AAS in the year the Standard becomes first effective (see paragraphs BC101-BC104 for further considerations by the Board on the effective date).

BC97 However, the Board noted the particular importance for users:

(a) to understand the effect of an entity's transition from SPFS to Tier 2 GPFS on its assets, liabilities and equity; and

(b) to have comparative information in the statement of profit or loss and other comprehensive income to facilitate trend analysis.

BC98 To balance the needs of users and the costs to preparers, the Board decided that a pragmatic approach would be to require an entity to:

(a) present two statements of financial position ie as at the reporting date and at the beginning of the reporting period, with a comparative statement of financial position as presented in the entity's last SPFS disclosed in the notes, with a description of the main adjustments that were required to make the opening statement of financial position compliant with AAS. To reduce costs, the Board decided an entity need not quantify those adjustments; and

(b) present its statement of profit or loss and other comprehensive income as presented in its last SPFS as comparative information, but clearly labelled, where applicable, that such comparative information is not AAS compliant, with disclosure in the notes describing the main adjustments that would have been required to make the comparative information compliant with AAS. Also to reduce costs, the Board decided an entity need not quantify those adjustments.

BC99 The Board also observed that some entities may wish to present their last SPFS financial statements alongside their first Tier 2 GPFS, whilst also utilising the option to not restate comparative information. Accordingly, the Board decided that, if the entity had only differed from the R&M requirements of AAS in limited circumstances, the entity should be permitted to present its previous SPFS as a comparative period, as long as the entity makes this clear to users by labelling any information included that is not prepared in accordance with AAS, and disclosing the nature and amounts of the main adjustments that would make the information comply with AAS. The Board decided to limit this option to entities that have only differed from the R&M requirements of AAS in limited circumstances to limit any confusion to users in regard to the reliability of the information presented, and to limit the choice of such an option only to entities that had limited divergences from the R&M requirements of AAS.

Commented [BJ7]: Note to Board Members: This paragraph may be subject to update as a result of the Board's responses to Questions 4 and 5 on page 12.

BC100 Because the purpose of any relief would be to facilitate transition from SPFS to Tier 2 GPFS, rather than a general first time adoption of GPFS, the Board decided the additional transitional relief from restatement of comparative information should not be available beyond the first year in which the Standard becomes effective ie assuming the proposed effective date is adopted, the proposed comparative information transitional relief would only be available for annual periods beginning on or after 1 July 2020 but before 1 July 2021. The Board also decided for pragmatic reasons that the transitional relief from restating comparatives will be available regardless of whether an entity had a legislative or other requirement to comply with AAS in prior periods.

Effective date

BC101 In considering an appropriate effective date, the Board considered available policies and precedent, including:

(a) the amendments to the tax law requiring SGEs to lodge GPFS with the ATO were issued in December 2015, and required lodgement to the ATO for 'income years' commencing on or after 1 July 2016. However, the ATO provided transitional concessions in the first year, whereby it allowed entities with reporting periods ending on 30 June 2017 to not lodge until 31 March 2018, and permitted foreign controlled entities to lodge financial statements in accordance with another set of Generally Accepted Accounting Principles (GAAP) rather than AAS (eg US GAAP);

(b) the AASB issued the first principal version of AASB 1 in July 2004, prior to the effective date of full adoption of the Australian-equivalents to IFRS Standards of annual periods beginning on or after 1 January 2005. The FRC provided the AASB with the directive to adopt IFRS Standards in 2002. Given that all entities would have applied AASB 1 on Australia's transition to IFRS Standards, this length of time is arguably indicative of how much time might need to be provided for a transition from SPFS to GPFS; and

(c) the AASB *Policies and Processes* outlines in paragraph 32 that "when determining the effective date of Standards the AASB seeks to ensure that constituents have adequate time to prepare for their implementation. In normal circumstances the AASB will issue a Standard a significant time before its effective date, say, during the previous annual reporting period and generally permits entities to apply those requirements early should they wish to do so".

BC102 The Board also noted that a timely effective date would be welcomed by users of financial statements, and may also be preferred by preparers. This is because:

(a) the regulations in relation to the doubling of thresholds for large proprietary companies are applicable to financial years beginning on or after 1 July 2019. The Board noted that the commentary contained in the Explanatory Statement to those regulations may be persuasive in an entity reconsidering its status as a non-reporting entity. As such, if entities were to reassess as reporting entities, it would be preferable for the RCF to be applicable at the same time as other publicly accountable for-profit entities (annual periods beginning on or after 1 January 2020); and

(b) a large proportion of affected entities (76%) are already complying with the R&M requirements of AAS.

BC103 As noted in the table following paragraph BC94, the Board also concluded that providing relief from restating comparative information in the year of transition would be particularly beneficial as it could allow for an earlier effective date. As such, with regard to the above considerations, the Board decided to propose an effective date of annual periods beginning on or after 1 July 2020. The Board noted this would effectively align with the effective date of the RCF, given most Australian for-profit private sector entities would have reporting dates of 30 June.

BC104 Further, the Board noted the timeliness of completing this project, in order to provide an option for large proprietary companies to early adopt the RCF, applicable transitional relief and Tier 2 GPFS framework for periods beginning on or after 1 July 2019 (ie aligned with the doubling of the large proprietary thresholds). As such, the Board intends to issue a final amending Standard by 30 June 2020.

