AASB Invitation to Comment

ITC 39
May 2018

CONSULTATION PAPER

Applying the IASB's Revised Conceptual Framework and Solving the Reporting Entity and Special Purpose Financial Statement Problems

Comments to the AASB by:

- 9 August 2018 for Phase 1: Short-term approach; and
- 9 November 2018 for Phase 2: Medium-term approach (refer to inside cover)

Australian Government
Australian Accounting Standards Board

How to Comment on this AASB Invitation to Comment

Comments on Phase 1: short-term approach and Appendix A of this Consultation Paper are requested by 9 August 2018.

Comments on Phase 2: medium-term approach of this Consultation Paper are requested by 9 November 2018.

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.

Contents

CONSULTATION PAPER

APPLYING THE IASB'S REVISED CONCEPTUAL FRAMEWORK AND SOLVING THE REPORTING ENTITY AND SPECIAL PURPOSE FINANCIAL STATEMENT PROBLEMS

Executive summary

1 The International Accounting Standards Board (IASB) issued a revised Conceptual Framework titled *Conceptual Framework for Financial Reporting* (referred to throughout this Consultation Paper as 'RCF') in March 2018.

2 The Conceptual Framework describes the objective and concepts for general purpose financial reporting under International Financial Reporting Standards (IFRS). Its purpose is to assist standard-setters 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.

3 Making the IASB's RCF applicable in Australia is essential as in accordance with the AASB's strategy[1] and Financial Reporting Council directive:

(a) publicly accountable for-profit entities and other entities voluntarily reporting compliance with IFRS must be able to maintain compliance with International Financial Reporting Standards (IFRS); and

(b) IFRS is used 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 Not-for-Profit Entities*[2].

4 In order to apply the RCF in Australia, the AASB has to address a 'reporting entity' definition clash as outlined below. This first problem is unique to Australia and highlights the importance of solving the second more significant financial reporting problem. There is currently a lack of comparability, trust and transparency, resulting from entities self-assessing that they can prepare special purpose financial statements (SPFS)).

Two problems tackled within this Consultation Paper

The first problem – resolving the 'reporting entity' definition clash

5 The reporting entity concept (referred to throughout this document as 'the Australian reporting entity concept') in Statement of Accounting Concepts SAC 1 *Definition of the Reporting Entity* and some of the Australian Accounting Standards (AAS) is defined and used differently compared to the RCF[3]. Therefore, applying the RCF without modification in Australia would remove the Australian reporting entity definition so that the IASB's definition of RCF could be applied throughout AAS. Removing SAC 1 and the Australian reporting entity concept would remove the ability for entities to prepare SPFS. Refer to Section 1 paragraphs 33-43 and Appendix C paragraphs 1-17 for more information on the first problem.

The second problem – SPFS

6 Australia is the only country to have a concept that effectively permits entities to self-assess what type of financial reporting is required when legislation or otherwise (ie such as a constitutional document) requires the preparation of financial statements in accordance with accounting standards. Unlike other countries, in Australia, two similar entities can prepare very different sets of financial reports, one preparing general purpose financial statements (GPFS) using a robust and consistent framework and the other SPFS, with self-selected requirements. This reduces comparability for entities of similar economic circumstances and undermines the fundamentals of trust and transparency.

7 Previous research by the AASB[4] indicates that many entities (approximately 55-60%) 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.

8 This second problem must be resolved by the AASB as legislatively the AASB must ensure that there are appropriate accounting standards for each type of entity that must comply with accounting standards (ASIC Act S229(2)(c)) and facilitate comparability (S224). The ability to self-assess sits within the AAS. Currently AAS specify only minimum disclosures for statutory SPFS. Other regulators have provided

1 Refer to *AASB and AUASB Strategy 2017-2019*. The strategy was subject to public consultation in July-August 2017.
2 Refer to *The AASB's For-Profit Entity Standard-Setting Framework* and *The AASB's Not-For-Profit Entity Standard-Setting Framework*.
3 Refer to paragraphs 34-35 and Appendix C paragraphs 4-12 for more details.
4 Refer to AASB Research Report No. 1 *Application of the Reporting Entity Concept and Lodgement of Special Purpose Financial Statements* (referred to throughout this Consultation Paper as 'Research Report No. 1') and Appendix C paragraphs 37-61.

guidance indicating that there is a need for minimum recognition and measurement requirements for SPFS also. Preliminary discussions with users, including lenders and insolvency practitioners, indicate that their needs for information about liquidity, solvency, cash flows, commitments and contingencies are currently not being provided for in most SPFS and in some instances GPFS.

9 To retain SPFS in its current form would require modification to IFRS and for the above reasons the AASB does not believe such modifications would satisfy its legislative requirements, nor *The AASB's Standard-Setting Frameworks for For-Profit and Not-for-Profit Entities*[5]. 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 who are required to prepare financial statements in accordance with AAS. Refer to Section 1 paragraphs 44-54 for more information on the second problem.

Options considered to solve the above problems

10 The AASB considered five options to solve the above problems:

(a) Option 1: Two-phased approach to applying the IASB's RCF – in the short term maintain IFRS compliance for publicly accountable entities[6] and entities voluntarily claiming IFRS compliance (phase 1); and in the medium term maintain IFRS as a base by removing the Australian reporting entity concept, removing SPFS from AAS and providing an alternative Tier 2 GPFS framework (phase 2).

(b) Option 2: Operate with two Conceptual Frameworks – apply IASB's RCF to some entities to maintain IFRS compliance and retain the existing *Framework*[7] for others (ie retain the Australian reporting entity concept and SPFS for others).

(c) Option 3: All entities to apply the IASB's RCF when it first becomes applicable to maintain IFRS compliance and IFRS as a base – remove the Australian reporting entity concept and SPFS by 1 January 2020.

(d) Option 4: Do nothing and lose IFRS compliance – retain the existing *Framework* (ie retain the Australian reporting entity concept and SPFS).

(e) Option 5: All entities to apply the IASB's RCF when it first becomes applicable to maintain IFRS compliance and IFRS as a base, change the name of the Australian reporting entity concept and prescribe minimum requirements for SPFS (ie retain the self-assessment mechanism and SPFS but set minimum requirements for SPFS) by 1 January 2020.

11 The AASB considered the benefits and barriers of each of the above options, as detailed in Section 2 of this Consultation Paper. The Board concluded that the optimal approach would be to follow Option 1.

The AASB's preferred option – Option 1: Two-phased approach to applying the IASB's RCF

Why was Option 1 preferred by the AASB?

12 The AASB considers Option 1 to yield the greatest net benefit to the Australian economy. This option:

(a) **allows maintaining IFRS compliance on a continuous basis** for publicly accountable for-profit entities (eg listed and disclosing entities) and other entities that voluntarily report compliance with IFRS;

(b) **maintains the status quo for all other entities in the short term,** allowing time for the AASB to consult and determine an alternative Tier 2 GPFS framework to replace SPFS in AAS after which there will no longer be an option for entities to prepare SPFS when required by legislation or otherwise to prepare financial statements in accordance with AAS;

(c) **maintains IFRS as a base for all entities, allowing alignment between the RCF and AAS for all entities in the medium term**, which reduces confusion and the risk of inappropriate accounting policy and interpretation decisions likely to arise from operating with two conceptual frameworks and one suite of AAS;

(d) **solves the reporting entity problem in the medium term** as all entities will apply the RCF and the term 'reporting entity' as defined in the RCF would be consistently applied within AAS;

5 Refer to *The AASB's For-Profit Entity Standard-Setting Framework* and *The AASB's Not-For-Profit Entity Standard-Setting Framework*.
6 Public Accountability is defined in AASB 1053, refer to paragraphs 159-160 for more details.
7 The AASB's existing *Framework for the Preparation and Presentation of Financial Statements* is referred to throughout this Consultation Paper as the 'existing *Framework*'.

(e) **solves the SPFS problem in the medium term** facilitating consistent, comparable, transparent and useful financial statements;

(f) **allows time for the AASB to consult and determine the not-for-profit (NFP) modifications that may be necessary for the RCF** in accordance with the NFP Standard-Setting Framework; and

(g) **meets the AASB's legislative obligations to facilitate comparability** and ensure there are appropriate accounting standards for each entity required to comply with AAS (ASIC Act sections 224 and 229).

Summary of Option 1: Two-phased approach to applying the IASB's RCF

13 Phase 1: Short-term approach – operate with two conceptual frameworks to maintain IFRS compliance for publicly accountable entities. This involves:

(a) the RCF being applied to publicly accountable for-profit entities and other entities voluntarily reporting compliance with IFRS to enable them to maintain IFRS compliance;

(b) all other entities continuing to apply the existing *Framework*, enabling them to continue using the 'Australian reporting entity concept'; and

(c) amendments being made to the definition of 'public accountability in AASB 1053 *Application of Tiers of Australian Accounting Standards* to align with the revised IASB definition in IFRS for Small and Medium-sized Entities (SMEs)[8].

14 Phase 2: Medium-term approach – maintain IFRS compliance for publicly accountable entities and entities voluntarily claiming IFRS compliance, maintain IFRS as a base for all other entities, by having one conceptual framework, remove SPFS and provide a new GPFS Tier 2 alternative. This involves:

(a) the RCF being applied to all entities required by legislation or otherwise to comply with AAS;

(b) the Tier 2 framework in AASB 1053 being revised to be **one** of the following:

(i) Alternative 1: GPFS – Reduced Disclosure Requirements (RDR) – Existing Tier 2 (full recognition and measurement with **reduced disclosures** from each Accounting Standard, includes consolidation and equity accounting where applicable); **<u>OR</u>**

(ii) Alternative 2: GPFS – Specified Disclosure Requirements (SDR) – New Tier 2 (full recognition and measurement with **specified disclosures** from some Accounting Standards[9], includes consolidation and equity accounting where applicable); and

(c) Consequential amendments being made to AAS[10] and transitional relief provided for entities moving from SPFS to GPFS or to another tier of reporting.

The impact of adopting Option 1

15 The most significant impact to these proposals will be on entities that are currently preparing SPFS without doing full recognition and measurement or consolidation or equity accounting. For those entities, the requirement to prepare GPFS under one of the Tier 2 alternatives would be a considerable step-up. The AASB is committed to extensive consultation and engagement with stakeholders and regulators to understand what transitional relief may be required to alleviate the additional reporting burden for those entities and other entities required to step-up their reporting requirements.

16 Diagram 1 depicts the current spectrum of financial statements and impact (ie step-up) of adopting Option 1 on entities required by legislation or otherwise to prepare financial statements in accordance with AAS. The impacts and extent of the impacts are discussed further in paragraphs 72-80.

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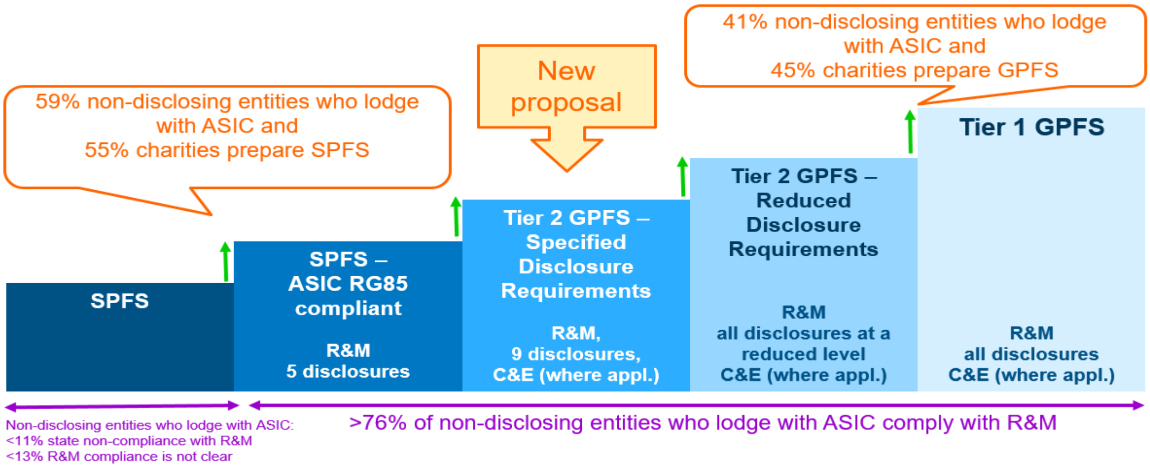
8 The AASB is also proposing additional guidance as per *IFRS for SMEs* to clarify the term 'fiduciary capacity', as specified in *IFRS for SMEs*.

9 Proposed specified disclosures are: 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*, AASB 1054 *Australian Additional Disclosures* plus related party, revenue, impairment of assets and income tax disclosures (the AASB is consulting on these specified disclosures as part of the consultation process to ascertain whether they best meet users' needs.).

10 Amendments resulting from Phase 2 will be considered in the next stage of the consultation process (ie once the alternative for revising Tier 2 has been determined). Refer to APPENDIX B of this Consultation Paper for illustrative amendments.

Diagram 1 Current spectrum of financial statements[11]



Notes

5 Disclosures:	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*, AASB 1054 *Australian Additional Disclosures*
9 Disclosures:	Includes the 5 disclosures listed above plus related party, revenue, impairment of assets and income tax disclosures
R&M:	Recognition and measurement with AASB Standards
C&E:	Consolidation and equity accounting (where required by AASB Standards)

Statistics sourced from AASB Research Report No.1 *Application of the Reporting Entity Concept and Lodgement of Special Purpose Financial Statements.*

17 The above diagram is based on Research Report No. 1, which includes data from 2010-11. At that time there were a total of 21,711 non-disclosing entities lodging financial reports with ASIC, which represents just over 1% of the 1.84 million companies registered with ASIC[12].

Overall benefits of Option 1

18 The Option 1 approach:

(a) **allows time for further research and constituent feedback** – the phased approach allows time to conduct further research and outreach to better understand constituents' needs and to provide mitigating actions to alleviate the additional burden for some entities (such as transitional relief, education and support).

(b) **facilitates for users consistent, comparable, transparent and useful financial statements** for entities required to prepare financial statements in accordance with AAS, as:

(i) all publicly accountable entities and those who voluntarily choose to report compliance with IFRS maintain IFRS compliance; and

(ii) all other entities would ultimately prepare Tier 2 GPFS using Alternative 1 or Alternative 2, with full recognition and measurement, consolidation and equity accounting (where required), and minimum disclosure requirements.

(c) **has the greatest net benefit to users, directors, preparers, regulators, and auditors** as it removes the inconsistencies and risks associated with self-assessment, ensures a 'level playing field' between entities and increases stakeholder confidence in reporting. Removing the subjectivity of self-assessment will also improve regulation of reporting and assists Trans-Tasman harmonisation by aligning Australian requirements with New Zealand for a larger population of for-profit entities.

What actions are being taken to mitigate the increased reporting burden for some entities as a result of the Option 1 outcomes?

19 To alleviate the increased reporting burden for some entities as a result of the Option 1 outcomes, the AASB is proposing:

(a) **the new Tier 2 SDR framework**, which if chosen will replace the current GPFS Tier 2 RDR framework and although it is similar to GPFS RDR, it requires disclosures from only nine

11 The spectrum of financial statements would apply to entities required by legislation or otherwise to comply with AAS. However the statistics quoted within this diagram relate to findings from Research Report No. 1 and the the findings from the Australian Charities and Not-for-profits Commission's (ACNC's) latest monitoring of Annual Information Statements and Annual Financial Reports, *Reporting trends in the 2016 Annual Information Statement* on entities that have publicly lodged with ASIC or the ACNC. It does not cover all entities that have prepared financial statements but have not publicly lodged.

12 Refer to ASIC's 2010-11 Annual Report

Standards (to be made in full), as opposed to RDR which requires disclosures from most Standards, albeit at a reduced level.

(b) **transitional relief** for entities required to apply consolidation and equity accounting (in addition to relief within specific AAS) and for those moving to a different tier of reporting;

(c) **staggered phase 2 implementation timing**, whereby the AASB will consider constituents views on whether the implementation of phase 2 could happen in stages (for example for-profit entities could be implemented first and then Not-for-profits (NFPs); and

(d) **education, support and tools** (such as templates and guidance) to help preparers manage the new requirements.

Other important considerations

Why was *IFRS for SMEs* not chosen as another alternative Tier 2 framework

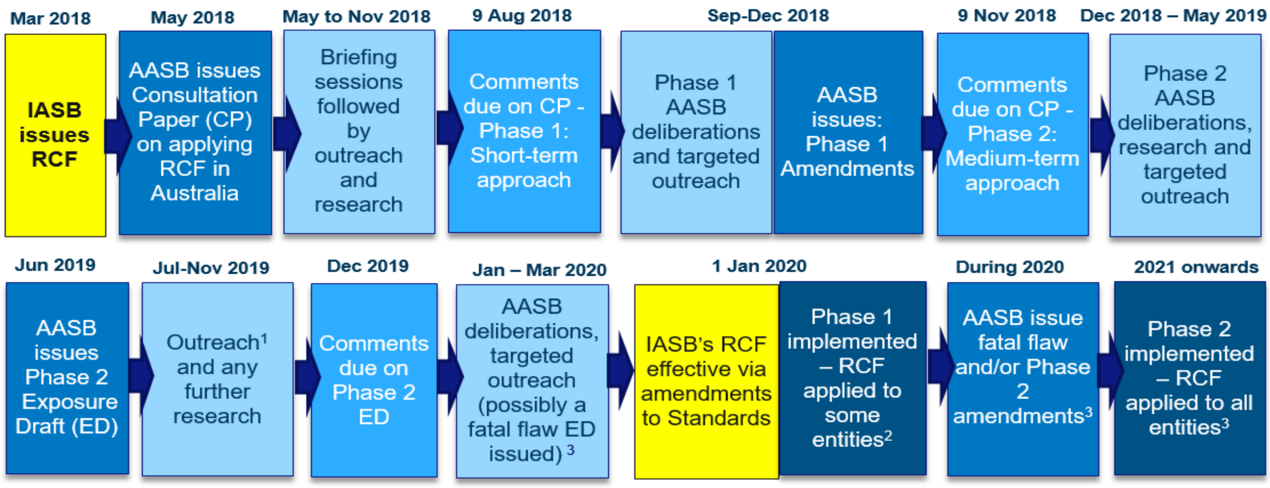
20 The AASB considered *IFRS for SMEs* as an alternative for Tier 2 and decided not to pursue that alternative at the present time for the reasons outlined in Appendix C paragraphs 18 to 36.

21 Most notably, *IFRS for SMEs* has different recognition and measurement requirements compared with IFRS. Previous research by the AASB[13] indicates more than 75% of non-disclosing entities that need to publicly lodge financial statements in accordance with AAS with ASIC are currently complying with recognition and measurement requirements of AAS. Therefore, moving to a framework which moves away from this seems counter-intuitive when trying to improve the consistency, comparability, usefulness and credibility of financial reporting in Australia.

Additional tiers of reporting

22 The AASB would be very supportive, if objective criteria and thresholds are determined from findings and recommendations of the ACNC's legislative review, developing another tier of reporting (eg modified accruals or cash accounting for small charities in the NFP sector). This alternative has not been included in the Consultation Paper as ACNC's legislative review has not been finalised.

Project timeline



Notes
1. Outreach conducted in 2019 will also include outreach on any proposals to amend the RCF or AAS for NFP specific issues.
2. Phase 1 implementation of the RCF applies to publicly accountable for-profit entities and entities voluntarily claiming IFRS compliance.
3. The timing of the Phase 2 deliberations and implementation dates may be staggered (e.g. for profit entities first followed by NFPs). Depending on feedback received, Phase 2 for the for-profit sector may be completed earlier than detailed.

Current requirements not impacted by proposals in this Consultation Paper

23 These proposals would not impact the 'public lodgement relief' granted to 'grandfathered proprietary companies' under s1408 of the *Corporations Act*. The proposals would also not impact reporting requirements of trusts and other entities (eg self-managed superannuation funds) that are not currently required by legislation or otherwise to prepare financial statements in accordance with AAS.

13 Refer to Research Report No. 1 and Appendix C paragraphs 46-66.

Matters for comment

Specific matters for comment on Phase 1 due 9 August 2018

24 As set out in paragraph 164, the AASB would particularly value comments on the proposals in Phase 1 and Appendix A:

Q1 – Do you agree with the short-term approach to maintain IFRS compliance by introducing the RCF in Australia? That is, do you agree that the RCF should be applicable for publicly accountable for-profit entities that are required to prepare Tier 1 GPFS and other entities that are voluntarily reporting compliance with IFRS, and the existing *Framework* should continue to be applicable to other entities in the short term until the medium term solution is implemented? Please indicate reasons for your response and if you disagree, please provide suggestions for an alternative approach for the AASB to consider.

Q2 – Do you agree that the short-term approach should be made applicable to both publicly accountable for-profit private sector and public sector entities? That is, do you agree that the RCF should be applicable for publicly accountable public sector entities that are required to prepare GPFS in accordance with Tier 1 reporting requirements (who are currently claiming compliance with IFRS) as well? Please indicate reasons for your response and if you disagree please provide suggestions for an alternative approach for the AASB to consider.

Q3 – Are you aware of publicly accountable for-profit entities currently self-assessing as non-reporting entities and preparing SPFS that would have implications under the AASB's short-term approach?
If so please provide specific examples including why these entities are not currently applying AASB 1053 and preparing Tier 1 GPFS although they would otherwise meet the definition of public accountability.

Q4 – Do you agree with the AASB's amendments to the definition of 'public accountability' in AASB 1053 per *IFRS for SMEs* Standard (refer to Appendix A)? Please indicate reasons for your response and if you disagree, please provide suggestions for the AASB to consider.

Q5 – Do you agree with the proposed amendments to SAC 1 *Definition of the Reporting Entity* and the following Australian Accounting Standards, as set out in Appendix A.

General matters for comment on Phase 1 due 9 August 2018

25 As set out in paragraph 165, the AASB would also value comments on the following general matters with respect to Phase 1:

(a) **Q6 –** Whether *The AASB's Standard-Setting Frameworks for For-Profit and Not-for-Profit Entities*[14] has been applied appropriately in developing the proposals in Phase 1.

(b) **Q7 –** Whether there are any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals.

(c) **Q8 –** Whether, overall, the proposals would result in financial statements that would be useful to users.

(d) **Q9 –** Whether the proposals are in the best interests of the Australian economy.

(e) **Q10 –** Unless already provided in response to specific 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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14 Refer to *The AASB's For-Profit Entity Standard-Setting Framework* and *The AASB's Not-For-Profit Entity Standard-Setting Framework*.

Specific matters for comment on Phase 2 due 9 November 2018

26 As set out in paragraph 195, the AASB would particularly value comments with respect to Phase 2:

Q11 – Do you agree with the AASB's Phase 2 approach (described in paragraph 166) Why or why not?

Q12 – Which of the AASB's two GPFS Tier 2 alternatives (described in paragraphs 167-170) do you prefer? Please provide reasons for your preference.

Q13 – Do you agree that we only need one Tier 2 GPFS alternative in Australia (either Alternative 1 GPFS – RDR or the new Alternative 2 GPFS – SDR described in paragraphs 167-170)? Why or why not?

Q14 – Do you agree with the AASB's decision that GPFS – *IFRS for SMEs* (outlined in Appendix C paragraphs 18 to 36) should not be made available in Australia as a Tier 2 alternative for entities to apply? Please give reasons to support your response, including applicability for the for-profit and not-for-profit sectors.

Q15 – If the AASB implements one of the two proposed alternatives (described in paragraphs 167-170) as a GPFS Tier 2, what transitional relief do you think the AASB should apply (in addition to what is available in AASB 1)? Please provide specific examples and information.

Q16 – What concerns do you have on consolidating subsidiaries and equity accounting associates and joint ventures as proposed in the AASB's medium-term approach? What transitional relief do you think the AASB should apply? Please provide specific examples and information.

Q17 – If the new Alternative 2 GPFS – SDR described in paragraphs 167-170) is applied, do you agree that the specified disclosures would best meet users' needs? If not, please explain why and provide examples of other disclosures that you consider useful.

Q18 – Do you have any other suggested alternative for the AASB to consider as a GPFS Tier 2 and whether this would be applicable for for-profit and not-for-profit sectors? Please explain rationale (including advantages and disadvantages and the costs and benefits expected).

Q19 – Do you think service performance reporting, fundraising and administration cost disclosures for NFP private sector entities should be included as part of the chosen GPFS Tier 2 alternative? Please explain rationale (including advantages and disadvantages).

Q20 – Are you aware of any legislation that refers to SPFS that might be impacted by these proposals? If yes, please provide specific information.

General matters for comment on Phase 2 due 9 November 2018

27 As set out in paragraph 196, the AASB would also value comments on the following general matters with respect to this Consultation Paper:

Q21 – Whether *The AASB's Standard-Setting Frameworks for For-Profit and Not-for-Profit Entities*[15]. have been applied appropriately in developing the proposals in Phase 2 regarding the reporting entity problem (note the AASB will consult further on other NFP amendments required for the RCF).

Q22 – Whether there are any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals.

Q23 – Whether, overall, the proposals would result in financial statements that would be useful to users.

Q24 – Whether the proposals are in the best interests of the Australian economy.

Q25 – Unless already provided in response to specific 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.

15 Refer to *The AASB's For-Profit Entity Standard-Setting Framework* and *The AASB's Not-For-Profit Entity Standard-Setting Framework*.

Section 1: What are the problems we are trying to solve and why is our action needed?

Background

28 The AASB's existing *Framework* incorporates the *Conceptual Framework for Financial Reporting* ('IASB's existing *Conceptual Framework*') as issued by the IASB in July 2004 and revised in 2013.

29 In March 2018, the IASB issued its RCF, which replaces the IASB's existing *Conceptual Framework*. The IASB's RCF is a comprehensive framework that discusses the topics that the IASB needs to think about when it sets IFRS Standards. It also assists preparers to develop consistent accounting policies when no Standard applies to a particular transaction or other event, or when a Standard allows a choice of accounting policy; and assists everyone understand and interpret the Standards. The IASB and the IFRS Interpretations Committee started using the RCF immediately after it was issued.

30 To achieve transition for preparers who develop accounting policies by reference to the IASB's RCF, the IASB also issued *Amendments to References to the Conceptual Framework in IFRS Standards* in March 2018. That document updates references to previous versions of the IASB's *Conceptual Framework* in IFRS Standards, their accompanying documents and IFRS practice statements. Those updated references are effective for annual periods beginning or after 1 January 2020.

What objective are we trying to achieve?

31 Making the IASB's RCF applicable in Australia is essential as in accordance with the AASB's strategy[16] and Financial Reporting Council directive:

(a) publicly accountable for-profit entities and other entities voluntarily reporting compliance with IFRS must be able to maintain compliance with International Financial Reporting Standards (IFRS); and

(b) IFRS is used 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 Not-for-Profit Entities*[17].

32 In order to apply the RCF in Australia, the AASB has to address a 'reporting entity' definition clash as outlined below. This first problem is unique to Australia and highlights the importance of solving the second more significant financial reporting problem. There is currently a lack of comparability, trust and transparency, resulting from entities self-assessing that they can prepare special purpose financial statements (SPFS).

The first problem – applying the RCF and addressing the 'reporting entity' definition clash

33 In Australia, the application paragraphs of AAS and SAC 1 establish the term 'reporting entity' to denote entities that are required to prepare GPFS because they have users who depend on the GPFS to make decisions.

34 The IASB's RCF, in paragraph 3.10, creates a new definition of reporting entity as '*…an entity that is required, or chooses, to prepare financial statements. A reporting entity can be a single entity or a portion of an entity or can comprise more than one entity. A reporting entity is not necessarily a legal entity*.' In other words, according to the IASB's RCF**, an entity that is required by legislation or otherwise to prepare financial statements is a reporting entity** and the financial statements of reporting entities could differ based on the 'boundary' of economic activities included in their financial statements (ie a reporting entity's financial statements could be consolidated financial statements, single entity financial statements or part of an entity's financial statements). This is fundamentally different to the definition of reporting entity in Australia, where a reporting entity (as per SAC 1) is an entity that is required to prepare GPFS and an entity that is not a reporting entity (i.e. non-reporting entity) can choose to prepare SPFS.

35 This inconsistency between the RCF and AAS and SAC 1 could result in misinterpretation, the wrong application of AAS, non-compliance with IFRS, and potential liability for preparers and directors and those charged with governance. The likelihood of inconsistencies will increase as and when the IFRS

16 Refer to _AASB and AUASB Strategy 2017-2019_. The strategy was subject to public consultation in July-August 2017.
17 Refer to _The AASB's For-Profit Entity Standard-Setting Framework_ and _The AASB's Not-For-Profit Entity Standard-Setting Framework_.

Standards are amended/revised and there are more references to the term reporting entity as defined in the RCF.

36 Further exacerbating this issue are findings from AASB Research Report No. 1 *Application of the Reporting Entity Concept and Lodgement of Special Purpose Financial Statements* (referred to throughout this Consultation Paper as 'Research Report No. 1') which indicate the Australian reporting entity concept:

(a) is not well understood;

(b) is not applied consistently in practice;

(c) is too subjective for regulators to enforce effectively and accordingly does not create a level playing field; and

(d) increases risk for directors and those charged with governance who are responsible for determining what form of financial statements to prepare.

37 In Australia, consistent with the AASB's strategy and FRC directive, entities across all sectors who prepare financial statements in accordance with AAS are applying a single suite of AAS (which is based on IFRS). In order to retain the existing definition of reporting entity (and ability to prepare SPFS) for those entities who do not need to maintain IFRS compliance (ie those who are not publicly accountable and do not want to voluntarily claim IFRS compliance) the RCF would need to be modified (see option 5 below), or there would need to be two conceptual frameworks, (ie the existing *Framework* which applies the Australian reporting entity concept and the RCF that applies the IASB's reporting entity concept).

38 Introducing an unmodified RCF, as the AASB would normally do for IASB pronouncements for-profit entities, would result in entities currently preparing SPFS to move to a form of GPFS by 1 January 2020, when the RCF takes effect internationally for preparers. The AASB typically modifies IASB pronouncements for Not-for-profit entities and rarely adds additional requirements for for-profit entities, in accordance with its For-Profit and Not-for-profit Standard Setting Frameworks. Accordingly, the AASB is seeking a way of implementing the RCF in regards to the reporting entity concept that is consistent with its strategy and FRC directive but balances the needs of users with the costs to preparers of increased reporting requirements for some entities currently required to prepare financial reports in accordance with AAS.

Why having two conceptual frameworks is a problem

39 Having two Conceptual Frameworks would be untenable in the medium term. This is because AAS will be based on the RCF, which includes revised definitions and recognition criteria for assets and liabilities, a new chapter on reporting entity and a new chapter on measurement rather than the existing *Framework*. Therefore, if entities continue to apply the existing *Framework* when developing accounting policies or interpreting the AAS, they are likely to develop inappropriate accounting policies or wrongly interpret the AAS. This could result in inaccurate and inconsistent financial reporting and reduced comparability and transparency for users of financial statements. Updating the existing Framework with the changes in concepts in the RCF other than the reporting entity concept is also not feasible given the pervasive use of 'reporting entity' throughout the RCF.

40 The term 'reporting entity' (as defined in the RCF) is currently used within a number of AAS (including AASB 3 *Business Combinations*, AASB 7 *Financial Instruments: Disclosures*, AASB 9 *Financial Instruments* and AASB 12 *Disclosures of Interests in Other Entities*). To date, the AASB is not aware of any significant issues caused by using the term 'reporting entity' in these Standards as the term could be read in the context of the Australian reporting entity concept without causing confusion (ie until now the IASB has not defined the term). However, because the RCF includes a chapter specifically on the reporting entity and defines the term differently to the Australian reporting entity concept, it will become increasingly difficult to read the term in two different ways, particularly as and when AAS are amended/revised and there are more references to the term as defined in the RCF.

Why modifying the RCF is a problem

41 Simply renaming the Australian 'reporting entity' concept as something else and retaining SAC 1 is also not feasible, desirable or consistent with the AASB's legislative requirements to ensure there are appropriate accounting standards for each type of entity that must comply with accounting standards (ASIC Act S229(2)(c)) and to facilitate comparability (S224). The IASB specifically rejected the AASB's submission suggesting the IASB should state who must, should or could prepare GPFS. As noted in the RCF's basis for conclusions paragraph BC3.13, the IASB stated it does not have the authority to determine who must, should, or could prepare such statements. Accordingly, anyone required to prepare financial statements in accordance with IFRS is preparing GPFS (reporting requirements specified by the IASB).

42 The AASB, like the IASB, does not consider that it has the authority to determine who must, should, or could prepare such statements. The AASB's role is to determine the appropriate accounting framework and standards that should apply. In other words, anyone that is required to prepare financial statements in accordance with AAS should be preparing GPFS (ie reporting requirements specified by the AASB). The concepts in SAC 1 will remain helpful for other regulators in determining who should publicly lodge financial statements, however should not remain available for use by individual preparers.

43 The AASB does not consider it can justify retaining the ability to prepare SPFS by modifying the RCF as this will not meet its legislative obligations (discussed further in the second problem below) or its Standard Setting Frameworks (see option 5).

The second problem – SPFS

44 Australia is the only country to permit entities to self-assess what type of financial reporting is required when a regulator requires the preparation and public lodgement of financial statements. This means similar entities can report differently, with some preparing GPFS (because they have self-assessed that they are reporting entities) and others preparing SPFS (because they have self-assessed that they are not reporting entities). This reduces comparability for entities of similar economic circumstances and undermines the fundamentals of trust and transparency.

45 The numerous issues with this were identified in Research Report No. 1 and Appendix C to the Charity Discussion Paper[18]. Some of the more specific criticisms relate to the:

(a) significant judgement that is required when entities self-assess whether they are a reporting entity or not;

(b) inconsistency in how the reporting entity concept is understood and applied, resulting in entities with similar economic circumstances preparing different types of financial statements (some GPFS and some SPFS), reducing comparability for entities of similar economic circumstances and undermines the principles of trust and transparency; and

(c) variability in recognition, measurement and disclosure of similar items within the financial statements of entities preparing SPFS.

46 The ability to self-assess sits within the AAS. Currently AAS specify only minimum disclosures for statutory SPFS. Other regulators have provided guidance (eg ASIC's RG 85[19]) indicating that there is a need for minimum recognition and measurement requirements for SPFS also. Preliminary discussions with users, including lenders and insolvency practitioners, indicates their need for information about liquidity, solvency, cash flows, commitments and contingencies that are currently not being provided in most SPFS. To retain SPFS in its current form would require modification to IFRS and for the above reasons the AASB does not believe such modifications would satisfy its legislative requirements, nor its For-profit and Not-for-Profit Standard Setting Frameworks. 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 who are required to prepare financial statements in accordance with AAS.

47 Removing the Australian reporting entity concept would ensure there is no confusion about what the term 'reporting entity' means when the RCF is issued in Australia. All entities required by legislation or otherwise to prepare financial statements in accordance with AAS would have to prepare GPFS and apply the requirements of all the AAS. Therefore, entities currently self-assessing as non-reporting entities and preparing SPFS would no longer be able to do so.

48 The AASB notes the removal of the Australian reporting entity concept may result in additional costs for entities that currently prepare SPFS particularly on transition. The AASB is committed to extensive consultation and engagement with stakeholders and regulators to understand what transitional relief may be required to alleviate the additional reporting burden for these entities.

Are there users for entities that publicly lodge SPFS?

49 Some constituents have indicated to the AASB that for most entities that currently publicly lodge SPFS they believe there are no users who rely on GPFS information to make decisions, with key stakeholders and governments obtaining information they require in other ways.

50 SAC 1 indicates reporting entities include those with existing and potential users and those with economic significance.

18 Refer to Appendices to Charity Discussion Paper.
19 ASIC's RG 85 is for entities currently lodging SPFS with ASIC. Refer to Appendix C paragraphs 70-75.

51 The findings within the Incat Australia Pty Ltd ('Incat') versus ASIC High Court[20] case implied that 'users' should be given the widest possible interpretation and not restricted to shareholders, potential shareholders, creditors, potential creditors and customers. It also implied that a proprietary company classified as "large" based on the size test under the *Corporations Act 2001* (Corporations Act) is inherently economically significant because to be so classified, it has to satisfy criteria relating to its economic significance. Refer to Appendix C, paragraphs 62-69 for more details.

52 The Incat case provides insight into what regulators generally expect from entities required to publicly lodge (ie GPFS), highlights inherent difficulties with self-assessment between reporting entities and non-reporting entities, and suggests that the phrase 'users' should be viewed more broadly than how some constituents currently do.

53 Anecdotal evidence[21] also suggests that data aggregators collect financial statements of all entities lodging with ASIC and their clients (including analysts and banks) use these financial statements to facilitate credit risk assessment and receivables management.

54 In relation to the NFP sector, as noted in the *AASB's Discussion Paper Improving Financial Reporting for Australian Charities*, a common theme of available academic research indicated that 'whilst donors do not actively seek financial information of charities, they are given a sense of comfort that donations are being used wisely through the availability of financial information. The vast majority of respondents believed it was important or very important for charities to disclose information about how the funds are used and generally believed that a high level of transparency and access to information represented a well-run charity.

The bigger problem – improving the Australian Financial Reporting Framework

55 Removing the ability for entities to self-assess to be non-reporting entities and elect to prepare SPFS would result in:

(a) improved transparency and comparability amongst similar types of entities for users;

(b) increased certainty of requirements and lower risk of non-compliance for directors and preparers; and

(c) simpler enforceability for regulators.

56 This is however, just one element in improving the Australian Financial Reporting Framework. The ideal outcome would be that only those entities with users or that have economic significance are required to publicly lodge financial statements and those entities would prepare GPFS in accordance with AAS. The AASB is working with the Auditing and Assurance Standards Board (AUASB) and other regulators through its *Australian Financial Reporting Framework* project to support this outcome.

57 As set out in the AASB's submission to the ACNC legislative review, there is also a need for the tiers of financial reporting to be extended in the NFP charity sector, enabling differential reporting requirements between small, medium and large charities. This solution may also be suitable for other sectors.

58 The framework should set transparent, clear and objective criteria and thresholds for public lodgement in each of the sectors, with specified financial reporting and assurance requirements for each tier that are proportionate and fair and that meet the needs of users.

59 We encourage all stakeholders to contribute to this project to ensure that we establish a robust and straightforward reporting framework that is based on a broad consensus.

Why is our action needed?

60 Action is required by the AASB to:

(a) ensure entities required or voluntarily stating IFRS compliance can continue to do so;

(b) avoid any confusion with the use of the term 'reporting entity'; and

(c) alleviate the problems with SPFS

as discussed in paragraphs 5-54 above.

20 Refer *Incat Australia Pty Ltd v Australian Securities and Investment Commission - [2000] FCA 58*.

21 The AASB have conducted telephone interviews with a few data aggregators and analysts to better understand what users need with respect to financial reporting.

61 By addressing the above, the AASB would meet with the objectives of government action in s224 of the *Australian Securities and Investment Commission Act 2001* (ASIC Act) to 'facilitate the development of accounting standards that require the provision of financial information that

(i) allows users to make and evaluate decisions about allocating scarce resources; and

(ii) assists directors to discharge their obligations in relation to financial reporting; and

(iii) is relevant to assessing performance, financial position, financing and investment;

(iv) is relevant and reliable; and

(v) facilitates comparability;…'.

62 The AASB would also meet the objectives of government action in s229 to ensure that there are appropriate accounting standards for each type of entity that must comply with accounting standards.

63 The action taken by the AASB would also ensure that the core objectives for accounting standards in Australia, as set out by the ASIC Act are met, in that they support the Australian economy by:

(a) reducing the cost of capital and enabling Australian entities to compete effectively overseas, and maintain investor confidence in the Australian economy, including its capital markets;

(b) being clearly stated and easy to understand.

64 The AASB also has responsibilities under the Financial Reporting Council's (FRC's) broad strategic direction to work towards the adoption of accounting standards that are the same as those issued by the IASB.

Why not fix the reporting entity and SPFS problems through legislation?

65 The AASB does not determine which entities need to publicly lodge financial statements. This is determined by legislation. However, currently an entity required by legislation to prepare financial statements in accordance with AAS has the ability to self-assess whether it is a reporting entity or not in accordance with SAC 1. A reporting entity would need to prepare GPFS whereas a non-reporting entity could elect to prepare SPFS.

66 Some constituents may suggest that the removal of self-assessment and the ability to publicly lodge SPFS should ideally be driven through legislative change. However, the number of regulators required to make the necessary legislative changes means this would take significant time and effort to achieve, as indicated by past experience. Therefore, the AASB is proposing options to solve this problem without legislative amendments, which is important given the issue is currently part of the AAS framework (in SAC 1 and some of the AAS).

67 The AASB recognises that this is only improving one element within the Australian Financial Reporting Framework. The AASB will continue to work with the AUASB, other regulators and other key stakeholders as part of its Australian Financial Reporting Framework project to help regulators determine which entities need to publicly lodge financial statements and to undertake consultation as part of the *Australian Financial Reporting Framework* project to better understand users' needs.

Section 2: Options considered

Five options considered

68 The AASB considered five options to solve the problems detailed in Section 1:

(a) Option 1: Two-phased approach to applying the IASB's RCF – maintain IFRS compliance (phase 1), remove the Australian reporting entity concept, remove SPFS and provide an alternative Tier 2 GPFS framework (phase 2).

(b) Option 2: Operate with two Conceptual Frameworks – apply IASB's RCF to some entities to maintain IFRS compliance and retain the existing *Framework* for others (ie retain the Australian reporting entity concept and SPFS for others).

(c) Option 3: All entities to apply the IASB's RCF when it first becomes applicable to maintain IFRS compliance – remove the Australian reporting entity concept and SPFS by 1 January 2020.

(d) Option 4: Do nothing and lose IFRS compliance – retain the existing *Framework* (ie retain the Australian reporting entity concept and SPFS).

(e) Option 5: All entities to apply the IASB's RCF when it first becomes applicable to maintain IFRS compliance, change the name of the Australian reporting entity concept and prescribe minimum requirements for SPFS (ie retain the self-assessment mechanism and SPFS but set minimum requirements for SPFS) by 1 January 2020.

69 In order to determine which option to pursue the AASB considered the benefits and barriers to proposals within each option.

Option 1: Two-phased approach to applying the IASB's RCF

Overview of Option 1

70 **Phase 1: Short-term approach - operate with two conceptual frameworks to maintain IFRS compliance:**

(a) the IASB's RCF will apply to publicly accountable for-profit entities and other entities voluntarily reporting compliance with IFRS to enable them to maintain IFRS compliance. These entities will no longer be able to apply SAC 1 and amendments would be made to AASB 1053 *Application of Tiers of Australian Accounting Standards* and other AAS[22] to make the Australian reporting entity concept not applicable to these entities;

(b) all other entities will continue to apply the AASB's existing *Framework*, enabling them to continue using the Australian reporting entity concept; and

(c) there would be amendments to the definition of 'public accountability in AASB 1053 to align with the revised IASB definition in *IFRS for SMEs*. The AASB is also proposing additional guidance as per *IFRS for SMEs* to clarify the term 'fiduciary capacity', as specified in *IFRS for SMEs*.

71 **Phase 2: Medium-term approach – maintain IFRS compliance, one conceptual framework, removal of SPFS and a new GPFS Tier 2 alternative**

(a) the RCF will apply to all entities required by legislation or otherwise to comply with AAS;

(b) the Tier 2 framework in AASB 1053 will be revised to include one of the following alternatives (these alternatives are described in more detail in Section 5 paragraphs 154-172):

(i) Alternative 1: GPFS –RDR – Existing Tier 2 (full recognition and measurement with reduced disclosures from each Accounting Standard, includes consolidation and equity accounting where applicable); **<u>or</u>**

(ii) Alternative 2: GPFS –SDR – New Tier 2 (full recognition and measurement with specified disclosures from some Accounting Standards[23], includes consolidation and equity accounting where applicable)

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22 Reporting entity is defined in AASB 1057, other Australian Accounting Standards and SAC 1 which the AASB can amend or remove, to ensure consistency with the term 'reporting entity' after the revised *Conceptual Framework* is made applicable to all entities in Australia as part of the proposed medium-term approach.

23 Specified disclosures are: 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*, AASB 1054 *Australian Additional Disclosures* plus related party, revenue, impairment of assets and income tax disclosures.

Option 1: who will be impacted and to what extent?

72 Table 1 depicts the impact of adopting Option 1: Two-phased approach to applying the IASB's RCF proposals:

Table 1: Who will be impacted?

	Short-term approach	**Medium-term approach**	
		Alternative 1: RDR	**Alternative 2: SDR**
For-profit entities			
Publicly accountable entities (Tier 1 GPFS) and entities voluntarily reporting compliance with IFRS	RCF – no impact	Not applicable	Not applicable
Reporting entities preparing GPFS Tier 2 RDR	Not applicable – no change	RCF, no other impact	RCF, ↓ disclosures[24]
Non-reporting entities preparing SPFS RG 85[25] compliant who are consolidating and equity accounting (or single entity who is RG 85 compliant)	Not applicable – no change	RCF, ↑ disclosures to RDR level	RCF, ↑ 4 disclosures[26]
Non-reporting entities preparing SPFS, RG 85 compliant only (ie who are not consolidating or equity accounting)	Not applicable – no change	RCF, ↑ disclosures to RDR level plus consolidation and equity accounting[28]	RCF, ↑4 disclosures[26] plus consolidation and equity accounting[28]
Non-reporting entities preparing SPFS (non-RG 85 compliant)	Not applicable – no change	RCF*, other changes depend on specific SPFS selections* => ↑ full recognition & measurement, disclosures to RDR level plus consolidation and equity accounting[28]	RCF, *other changes depend on specific SPFS selections* =>↑ full recognition and measurement, 9 disclosures[27] plus consolidation and equity accounting[28]
Not-for-profit public sector entities			
Entities preparing Tier 1 GPFS (mandatorily or voluntarily)	Not applicable – no change	RCF – no impact	RCF – no impact
Entities preparing GPFS Tier 2 RDR	Not applicable – no change	RCF – no other impact	RCF, ↓disclosure[28]

24 Reduced disclosure change from all (at a reduced level) to just 9 disclosures (see note 28 below) albeit these will be disclosed in full.