Application of *The AASB's For-profit Entity Standard-Setting Framework*

BC105 In developing the proposals contained in this ED, the Board considered the principles in *The AASB's For-profit Entity Standard-Setting Framework*, which outlines the matters the Board must consider when determining whether or not to make amendments to IFRS Standards or develop Australian specific guidance.

BC106 *The AASB's For-profit Entity Standard-Setting Framework* states that, when developing accounting standards for non-publicly accountable for-profit entities, the AASB's objective is to use IFRS Standards and transaction neutrality as a starting point, with modifications where justified to address:

(a) Australian-specific legislation, user needs, or public interest issues relevant to financial reporting or beyond financial reporting;

(a) issues specific to the (for-profit) public sector of such prevalence and magnitude that users are likely to make inappropriate decisions based on the financial statements;

(b) where the objectives and qualitative characteristics of financial reporting as set out in the AASB *Framework for the Preparation and Presentation of Financial Statements* (Conceptual Framework) would not be met; and/or

(c) undue cost or effort considerations.

BC107 Consistent with this, the Board decided standard-setting activities as reflected in this ED were necessary after undertaking the following (as already noted throughout this ED):

(a) extensive public consultation and outreach including ITC 39, research into the needs of financial statement users (e.g. public surveys and targeted outreach), feedback obtained from stakeholders (including users) who participated in roundtable events along with other general and targeted outreach with stakeholders;

(b) engaging with Treasury and assessing the impact of regulatory changes to large proprietary companies, including understanding the number of entities expected to be affected by the increase in the large proprietary company thresholds from this ED;

(c) the preparation and review of various research reports, including AASB Research Report No.1, AASB Research Report No.4 *Review of Adoption of International Financial Reporting Standards in Australia* (March 2017), AASB Research Report No.7 and AASB Research Report XX *Financial Reporting Practices of For-Profit Entities Lodging SPFSs – 2019* to understand the current application of the reporting entity concept, as well as to understand the degree of non-compliance with R&M requirements in AAS. The objective of these research activities was to better understand the cost implications of disallowing the entities required to comply with AAS to prepare SPFS and require them to prepare GPFS instead;

(d) considering whether it was necessary to provide transitional relief in addition to that currently available under AASB 1 and AASB 108 with the objective of minimising any undue costs in relation to both the transition from SPFS to GPFS and the associated disclosure requirements; and

(e) undertaking a preliminary Regulation Impact Statement-like (RIS) process[19].

Amendments required to implement Phase 2

BC108 As noted in paragraph BC43BC43 above, in May 2019, the Board made AASB 2019-1 to implement Phase 1 of the the Board's phased approach to implementing the RCF, limiting the mandatory application of the RCF to for-profit private sector entities with public accountability that are required by legislation to prepare financial statements that comply with AAS.

BC109 In this ED, to facilitate the implementation of Phase 2, the following amendments are proposed:

(a) the applicability of the *Conceptual Framework for Financial Reporting* (RCF) is proposed to be extended so that it applies to:

19 A RIS (or RIS-like process) will be completed to accompany the final amending Standard.

(i) for profit-private sector entities that are required by legislation to comply with either Australian Accounting Standards or accounting standards (with the previous limitation to entities with public accountability removed);

(ii) other for-profit private sector entities that are required only by their constituting document or another document to comply with Australian Accounting Standards (and so excluding requirements to comply merely with 'accounting standards'), provided that the relevant document was created or amended on or after 1 July 2020; and

(iii) other for-profit entities (including for-profit public sector entities) that elect to apply the Conceptual Framework and the consequential amendments to other pronouncements;

(b) the *Framework for the Preparation and Presentation of Financial Statements* and Statement of Accounting Concepts SAC 1 *Definition of the Reporting Entity* are also proposed to be amended so that they will continue not to apply to all for-profit entities that are applying the Conceptual Framework. Consequential amendments are made to the applicability of the reporting entity definition in AASB 1057 Application of Australian Accounting Standards, which is not relevant to entities applying the Conceptual Framework.

BC110 Therefore, with these amendments, an entity that is required to apply the *Conceptual Framework* cannot identify as a non-reporting entity under SAC 1 or AASB 1057. As a consequence, the ability for such an entity to prepare special purpose financial statements is removed and it will be required to prepare general purpose financial statements that comply with Australian Accounting Standards (or accounting standards under legislative requirements).

BC111 The application paragraph of AASB 1057 is proposed to be extended to state that it will apply to for-profit private sector entities that are required by legislation to comply with Australian Accounting Standards or accounting standards, and other for-profit private sector entities that are required only by their constituting document or another document to comply with Australian Accounting Standards (provided that the relevant document was created or amended on or after 1 July 2020). The application paragraphs of the other Standards and Interpretations, as set out in AASB 1057, are extended similarly.

BC112 The AusCF paragraphs in AAS that were introduced in AASB 2019-1 do not need to be amended in this ED. The definition of AusCF entities as not-for-profit entities and for-profit entities that are not applying the Conceptual Framework as introduced in AASB 2019-1 will continue to apply unchanged. The phase 2 amendments reduce the set of for-profit entities that are not applying the Conceptual Framework.