16 ASIC's Regulatory Guide 85 *Reporting requirements for non-reporting entities* is for entities currently lodging SPFS with ASIC. Refer to Appendix C paragraphs 70-75.

26 Four disclosures: Related Party Disclosures, Impairment of Assets, Revenue and Income Taxes.

27 Nine disclosures: 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*, AASB 1054 *Australian Additional Disclosures*, Related Party Disclosures, Impairment of Assets, Revenue and Income Taxes (the AASB is consulting on these specified disclosures as part of the consultation process to ascertain whether they best meet users' needs).

28 The extent of the changes to these entities will depend of the entity (single entity or part of a consolidated group) as well as the state of its current SPFS (ie if they are currently meeting full recognition and measurement and what disclosures are currently covered).

	Short-term approach	Medium-term approach	
		Alternative 1: RDR	**Alternative 2: SDR**
Not-for-profit private sector entities			
Reporting entities voluntarily preparing Tier 1 GPFS	Not applicable – no change	RCF – no impact	RCF – no impact
Reporting entities preparing GPFS Tier 2 RDR	Not applicable – no change	RCF – no other impact	RCF, ↓ disclosures[29]
Non-reporting entities preparing SPFS, full recognition and measurement, minimum disclosures[30] and if parent, are consolidating and equity accounting	Not applicable – no change	RCF, ↑disclosures to RDR level	RCF, ↑4 disclosures[26]
Non-reporting entities preparing SPFS, full recognition and measurement, minimum disclosures[30] and if parent, are not consolidating or equity accounting	Not applicable – no change	RCF, ↑disclosures to RDR level plus consolidation and equity accounting[28]	RCF, ↑4 disclosures[26] plus consolidation and equity accounting[28]
Non-reporting entities preparing SPFS, without full recognition and measurement and varying disclosures	Not applicable – no change	RCF *changes depend on current state of SPFS* =>↑disclosures to RDR level plus consolidation and equity accounting[9]	RCF *changes depend on current state of SPFS* => ↑full recognition and measurement, 9 disclosures[27] plus consolidation and equity accounting[28]

73 Based on Research Report No. 1, which includes data from 2010-11, an estimated 59% of reports publicly lodged with ASIC by non-disclosing entities are SPFS. At that time there were a total of 21,711 non-disclosing entities lodging financial reports with ASIC, which represents just over 1% of the 1.84 million companies registered with ASIC[31].

74 Further analysis of Research Report No. 1[32] findings indicates more than three-quarters (76.1%) of non-disclosing entities that need to publicly lodge financial statements in accordance with AAS are complying with recognition and measurement requirements of AAS.

75 This suggests that less than one quarter (23.9%) of all financial statements publicly lodged in accordance with AAS do not explicitly state compliance with the recognition and measurement of AAS.

76 Of that number, only 11.4% explicitly state that recognition and measurement (R&M) have not been complied with. Research Report No. 1 did not examine the extent of non-compliance for these entities, meaning that they may have not complied with only one or two requirements. The remaining 12.5% of reports examined revealed either 'no clear statement of application of R&M' or 'minor non-application' of R&M. Once again, this does not conclusively mean that these entities did not comply with the majority requirements.

77 In relation to the NFP private sector, the findings from the Australian Charities and Not-for-profits Commission's (ACNC's) latest monitoring of Annual Information Statements and Annual Financial Reports, *Reporting trends in the 2016 Annual Information Statement* (referred to throughout this Consultation Paper as 'ACNC Report'), suggest similar proportions of GPFS (45%) versus SPFS (55%). ACNC regulations require minimum disclosures (consistent with ASIC's RG 85[33]) and state that the financial statements must give a true and fair view of the financial position and performance of the registered entity.

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29 Reduced disclosure change from all (at a reduced level) to just 9 disclosures (see note 28) albeit these will be disclosed in full.

30 Minimum disclosures: 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*, AASB 1054 *Australian Additional Disclosures*.

31 Refer to ASIC's 2010-11 Annual Report.

32 Refer to Research Report No. 1 and Appendix C paragraphs 46-61.

33 ASIC's RG 85 is for entities currently lodging SPFS with ASIC. Refer to Appendix C paragraphs 70-75.

78 The AASB is currently undertaking further empirical research to determine the number of entities lodging SPFS with ASIC or ACNC and the proportions of these entities not applying full R&M. The AASB is also seeking further data on the extent of SPFS usage in the NFP sector for entities required to comply with AAS and not regulated by the ACNC.

79 The NFP public sector does not generally allow preparation of SPFS, and there has only been limited take up of Tier 2 RDR[34]. Generally NFP public sector entities apply full R&M. Accordingly, the main impact for NFP public sector entities is likely to be a change in disclosures for those using RDR if the SDR option is chosen.

80 The AASB does not have access to data or research findings on entities currently preparing SPFS but not consolidating and equity accounting in accordance with AAS (where relevant). As these entities would be required to consolidate and equity account (where relevant) under the proposed medium-term approach, the AASB has asked a specific matter for comment about any concerns constituents might have on this proposed requirement. This would help the AASB gain a better understanding of the extent of this issue in order to provide appropriate transitional relief (if any) for such entities.

81 The proposed requirements for entities to prepare consolidated financial statements would not affect how entities would apply the thresholds in legislation (for example the large and small proprietary company test in the Corporations Act) to determine 'who' is required to publicly lodge financial statements.

Relevance of Option 1 to other entities not impacted

Publicly accountable entities currently self-assessing as non-reporting entities and preparing SPFS

82 The AASB has been advised there could be some entities that are publicly accountable but have self-assessed as being non-reporting entities. The AASB has included a specific matter for comment (refer to Q3 in paragraph 24) seeking feedback on these types of entities and whether they would have any implications under the AASB's short-term approach. The AASB's current expectation is that transitioning to Tier 1 GPFS for these entities would involve additional disclosures only.

The small/large proprietary company test in the Corporations Act 2001

83 The proposed requirements for entities to prepare consolidated financial statements would not affect how entities apply the thresholds in legislation (for example the large and small proprietary company test in the Corporations Act) to determine 'who' is required to publicly lodge financial statements. Specifically, Section 45A of the Corporations Act 2001[35] requires thresholds to be based on a consolidated basis in accordance with the accounting standards even if the standards do not otherwise apply to the company. There is no change to this requirement as a result of these proposals.

84 However, the AASB recognises that there may be some proprietary companies not currently publicly lodging because they have not applied the small / large proprietary company test in the Corporations Act on a consolidated basis in accordance with AAS (noting that this is a requirement in the Act even if the AAS do not otherwise apply to the company ie this is not a change being made by the AASB). Furthermore, there may be small proprietary companies that may become large as a result of new standards increasing assets on the balance sheet such as AASB 16 *Leases*.

Option 1: Benefits of proposals

85 **The phased approach allows time for further research and constituent feedback:** Given the impact that these proposals may have on some entities, time is required to better understand the needs of constituents (including regulators, preparers, directors and those charged with governance, users and auditors). By having a phased approach, entities that require IFRS compliance can continue to do so by having the IASB's RCF available when it first becomes applicable, yet all other entities will not be impacted until sufficient time is provided to fully identify the impact of medium term proposals and determine appropriate mitigation to ensure that overall the proposals are beneficial to the Australian economy.

86 **IFRS compliance and/or alignment is maintained:** all publicly accountable for-profit entities and entities voluntarily reporting compliance with IFRS can maintain IFRS compliance by applying the IASB's RCF in the short term. All other entities will continue to use IFRS as a base in the medium term as they too will be using the IASB's RCF and AAS, which will be amended/revised or superseded based on the concepts and principles in the IASB's RCF.

87 **The reporting entity problem would be resolved:** All entities will apply the IASB's RCF and the term 'reporting entity' – as defined in the RCF – would be consistently applied within AAS. Furthermore:

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34 Refer to AASB Research Report No.6 Financial Reporting Requirements Applicable to Australian Public Sector Entities

35 Refer Section 45A *Corporations Act 2001*.

(a) this outcome mitigates challenges (see paragraph 33-40) relating to variation in the application of the reporting entity concept and disparity in the quality and content of SPFS (as evident in Research Report No. 1[36] undertaken on these matters).

(b) this outcome aligns with the FRC's strategic directive that requires the AASB to work towards the adoption of accounting standards that are the same as those issued by the IASB.

(c) having a single Conceptual Framework that aligns with the AAS, will also facilitate comparability when the AASB performs its role under section 224 and 229 of the ASIC Act, which is to consider the suitability of a proposed standard for different types of entities and to ensure there are appropriate accounting standards for each type of entity that must comply with accounting standards.

(d) as detailed in *The AASB's Standard-Setting Frameworks for For-Profit and Not-for-Profit Entities*[37], like transactions and events should be accounted for in a like manner for all types of entities, reflecting their economic substance, unless there is a justifiable reason not to do so. This option will facilitate consistency, transaction neutrality between sectors and tiers, enable greater comparability between entities, and ensure global transferability.

88 **The SPFS problem would be resolved:** there will no longer be a requirement for entities to self-assess as reporting entities or non-reporting entities and no longer the ability to prepare SPFS when required by legislation or otherwise to prepare financial statements in accordance with AAS. All non-publicly accountable entities would be preparing Tier 2 GPFS (which would either be Alternative 1 or Alternative 2, depending on which alternative is adopted by the AASB). The benefits of this include:

(a) By having full recognition and measurement, consolidation and equity accounting (where required), and minimum disclosure requirements, the financial statements will be more consistent, comparable, transparent, and include disclosures tailored to meet user needs.

(b) By ensuring a level playing field, the proposed changes will also facilitate more consistent and transparent financial reporting and contribute towards improving the credibility of financial statements and increased stakeholder confidence.

(c) The minimum requirements proposed in Alternatives 1 and 2 also meet ASIC's minimum requirements in RG 85 and will assist in Trans-Tasman harmonisation by providing consistent recognition and measurement requirements with New Zealand.

(d) Alternative 2 proposes only incremental changes to the minimum requirements in RG 85 for SPFS. If this alternative is adopted, the AASB will undertake further consultation to confirm which incremental disclosures should be included to best meet the needs of users.

(e) There are also benefits for directors and preparers with respect to:

(i) reducing risks in self-assessing whether the entity is a reporting entity or not and determining the appropriate level of compliance with AAS; and

(ii) simplifying how to determine reporting requirements because all entities will be required to prepare either Tier 1 or Tier 2 GPFS, depending on whether they are publicly accountable or not (noting that the criteria for determining whether an entity is publicly accountable or not, is internationally recognised as it is the same definition used in *IFRS for SMEs*).

89 **Reduced risks for regulators and auditors:** the outcomes of Option 1 will also reduce risks for auditors and regulators and alleviate difficulties with enforcement of reporting requirements by reducing the subjectivity of the underlying criteria.

Option 1: Barriers to proposals and potential mitigation

90 **Increase in regulatory burden (eg transitioning to new requirements may be costly and difficult)** – given the number of entities currently preparing SPFS, in order to help mitigate the increase in regulatory burden, the AASB would provide:

(a) a GPFS Tier 2 alternative aimed at balancing the costs to preparers and benefits to users;

(b) appropriate education, implementation support, transitional relief and adequate timeframes to implement the requirements (including consideration of a staggered implementation process, whereby the medium-term approach may be for example applied to for-profit entities first before NFPs on the basis that few NFPs are expected to be applying full R&M).

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36 Refer to AASB Research Report No. 1 *Application of the Reporting Entity Concept and Lodgement of Special Purpose Financial Statements*

37 Refer to *The AASB's For-Profit Entity Standard-Setting Framework* and *The AASB's Not-For-Profit Entity Standard-Setting Framework*.

The AASB notes that transitional costs will be somewhat offset by reduced advisory costs in determining whether an entity is a reporting entity or not, as well as reduced preparer risk from not having to self-assess and less time determining reporting requirements. A specific matter for comment will be included regarding transitional relief needed to minimise the impact of these proposals.

Furthermore, anecdotal evidence[38] indicates that many entities preparing SPFS are already preparing additional disclosures (including related party disclosures, revenue and income tax disclosures) for the purposes of securing funding. Therefore, the increased reporting requirements (particularly to Tier 2, Alternative 2) may not be overly onerous.

91 **Concern about consolidation and equity accounting -** the AASB does not have data to understand the impact of this requirement (ie the number of entities that would need to prepare consolidated or equity accounted financial statements that are currently not doing so, is not known. The AASB will conduct further research and undertake outreach activities to better understand the extent of this requirement and constituent views. A specific matter for comment is included to understand transitional relief needed to minimise the impact of this change.

Anecdotal evidence[38] indicates that some entities preparing SPFS are consolidating and equity accounting for the purposes of securing funding. Therefore, preparing consolidated and equity accounted financial statements for parent entities may not be overly onerous.

Option 2: Operate with two conceptual frameworks

Overview of Option 2

92 This option just applies Phase 1 of Option 1: Two-phased approach to applying the IASB's RCF. Specifically, Option 2 involves **operating with two conceptual frameworks:**

(a) the IASB's RCF will apply to publicly accountable for-profit entities and other entities voluntarily reporting compliance with IFRS to enable them to maintain IFRS compliance. SAC 1 would be made not applicable to these entities and amendments would be made to, AASB 1053 *Application of Tiers of Australian Accounting Standards* and other AAS[39] to make the Australian definitions of 'reporting entity' not applicable to these entities;

(b) all other entities will continue to apply the AASB's existing *Framework*, enabling them to continue using the Australian reporting entity concept; and

(c) there would be amendments to the definition of 'public accountability in AASB 1053 to align with the revised IASB definition in *IFRS for SMEs*. The AASB is also proposing additional guidance as per *IFRS for SMEs* to clarify the term 'fiduciary capacity', as specified in *IFRS for SMEs*.

93 This option would result in having two conceptual frameworks for a single suite of AAS (based on IFRS), that are applicable across all sectors (albeit with some modifications). Each conceptual framework would describe the elements of financial statements differently and have different recognition and measurement guidance, impacting:

(a) standard-setters who use the conceptual frameworks to develop Standards based on consistent concepts;

(b) preparers who use the conceptual frameworks to develop consistent accounting policies when no Standard applies to a particular transaction or event, or when a Standard allows a choice of accounting policy; and

(c) all parties when using the conceptual frameworks to understand and interpret the Standards.

Option 2: who will be impacted and to what extent?

94 All publicly accountable for-profit entities that are required to prepare Tier 1 GPFS and those entities that voluntarily report compliance with IFRS would be required to apply the RCF issued by the IASB. The changes are not expected to have any impact on these entities as they are currently preparing full GPFS (Tier 1) in accordance with the AAS.

95 The AASB has been advised there may be some entities who are publicly accountable that have self-assessed as not being reporting entities and may be preparing SPFS. Option 2 will impact these entities.

38 The AASB have conducted telephone interviews with representatives from three of the major four banks in Australia and learnt that related party, income taxes and revenue disclosures are critical when making lending decisions. Consolidation and equity accounting is also important when lending to a parent entity. If these items are not provided with the borrower's financial statements, the banks ask for these items to be separately prepared.

39 Reporting entity is defined in AASB 1057, other Australian Accounting Standards and SAC 1 which the AASB can amend or remove, to ensure consistency with the term 'reporting entity' after the revised *Conceptual Framework* is made applicable to all entities in Australia as part of the proposed medium-term approach.

However, the AASB's expectation is that transitioning to Tier 1 GPFS for these entities would involve additional disclosures only.

96 There would be no changes to the existing reporting requirements for all other entities as the existing *Framework*, and the reporting entity concept as per SAC 1 and the use of the term in AAS, would continue to apply to these entities. This means, other entities would still have the ability to prepare SPFS. However, these other entities will gradually lose alignment between the AAS and the existing *Framework* and there is likely to be more inaccuracies in financial reporting due to how the term 'reporting entity' is interpreted.

97 Table 1 depicts the impact and extent of adopting Option 1: Two-phased approach to applying the IASB's RCF. The "Short-term approach" depicted in Table 1 demonstrates the impact and extent of the impact of Option 2.

Option 2 – benefits to proposals

98 **IFRS compliance and alignment maintained for some entities** – publicly accountable for-profit entities and others currently voluntarily claiming IFRS compliance can continue to do so with no additional reporting burden as they are already doing Tier 1 GPFS. This also contributes to the efforts to align the reporting entity definition with other international frameworks.

99 **No change to existing reporting requirements for other entities** as this option retains use of the existing *Framework* and use of the reporting entity concept and its term as per SAC 1 in the AAS for these entities.

100 **Provides time for legislators and regulators to reshape the Australian Financial Reporting Framework**, as the AASB, legislators, regulators and other key stakeholders are currently working together through extensive consultation to influence changes in legislation to determine which entities need to prepare financial statements in accordance with the AAS and what the thresholds and criteria should be for the different tiers of reporting.

Option 2 – barriers to proposals

101 **Having two Conceptual Frameworks for a single suite of AAS would be untenable** – because the AAS will be based on the RCF. Therefore, entities applying the existing *Framework* to develop accounting policies or interpret the AAS, are likely to develop inconsistent accounting policies and/or wrongly interpret the AAS, which would result in inaccuracies in financial reporting.

102 **Other entities will lose alignment between AAS and RCF** – all other entities will lose alignment between the AAS and the RCF as the principles and guidance in the IASB's RCF get incorporated into the AAS when they are revised/ amended or superseded.

103 **This does not resolve the reporting entity problem** – the term 'reporting entity' – as defined in the RCF – is currently used within a number of AAS (including AASB 3 and AASB 12). To date, the AASB is not aware of any significant issues caused by this as the term could be read in the context of the existing definition in SAC 1 without causing confusion. However, with the issue of the IASB's RCF that specifically has a chapter on Reporting Entity and defines the term differently to what is in SAC 1 and some AAS (for example AASB 1053), it will become increasingly difficult to read the term in two fundamentally different ways, particularly as the AAS are amended/revised and there are more references to the term as defined in the RCF. (Refer to Appendix C paragraphs 4 to 17 for a detailed explanation of the issues with the use of the term 'reporting entity' in the RCF, AAS and SAC 1).

104 **This does not resolve the SPFS problem** – because maintaining the status quo for other entities would mean the current 'reporting entity concept' is retained. This means entities will continue 'self-assessing' (whether they are reporting entities or not) and opt to prepare SPFS if they assess themselves to be non-reporting entities. Changing this through legislation could take time, and in the meantime, the lack of comparability and the absence of a level playing field for entities of similar economic circumstances would continue undermining the fundamentals of trust and transparency.

Option 3: All entities to apply the RCF when it first becomes applicable

Overview of Option 3

105 This option involves **making the IASB's RCF applicable to all entities when it first becomes available as outlined below:**

(a) the RCF will be made applicable to all entities required by legislation or otherwise to comply with AAS, SAC 1 would be removed and amendments would be made to, AASB 1053 and other AAS[40] to remove the Australian definitions of 'reporting entity';

(b) there would be amendments to the definition of 'public accountability in AASB 1053 to align with the revised IASB definition in *IFRS for SMEs*. The AASB is also proposing additional guidance as per *IFRS for SMEs* to clarify the term 'fiduciary capacity', as specified in *IFRS for SMEs*.

Option 3: who will be impacted and to what extent?

106 Under Option 3, the RCF will be made applicable to all entities required by legislation or otherwise to comply with AAS, SAC 1 would be removed and amendments would be made to, AASB 1053 and other AAS to remove the Australian definitions of 'reporting entity'. This means that all entities will be required to prepare GPFS.

107 This option is not expected to have any impact on publicly accountable for-profit entities or entities that voluntarily report compliance with IFRS as they currently prepare full GPFS (Tier 1) in accordance with the AAS.

108 The AASB has been advised there may be some entities who are publicly accountable that have self-assessed as not being reporting entities and may be preparing SPFS. Option 3 will impact these entities. However, the AASB's current expectation is that transitioning to Tier 1 GPFS for these entities would involve additional disclosures only.

109 All other entities will be affected by the Option 3 as follows:

(a) entities that have self-assessed as non-reporting entities and are currently preparing SPFS when required to prepare financial statements in accordance with AAS, will no longer be able to do so. Under Option 3, these entities will need to prepare full GPFS or GPFS – RDR;

(b) parent entities currently preparing SPFS but not consolidating or equity accounting or not applying full recognition and measurement in accordance with AAS would need to do so under the Tier 2 GPFS requirements.

110 Based on Research Report No. 1, an estimated 59% of all non-disclosing entity reports publicly lodged with ASIC are SPFS.

111 Further analysis of the findings in Research Report No. 1[41] indicate more than three-quarters (76.1%) of non-disclosing entities that need to publicly lodge financial statements in accordance with AAS are complying with recognition and measurement requirements of AAS.

112 This suggests that less than one quarter (23.9%) of all such financial statements publicly lodged in accordance with AAS do not explicitly state compliance with the recognition and measurement of AAS.

113 Of that number, only 11.4% explicitly state that recognition and measurement (R&M) have not been complied with. Research Report No. 1 did not examine the extent of non-compliance for these entities, meaning that they may have not complied with only one or two requirements. The remaining 12.5% of reports examined revealed either 'no clear statement of application of R&M' or 'minor non-application' of R&M. Once again, this does not conclusively mean that these entities did not comply with the majority requirements.

114 In relation to the NFP private sector, the findings from the ACNC Report suggest similar proportions of GPFS (45%) versus SPFS (55%). ACNC regulations require minimum disclosures (consistent with ASIC's RG 85[42]) and state that the financial statements must give a true and fair view of the financial position and performance of the registered entity.

115 The AASB is currently undertaking further empirical research to determine the number of entities lodging SPFS with ASIC or ACNC and the proportions of these entities not applying full R&M. The AASB is also seeking further data on the extent of SPFS usage in the NFP sector for entities required to comply with AAS and not regulated by the ACNC.

116 The NFP public sector does not generally allow preparation of SPFS, and there has only been limited take up of Tier 2 RDR[43]. Generally NFP public sector entities apply full R&M. Accordingly, the main impact for NFP public sector entities is likely to be a change in disclosures for those using RDR if the SDR option is chosen.

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40 Reporting entity is defined in AASB 1057, other Australian Accounting Standards and SAC 1 which the AASB can amend or remove, to ensure consistency with the term 'reporting entity' after the revised *Conceptual Framework* is made applicable to all entities in Australia as part of the proposed medium-term approach.

41 Refer to Research Report No. 1 and Appendix C paragraphs 39-52.

42 ASIC's RG 85 is for entities currently lodging SPFS with ASIC. Refer to Appendix C paragraphs 70-75.

43 Refer to AASB Research Report No. 6 *Financial Reporting Requirements Applicable to Australian Public Sector Entities*

117 The AASB does not have access to data or research findings on entities currently preparing SPFS but not consolidating and equity accounting in accordance with AAS (where relevant). As these entities would be required to consolidate and equity account (where relevant) under the proposed medium-term approach, the AASB has asked a specific matter for comment about any concerns constituents might have on this proposed requirement. This would help the AASB gain a better understanding of the extent of this issue to provide transitional relief (if any) for such entities.

118 The proposed requirements for entities to prepare consolidated financial statements would not affect how entities would apply the thresholds in legislation (for example the large and small proprietary company test in the Corporations Act) to determine 'who' is required to publicly lodge financial statements.

Relevance of Option 3 to other entities not impacted

Publicly accountable entities currently self-assessing as non-reporting entities and preparing SPFS

119 The AASB has been advised there could be some entities that are publicly accountable but have self-assessed as being non-reporting entities. The AASB has included a specific matter for comment (refer to Q3 in paragraph 24) seeking feedback on these types of entities and whether they would have any implications under the AASB's short-term approach. The AASB's current expectation is that transitioning to Tier 1 GPFS for these entities would involve additional disclosures only.

The small/large proprietary company test in the Corporations Act 2001

120 The proposed requirements for entities to prepare consolidated financial statements would not affect how entities would apply the thresholds in legislation (for example the large and small proprietary company test in the Corporations Act) to determine 'who' is required to publicly lodge financial statements. Specifically, Section 45A of the *Corporations Act 2001*[44] requires thresholds to be based on a consolidated basis in accordance with the accounting standards even if the standards do not otherwise apply to the company. There is no change to this requirement as a result of these proposals.

121 However, the AASB recognises that there may be some proprietary companies not currently publicly lodging because they have not applied the small / large proprietary company test in the Corporations Act on a consolidated basis in accordance with AAS (noting that this is a requirement in the Act even if the AAS do not otherwise apply to the company ie this is not a change being made by the AASB). Furthermore, there may be small proprietary companies that may become large as a result of new standards increasing assets on the balance sheet such as AASB 16 *Leases*.

Option 3 – benefits to proposals

122 **IFRS compliance and/or alignment is maintained for all entities** - all publicly accountable and entities voluntarily reporting compliance with IFRS can maintain IFRS compliance by applying the IASB's RCF. All other entities will continue to use IFRS as a base, as they too will be using the IASB's RCF and AAS, which will be amended/revised or superseded based on the concepts and principles in the IASB's RCF.

123 **The reporting entity problem would be resolved:** All entities will apply the IASB's RCF and the term 'reporting entity' – as defined in the RCF – would be consistently applied within AAS. Furthermore:

(a) this outcome mitigates challenges (see paragraph 33-40) relating to variation in the application of the reporting entity concept and disparity in the quality and content of SPFS (as evident in Research Report No. 1[45] undertaken on these matters).

(b) this outcome aligns with the FRC's strategic directive that requires the AASB to work towards the adoption of accounting standards that are the same as those issued by the IASB.

(c) having a single Conceptual Framework that aligns with the AAS, will also facilitate consistency when the AASB performs its role under section 229 of the ASIC Act, which is to consider the suitability of a proposed standard for different types of entities and to ensure there are appropriate accounting standards for each type of entity that must comply with accounting standards.

(d) as detailed in *The AASB's Standard-Setting Frameworks for For-Profit and Not-for-Profit Entities*[46], like transactions and events should be accounted for in a like manner for all types of entities, reflecting their economic substance, unless there is a justifiable reason not to do so. This option will facilitate consistency, transaction neutrality between sectors and tiers, enable greater comparability between entities, and ensure global transferability.

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44 Refer Section 45A *Corporations Act 2001*.

45 Refer to AASB Research Report No. 1 *Application of the Reporting Entity Concept and Lodgement of Special Purpose Financial Statements*

46 Refer to *The AASB's For-Profit Entity Standard-Setting Framework* and *The AASB's Not-For-Profit Entity Standard-Setting Framework*.

124 **The SPFS problem would be resolved -** there will no longer be a requirement for entities to self-assess as reporting entities or non-reporting entities and no longer the ability to prepare SPFS when required by legislation or otherwise to prepare financial statements in accordance with AAS. All non-publicly accountable entities would be able to prepare Tier 2 GPFS RDR. The benefits of this include:

(a) By having full recognition and measurement, consolidation and equity accounting (where required), and reduced disclosure requirements, the financial statements will be more consistent, comparable and transparent.

(b) By ensuring a level playing field, the proposed changes will also facilitate more consistent and transparent financial reporting and contribute towards improving the credibility of financial statements and increased stakeholder confidence.

(c) There are also benefits for directors and preparers with respect to:

(i) reducing risks in self-assessing whether the entity is a reporting entity or not; and

(ii) determining the level of reporting required because all entities will be required to prepare either Tier 1 or Tier 2 GPFS, depending on whether they are publicly accountable or not (noting that the criteria for determining whether an entity is publicly accountable or not, is internationally recognised as it is the same definition used in *IFRS for SMEs*).

125 **Reduced risks for regulators and auditors -** the outcomes of Option 3 will also reduce risks for auditors and regulators and alleviate difficulties with enforcement of reporting requirements by reducing the subjectivity of the underlying criteria.

Option 3: Barriers to proposals and potential mitigation

126 **Increase in regulatory burden (eg transitioning to new requirements may be costly and difficult)** – given the number of entities currently preparing SPFS, transitioning to Tier 2 GPFS RDR would be a considerable step up for many entities.

The AASB notes that transitional costs will be somewhat offset by reduced advisory costs in determining whether an entity is a reporting entity or not, as well as reduced preparer risk from not having to self-assess and less time determining reporting requirements. Furthermore, anecdotal evidence[47] indicates that many entities preparing SPFS are already preparing additional disclosures for the purposes of securing funding. Therefore, the increased reporting requirements may not be overly onerous.

127 **Concern about consolidation and equity accounting without enough time for implementation** – the AASB does not have data to understand the impact of this requirement (ie the number of entities that would need to prepare consolidated or equity accounted financial statements that are currently not doing so, is not known). Under this option, the changes would become effective on 1 January 2020, accordingly, there will not be much time for entities to assess the impact of the changes and what they would need to do to transition.

Anecdotal evidence[47] indicates that some entities preparing SPFS are consolidating and equity accounting for the purposes of securing funding. Therefore, preparing consolidated and equity accounted financial statements for parent entities may not be overly onerous.

Option 4: Do nothing and lose IFRS compliance

Option 4: Overview

128 This option involves continuing to apply the AASB's existing *Framework*, which incorporates the IASB's existing *Conceptual Framework* to all entities required by legislation or otherwise to prepare financial statements in accordance with AAS. Under this option all entities could continue to apply the Australian reporting entity concept within SAC 1 and AAS, enabling entities that self-assessing as non-reporting entities to continue to prepare SPFS when they are required to prepare financial statements in accordance with the AAS.

Option 4: who will be impacted and to what extent?

129 Under this option, all entities that claim IFRS compliance would no longer be able to categorically claim IFRS compliance when the IASB's RCF becomes applicable (1 January 2020).

47 The AASB have conducted telephone interviews with representatives from three of the major four banks in Australia and learnt that related party, income taxes and revenue disclosures are critical when making lending decisions. Consolidation and equity accounting is also important when lending to a parent entity. If these items are not provided with the borrower's financial statements, the banks ask for these items to be separately prepared.

130 There would be no changes to the existing reporting requirements for all other entities. The existing *Framework* would continue to apply all entities and entities would still have the ability to prepare SPFS if they self-assess as non-reporting entities. However, all entities will gradually lose alignment between the AAS and the existing *Framework* as the AAS would be incorporating the principles and guidance in the IASB's RCF when the AAS get amended/revised or superseded.

Option 4: Benefits to proposals

131 **No change on current reporting requirements for entities** as this option retains use of the existing *Framework* and use of the reporting entity concept and its term as per SAC 1 in the AAS for these entities.

132 **Provides time for legislators and regulators to reshape the Australian Financial Reporting Framework**, as the AASB, legislators, regulators and other key stakeholders are currently working together through extensive consultation to influence changes in legislation to determine which entities need to prepare financial statements in accordance with the AAS and what the thresholds and criteria should be for the different tiers of reporting.

Option 4: Barriers to proposals and potential mitigation

133 **Entities lose IFRS compliance** – publicly accountable for-profit entities and others currently voluntarily claiming IFRS compliance would no longer be able to categorically do so as they will be applying the existing *Framework* instead of the IASB's RCF.

134 **Entities will lose alignment between AAS and conceptual framework** – all entities will lose alignment between the AAS and the existing *Framework* as the principles and guidance in the IASB's RCF get incorporated into the AAS when they are revised/ amended or superseded.

135 **This does not resolve the reporting entity problem** – the term 'reporting entity' – as defined in the RCF – is currently used within a number of AAS (including AASB 3 *s* and AASB 12). To date, the AASB is not aware that this has caused significant issues as the term can be read in the context of the existing definition in SAC 1 without causing confusion. However, once the IASB's RCF is issued and the specific definition of 'reporting entity' in the RCF is different to what is in SAC 1 and some AAS (ie AASB 1053), it will become increasingly difficult to read that term in two different ways. (Refer to Appendix C paragraphs 4 to 17 for a detailed explanation of the issues with the use of the term 'reporting entity' in the RCF, AAS and SAC 1).

136 **This does not resolve the SPFS problem** – because maintaining the status quo for other entities would mean the current 'reporting entity concept' is retained. This means entities will continue 'self-assessing' (whether they are reporting entities or not) and preparing SPFS if they assess themselves to be non-reporting entities. This compromises comparability by allowing entities of similar economic circumstances to determine whether they should prepare GPFS or SPFS, which in turn undermines the fundamentals of trust and transparency.

Option 5: All entities to apply the RCF, change the name of the Australian reporting entity concept and prescribe minimum requirements for SPFS

Overview of Option 5

137 This option involves**:**

(a) making the RCF applicable when it first becomes available to all entities required by legislation or otherwise to comply with AAS;

(b) making amendments to the definition of 'public accountability' in AASB 1053 to align with the revised IASB definition in *IFRS for SMEs*. The AASB is also proposing additional guidance as per *IFRS for SMEs* to clarify the term 'fiduciary capacity', as specified in *IFRS for SMEs*;

(c) changing the name of the Australian reporting entity concept (for example, to "GPFS reporters") in SAC 1, AASB 1053 and other AAS to retain the ability for entities to self-assess whether they need to prepare GPFS or not; and

(d) setting minimum reporting requirements in AAS for SPFS (ie "non-GPFS reporters") in order to meet the AASB's obligations under S224 and S229 of the ASIC Act to facilitate comparability and ensure appropriate accounting standards for each type of entity that must comply with accounting standards. This is likely to include full R&M, consolidation and equity accounting as well as minimum disclosures (effectively Alternative 2 GPFS Tier 2 SDR detailed in Option 1).

138 Under this option all entities could continue to apply the Australian reporting entity concept within SAC 1 and AAS, albeit under a different name, enabling entities that self-assess as non-reporting entities to continue to prepare SPFS when they are required to prepare financial statements in accordance with the

AAS. However, given all the issues noted in Section 1 with the current use of the reporting entity concept, other regulator guidance such as ASIC RG 85, and preliminary feedback from users, the AASB will still need to mandate minimum reporting requirements. These are unlikely to be any different to those proposed as SDR in Option 1. However, as noted in Section 1, the AASB is awaiting the outcomes of the ACNC legislative review to determine whether three tiers are required for the NFP sector, which may include modified recognition and measurement.

Option 5: who will be impacted and to what extent?

139 All publicly accountable for-profit entities that are required to prepare Tier 1 GPFS and those entities that voluntarily report compliance with IFRS would be able to continue maintaining IFRS compliance. The changes are not expected to have any impact on these entities as they are currently preparing full GPFS (Tier 1) in accordance with the AAS.

140 All other entities would apply the RCF and the Australian reporting entity concept in SAC 1 and AAS would continue to apply to these entities, albeit under a different name. This means other entities would still have the ability to prepare SPFS. However, there will be minimum reporting requirements prescribed by the AASB for SPFS.

Option 5 – benefits to proposals

141 **IFRS compliance and/or alignment is maintained for all entities** – All publicly accountable for-profit entities and entities voluntarily reporting compliance with IFRS can maintain IFRS compliance by applying the IASB's RCF. All other entities will continue to use IFRS as a base, as they too will be using the IASB's RCF and AAS, which will be amended/revised or superseded based on the concepts and principles in the IASB's RCF.

142 **The reporting entity problem would be resolved** – All entities will apply the IASB's RCF and the term 'reporting entity' – as defined in the RCF – would be consistently applied within AAS. Furthermore:

(a) this outcome aligns with the FRC's strategic directive that requires the AASB to work towards the adoption of accounting standards that are the same as those issued by the IASB.

(b) having a single Conceptual Framework that aligns with the AAS, will also facilitate consistency when the AASB performs its role under section 229 of the ASIC Act, which is to consider the suitability of a proposed standard for different types of entities and to ensure there are appropriate accounting standards for each type of entity that must comply with accounting standards.

(c) as detailed in *The AASB's Standard-Setting Frameworks for For-Profit and Not-for-Profit Entities*, like transactions and events should be accounted for in a like manner for all types of entities, reflecting their economic substance, unless there is a justifiable reason not to do so. This option will facilitate consistency, transaction neutrality between sectors and tiers, enable greater comparability between entities, and ensure global transferability.

143 **The SPFS problem would be resolved** – Although there will still be the ability for entities to self-assess as 'GPFS reporters' or not, the ability to choose what gets reported in SPFS prepared in accordance with AAS will no longer be available. The benefits of this include:

(a) By having prescribed reporting requirements for SPFS, the financial statements will be more consistent, comparable and transparent and will contribute towards improving the credibility of financial statements and increased stakeholder confidence.

(b) There are also benefits for directors, preparers, regulators and auditors in having prescribed reporting requirements, although the risks of self-assessment would not be alleviated.

Option 5 – barriers to proposals

144 **Increase in regulatory burden (eg transitioning to new requirements may be costly and difficult)** – Given the number of entities currently preparing SPFS, transitioning to prescribed reporting requirements (ie full recognition and measurement, consolidation and equity accounting) could be a considerable step up for some entities. The AASB notes that transitional costs will be somewhat offset by reduced advisory costs in determining reporting requirements.

145 **Concern about applying the prescribed minimum requirements without enough time for implementation** – Under this option, as the changes would become effective on 1 January 2020, there will not be much time for entities to assess the impact of the changes and what they would need to do to transition to the new requirements.

146 **Concern that changing the name of the Australian reporting entity concept would not be justifiable under the AASB's Standard-Setting Frameworks** – To maintain confidence in the Australian economy (including the NFP sector), obtain the benefits of comparability within and across

sectors, facilitate movement of professionals across sectors, *The AASB's Standard-Setting Frameworks for For-Profit Entities and Not-for-Profit Entities*[48] set out circumstances when modifications or amendments to AAS are justifiable. Amending SAC 1 and AAS to change the name of the Australian reporting entity concept to something else (eg to 'GPFS reporters') would be difficult to justify as it would involve retaining self-assessment problem that undermines confidence in the Australian economy, compromises comparability within and across sectors and does not help to achieve the objectives and qualitative characteristics of financial reporting as set out in the *Conceptual Framework*.

147 **Concern about developing a framework for SPFS** – The AASB should not set standards for SPFS, as SPFS should only be prepared where the users can tailor them to their own information needs, and therefore do not need a standard setter or regulator to determine the reporting requirements for them. The AASB, like the IASB, does not consider that it has the authority to determine who must, should, or could prepare such statements. The AASB's role is to determine the appropriate accounting framework and standards that should apply. In other words, anyone that is required to prepare financial statements in accordance with AAS should be preparing GPFS.

148 **Concern that there will be effectively two Tier frameworks** – Given the minimal differences between GPFS Tier 2 RDR and a prescribed SPFS framework, there would be significant costs in maintaining two alternatives effectively doing the same thing.

48 Refer to *The AASB's For-Profit Entity Standard-Setting Framework* (page 11) and *The AASB's Not-For-Profit Entity Standard-Setting Framework* (page 9) for more information on when amendments to Australian Accounting Standards might be justified.

Section 3: Who will the AASB consult and how?

Who will the AASB consult and how?

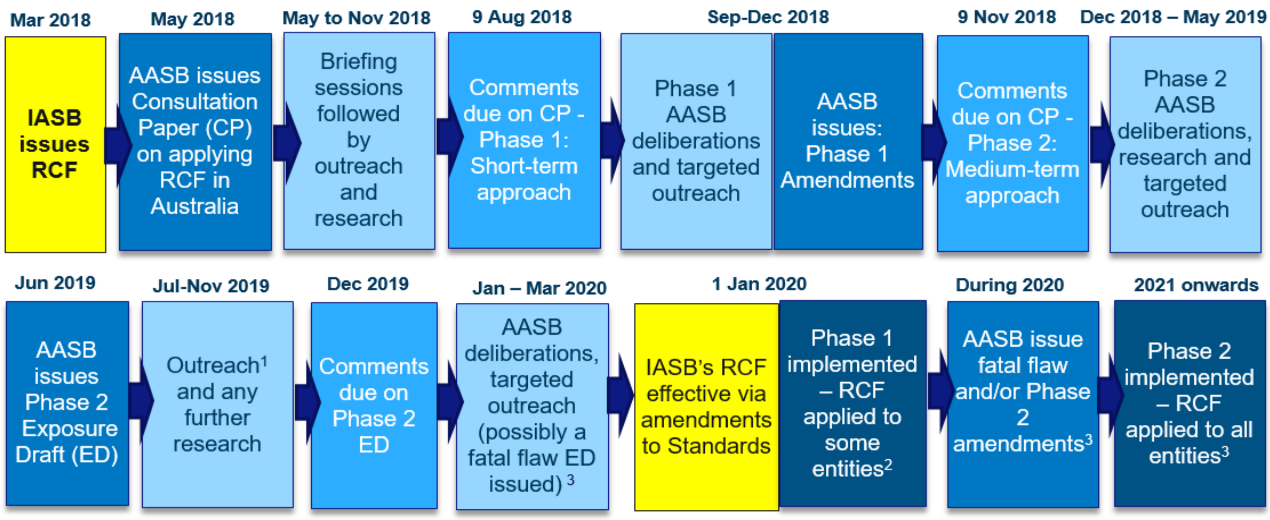
149 The AASB members are appointed for their expertise in a range of areas of business and government and bring to the board a wealth of experience in preparing, auditing and using financial statements that comply with accounting standards. They therefore have a good appreciation of the impact of changes to accounting standards and have strong contacts within the AASB's core constituencies, which the AASB consults. Accordingly, the AASB's public consultation processes are well-regarded and the AASB members are in a sound position to consider constituent responses.

150 The proposed consultation process for applying the AASB's preferred option to apply the IASB's RCF in Australia and to solve the reporting entity and SPFS problems is as follows:

***Table* 2 Consultation process for applying the IASB's RCF in Australia and solving the reporting entity and SPFS problems**

Who will be consulted	How
• regulators such as ASIC, State and Territory regulators, ACNC and the ATO; • firms (small, mid-tier and large firms); • Treasury (Ministers and advisors); • professional bodies, such as Chartered Accountants Australia & New Zealand (CA ANZ), Certified Practising Accountants Australia (CPA Australia), Institute of Public Accountants (IPA) and the Accounting Professional & Ethical Standards Board (APESB) ; • directors/users, via Australian Institute of Company Directors (AICD), Australian Council of Superannuation Investors Limited (ACSI), the Australian Shareholders Association (ASA) and the major banks (as proxy for users); • liquidators / administrators and related regulators, professional bodies such as McGrath Nichol, ASIC and The Australian Restructuring Insolvency and Turnaround Association (ARITA) • CFOs, preparers (all sectors and sizes) • AASB and AUASB Members	• Targeted meetings (teleconference and in-person) • Pre-issue draft Consultation Paper review • Consultation Documents (including this Consultation Paper and Exposure Drafts) • Roundtables in Melbourne, Sydney, Brisbane, Adelaide and Perth • Webinars on Consultation Paper and Exposure Drafts • Research activities to better understand impact on constituents

Project timeline



Notes

1. Outreach conducted in 2019 will also include outreach on any proposals to amend the RCF or AAS for NFP specific issues.
2. Phase 1 implementation of the RCF applies to publicly accountable for-profit entities and entities voluntarily claiming IFRS compliance.
3. The timing of the Phase 2 deliberations and implementation dates may be staggered (e.g. for profit entities first followed by NFPs). Depending on feedback received, Phase 2 for the for-profit sector may be completed earlier than detailed.

Section 4: What is the AASB's preferred option and how will the AASB evaluate its preferred option?

The preferred option – Option 1: Two-phased approach to applying the RCF

151 Option 1 is the AASB's preferred option as the AASB considers that this option will yield the greatest net benefit to the Australian economy. This is because making the RCF applicable via a two-phased approach:

(a) **allows maintenance of IFRS compliance on a continuous basis** for publicly accountable for-profit entities (eg listed and disclosing entities) and other entities that voluntarily report compliance with IFRS;

(b) **maintains the status quo for all other entities in the short term,** allowing time for the AASB to consult and determine an alternative Tier 2 GPFS framework to replace SPFS in AAS after which there will no longer be an option for entities to prepare SPFS when required by legislation or otherwise to prepare financial statements in accordance with AAS;

(c) **maintains IFRS as a base for all entities, allowing alignment between the RCF and AAS for all entities in the medium term**, which reduces confusion and the risk of inappropriate accounting policy and interpretation decisions likely to arise from operating with two conceptual frameworks and one suite of AAS;

(d) **solves the reporting entity problem in the medium term** as all entities will apply the RCF and the term 'reporting entity' as defined in the RCF would be consistently applied within AAS;

(e) **solves the SPFS problem in the medium term** facilitating consistent, comparable, transparent and useful financial statements;

(f) **allows time for the AASB to consult and determine the not-for-profit (NFP) modifications that may be necessary for the RCF** in accordance with the NFP Standard-Setting Framework; and

(g) **meets the AASB's legislative obligations to facilitate comparability** and ensure there are appropriate accounting standards for each entity required to comply with accounting standards. (ASIC Act sections 224 and 229).

152 Option 1 proposals:

(a) **facilitate consistent, comparable transparent and useful financial statements** for entities required to prepare financial statements in accordance with AAS, as:

(i) all publicly accountable entities and those that voluntarily chose to report compliance with IFRS; and

(ii) all other entities would prepare Tier 2 GPFS using Alternative 1 or Alternative 2, with full recognition and measurement, consolidation and equity accounting (where required), and minimum disclosure requirements.

(b) **has the greatest net benefit to users, directors and those charged with governance, preparers, regulators, and auditors**, achieved by:

(i) including disclosures tailored to meet users' needs;

(ii) reducing risks associated with self-assessing whether entities are reporting entities or not, which also ensures a level playing field with more consistent and transparent financial reporting and contributes towards improving the credibility of financial statements and increased stakeholder confidence;

(iii) assisting with Trans-Tasman harmonisation by providing consistent recognition and measurement requirements with NZ; and

(iv) alleviating difficulties with enforcement of reporting requirements by reducing the subjectivity of the underlying criteria.

(c) **allow time for further research and constituent feedback** - the phased approach allows time to conduct further research and outreach to better understand constituents' needs and to provide mitigating actions to alleviate the additional burden for some entities (such as transitional relief, education and support).

How will the AASB evaluate its option?

153 The AASB will evaluate whether to proceed with Option 1 through consultation with constituents such as those consulted through the consultation period with respect to this Consultation Paper (as detailed in Section 3). The AASB has also formed a Conceptual Framework Project Advisory Panel, which will be engaged throughout the evaluation process to ensure Option 1 is appropriately evaluated.

Section 5: Details of the AASB's preferred option, including Tier 2 alternatives, next steps and matters for comment

Details of Phase 1: Short-term approach – maintain IFRS compliance and operate with two conceptual frameworks

154 In Phase 1, the AASB is proposing having two Conceptual Frameworks as outlined below:

(a) a revised AASB *Conceptual Framework* which incorporates the IASB's RCF and is applicable to publicly accountable for-profit entities and others who are voluntarily claiming IFRS compliance; and

(b) the existing AASB *Framework*, applicable to all other entities.

155 This would allow publicly accountable for-profit entities to apply the RCF and therefore remain IFRS compliant. It would also maintain the status quo for other entities, including those that are currently preparing SPFS.

156 As part of the short-term approach, the AASB is proposing amendments to SAC 1 and the following AAS:

(a) AASB 9 *Financial Instruments*;

(b) AASB 14 *Regulatory Deferral Accounts*;

(c) AASB 101 *Presentation of Financial Statements*;

(d) AASB 1048 *Interpretation of Standards*;

(e) AASB 1053 *Application of Tiers of Australian Accounting Standards*; and

(f) AASB 1057 *Application of Australian Accounting Standards*.

157 The proposed amendments – which would become applicable at the same time the consequential amendments in relation to the RCF become applicable (periods beginning 1 January 2020) – will ensure there are no conflicts with AAS when the RCF becomes applicable for publicly accountable for-profit entities, or is adopted earlier.

158 Specific details of the amendments to SAC 1 and the Standards are set out in Appendix A of this Consultation Paper. Detailed analysis of the need to issue the IASB's RCF in Australia to enable publicly accountable for-profit private sector entities currently claiming IFRS compliance to continue to do so is provided in paragraphs 1 to 3 of Appendix C of this Consultation Paper. If the short-term approach is approved by the AASB after consideration of stakeholder views, including responses to the proposed amendments detailed in Appendix A, the AASB does not intend to issue an Exposure Draft with respect to the short-term approach or proposed amendments.

Changes to 'public accountability' definition

159 The term 'public accountability' is defined in AASB 1053 *Application of Tiers of Australian Accounting Standards*. This definition is referenced from the *IFRS for SMEs* Standard. In 2015, the definition of public accountability was revised in *IFRS for SMEs* to the following:

'An entity has public accountability if:

(a) its debt or equity instruments are traded in a public market or it is in the process of issuing such instruments for trading in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets); or

(b) it holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses.'

160 The AASB is proposing amendments to the definition of 'public accountability' in AASB 1053 to align with the revised IASB definition in *IFRS for SMEs*. The AASB is also proposing additional guidance as per *IFRS for SMEs* to clarify the term 'fiduciary capacity', as specified in *IFRS for SMEs*. Refer to Appendix A for amendments.

What happens next in respect to Phase 1?

161 The AASB will consider feedback received on Phase 1 of this Consultation Paper. Based on the information received, the AASB will determine whether the proposals should be finalised in the form of a Standard.

We need your feedback on Phase 1

162 Comments are invited on the proposals in Phase 1 of this Consultation Paper by 9 August 2018. Submissions play an important role in the decisions that the AASB will make. The AASB's preference is 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.

163 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.

Specific matters for comment on Phase 1

164 The AASB would particularly value comments on the proposals in Phase 1 and Appendix A:

(a) **Q1 – Do you agree with the short-term approach to maintain IFRS compliance by introducing the RCF in Australia?**
That is, do you agree that the RCF should be applicable for publicly accountable for-profit entities that are required to prepare Tier 1 GPFS and other entities that are voluntarily reporting compliance with IFRS (who are currently claiming compliance with IFRS), and the existing *Framework* should continue to be applicable to other entities in the short term until the medium term solution is implemented? Please indicate reasons for your response and if you disagree, please provide suggestions for an alternative approach for the AASB to consider.

(b) **Q2 – Do you agree that the short-term approach should be made applicable to both publicly accountable for-profit private sector and public sector entities?**
That is, do you agree that the RCF should be applicable for publicly accountable public sector entities that are required to prepare GPFS in accordance with Tier 1 reporting requirements (who are currently claiming compliance with IFRS) as well? Please indicate reasons for your response and if you disagree please provide suggestions for an alternative approach for the AASB to consider.

(c) **Q3 – Are you aware of publicly accountable for-profit entities currently self-assessing as non-reporting entities and preparing SPFS that will have implications under the AASB's short-term approach?**
If so please provide specific examples including why these entities are not currently applying AASB 1053 and preparing Tier 1 GPFS although they would otherwise meet the definition of public accountability.

(d) **Q4 – Do you agree with the AASB's amendments to the definition of 'public accountability' in AASB 1053 per *IFRS for SMEs* Standard (refer to Appendix A)?**
Please indicate reasons for your response and if you disagree, please provide suggestions for the AASB to consider.

(e) **Q5 – Do you agree with the proposed amendments to SAC 1 *Definition of the Reporting Entity* and the following Australian Accounting Standards, as set out in the Appendix A:**

(i) AASB 9 *Financial Instruments*;

(ii) AASB 14 *Regulatory Deferral Accounts*;

(iii) AASB 101 *Presentation of Financial Statements*;

(iv) AASB 1048 *Interpretation of Standards*;

(v) AASB 1053 *Application of Tiers of Australian Accounting Standards*; and

(vi) AASB 1057 *Application of Australian Accounting Standards*.

General matters for comment on Phase 1

165 The AASB would also value comments on the following general matters with respect to Phase 1:

(a) **Q6 –** Whether the AASB's For-Profit Entity Standard-Setting Framework has been applied appropriately in developing the proposals in Phase 1.

(b) **Q7 –** Whether there are any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals.

(c) **Q8 –** Whether, overall, the proposals would result in financial statements that would be useful to users.

(d) **Q9 –** Whether the proposals are in the best interests of the Australian economy.

(e) **Q10 –** Unless already provided in response to specific 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.

Details of Phase 2: Medium-term approach to apply the RCF to all entities

166 In Phase 2, the AASB is proposing the following medium-term approach:

(a) the RCF will be made applicable to all entities required by legislation or otherwise to comply with AAS;

(b) the Tier 2 framework in AASB 1053 will be revised to include one of the following alternatives (these alternatives are described in more detail in paragraphs 167-170):

(i) Alternative 1: GPFS – Reduced Disclosure Requirements (RDR) – Existing Tier 2 (full recognition and measurement with reduced disclosures from each Accounting Standard, includes consolidation and equity accounting where applicable); or

(ii) Alternative 2: GPFS – Specified Disclosure Requirements (SDR) – New Tier 2 (full recognition and measurement with specified disclosures from some Accounting Standards, includes consolidation and equity accounting where applicable)

(c) Consequential amendments to AASB 1048 *Interpretation of Standards* and other Standards will be required as a result of changes in paragraph 166(a)-(b) (these will be detailed in the next phase of the consultation process, once the alternative for revising Tier 2 has been determined); and transitional relief would be provided for entities moving from SPFS to GPFS and from one tier to another. Refer to Appendix B for illustrative amendments to pronouncements resulting from the AASB's medium-term approach.

Proposed Tier 2 alternatives

167 The AASB proposes that one of the alternatives described in this section should be made available in AASB 1053 as the Tier 2 reporting requirements for GPFS of other entities (other than publicly accountable for-profit private sector entities and those voluntarily reporting compliance with IFRS) after the RCF is made applicable to all entities preparing and lodging financial statements in accordance with the AAS (see paragraph 166).

168 ***Table 3: Details of Alternatives 1 and 2 proposed in Phase 2: Medium-term approach***

Alternative 1: GPFS – Reduced Disclosure Requirements (RDR) – Existing Tier 2	**Alternative 2: GPFS – Specified Disclosure Requirements (SDR) – New Tier 2**
Alternative 1 is the existing Tier 2 RDR under AASB 1053 established in Australia. It requires: • full recognition and measurement requirements of IFRS (as amended for NFP specific issues); • reduced disclosure requirements (minimum disclosures specified in each standard); and • consolidation of subsidiaries (and equity accounting) if the entity is required to prepare consolidated financial statements under AASB 10 *Consolidated Financial Statements*[49].	Alternative 2 is a new GPFS Tier 2 reporting framework, largely based on what is currently required in ASIC's Regulatory Guide 85 *Reporting requirements for non-reporting entities* ('RG 85'), that is for entities currently lodging SPFS with ASIC. It will require: • full recognition and measurement of IFRS (as amended for NFP specific issues); • disclosure Standards currently required by RG 85 (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*); • new disclosure Standards (Related Party Disclosures, Impairment of Assets, Revenue and Income Taxes[50]); and • consolidation of subsidiaries (and equity accounting) if the entity is required to prepare consolidated financial statements under AASB 10[50].

169 ***Table 4: Comparison of advantages of Alternatives 1 and 2***

Alternative 1: GPFS – Reduced Disclosure Requirements (RDR) – Existing Tier 2	**Alternative 2: GPFS – Specified Disclosure Requirements (SDR) – New Tier 2**
(a) Maintains the recognition and measurement requirements of full IFRS which satisfies the requirements in RG 85 and facilitates a 'true and fair view' as required by legislation and regulators (eg ACNC).	(a) Maintains the recognition and measurement requirements with full IFRS, which satisfies the requirements in RG 85 and facilitates a 'true and fair view' as required by legislation and regulators (for example ACNC).
(b) Provides a significant reduction in disclosure requirements compared to full IFRS.	(b) Provides a significant reduction in disclosure requirements compared with full IFRS and will only require specified disclosures for significant matters, (ie related party transactions, impairment, revenue and tax) as requested by users of financial statements (based on targeted feedback received by AASB)[51]. Furthermore, having taxation disclosures would be consistent with Significant Global Entity requirements[52] introduced by the ATO in 2015.

49 AASB 10 paragraph 4 includes an exemption from preparing consolidated financial statements if certain conditions are met (ie if the parent is a wholly- or partially- owned subsidiary and its owners have been informed and do not object to it not preparing consolidated financial statements, it is not traded in a public market place or a listed entity; and its ultimate or intermediate parent prepares publicly available IFRS-compliant consolidated financial statements).

50 The AASB is consulting on these specified disclosures as part of the consultation process to ascertain whether they best meet users' needs.

51 Refer to AASB Discussion Paper *Improving Financial Reporting for Australian Charities* for more details.

52 The significant global entity (SGE) concept determines whether an entity is within the scope of several requirements of the Australian Taxation Office (refer www.ato.gov.au/business/public-business-and-international/significant-global-entities)

Alternative 1: GPFS – Reduced Disclosure Requirements (RDR) – Existing Tier 2	Alternative 2: GPFS – Specified Disclosure Requirements (SDR) – New Tier 2
(c) Requires preparation of consolidated financial statements for entities meeting AASB 10 requirements. (Refer to the AASB's *Australian Financial Reporting Framework* project where a Research Paper is being prepared on consolidation and individual financial statements, which will provide research and background information on why consolidated financial statements are useful in decision-making.)	(c) Would require the preparation of consolidated financial statements for entities meeting the requirements of AASB 10. (Refer to the AASB's *Australian Financial Reporting Framework* project where a Research Paper is being prepared on consolidation and individual financial statements, which will provide research and background information on why consolidated financial statements are useful in decision-making.)
(d) Entities applying this framework do not get to choose what disclosures they want to make (ie the disclosures, though reduced, are clearly specified) meaning there is more transparency, comparability and ability to enforce requirements compared to entities preparing SPFS.	(d) Entities applying this framework would not get to choose what disclosures they want to make (ie the disclosures, though reduced, are clearly specified), meaning there would be more transparency, comparability and ability to enforce requirements compared with entities preparing SPFS.
(e) Includes specific modifications for NFP private and public sector entities (through additional Australian specific paragraphs). These modifications are also available to entities in these sectors that are otherwise applying full IFRS).	(e) This framework would include specific modifications for NFP private and public sector entities (through additional Australian specific paragraphs). These modifications are also available to entities in these sectors that are otherwise applying full IFRS).
(f) Consistent with Tier 2 reporting requirements in NZ (referred to as NZ IFRS RDR).	(f) This alternative would be consistent with Tier 2 recognition and measurement requirements in NZ IFRS RDR.
(g) Ensures comparability with entities preparing full IFRS (due to full recognition and measurement and same types of disclosures as IFRS albeit at a reduced level). This would make it easier to transition to Tier 1 reporting (ie full IFRS) compared to other frameworks; and makes consolidation easier for parent entities that have subsidiaries reporting under this framework.	(g) Similar to Alternative 1, this framework would ensure comparability with entities preparing full IFRS and make it easier to transition to Tier 1 reporting and make consolidation easier for parent entities that have subsidiaries reporting under this framework.
(h) Is established within AASB 1053 which most entities are familiar with and that a number of entities are already applying (ie no change for these entities).	(h) It is anticipated that this framework will be easier to prepare than GPFS – RDR (Alternative 1) as disclosure requirements would be clearly specified as relating to only some standards (for example related parties) (ie preparers will not have to search through all the Standards to determine what disclosures apply to them). That being said, Alternatives 1 and 2 are very similar, just with different approaches to disclosure. (i) There will be minimal additional costs for corporates who are currently preparing SPFS and complying with RG 85, as the main change will be the additional disclosures (and consolidation and equity accounting if any) required under this framework. Noting that this framework is based on existing SPFS guidance with additional disclosure requirements[53] as outlined above.

53 Additional disclosures have been identified based on feedback the AASB has received from users as part of its consultation on the existing RDR framework (refer to Comment letters to AASB ED 277 *Reduced Disclosure Requirements for Tier 2 Entities*) as well as ACNC submissions in relation to its legislative review (refer to ACNC submission).

170 ***Table 5: Comparison of disadvantages of Alternatives 1 and 2***

Alternative 1	**Alternative 2**
GPFS – Reduced Disclosure Requirements (RDR) – Existing Tier 2	**GPFS – Specified Disclosure Requirements (SDR) – New Tier 2**
(a) Some entities previously preparing SPFS but not preparing consolidated or equity accounted financial statements would need to prepare consolidated and equity accounted financial statements.	(a) Some entities previously preparing SPFS but not preparing consolidated or equity accounted financial statements would need to prepare consolidated or equity accounted financial statements.
(b) May be more difficult for preparers to apply (ie to determine what the disclosure requirements are) than Alternative 2 because preparers applying this framework need to examine each accounting Standard to determine the reduced disclosure requirements.	(b) Some entities previously preparing SPFS may not have been complying with all recognition and measurement requirements and therefore could have more transitional costs compared with those already complying with full recognition and measurement requirements.
(c) Contains more onerous disclosure requirements compared with Alternative 2.	(c) Entities currently preparing SPFS would have to provide more disclosures under this framework than what is currently required (as currently these entities only need to comply with the disclosure requirements in AASB 101, AASB 107, AASB 108, AASB 1048 and AASB 1054 as a minimum).
(d) Some entities may consider that if regulators reviewed existing requirements to publicly lodge financial statements they would not be identified as entities requiring public lodgement (ie some requirements have not been reviewed or revised for many years).	(d) Some entities may consider that if regulators reviewed existing requirements to publicly lodge financial statements they would not be identified as entities requiring public lodgement (ie some requirements have not been reviewed or revised for many years).
(e) This framework was established in Australia in 2010 by the AASB. Since then it has not had a large take-up by non-publicly accountable reporting entities required to prepare GPFS. Refer to *Reduced Disclosure Requirements* Project for further analysis of this framework since its establishment.	(e) This framework would have different disclosure requirements to Tier 2 NZ IFRS RDR.

Important considerations for a Tier 2 reporting framework

171 In deciding whether to retain the existing GPFS – RDR – Tier 2 framework or to embrace a new Tier 2 framework, specific consideration should be given to:

(a) **Current legislative requirements**: whether there are any specific legislative or regulatory requirements that define the 'reporting entity' in which case these requirements will also need to be amended when the RCF is made applicable for all entities. The AASB has included a specific matter for comment asking constituents if they are aware of any specific legislative or regulatory requirements that may need amendments. The AASB is also consulting with regulators and policy-makers to research this matter.

(b) **Red-tape reduction**: the Australian Government is committed to reducing red-tape, meaning that each alternative of Tier 2 should be considered from a cost-benefit perspective, while striving to achieve international comparability and more transparency amongst like-entities. As such, when proposing alternatives, the AASB has suggested alternatives that maintain international comparability and transparency (ie Alternatives 1 and 2 maintain the recognition and measurement requirements in IFRS), while reducing the reporting burden of other entities through simplified and reduced disclosures.

(c) **User needs**: when considering user needs, the AASB reflected on the RDR Decision-making Framework[54], including feedback from constituents on that ED[55], together with consideration of what report users need (as outlined in AASB Discussion Paper *Improving Financial Reporting for Australian Charities*). In doing so, the AASB has aimed to balance user needs with the

54 The RDR Decision-making Framework is described in Exposure Draft (ED) 277 *Reduced Disclosure Requirements for Tier 2 Entities* (January 2017)

55 Feedback from constituents on ED 277 is summarised in AASB staff analysis paper *Application of proposed RDR decision-making framework in AASB ED 277 to accounting standards and interpretations – Australian perspective*.

Australian Government's aim to reduce red tape and cost-benefit considerations described in paragraph 171(b) above.

172 It should also be noted that the AASB has not made any recommendations within this Consultation Paper on whether Alternative 1 or 2 is preferred. Instead, the AASB will publish an Exposure Draft after considering feedback received on this Consultation Paper and on similar matters contained in related projects including the AASB's *Australian Financial Reporting Framework* project.

Why *IFRS for SMEs* is not considered a viable Tier 2 Alternative

173 The AASB considered *IFRS for SMEs* as an alternative for Tier 2 and decided not to pursue that alternative at the present time for the reasons outlined in Appendix C paragraphs 18 to 36.

174 Most notable is the fact that *IFRS for SMEs* has different recognition and measurement requirements compared with IFRS. Research undertaken in Research Report No. 1 suggests that more than 75% of entities that need to publicly lodge financial statements in accordance with AAS are currently complying with recognition and measurement requirements of AAS[56] (which is based on IFRS). Therefore moving away from this to *IFRS for SMEs* would result in additional costs with reduced benefits.

175 Furthermore, *IFRS for SMEs* could be inconsistent with ASIC's view on what is required to provide a true and fair view per RG 85 and also makes it more difficult for subsidiaries required to consolidate into parent entity's consolidated financial statements, which are based on IFRS.

176 Regulation Impact Statement *Reducing the Financial Reporting Burden: a second tier of requirements for general purpose financial statements* sets out a more in-depth discussion on *IFRS for SMEs* and why the AASB chose not to adopt this framework in Australia (June 2010). The AASB does not consider that these factors have substantially changed since that time.

177 AASB staff have published a Staff Paper *Comparison of Standards for Smaller Entities* summarising the simplified recognition and measurement frameworks currently available in a number of international jurisdictions. For example, the paper covers frameworks in the United Kingdom and NZ and compare them with *IFRS for SMEs* and AASB Standards. The paper indicates there are a number of modifications made by *IFRS for SMEs* to IFRS – notably that the new standards on revenue, financial instruments, and leases – have not been included.

178 Adoption of *IFRS for SMEs* would mean every entity not currently preparing Tier 1 financial statements would have to modify their current recognition and measurement criteria to SMEs, and that those entities currently preparing SPFS would have to significantly increase their disclosures. Subsidiaries of consolidated entities would then have to provide amended information for consolidation purposes.

179 The IASB is undertaking research on SMEs that are subsidiaries to feed into its next comprehensive review of *IFRS for SMEs* Standard. As part of this research, the IASB is expected to consider whether full recognition and measurement is needed for SME subsidiaries that are being consolidated into group financial statements prepared in accordance with full IFRS, and if so, what reduced disclosures are required. The AASB will closely monitor this project as, should it progress quickly enough, it is expected to be similar in outcomes to both Alternatives 1 and 2 and accordingly, likely to be suitable for adoption in Australia.

Why a Tier 3 reporting framework was not considered as part of this project

180 The AASB is not proposing a Tier 3 reporting framework as part of this Consultation Paper. Through its *Australian Financial Reporting Framework* project, the AASB is strongly encouraging regulators, government policy makers and key stakeholders to determine which entities should lodge GPFS and the criteria for different Tiers of GPFS as they are better positioned to do this. Through the same project, the AASB is working to provide general purpose reporting requirements options for the different Tiers, once the criteria for entities reporting in the different Tiers has been determined.

181 The determination of which entities would be reporting under Tiers 1 and 2 in Australia is currently based on the criterion of 'public accountability' (which is consistent with the IASB). The introduction of a third tier requires a concept different to public accountability and would likely differ by sector (see AASB Discussion Paper *Improving Financial Reporting for Australian Charities*).

182 As noted, the AASB Staff Paper *Comparison of Standards for Smaller Entities* summarises the simplified recognition and measurement frameworks currently available in a number of international jurisdictions that could be considered when exploring the options for additional Tiers of GPFS.

56 Refer to Appendix C, paragraphs 37-61 for a more detailed discussion on this matter.

Additional considerations – service performance reporting, fundraising and administration cost disclosures

183 A specific matter for comment has been included in paragraph 195(i) that asks constituents if service performance reporting, fundraising and administration cost disclosures should be included as part of the mandatory requirements within the chosen Tier 2 Alternative applicable to NFP private sector entities.

184 The ACNC and other charity stakeholders have identified that fundraising and administrative costs are not clearly disclosed in financial reports due to the lack of consistent definitions and guidance. AASB outreach confirmed that donors and grantors to charities require reporting of services delivered using the funds provided.

185 The AASB will work closely with the ACNC, state and territory regulators and charity stakeholders to determine what additional information may be required in financial reports or supplemental reports to address fundraising and service performance reporting issues. The AASB will also progress its project on Service Performance Reporting, following the New Zealand External Reporting Board's recent issuance of Public Benefit Entity Financial Reporting Standard 48 *Service Performance Reporting*, to see how this might be tailored for Australia.

Grandfathered proprietary company lodgement relief unchanged by these proposals

186 Certain proprietary companies ('grandfathered' companies) are exempt from lodging their audited financial reports with ASIC (provided they meet certain conditions) by virtue of s1408 of the Corporations Act. Proposals in this Consultation Paper will not change the public lodgement exemption. Companies that are currently required to prepare financial statements in accordance with AAS however would not be able to prepare SPFS after the medium-term approach takes effect.

Will there be any special purpose financial statements options?

187 The removal of SPFS will only apply where public lodgement of financial statements is required, or where legislation, constitutional documents or grant acquittals require preparation of financial statements in accordance with AAS. Where trust deeds or other constituent documents only require the preparation of financial statements, then trustees/directors and those charged with governance will have the option of preparing those financial statements as 'special purpose' financial statements, being for beneficiary use.

188 The AASB is aware of legislation that refers to SPFS and will work with the relevant regulator to determine the implications of these proposed changes for that legislation. The AASB has included a specific matter for comment requesting information on what legislation might be impacted by these proposals.

Will the requirement to prepare consolidated financial statements affect how entities apply the small/large proprietary company test in the Corporations Act 2001?

189 The proposed requirements for entities to prepare consolidated financial statements would not affect how entities would apply the thresholds in legislation (for example the large and small proprietary company test in the Corporations Act) to determine 'who' is required to publicly lodge financial statements. Specifically, Section 45A of the Corporations Act 2001[57] requires thresholds to be based on a consolidated basis in accordance with the accounting standards even if the standards do not otherwise apply to the company. There is no change to this requirement as a result of these proposals.

What would the revised framework look like after implementation of Option 1?

190 Diagrams 2 and 3 below depict the Australian Financial Reporting Framework before and after adopting the AASB's proposed Two-phased approach to applying the IASB's RCF

57 Refer Section 45A *Corporations Act 2001*.

Diagram **2 Current reporting framework**

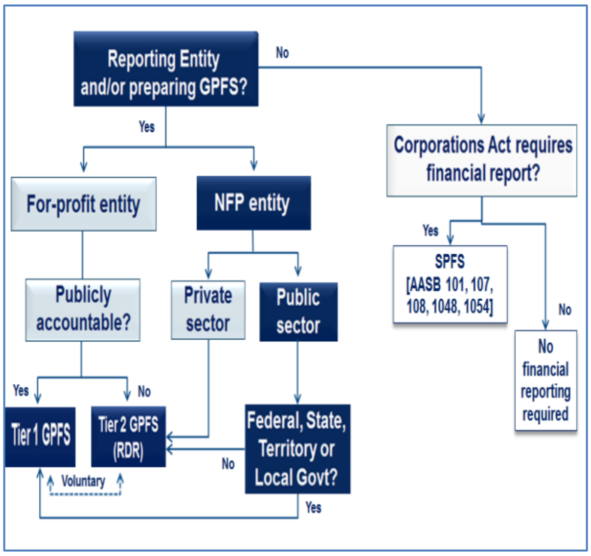
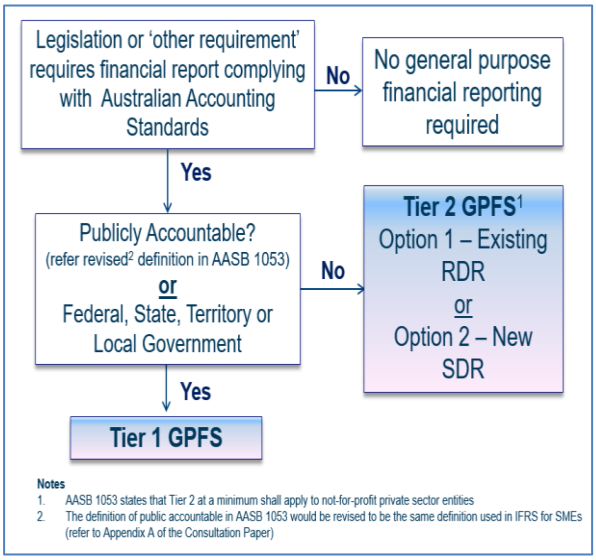


Diagram 3 Revised simplified reporting framework



What happens next with respect to Phase 2?

191 The AASB will consider feedback received on Phase 2 of this Consultation Paper at future meetings and based on the information received and with consideration of feedback received in relation to the *Australian Financial Reporting Framework* project will determine when and how the medium-term approach should be pursued. The next phase will include development of an Exposure Draft with more specific proposals on the Tier 2 GPFS, including transition provisions, to enable further consultation with stakeholders. The AASB will particularly review the outcomes of the ACNC legislative review process in determining how to proceed with these proposals for the NFP private sector

We need your feedback on Phase 2

192 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.

193 The AASB also values feedback received at its roundtables and individual discussions with constituents. All such feedback is collated and reviewed by the Board

194 Comments are invited on the proposals in Phase 2 of this Consultation Paper by 9 November 2018.

Specific matters for comment on Phase 2

195 The AASB would particularly value comments with respect to Phase 2:

(a) **Q11 – Do you agree with the AASB's Phase 2 approach (described in paragraph 166)?** Why or why not?

(b) **Q12 – Which of the AASB's two GPFS Tier 2 alternatives (described in paragraphs 167-170) do you prefer?** Please provide reasons for your preference.

(c) **Q13 – Do you agree that we only need one Tier 2 GPFS alternative in Australia (either Alternative 1 GPFS – RDR or the new Alternative 2 GPFS – SDR described in paragraphs 167-170)?** Why or why not?

(d) **Q14 – Do you agree with the AASB's decision that GPFS – *IFRS for SMEs* (outlined in Appendix C paragraphs 18 to 36) should not be made available in Australia as a Tier 2 alternative for entities to apply?** Please give reasons to support your response, including applicability for the for-profit and not-for-profit sectors.

(e) **Q15 – If the AASB implements one of the two proposed alternatives (described in paragraphs 167-170) as a GPFS Tier 2, what transitional relief do you think the AASB should apply (in addition to what is available in AASB 1) Should AASB 1 be applied, or simpler relief provided?** Please provide specific examples and information.

(f) **Q16 – What concerns do you have on consolidating subsidiaries and equity accounting associates and joint ventures as proposed in the AASB's medium-term approach? What transitional relief do you think the AASB should apply?** Please provide specific examples and information.

(g) **Q17 – If the new Alternative 2 GPFS – SDR described in paragraphs 167-170) is applied, do you agree that the specified disclosures would best meet users' needs?** If not, please explain why and provide examples of other disclosures that you consider useful.

(h) **Q18 – Do you have any other suggested alternatives for the AASB to consider as a GPFS Tier 2 and whether this would be applicable for for-profit and not-for-profit sectors?** Please explain rationale (including advantages and disadvantages and the costs and benefits expected).

(i) **Q19 – Do you think service performance reporting, fundraising and administration cost disclosures for NFP private sector entities should be included as part of the chosen GPFS Tier 2 alternative?** Please explain rationale (including advantages and disadvantages).

Q20 – Are you aware of any legislation that refers to SPFS that might be impacted by these proposals? If yes, please provide specific information.

General matters for comment on Phase 2

196 The AASB would also value comments on the following general matters with respect to this Consultation Paper:

(a) **Q21 –** Whether *The AASB's Standard-Setting Frameworks for For-Profit and Not-for-Profit Entities* have been applied appropriately in developing the proposals in Phase 2 regarding the reporting entity problem (note the AASB will consult further on other NFP amendments required for the RCF).

(b) **Q22 –** Whether there are any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals.

(c) **Q23 –** Whether, overall, the proposals would result in financial statements that would be useful to users.

(d) **Q24 –** Whether the proposals are in the best interests of the Australian economy.

(e) **Q25 –** Unless already provided in response to specific 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.

APPENDIX A

Proposed amendments to pronouncements resulting from Phase 1

Preface

1 This Appendix includes proposed amendments to Australian Accounting Standards and Statement of Accounting Concepts that would enable application of the revised *Conceptual Framework* by publicly accountable for-profit entities and by other for-profit entities that elect to apply the revised *Conceptual Framework*. The AASB would also have to amend references in Australian Accounting Standards to the *Conceptual Framework* for these entities, based on the IASB's consequential amendments set out in the IFRS Standard *Amendments to References to the Conceptual Framework in IFRS Standards*.

2 If the short-term approach is approved by the AASB after consideration of stakeholder views, including responses to the proposed amendments detailed in this Appendix, the AASB does not intend to issue an Exposure Draft with respect to the short-term approach or these proposed amendments.

3 This Appendix uses underlining to identify new text and striking out to indicate deleted text, in order to make the proposed amendments more understandable.

4 Ellipses (…) are used to help provide the context within which amendments are proposed and also to indicate text that is not proposed to be amended.

Amendments to AASB 9 *Financial Instruments*

Paragraph Aus1.1 is amended.

Chapter 1 Objective and application

…

Aus1.1 This Standard 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;

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

(c) financial statements that are, or are held out to be, general purpose financial statements<u>; and</u>

<u>(d)</u> <u>for-profit entities that have public accountability that are required to comply with Australian Accounting Standards</u>.

Amendments to AASB 14 *Regulatory Deferral Accounts*

Paragraph Aus4.1 is amended.

Application

Aus4.1 This Standard 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;

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

(c) financial statements that are, or are held out to be, general purpose financial statements<u>; and</u>

<u>(d)</u> <u>for-profit entities that have public accountability that are required to comply with Australian Accounting Standards</u>.

Amendments to AASB 101 *Presentation of Financial Statements*

The definition of reporting entity in paragraph Aus7.2 is deleted.

Appendix A

Australian defined terms

…

Aus7.2 In respect of public sector entities, *local governments*, *governments* and most, if not all, *government departments* are reporting entities:

~~***reporting entity* means an entity in respect of which it is reasonable to expect the existence of users who rely on the entity's general purpose financial statement 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.**~~

***government* means …**

Amendments to AASB 1048 *Interpretation of Standards*

In paragraph 10, a new row is added to Table 3: Australian conceptual framework pronouncements.

Conceptual framework

10 Each reference to the *Framework for the Preparation and Presentation of Financial Statements* (or *Framework*) in other Australian Accounting Standards (including Interpretations) is taken to be a reference to the relevant pronouncement listed in Table 3 below. Each row in Table 3 is to be treated as a separate provision of this Standard.

Table 3: Australian conceptual framework pronouncements

Issue Date	**Title**	**Application Date** (annual reporting periods)
<u>[date 2018]</u>	<u>Conceptual Framework for Financial Reporting</u> <u>Note – this pronouncement is applicable only to for-profit entities that have public accountability that are required to comply with Australian Accounting Standards and other for-profit entities that elect to apply this Framework</u>	<u>(beginning)</u> <u>…[date]</u>
June 2014 [as amended to]	Framework for the Preparation and Presentation of Financial Statements (or Framework)	(beginning) 1 July 2014

Amendments to AASB 1053 *Application of Tiers of Australian Accounting Standards*

Paragraphs 2 and 9 and Appendix A are amended. Paragraphs B3 and B4 are added in Appendix B.

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*;**

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

(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 entities that have public accountability that are required to comply with Australian Accounting Standards.**

…

Tiers of Reporting Requirements

…

9 Tier 2 comprises the recognition and measurement requirements of Tier 1 (including consolidation and the equity method of accounting) but substantially reduced disclosure requirements. Except for the presentation of a third statement of financial position under Tier 1[2], the presentation requirements under Tier 1 and Tier 2 are the same.

…

Appendix A
Defined Terms

…

Public accountability ~~means accountability to those existing and potential resource providers and others external to the entity who make economic decisions but are not in a position to demand reports tailored to meet their particular information needs.~~

~~A for-profit private sector~~ – an entity has public accountability if:

(a) its debt or equity instruments are traded in a public market or it is in the process of issuing such instruments for trading in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets); or

(b) it holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses. ~~This is typically the case for banks, credit unions, insurance companies, securities brokers/dealers, mutual funds and investment banks.~~

Reporting entity means 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.

The reporting entity definition is not relevant to:

(a) for-profit entities that have public accountability that are required to comply with Australian Accounting Standards; and

(b) other for-profit entities that elect to apply the *Conceptual Framework for Financial Reporting* and the consequential amendments to other pronouncements set out in AASB 2018-X *Amendments to Australian Accounting Standards – References to the Conceptual Framework*.

Appendix B
Public Accountability

…

B3 Some entities may also hold assets in a fiduciary capacity for a broad group of outsiders because they hold and manage financial resources entrusted to them by clients, customers or members not involved in the management of the entity. However, if they do so for reasons incidental to a primary business (as, for example, may be the case for travel or real estate agents, schools, charitable organisations, co-operative enterprises requiring a nominal membership deposit and sellers that receive payment in advance of delivery of the goods or services such as utility companies), that does not make them publicly accountable.

B4 Examples of entities that hold assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses are most likely to include banks, credit unions, insurance companies, securities brokers/dealers, mutual funds and investment banks.

Amendments to AASB 1057 Application of Australian Accounting Standards

Paragraphs 2, 5-9, 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; ~~and~~

(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 entities that have public accountability that are required to comply with Australian Accounting Standards.

…

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; ~~and~~

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

(d) for-profit entities that have public accountability that are required to comply with Australian Accounting Standards.

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; ~~and~~

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

(d) for-profit entities that have public accountability that are required to comply with Australian Accounting Standards.

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; ~~and~~

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

(d) for-profit entities that have public accountability that are required to comply with Australian Accounting Standards.

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; ~~and~~

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

<u>(d)</u> <u>for-profit entities that have public accountability that are required to comply with Australian Accounting Standards</u>.

9 AASB 133 *Earnings per Share* applies to<u>:</u>

(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<u>; and</u>

<u>(b)</u> <u>for-profit 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</u>.

...

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; ~~or~~

(e) prepares financial statements that are, or are held out to be, general purpose financial statements<u>; or</u>

<u>(f)</u> <u>is a for-profit entity that has public accountability that is required to comply with Australian Accounting Standards</u>.

…

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; ~~and~~

(d) financial statements of GGSs prepared in accordance with AASB 1049<u>; and</u>

<u>(e)</u> <u>for-profit entities that have public accountability that are required to comply with Australian Accounting Standards</u>.

...

20 AASB 1056 *Superannuation Entities* applies to:

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

(b) financial statements of a superannuation entity that are held out to be general purpose financial statements<u>; and</u>

<u>(c)</u> <u>each for-profit superannuation entity that has public accountability that is required to comply with Australian Accounting Standards</u>.

...

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; ~~and~~

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

(d) each for-profit entity that has public accountability that is required to comply with Australian Accounting Standards.

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; ~~and~~

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

(d) each for-profit entity that has public accountability that is required to comply with Australian Accounting Standards.

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; ~~and~~

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

(d) each for-profit superannuation plan that has public accountability that is required to comply with Australian Accounting Standards.

…

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; ~~and~~

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

(d) each for-profit entity that has public accountability that is required to comply with Australian Accounting Standards.

…

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.

The reporting entity definition is not relevant to:

(a) for-profit entities that have public accountability that are required to comply with Australian Accounting Standards; and

(b) other for-profit entities that elect to apply the *Conceptual Framework for Financial Reporting* and the consequential amendments to other pronouncements set out in AASB 2018-X *Amendments to Australian Accounting Standards – References to the Conceptual Framework*.

Amendments to SAC 1 *Definition of the Reporting Entity*

Paragraph 2A is added.

Application and Operative Date

…

2A This Statement does not apply in relation to reporting periods beginning on or after …[date] to:

(a) for-profit entities that have public accountability that are required to comply with Australian Accounting Standards; and

(b) other for-profit entities that elect to apply the *Conceptual Framework for Financial Reporting* and the consequential amendments to other pronouncements set out in AASB 2018-X *Amendments to Australian Accounting Standards – References to the Conceptual Framework*.

APPENDIX B

Illustrative amendments to pronouncements resulting from Phase 2

Preface

1 This Appendix illustrates amendments to Australian Accounting Standards and Statement of Accounting Concepts that would enable application of the revised *Conceptual Framework* by all entities resulting from the AASB's medium-term approach. It has been included purely for illustrative purposes. It is not intended to depict the final or complete outcome and would be subject to changes resulting from feedback from constituents on the AASB's medium-term approach. The details of revisions to the following amendments and any additional amendments would be included in an Exposure Draft if the AASB's medium-term approach is to be implemented.

2 In putting the revised *Conceptual Framework* in place, references to the *Framework for the Preparation and Presentation of Financial Statements* would be amended to the *Conceptual Framework for Financial Reporting* in Australian Accounting Standards as required, based on the IASB's consequential amendments set out in the IFRS Standard *Amendments to References to the Conceptual Framework in IFRS Standards*.

3 This Appendix uses underlining to identify new text and striking out to indicate deleted text, in order to make the proposed amendments more understandable.

4 Ellipses (…) are used to help provide the context within which amendments are proposed and also to indicate text that is not proposed to be amended.

Amendments to AASB 9 *Financial Instruments*

Paragraph Aus1.1 is amended.

Chapter 1 Objective and application

…

Aus1.1 This Standard 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~~; <u>and</u>

(b) ~~general purpose~~ financial statements ~~of each other reporting entity~~ <u>that are required to comply with Australian Accounting Standards</u>~~;~~

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

~~(d) for-profit entities that have public accountability that are required to comply with Australian Accounting Standards.~~

Amendments to AASB 14 *Regulatory Deferral Accounts*

Paragraph Aus4.1 is amended.

Application

Aus4.1 This Standard 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~~; <u>and</u>

(b) **~~general purpose~~ financial statements ~~of each other reporting entity~~ that are required to comply with Australian Accounting Standards~~;~~**

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

~~**(d) for-profit entities that have public accountability that are required to comply with Australian Accounting Standards.**~~

Amendments to AASB 101 *Presentation of Financial Statements*

Paragraph Aus7.2 in Appendix A is amended.

Appendix A

Australian defined terms

…

Aus7.2 ~~**In respect of public sector entities, *local governments*, *governments* and most, if not all, *government departments* are reporting entities:**~~

government **means …**

Amendments to AASB 1048 *Interpretation of Standards*

Paragraphs 1, 10 and 11 are amended.

Objective

1 The objective of this Standard is to provide an up-to-date listing of Australian Interpretations and to ensure the effectiveness of references in Australian Accounting Standards to Australian Interpretations and to the ~~*Framework for the Preparation and Presentation of Financial Statements (Framework)*~~ *Conceptual Framework for Financial Reporting* (*Conceptual Framework*). AASB and UIG Interpretations are referred to collectively in this Standard as Australian Interpretations.

…

Conceptual framework

10 **Each reference to the ~~*Framework for the Preparation and Presentation of Financial Statements* (or *Framework*)~~ *Conceptual Framework for Financial Reporting* (or *Conceptual Framework*) in other Australian Accounting Standards (including Interpretations) is taken to be a reference to the relevant pronouncement listed in Table 3 below. Each row in Table 3 is to be treated as a separate provision of this Standard.**

Table 3: Australian conceptual framework pronouncements

Issue Date	**Title**	**Application Date** (annual reporting periods)
…[date]	Conceptual Framework for Financial Reporting	(beginning) …[date]
~~[date 2018]~~	~~Conceptual Framework for Financial Reporting~~ ~~Note – this pronouncement is applicable only to for-profit entities that have public accountability that are required to comply with Australian Accounting Standards and other for-profit entities that elect to apply this Framework~~	~~(beginning) …[date]~~

Table 3: Australian conceptual framework pronouncements

Issue Date	**Title**	**Application Date** (annual reporting periods)
~~June 2014~~ ~~[as amended to]~~	~~Framework for the Preparation and Presentation of Financial Statements (or Framework)~~	~~(beginning)~~ ~~1 July 2014~~

11 This Standard updates references to the <u>*Conceptual*</u> *Framework* in Australian Accounting Standards (including Interpretations) to the relevant amended version of the <u>*Conceptual*</u> *Framework*. The principal application date listed in each row of Table 3 is a reference to annual reporting periods beginning or ending (as indicated) on or after the date specified. An entity may elect to apply an amended version of the pronouncement to annual reporting periods in advance of that stated in Table 3, subject to any early application paragraphs.

Amendments to AASB 1053 *Application of Tiers of Australian Accounting Standards*

Paragraph 2 and Appendix A are amended.

Application

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~~ <u>that are required to comply with Australian Accounting Standards</u>; <u>and</u>

(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 entities that have public accountability that are required to comply with Australian Accounting Standards~~.

Appendix A
Defined terms

…

~~***General purpose financial statements*** are those intended to meet the needs of users who are not in a position to require an entity to prepare reports tailored to their particular information needs.~~

…

~~***Reporting entity*** means 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.~~

~~The reporting entity definition is not relevant to:~~

~~(a)~~ ~~for-profit entities that have public accountability that are required to comply with Australian Accounting Standards; and~~

~~(b)~~ ~~other for-profit entities that elect to apply the *Conceptual Framework for Financial Reporting* and the consequential amendments to other pronouncements set out in AASB 2018-X *Amendments to Australian Accounting Standards – References to the Conceptual Framework*.~~

Amendments to AASB 1057 *Application of Australian Accounting Standards*

Paragraphs 2, 5, 6, 8-12, 14-20 and 22-26 are amended. Paragraph 7 and the Appendix are deleted.

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*~~ <u>that are required to comply with Australian Accounting Standards</u>; <u>and</u>

~~(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 entities that have public accountability that are required to comply with Australian Accounting Standards~~.

…

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~~; <u>and</u>

(b) ~~general purpose~~ financial statements ~~of each other reporting entity~~ <u>that are required to comply with Australian Accounting Standards</u>~~;~~

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

~~(d) for-profit entities that have public accountability that are required to comply with Australian Accounting Standards~~.

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~~; <u>and</u>

(b) ~~general purpose~~ financial statements of each other for-profit ~~reporting~~ entity <u>that are required to comply with Australian Accounting Standards</u>~~;~~

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

~~(d) for-profit entities that have public accountability that are required to comply with Australian Accounting Standards~~.

7 <u>[Deleted]</u> ~~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 entities that have public accountability that are required to comply with Australian Accounting Standards.~~

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~~; <u>and</u>

(b) ~~general purpose~~ financial statements of each other for-profit ~~reporting~~ entity that are required to comply with Australian Accounting Standards~~;~~

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

~~(d)~~ ~~for-profit entities that have public accountability that are required to comply with Australian Accounting Standards~~.

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 entities that have public accountability and are required to prepare financial reports in accordance with Part 2M.3 of the Corporations Act or discloses 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; and

(b) interim financial reports that are ~~general purpose financial statements of each other reporting entity~~ required to comply with Australian Accounting Standards~~; and~~

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

11 AASB 1004 *Contributions* applies to:

(a) each not-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 not-for-profit entity that ~~is a reporting entity~~ are required to comply with Australian Accounting Standards; and

(c) ~~financial statements of not-for-profit entities that are, or are held out to be, general purpose financial statements; and~~

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

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; or

(d) ~~is an other reporting entity and~~ prepares ~~general purpose~~ financial statements that are required to comply with Australian Accounting Standards~~;~~

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

~~(f)~~ ~~is a for-profit entity that has public accountability that is required to comply with Australian Accounting Standards~~.

…

14 AASB 1049 applies to each government's whole of government ~~general purpose~~ financial statements that are required to comply with Australian Accounting Standards and GGS financial statements.

15 AASB 1050 *Administered Items* applies to ~~general purpose~~ financial statements of government departments that are required to comply with Australian Accounting Standards.

16 AASB 1051 *Land Under Roads* applies to ~~general purpose~~ financial statements of local governments, government departments and whole of governments that are required to comply with Australian Accounting Standards, and financial statements of GGSs.

17 AASB 1052 *Disaggregated Disclosures* applies to ~~general purpose~~ financial statements of local governments and government departments that are required to comply with Australian Accounting Standards.

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~~ <u>that are required to comply with Australian Accounting Standards</u>; <u>and</u>

(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)~~ ~~each for-profit entity that has public accountability that is required to comply with Australian Accounting Standards~~.

19 **AASB 1055 *Budgetary Reporting* applies to:**

(a) whole of government ~~general purpose~~ financial statements of each government <u>that are required to comply with Australian Accounting Standards</u>;

(b) financial statements of each government's GGS; <u>and</u>

(c) ~~general purpose~~ financial statements of each not-for-profit ~~reporting~~ entity within the GGS <u>that are required to comply with Australian Accounting Standards</u>~~; and~~

~~(d)~~ ~~financial statements of each not-for-profit entity within the GGS that are, or are held out to be, general purpose financial statements~~.

20 **AASB 1056 *Superannuation Entities* applies to~~:~~**

~~(a)~~ ~~general purpose~~ financial statements of each superannuation entity ~~that is a reporting entity~~ <u>that are required to comply with Australian Accounting Standards</u>~~;~~

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

~~(c)~~ ~~general purpose financial statements of each for-profit superannuation entity that has public accountability that is required to comply with Australian Accounting Standards~~.

…

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~~; <u>and</u>

(b) ~~general purpose~~ financial statements ~~of each other reporting entity~~ <u>that are required to comply with Australian Accounting Standards</u>~~;~~

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

~~(d)~~ ~~each for-profit entity that has public accountability that is required to comply with Australian Accounting Standards~~.

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~~; <u>and</u>

(b) ~~general purpose~~ financial statements of each other for-profit ~~reporting~~ entity <u>that are required to comply with Australian Accounting Standards</u>~~;~~

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

~~(d)~~ ~~each for-profit entity that has public accountability that is required to comply with Australian Accounting Standards~~.

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~~; <u>and</u>

(b) ~~general purpose~~ financial statements of each other superannuation plan ~~that is a reporting entity~~ <u>that are required to comply with Australian Accounting Standards</u>~~;~~

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

~~(d)~~ **~~each for-profit superannuation plan that has public accountability that is required to comply with Australian Accounting Standards~~.**

25 **Interpretation 1038 *Contributions by Owners Made to Wholly-Owned Public Sector Entities* applies to public sector entities 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~~; <u>and</u>**

(b) **~~general purpose~~ financial statements ~~of each other reporting entity~~ <u>that are required to comply with Australian Accounting Standards</u>~~; and~~**

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

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~~; <u>and</u>**

(b) **~~general purpose~~ financial statements ~~of each other reporting entity~~ <u>that are required to comply with Australian Accounting Standards</u>~~;~~**

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

~~(d)~~ **~~each for-profit entity that has public accountability that is required to comply with Australian Accounting Standards~~.**

…

~~Appendix~~
~~Defined terms~~

~~This appendix is an integral part of AASB 1057.~~

~~general purpose financial statements~~

~~Financial statements that are intended to meet the needs of users who are not in a position to require an entity to prepare reports tailored to their particular information needs.~~

~~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.~~

~~The reporting entity definition is not relevant to:~~

~~(a)~~ ~~for-profit entities that have public accountability that are required to comply with Australian Accounting Standards; and~~

~~(b)~~ ~~other for-profit entities that elect to apply the *Conceptual Framework for Financial Reporting* and the consequential amendments to other pronouncements set out in AASB 2018-X *Amendments to Australian Accounting Standards – References to the Conceptual Framework*.~~

Withdrawal of SAC 1 *Definition of the Reporting Entity*

The Board withdraws SAC 1.

APPENDIX C

Detailed analysis of issues with incorporating the IASB's RCF in Australia

This Appendix provides additional background information and support for issues detailed throughout the main body of this Consultation Paper.

Applying the IASB's RCF in Australia

Maintaining IFRS compliance

1 To maintain IFRS compliance for publicly accountable for-profit private sector entities in Australia, the AASB has to issue the IASB's RCF in Australia. This is because paragraph 11, and the related footnote 3 in AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*, state that when applying judgement in developing and applying accounting policies, management shall refer to the existing *Framework*.

2 To maintain IFRS compliance for publicly accountable for-profit private sector entities, this paragraph needs to be amended to refer to a revised AASB *Framework*, which incorporates the IASB's RCF. This would align with the FRC's strategic directive that requires the AASB to adopt accounting standards that are the same as those issued by the IASB for such entities.

3 Paragraph 12 of AASB 108 permits management to also "consider the most recent pronouncements of other standard-setting bodies that use a similar conceptual framework … to the extent that these do not conflict with the sources in paragraph 11", being AAS and the RCF. The RCF however, conflicts with the existing *Framework* as it introduces new topics and concepts (for example Measurement and the 'Reporting Entity' – discussed in more detail below). It also provides revised and updated guidance on several other areas like recognition of assets and liabilities. As such, if references in AAS, for example AASB 108, are not updated to refer to the RCF, there would be non-compliance with IFRS Standards.

The 'reporting entity' issue

Reporting entity in RCF versus Australian accounting requirements

4 As mentioned, the RCF has a chapter on 'Financial Statements and the Reporting Entity' that defines a 'reporting entity' differently from the notion of 'reporting entity' referred to in current AAS.

5 Paragraph 3.10 in the RCF defines a reporting entity as *'…an entity that is required, or chooses, to prepare financial statements. A reporting entity can be a single entity or a portion of an entity or can comprise more than one entity. A reporting entity is not necessarily a legal entity*.' In other words, according to the RCF**,** an entity that prepares financial statements is a reporting entity and the financial statements of reporting entities could differ based on the 'boundary' of economic activities included in their financial statements (ie a reporting entity's financial statements could be consolidated financial statements, single entity financial statements or part of an entity's financial statements).

6 The term 'reporting entity' in some AAS, eg AASB 1057 *Application of Australian Accounting Standards* and AASB 1053 *Application of Tiers of Australian Accounting Standards*, refers to entities required to prepare GPFS because they have users who depend on the GPFS to make decisions. This concept was introduced in Australia in 1990 through the publication of SAC 1. SAC 1 created a notion of differential reporting in Australia by distinguishing reporting entities from non-reporting entities.

7 The use of the term 'reporting entity' in AAS is consistent with the definition of 'general purpose financial statements' in IAS 1 *Presentation of Financial Statements* which states that "General purpose financial statements (referred to as 'financial statements') are those intended to meet the needs of users who are not in a position to require an entity to prepare reports tailored to their particular information needs."

8 IAS 1 does not determine *who* needs to prepare GPFS, and neither do any other IFRS Standards. The IASB relies on regulators of the jurisdictions that adopt IFRS to specify which entities should prepare GPFS through legislation. As noted in the RCF's basis for conclusions paragraph BC3.13, the IASB stated it does not have the authority to determine who must, should, or could prepare such statements. Accordingly, anyone required to prepare financial statements in accordance with IFRS is preparing GPFS.

9 The AASB, like the IASB, does not consider that it has the authority to determine who must, should, or could prepare such statements. The AASB's role is to determine the appropriate accounting framework

and standards that should apply. In other words, anyone that is required to prepare financial statements in accordance with AAS should be preparing GPFS. The concepts in SAC 1 will remain helpful for other regulators in determining who should publicly lodge financial statements, however should not remain available for use by individual preparers.

10 In Australia, current legislation generally requires specified entities to prepare financial statements in accordance with AAS. The reporting entity concept is given effect by AASB 1057, which only requires 'reporting entities' to prepare GPFS. If an entity self-assesses (via the criteria in SAC 1) not to be a reporting entity, it can elect to prepare SPFS, that need not comply with AAS (other than a limited number[1]).

11 AASB 1053 sets out that there are currently two tiers of GPFS with both requiring compliance with all recognition and measurement requirements of AAS, but different levels of disclosure. AASB 1053 distinguishes those entities required to prepare full GPFS (Tier 1), and those entities which may elect to prepare GPFS with reduced disclosures requirements (Tier 2) based on the IASB's concept of 'public accountability'. Accordingly, in Australia, there has been no presumption that regulators requiring preparation of financial statements require those financial statements to be GPFS.

12 Therefore, references to 'reporting entity' in some AAS like AASB 1057 and AASB 1053 address the questions of who should report GPFS rather than *what is the boundary* of the GPFS. As such, the use of the term 'reporting entity' in these AAS is different to what is used in the RCF (and also the International Public Sector Accounting Standards Board (IPSASB)'s *Conceptual Framework*).

IPSASB's use of the term reporting entity

13 The *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities*, published in 2014 by the IPSASB, states the key characteristics of a public sector reporting entity are:

(a) that it is an entity that raises resources from, or on behalf of, constituents and/or uses resources to undertake activities for the benefit of, or on behalf of, those constituents; and

(b) there are service recipients or resource providers dependent on GPFS of the entity for information for accountability or decision-making purposes.

This is consistent with how the term is currently used in SAC 1 and AASB 1053. However, because the AAS are based on IFRS, it is necessary to for the AASB to align the AAS to the IASB's RCF and the definition of reporting entity contained within the RCF.

Why do we need to move to the reporting entity concept in the RCF?

14 In Australia, entities across all sectors who prepare financial statements in accordance with AAS are applying a single suite of AAS (which is based on IFRS).

15 The *Conceptual Framework* describes the objective and concepts for general purpose financial reporting. Its purpose is to assist:

(a) standard-setters develop Standards that are based on consistent concepts;

(b) preparers to develop consistent accounting policies when no Standard applies to a particular transaction or event, or when a Standard allows a choice of accounting policy; and

(c) all parties to understand and interpret the Standards.

16 Having two Conceptual Frameworks, particularly in the medium to longer term, for a single suite of AAS that is applied by entities across all sectors and tiers of reporting would be untenable because the AAS (particularly when they are superseded, revised or amended) will be based on the RCF. Therefore, if entities apply the existing *Framework* to develop accounting policies or interpret the AAS, they are likely to develop inappropriate accounting policies, account for transactions incorrectly and/or wrongly interpret the AAS, which could result in inaccuracies in financial reporting.

17 The term 'reporting entity' (as defined in the RCF) is currently used within a number of AAS (including AASB 3 *Business Combinations*, AASB 7 *Financial Instruments: Disclosures*, AASB 9 *Financial Instruments* and AASB 12 *Disclosures of Interests in Other Entities*). To date, the AASB is not aware of any significant issues caused by using the term 'reporting entity' in these Standards as the term could be read in the context of the Australian reporting entity concept without causing confusion (ie until now the IASB has not defined the term). However, because the RCF includes a chapter specifically on the reporting entity and defines the term differently to the Australian reporting entity concept, it will become

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1 Australian Securities & Investments Commission's (ASIC's) Regulatory Guide (RG) 85: *Reporting requirements for non-reporting entities* applies the following Australian Accounting Standards to all entities required to prepare a financial report in accordance with Chapter 2M of the *Corporations Act 2001*, whether they are reporting entities or not: 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 1057 *Application of Australian Accounting Standards*.

increasingly difficult to read the term in two different ways, particularly as and when AAS are amended/revised and there are more references to the term as defined in the RCF.

The AASB's medium to longer term considerations

Why *IFRS for SMEs* was not considered a viable GPFS Tier 2 Alternative

What is IFRS for SMEs?

18 *IFRS for SMEs* (as issued by the IASB) is a modified and simplified version of full IFRS, which is aimed at meeting the needs of private company financial reporting users. It includes:

(a) differential recognition and measurement requirements compared with IFRS;

(b) limited accounting policy options (ie some topics have limited accounting policy options);

(c) the omission of topics not expected to be relevant to SMEs; and

(d) consolidation of subsidiaries if the entity is required to prepare consolidated financial statements (under Section 9 *Consolidated and Separate Financial Statements* within *IFRS for SMEs* which also includes a scope exemption from preparing consolidated financial statements where the parent is a subsidiary itself and its ultimate parent (or any intermediate parent) produces GPFS that are fully compliant with *IFRS or IFRS* for SMEs).

19 This framework only undergoes periodic reviews (the first review after two years of adoption and subsequent reviews every three years).

20 *IFRS for SMEs* is not currently available for application in Australia for financial statements required by regulation. However, it could be applied in other circumstances (eg small proprietary companies).

Advantages and disadvantages of *IFRS for SMEs*

Advantages of IFRS for SMEs

21 This framework is an established international framework developed by the IASB.

22 This framework removes ambiguity about what needs to be reported, leading to comparable financial statements for those adopting the framework.

23 This framework provides simplified recognition and measurement requirements compared to Alternatives 1 and 2, which are being proposed. This could be a cost effective alternative for entities preparing SPFS that are not doing full R&M to move to GPFS.

24 For some entities, the simplified recognition and measurement requirements might appropriately meet the needs of users of their financial statements and not result in overload of information.

25 The requirements of *IFRS for SMEs* are separately contained in a separate Standard/Book. This might make it easier for preparers to identify reporting requirements under this framework compared to preparers using frameworks described in Alternatives 1 or 2.

Disadvantages of IFRS for SMEs

26 Simplified recognition and measurement within this framework are not consistent with ASIC and other regulators' view that the full recognition and measurement requirements of accounting standards must be applied in order to give a 'true and fair view' of the financial position and performance of an entity.

27 Simplified recognition and measurement could disadvantage entities engaging in business combinations or being compared for funding or other reasons with peers applying Tier 1.

28 If this framework was adopted, significant modifications or amendments would have to be made to address Australian-specific circumstances (eg *IFRS for SMEs* has a for-profit entity focus so is likely to require substantial rework to ensure that it is applicable to NFP and public sector entities).

29 This framework may not meet some of the users' needs (ie insufficient information). Users may also find differing approaches to measuring equity, assets, liabilities and profit or loss compared with Tier 1 confusing.

30 This framework only undergoes periodic reviews (the first review after two years of adoption and subsequent reviews every three years) compared with the proposed Alternatives 1 and 2 which are/will be updated in line with IFRS (at a minimum).

31 If this framework was adopted, additional short-term costs during the transition period will be required. These transition costs include educating preparers and users, the accounting profession and regulators.

32 Additional transitional costs will arise because:

(a) all entities currently preparing Tier 2 GPFS-RDR and SPFS will need to change to the *IFRS for SMEs* recognition and measurement criteria. Analysis of the findings in Research Report No. 1[2] indicate more than three-quarters (76.1%) of non-disclosing entities that need to publicly lodge financial statements in accordance with AAS are complying with recognition and measurement requirements of AAS. Therefore, *IFRS for SMEs* exemptions and modifications are unlikely to be cost effective enough to warrant moving to this new framework (eg deferred taxes are required, borrowing costs must be expensed etc).

(b) subsidiaries would need to provide additional information to be compliant with IFRS for the purpose of consolidating into their parent's consolidated financial statements. This would be a significant issue for the public sector where all public sector entities are subsidiaries for whole of government reporting.

(c) if adopted, this framework would lead to two sets of standards that would not always be synchronised (ie given it is reviewed/updated only once every three years), but whose relationship would need to be carefully tracked by professionals, commentators and students.

33 This framework results in reduced comparability with entities that are preparing full IFRS and will be more difficult to transition to Tier 1 reporting (ie full IFRS) because of different accounting policy alternatives, differential recognition and measurement requirements and the disparity of when Standards are being updated (ie periodically versus 'as needs' basis).

34 Some entities previously preparing SPFS but not preparing consolidated financial statements would need to prepare consolidated financial statements under this framework (noting the exception in this framework differs slightly to the exception in AASB 10, which is applicable to Alternatives 1 and 2).

35 Adopting this framework may put additional strain on the resources of smaller accounting firms in terms of training required on the different recognition and measurement requirements of this framework compared to Tier 1. After bearing the additional costs of training and updating manuals however, there may be savings for firms that only deal with SMEs but this could adversely affect the ability of staff to move across the profession.

Why was *IFRS for SMEs* not considered a viable Tier 2 Alternative?

36 The AASB had considered *IFRS for SMEs* as an alternative for Tier 2 and decided not to pursue that alternative for the reasons outlined above at this time.

Who will be affected by these proposals?

A breakdown of corporates preparing GPFS versus SPFS

37 The following information has been extracted from Research Report No. 1. Even though this report was issued in 2014, evidence in it provides useful insights into the impact proposals may have on various types of entities.

38 Research Report No. 1 analysed the application of the reporting entity concept and the adoption of SPFS, particularly by entities lodging financial statements with the ASIC. It did not address entities that had their equity interests traded in a public market, such as listed companies, or other entities with 'public accountability'.

39 It examined reporting practices of companies lodging with the ASIC, by analysing a random sample of 1,546 companies required to publicly lodge with ASIC (both for-profit and NFP) drawn from 2008-09 population counts provided by ASIC. The data analysed was hand collected from Portable Document Format (PDF) copies of company lodgements provided by the ASIC. The data years subject to analysis were the most recently available annual report years – starting in 2006 but with most report years ending in 2009 and 2010. To enable additional analysis on aspects of financial reporting quality for large proprietary companies, additional company year observations were obtained up to and including 2010 for these companies. It provided results that were generalised, to a 95% confidence level, across the following five populations of companies:

(a) large proprietary companies;

(b) small proprietary companies controlled by a foreign company (also referred to as 'Foreign-controlled companies');

(c) small proprietary companies required to lodge reports with the ASIC (also referred to as 'Small proprietary companies');

2 Refer to Research Report No. 1 and Appendix C paragraphs 40-61.

(d) unlisted public companies other than those limited by guarantee (also referred to as 'Unlisted public companies'); and

(e) public companies limited by guarantee.

40 An extract of some of the key findings from Research Report No. 1 with respect to the above analysis has been included below to help better understand the impact of the AASB's proposals contained in this Consultation Paper.

41 'A majority of companies lodging financial statements with the ASIC (58.7%) across the five sample groups classify themselves as non-reporting entities and lodge special purpose financial statements (SPFS) rather than general purpose financial statements (GPFS). For large proprietary companies, this percentage increases to nearly 80 percent. The summary table below captures the frequency of the type of financial statements lodged by the different types of companies.'[3]

42 It should also be noted that these findings include data on charities (ie Public companies limited by guarantee) as this data was sourced before the ACNC was established (in 2012).

43 ***Table 9: Summary of type of statements lodged with the ASIC by different types of companies for the period covering 2008-09 and 2010-11***

	GPFS		**SPFS**		**Total sample**	**Total population**
	Frequency[2]	**%[2]**	**Frequency[2]**	**%[2]**	**Frequency**	**Frequency[2]**
Large proprietary companies	79	20.1	315	79.9	394	5097
Foreign-controlled companies	53	15.6	287	84.4	340	2237
Small proprietary companies	23	24.2	72	75.8	95	131
Unlisted public companies	242	69.7	105	30.3	347	3884
Public companies limited by guarantee	239	65.5	126	34.5	365	9673
Total	**636**	**41.3**	**905**	**58.7**	**1541**	**21,022**

(Total sample calculated by the AASB staff based frequency GPFS plus SPFS)

44 More recent analysis (presented at the AASB's 2016 Research Forum) in *Financial Reporting by Private Companies in Australia: Current Practice and Opportunities for Research*, an unpublished working paper by Brad Potter (The University of Melbourne), George Tanewski (Deakin University), Sue Wright (Macquarie University) is largely consistent with the analysis in Research Report No. 1 in relation to large proprietary companies. In the unpublished working paper, 211 large proprietary companies were examined, of which 27% prepared GPFS (including 4.7% that shifted to GPFS-RDR) and the remaining 73% prepared SPFS. This indicates a slight shift by large proprietary companies preparing GPFS compared to Research Report No. 1.

Who's disclosing compliance with recognition and measurement?

45 Research Report No. 1 also examined the financial reporting practices of the sample of companies lodging SPFS with ASIC to gauge the quality of the SPFS. One of the dimensions analysed was the information provided in the significant accounting policies note of the SPFS of the five groups of companies in relation to the disclosure of the application of recognition and measurement in accordance with the AAS.

46 In order to gain a broader overall picture, the AASB used the breakdown of statistical findings from Research Report No. 1 which examined within each population of companies that prepared SPFS, how many stated compliance with recognition and measurement of AAS (R&M), those that explicitly stated that R&M had not been complied with and those that did not specify compliance with R&M.

47 These findings are detailed in the following two tables, noting that where a calculation has been performed by the AASB (based on information in Research Report No. 1), it has been explained below. All other figures have been extracted directly from Research Report No. 1.

3 Source: AASB Research Report No. 1.

48 *Table 10: AASB R&M analysis of sampled companies lodging SPFS with ASIC*

	Preparing SPFS	SPFS – stated R&M		SPFS – incomplete disclosure[4]		SPFS – state R&M not applied		Total SPFS incomplete disclosure or R&M not applied	
	No.	No.	%	No.	%[6]	No.	%[6]	No.	%
Large proprietary companies	315	209	66.2	61	19.5	45	14.3	106	33.8
Foreign-controlled companies	287	178	62.2	93	32.3	16	5.5	109	37.8
Small proprietary companies	72	38	52.9	8	11.1	26	36.1	34	47.1
Unlisted public companies	105	68	64.8	11	10.5	26	24.8	37	35.2
Public companies limited by guarantee	126	44	35.8	19[5]	14.2	63	50.0	82[5]	64.2
Total[6]	**905**	**537**	**59.3**	**192**	**21.2**	**176**	**19.4**	**368**	**40.7**
% of Total	**100%**	**59.3%**		**21.2%**		**19.4%**		**40.7%**	

(Unless otherwise explained in the footnote, the source of the above details is Research Report No. 1)

49 ***Table 11: AASB analysis of sampled companies lodging with ASIC – who is complying with R&M overall?***

	Total Population per Research Report No. 1 (GPFS and SPFS No.)			Full recognition and measurement (GPFS plus SPFS stating R&M)				SPFS – incomplete disclosure		SPFS – state R&M not applied	
	(A)[7]	**(B)[8]**	**(C)[8]**	**(A)[8]**	**(D)[8]**	**(E)[8]**	**(F)[8]**	**(G)[8]**	**(H)[8]**	**(I)[8]**	**(J)[8]**
	GPFS	**SPFS**	**Total**	**GPFS all (No.)**	**SPFS R&M (No.)**	**Total (No.)**	**% of total**	**Total (No.)**	**% of total**	**Total (No.)**	**% of total**
Large proprietary companies	79	315	394	79	209	288	73.1	61	15.5	45	11.4
Foreign-controlled companies	53	287	340	53	178	231	67.9	93	27.4	16	4.7
Small proprietary companies	23	72	95	23	38	61	64.2	8	8.4	26	27.4
Unlisted public companies	242	105	347	242	68	310	89.3	11	3.2	26	7.5
Public companies limited by guarantee	239	126	365	239	44	283	77.5	19	5.2	63	17.3
Total[9]	**636**	**905**	**1541**	**636**	**537**	**1173**	**76.1[9]**	**192**	**12.5**	**176**	**11.4**
% of total	**41.3%**	**58.7%**	**100%**	**76.1%**				**12.5%**		**11.4%**	

4 It should be noted that Research Report further breaks down the 'Incomplete Disclosure' category into a 'no clear statement of application of R&M' category and a 'minor non-application' category. The latter category refers to companies that had stated compliance with R&M but with minor exemptions. The 'no clear statement of application of R&M' category was more commonly seen for large proprietary companies, foreign-controlled companies and public companies limited by guarantee, whereas small proprietary companies and unlisted public companies were categorised mostly into the 'minor non-application' category. Finally the extent of non-compliance with R&M is not clear for companies in the 'no clear statement of application of R&M' category (ie just because they don't state compliance, does not mean that they are not complying).

5 These numbers include 3 companies which were classed as 'unable to determine' within Table 20 of the Research Report No. 1.

6 These items were calculated by the AASB.

7 Source: AASB Research Report No. 1.

8 Calculated by the AASB: (C) = (A) + (B), (E) = (A) + (D), (F) = (E) / (C), (H) = (G) / (C) and (J) = (I) / (C)

9 These items have been calculated by the AASB.

50 The above analysis looks at the entire population of entities sampled in Research Report No. 1, both those entities that prepared GPFS and those that prepared SPFS (contrasted with results in Table 10 which looks purely as the results of those that prepare SPFS).This analysis includes reporting results of NFPs (typically public companies limited by guarantee), which are now regulated by the ACNC as the research was undertaken prior to the establishment of the ACNC.

51 The data in the above analysis is based on a random sample of companies drawn from 2008-09 population counts provided by ASIC. As mentioned above (in paragraph 44 to Appendix C), more recent analysis in an unpublished working paper by Brad Potter, George Tanewski and Sue Wright is largely consistent with the analysis in Research Report No. 1 in relation to the proportion of large proprietary companies preparing SPFS versus GPFS. Findings within the ACNC's latest report, *Reporting trends in the 2016 Annual Information Statement* also indicate the proportion of entities preparing SPFS versus GPFS has remained largely consistent to what was found in Research Report No. 1 (refer to Appendix C paragraph 57). In terms of R&M, anecdotal evidence gathered by the AASB via discussions with various accounting firms (medium to large) suggests that most entities that these firms deal with are applying full R&M. Therefore it could be implied that there might be more entities complying with R&M compared to the findings in Research Report No. 1.

52 Based on the above analysis, 76.1% of non-disclosing entities who publicly lodge with ASIC comply with R&M, with less than one quarter of companies not stating compliance with R&M. Of the 23.9% not stating compliance with R&M, only 11.4% explicitly state that R&M has not been complied with. Research Report No. 1 did not examine the extent of non-compliance for these entities. This could mean that these entities might have only not complied with one or two R&M requirements. The remaining 12.5% of reports examined revealed either 'no clear statement of application of R&M' or 'minor non-application' of R&M. Once again, this does not conclusively mean that these entities did not comply with the majority of R&M requirements, despite not explicitly disclosing it and/or if they did only partially comply, the extent of non-compliance varies (many of the reports observed had moved away from just one or two of the R&M requirements).

A breakdown of non-corporate entity reporting

53 Research Report No. 1 also examined a further random sample of 1,163 from entities lodging with state-based regulators, that is, Consumer Affairs Victoria (400 entities), NSW Fair Trading (377 entities) and Queensland Office of Fair Trading (386 entities), in order to provide evidence of the reporting practices of various types of other entities – including co-operatives and associations. The sample of entities examined in this part of the Research Report No. 1 also included some that were focused on charitable, community purpose and fundraising activities – for which additional state-based regulations typically apply[10].

54 An extract of some of the key findings from Research Report No. 1 with respect to the above analysis has been included below to help better understand the impact of the AASB's proposals contained in this Consultation Paper.

55 'The analysis of lodgements of financial statements made in Victoria, NSW and Queensland reveals great variation in the quantity and quality of information lodged. However, for larger associations and co-operatives, the variations appear less significant. A large proportion of entities examined across the three states provided no explicit indication as to whether the financial statements were GPFSs or SPFSs (i.e., 78% in Victoria, 71% in NSW and 40% in Queensland). Around 18 per cent of entities in Victoria, 24 per cent in NSW, and 53 per cent in Queensland lodged SPFSs with their state-based regulator, while only around five per cent of entities lodged statements identified as GPFSs across the three states. The summary table below outlines the frequency of the type of statements lodged by the different groups of state-based entities'[11].

10 The Australian Charities and Not-for-profits Commission Act 2012 (Cth) established the Australian Charities and Not-for-profits Commission (ACNC) in 2012. The ACNC does not substitute the state supervising bodies and it has stated that it will co-operate with other government agencies to oversee a simplified and streamlined regulatory framework for not-for-profit entities.

11 Source: Research Report No. 1.

56 *Summary of descriptions of financial statements lodged with state-based regulators by different types of entities*[12]

Victoria				NSW				Queensland			
Type of Entity	**GPFS %**	**SPFS %**	**No clear statement %**	**Type of Entity**	**GPFS %**	**SPFS %**	**No clear statement %**	**Type of Entity**	**GPFS %**	**SPFS %**	**No clear statement %**
Prescribed Associations	17	60	23	Tier-One Incorporated Associated	10	67	24	Level-One Incorporated Associated	7	73	20
Non-Prescribed Associations	0	9	91	Tier-Two Incorporated Associated	2	17	82	Level-Two Incorporated Associated	2	62	36
								Level-Three Incorporated Associated	0	36	64
Co-operatives	0	50	50	Co-operatives	67	33	0	Co-operatives	33	33	33
Fundraisers	30	35	35					Charities	50	35	15
Patriotic Funds	0	18	82					Community Purpose Entities	20	50	30
Total	**4**	**18**	**78**	**Total**	**5**	**24**	**71**	**Total**	**7**	**53**	**40**

(Source: Research Report No. 1, some panels do not add to 100 per cent due to rounding)

A breakdown of charities preparing GPFS versus SPFS

57 The Australian Charities and Not-for-profits Commission (ACNC) conducts proportionate, risk-based monitoring of Annual Information Statements and Annual Financial Reports. This helps the ACNC identify trends and errors that charities make in their Annual Information Statements, and enables the ACNC to make evidence-based decisions when improving the Annual Information Statement. The ACNC collates findings from its monitoring activities into an annual report. Refer to the ACNC's latest report, *Reporting trends in the 2016 Annual Information Statement* ('ACNC Report').

58 The ACNC Report explains the trends and errors identified in charities' 2016 Annual Information Statements. As part of this, the ACNC conducted a detailed review of the Annual Financial Reports prepared by medium and large charities. A total of 143[13] charities and 8[14] ACNC Groups were checked as part of this analysis.

59 Some of the key findings from the ACNC Report with respect to the above analysis are included below to help better understand the impact of the AASB's proposals contained in this Consultation Paper.

60 The ACNC's analysis of the accounting policies provided in the 'basis of preparation' section within the 151 Annual Financial Reports checked showed:

(a) 68 (45%) were GPFS (including 25 (17%) GPFS-RDR); and

(b) 83 (55%) were SPFS.

61 Another report titled *Reporting Framework Choice and Auditor Characteristics and Value among Australian Large and Medium Sized Charities in 2014-2015* ('Charities Report'), prepared by Yitang (Jenny) Yang (PhD Student) under the supervision of Roger Simnett (in his capacity as a Scientia Professor) and Elizabeth Carson from School of Accounting, UNSW Business School, UNSW Sydney, examined 7,828 large charities and 494 medium charities registered with ACNC in 2014 and 2015. Findings from this report indicate 42% of large charities examined prepared SPFS and 64% of medium charities prepared SPFS. This appears to be largely consistent with the ACNC Report findings above, which includes both medium and large charities.

12 Some panels do not add to 100 percent due to rounding
13 Source: *Reporting trends in the 2016 Annual Information Statement*.
14 The ACNC can allow several charities to report as a group. This group is required to submit one Annual Information Statement (on behalf of the group) and one Annual Financial Report (if applicable).

Further evidence on merits of proposals

Case law supports public lodgement of GPFS

62 The inappropriateness of entities being assessed as non-reporting entities is evident even in case law. For example, the Incat Australia Pty Ltd ('Incat') versus ASIC[15] High Court case included a number of valuable facts supporting public lodgement of GPFS; and discusses that users of GPFS, extends beyond banks and other major financiers, major creditors, export credit insurers, underwriters and credit rating agencies, to include employees and others who cannot command SPFS.

63 In that case, the applicants appealed from a decision of the Administrative Appeals Tribunal (AAT) which affirmed a decision of the ASIC declining to relieve the directors of Incat from the obligation to lodge annual accounts for the financial years ending 30 June 1996, 1997 and 1998. Incat also contended that the AAT should have found that the Incat companies were "non-reporting entities" and that the lodgement of their accounts was "inappropriate in the circumstances" because if they were obliged to lodge accounts customers and competitors would be able to ascertain their profits per product, which would put them at a severe negotiating and competitive disadvantage. The Federal Court of Australia dismissed the application.

Reasons for the judgement

64 At the time of the case, 'a "large proprietary company" was required to lodge, inter alia, its financial statements: s 317B. The definition of "large proprietary company" depended on certain minimum revenue ($10 million) gross assets ($5 million) and employee numbers (50) criteria. It was common ground that Incat substantially exceeded all these criteria and were obliged to lodge accounts, unless the relief sought was granted'[15].

65 'The content of the actual obligations of a particular company depended on whether it was a "reporting entity", a concept which the Corporations Law left to regulations to define: s 294A(1). The Statement of Accounting Concepts SAC 1 defined a "reporting entity" as follows:

> *"Reporting entities are all entities (including economic entities) in respect of which it is reasonable to expect the existence of users dependent on general purpose financial reports for information which will be useful to them for making and evaluating decisions about the allocation of scarce resources.'* [15]

66 'Incat contended that the Incat companies were "non-reporting entities" and that their accounts were not required to be, and were not in fact, general purpose accounts. Incat only supplied limited, special purposes financial statements to banks and other major financiers, major creditors, export credit insurers, underwriters and credit rating agencies. It was said that it was not reasonable to expect there would be users dependent on general purposes accounts. There was "no need for financial information to be made available on the public domain via lodgment of accounts". Thus it was "inappropriate" to require the lodgement of accounts.' [15]

67 'The AAT said:

> *"52. At the end of the day it is not a question of whether a company is a reporting entity but whether or not it is a large proprietary company. The introduction of a distinction between "small" and "large" in the 1995 Act in place of the former distinction between exempt and non exempt proprietary companies meant that financial reporting obligation are based on criteria relating to the economic significance of a company. A proprietary company classified as "large" is inherently economically significant because to be so classified it has to satisfy criteria relating to its economic significance. The obligation to lodge accounts flows from its status as a large proprietary company following the legislative distinction made between small and large proprietary companies not whether it is a reporting entity, a concept removed from the Law. As the Explanatory Memorandum to the legislation noted, the financial reporting requirements have been strengthened for companies which have significant economic impact. Furthermore the legislative policy underlying the requirement to lodge accounts is indicative of the expectation that there are users of the accounts.*
>
> *53. Because the applicants fulfil the criteria for classification as large public companies it is reasonable to expect there will be users of the accounts. I would respectfully agree with the view of the Tribunal in Mazda that 'users' should be given the widest possible interpretation and not restricted to shareholders, potential shareholders, creditors, potential creditors and customers: see Liquid Air at 34.*
>
> *54. The Incat group is a major player in the production of fast ferries worldwide producing 3-4 vessels per year in a worldwide demand of approximately 10 per year. The Incat group is economically significant in the market in which it operates both in economic and political*

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15 Refer *Incat Australia Pty Ltd v Australian Securities and Investment Commission - [2000] FCA 58.*

terms, particularly to the Tasmanian economy, not only in generating export earnings but in the development and utilisation of a skilled manufacturing base.

55. While it is noted that the applicants provide financiers, export credit insurers, credit rating agencies, underwriters and major creditors with special purpose financial statements, on the other hand fiscal information for trade creditors appears to be provided by the applicants on a discretionary basis and is not made available to 'minor' goods and services providers and potential investors. Trust unit holders are permitted to peruse financial statements and to discuss this information with a financial executive. This practice of providing relevant information only to selected groups seems to be to be inconsistent with the intent of the legislation.

56. Another potential category of 'users' is the Incat workforce. The focus of the system of industrial regulation in recent years has shifted from one of conciliation and arbitration in determining award entitlements to one of enterprise and workplace bargaining. Whereas in the past there was a centralised system of wage accords, this has been replaced by collective and/or individual bargaining based on the primacy of enterprise bargaining as enshrined in legislation in recent years. The focus of the system is the facilitation of agreements. Awards are now only to be regarded as a basic safety net with most conditions of employment regulated by enterprise agreements: see Workplace Relations Act 1990 (C'th) also Part IVA of the Industrial Relations Act 1984 (Tas). The Tasmanian legislation makes provision for an enterprise agreement that may or may not involve employee organisations and may be collective or individual. In a bargaining exercise of this nature where the balancing of that which can be afforded against that which may be given up, it is reasonable to expect that as an aid to the decision making process in the present climate of enterprise bargaining, employees may property be regarded as potential 'users' of accounts. The fact that employees or unions were not supplied with any financial statements (or may not have requested any) in negotiating the existing industrial agreement covering production employees, is not to the point."[15]

68 'The AAT therefore concluded that it was not "inappropriate for Incat to lodge accounts". This reasoning seems to me free of legal error. I do not see how there has been any failure to make relevant findings. Contrary to Incat's submissions, the AAT's findings necessarily involve a conclusion, which must be one of fact, that the Incat companies were "reporting entities". In any case, the ultimate question is whether a company is a "large proprietary company"'[15].

69 The above excerpts from the Incat versus ASIC case provide insight into what regulators generally expect from entities required to publicly lodge (ie GPFS) and highlight inherent difficulties with self-assessment between reporting entities and non-reporting entities. Under the AASB's proposed medium-term approach both of these issues will be alleviated as all entities required to publicly lodge will be preparing GPFS and will no longer be required to assess as reporting entities or non-reporting entities.

RG 85 requires full recognition and measurement for non-reporting entities and emphasises the significance of the reporting entity assessment for directors

70 Regulatory Guide RG 85 *Reporting requirements for non-reporting entities*, was issued 1 July 2005. It provides guidance on application of the reporting entity test and the reporting obligations for non-reporting entities. It demonstrates that ASIC believes that non-reporting entities, which are required to prepare financial reports in accordance with Chapter 2M of the *Corporations Act 2001* ('the Act'), should comply with the recognition and measurement requirements of accounting standards to provide a true and fair view.

71 Section 2: Accounting provisions applicable to non-reporting entities of RG 85 provides rationale for these requirements stating:

'2.1 The accounting standards provide a framework for determining a consistent meaning of 'financial position' and 'profit or loss' in financial reporting across entities.

2.2 In the absence of any such framework, the figures disclosed in financial statements would lose their meaning and could be determined completely at the whim of the directors of individual entities. The profit or loss reported by an individual entity would vary greatly depending upon which individuals were responsible for the preparation of its financial statements.

2.3 This would not be consistent with the requirements of the Act for financial reports to give a true and fair view (s297), prohibiting the giving of false and misleading information (s1308), and only permitting dividends to be paid out of profits (s254T).'[16]

72 Section 2 of RG 85 also sets minimum requirements within certain accounting standards that should apply to all entities reporting under Chapter 2M of the Act including various requirements within

16 Source: RG 85: *Reporting requirements for non-reporting entities*.

AASB 101 *Presentation of Financial Statements* and AASB 108 A*ccounting Policies, Changes in Accounting Estimates and Errors*. It also states the following:

> '2.9 Directors of non-reporting entities must also consider carefully the need to make disclosures which are not directly prescribed by accounting standards, but which may be necessary in order for the financial statements to give a true and fair view. Such disclosures could include certain significant related party transactions.
>
> 2.10 ASIC will look closely at cases where non-reporting entities have not complied with the recognition and measurement requirements of accounting standards.'[16]

73 Section 3: *Significance of reporting entity status* of RG 85 provides guidance and emphasises the responsibilities of directors with respect to the determination of whether a company should be classified as a reporting entity or a non-reporting entity. It states:

> '3.2 The directors' determination as to whether a company should be classified as a reporting entity or a non-reporting entity is an important decision affecting the level of disclosure in the company's financial report. Directors are required under s295(4)(d) of the Act to make a declaration as to whether a company's financial statements comply with accounting standards. Directors need to make their decision regarding reporting entity status carefully in view of the requirement to make this declaration.
>
> 3.3 Directors of an entity that identifies itself as a non-reporting entity and elects not to adopt the requirements of all accounting standards would be in breach of the requirement to comply with accounting standards contained in s296 of the Act if the circumstances of the entity point to it being a reporting entity...' [16]

74 Section 3 of RG 85 also sets out that AASB 101, AASB 107 *Cash Flow Statements*, AASB 108, AASB 1048[17] *Interpretation of Standards* and AASB 1054 *Australian Additional Disclosures* should apply in full to all entities required to prepare a financial report in accordance with Chapter 2M of the Act, whether they are reporting entities or not.

75 Section 4: Classification as a non- reporting entity of RG 85 goes onto explain that when applying the definition of 'reporting entity', Directors and Auditors must consider whether there are existing or potential users who may be dependent on general purpose financial reports. Its states:

> '4.2 ASIC's review of financial reports has revealed that some companies that claimed to be non-reporting entities should have been classified as reporting entities. These companies had a significant number of creditors and employees and it was reasonable to expect the existence of users dependent on general purpose financial reports. The financial reports of these companies had been accessed on ASIC's public database on a number of occasions by external parties during a 12 month period.
>
> 4.3 ASIC will look closely at cases where entities claim to be non-reporting entities and will seek explanations from directors where it appears reasonable to expect that there are users dependent on general purpose financial reports.'[16]

The above excerpts from RG 85 are indicative of the importance ASIC places on full recognition and measurement with accounting standards to give a true and fair view of a company's financial performance and position and highlights inherent difficulties with self-assessment between reporting entities and non-reporting entities. Under the AASB's proposed medium-term approach both of these issues will be alleviated as all entities required to publicly lodge will be preparing GPFS, with full recognition and measurement and will no longer be required to assess as reporting entities or non-reporting entities.

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17 AASB 1048 was previously AASB 1048 *Interpretation and Application of Standards*. This is now covered by two Standards: AASB 1048 *Interpretation of Standards* and AASB 1054 *Australian Additional Disclosures*.

APPENDIX D

Conceptual Framework for Financial Reporting (IASB) Chapter 3 – Financial Statements and the Reporting Entity

Financial statements

3.1 Chapters 1 and 2 discuss information provided in general purpose financial reports and Chapters 3–8 discuss information provided in general purpose financial statements, which are a particular form of general purpose financial reports. Financial statements[7] provide information about economic resources of the reporting entity, claims against the entity, and changes in those resources and claims, that meet the definitions of the elements of financial statements (see Table 4.1).

Objective and scope of financial statements

3.2 The objective of financial statements is to provide financial information about the reporting entity's assets, liabilities, equity, income and expenses[8] that is useful to users of financial statements in assessing the prospects for future net cash inflows to the reporting entity and in assessing management's stewardship of the entity's economic resources (see paragraph 1.3).

3.3 That information is provided:

(a) in the statement of financial position, by recognising assets, liabilities and equity;

(b) in the statement(s) of financial performance,[9] by recognising income and expenses; and

(c) in other statements and notes, by presenting and disclosing information about:

(i) recognised assets, liabilities, equity, income and expenses (see paragraph 5.1), including information about their nature and about the risks arising from those recognised assets and liabilities;

(ii) assets and liabilities that have not been recognised (see paragraph 5.6), including information about their nature and about the risks arising from them;

(iii) cash flows;

(iv) contributions from holders of equity claims and distributions to them; and

(v) the methods, assumptions and judgements used in estimating the amounts presented or disclosed, and changes in those methods, assumptions and judgements.

Reporting period

3.4 Financial statements are prepared for a specified period of time (reporting period) and provide information about:

(a) assets and liabilities—including unrecognised assets and liabilities—and equity that existed at the end of the reporting period, or during the reporting period; and

(b) income and expenses for the reporting period.

3.5 To help users of financial statements to identify and assess changes and trends, financial statements also provide comparative information for at least one preceding reporting period.

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7 Throughout the *Conceptual Framework*, the term 'financial statements' refers to general purpose financial statements.

8 Assets, liabilities, equity, income and expenses are defined in Table 4.1. They are the elements of financial statements.

9 The *Conceptual Framework* does not specify whether the statement(s) of financial performance comprise(s) a single statement or two statements.

3.6 Information about possible future transactions and other possible future events (forward-looking information) is included in financial statements if it:

(a) relates to the entity's assets or liabilities—including unrecognised assets or liabilities—or equity that existed at the end of the reporting period, or during the reporting period, or to income or expenses for the reporting period; and

(b) is useful to users of financial statements.

For example, if an asset or liability is measured by estimating future cash flows, information about those estimated future cash flows may help users of financial statements to understand the reported measures. Financial statements do not typically provide other types of forward-looking information, for example, explanatory material about management's expectations and strategies for the reporting entity.

3.7 Financial statements include information about transactions and other events that have occurred after the end of the reporting period if providing that information is necessary to meet the objective of financial statements (see paragraph 3.2).

Perspective adopted in financial statements

3.8 Financial statements provide information about transactions and other events viewed from the perspective of the reporting entity as a whole, not from the perspective of any particular group of the entity's existing or potential investors, lenders or other creditors.

Going concern assumption

3.9 Financial statements are normally prepared on the assumption that the reporting entity is a going concern and will continue in operation for the foreseeable future. Hence, it is assumed that the entity has neither the intention nor the need to enter liquidation or to cease trading. If such an intention or need exists, the financial statements may have to be prepared on a different basis. If so, the financial statements describe the basis used.

The reporting entity

3.10 A reporting entity is an entity that is required, or chooses, to prepare financial statements. A reporting entity can be a single entity or a portion of an entity or can comprise more than one entity. A reporting entity is not necessarily a legal entity.

3.11 Sometimes one entity (parent) has control over another entity (subsidiary). If a reporting entity comprises both the parent and its subsidiaries, the reporting entity's financial statements are referred to as 'consolidated financial statements' (see paragraphs 3.15–3.16). If a reporting entity is the parent alone, the reporting entity's financial statements are referred to as 'unconsolidated financial statements' (see paragraphs 3.17–3.18).

3.12 If a reporting entity comprises two or more entities that are not all linked by a parent-subsidiary relationship, the reporting entity's financial statements are referred to as 'combined financial statements'.

3.13 Determining the appropriate boundary of a reporting entity can be difficult if the reporting entity:

(a) is not a legal entity; and

(b) does not comprise only legal entities linked by a parent-subsidiary relationship.

3.14 In such cases, determining the boundary of the reporting entity is driven by the information needs of the primary users of the reporting entity's financial statements. Those users need relevant information that faithfully represents what it purports to represent. Faithful representation requires that:

(a) the boundary of the reporting entity does not contain an arbitrary or incomplete set of economic activities;

(b) including that set of economic activities within the boundary of the reporting entity results in neutral information; and

(c) a description is provided of how the boundary of the reporting entity was determined and of what constitutes the reporting entity.

Consolidated and unconsolidated financial statements

3.15 Consolidated financial statements provide information about the assets, liabilities, equity, income and expenses of both the parent and its subsidiaries as a single reporting entity. That information is useful for existing and potential investors, lenders and other creditors of the parent in their assessment of the prospects for future net cash inflows to the parent. This is because net cash inflows to the parent include distributions to the parent from its subsidiaries, and those distributions depend on net cash inflows to the subsidiaries.

3.16 Consolidated financial statements are not designed to provide separate information about the assets, liabilities, equity, income and expenses of any particular subsidiary. A subsidiary's own financial statements are designed to provide that information.

3.17 Unconsolidated financial statements are designed to provide information about the parent's assets, liabilities, equity, income and expenses, and not about those of its subsidiaries. That information can be useful to existing and potential investors, lenders and other creditors of the parent because:

(a) a claim against the parent typically does not give the holder of that claim a claim against subsidiaries; and

(b) in some jurisdictions, the amounts that can be legally distributed to holders of equity claims against the parent depend on the distributable reserves of the parent.

Another way to provide information about some or all assets, liabilities, equity, income and expenses of the parent alone is in consolidated financial statements, in the notes.

3.18 Information provided in unconsolidated financial statements is typically not sufficient to meet the information needs of existing and potential investors, lenders and other creditors of the parent. Accordingly, when consolidated financial statements are required, unconsolidated financial statements cannot serve as a substitute for consolidated financial statements. Nevertheless, a parent may be required, or choose, to prepare unconsolidated financial statements in addition to consolidated financial statements.