



<b>Project:</b>	<b>Australian Financial Reporting Framework</b>	<b>Meeting</b>	AASB June 2018 (M165)
<b>Topic:</b>	<b>Consolidated and Separate/Individual Financial Statements</b>	<b>Agenda Item:</b>	7.2
<b>Contact(s):</b>	Neha Juneja <a href="mailto:njuneja@asb.gov.au">njuneja@asb.gov.au</a> (03) 9617 7639  Robert Keys <a href="mailto:rkeys@asb.gov.au">rkeys@asb.gov.au</a>	<b>Project Priority:</b>	High
		<b>Decision-Making:</b>	Medium
		<b>Project Status:</b>	First (working) draft Research Report for 'for-profit' sector presented to the Board at M165 (agenda paper 7.1)

## Introduction

1. This document outlines the project plan for completing Phase 1 (for-profit private sector entities)<sup>1</sup> of the Research Report on Consolidated and Separate/Individual Financial Statements as part of the Australian Financial Reporting Framework project. The objective of that project is to review and amend current financial reporting requirements to make them clearer, more objective and comparable across sectors, balancing costs and benefits.
2. The Report will address matters relating to consolidated financial information relative to parent and subsidiary entity financial information. In particular, the Report will attempt to identify whether there are users of separate parent and individual subsidiary financial statements/information and what their needs are.

## Project rationale, objective(s), approach and link to AASB strategy

### Project rationale

3. *Individual financial statements of a subsidiary:*
  - a. *Lack of research into user needs:* Based on initial discussions with the Academic Advisory Panel, there is limited research into users and their need for subsidiary financial statements.
  - b. *International requirements are less onerous:* The New Zealand (NZ) Companies Act 1993 provides a broader exemption for subsidiary financial reporting as compared to financial reporting requirements for subsidiaries in Australia. For example, the NZ Companies Act 1993 was amended in May 2017 which provided an exemption to the bottom subsidiary in a group from preparing financial statements if consolidated financial statements of the

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<sup>1</sup> Phase 2 will address not-for-profit private sector entities and public sector entities.

parent are prepared and filed in NZ. This provides a basis for evaluating whether a similar exemption should be provided for subsidiaries in Australia.

- c. *Benchmark to current requirements for parent financial statements:* The Australian Companies Act 2001 was amended in 2010 to effectively exempt parent companies (except APRA regulated companies) from providing separate financial statements. Instead such parent companies are required to disclose summary financial information in their consolidated financial statements<sup>2</sup>. This provides a basis for evaluating whether a similar exemption should be provided for subsidiaries by requiring them to disclose the same kind of summary financial information in the consolidated financial statements of the parent instead of preparing a full set of individual financial statements. This evaluation will involve revisiting, at least broadly, the rationale for the parent company exemption.

#### 4. *Separate financial statements of parent*

Undertaking the evaluation described in paragraph 3(c) above provides an opportunity to consider, at least in a broad way, the cost/benefit impact of the exemption for parent company separate financial statements.

#### Project objective

5. Consistent with the above rationale, the Research Report primarily addresses the following fundamental questions:
- (a) *Should subsidiaries continue to be required to prepare and lodge individual financial statements publicly, or would disclosure of certain summary financial information about subsidiaries in the consolidated financial statements of the parent (ultimate or intermediate Australian parent) satisfy user needs in a more cost effective way?*
- (b) *Where it is currently required, does the summary financial information disclosed in consolidated financial statements of the group about the parent (in lieu of separate financial statements) satisfy user needs in a cost effective way?*

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<sup>2</sup> This is in contrast to the recommendation in AASB Research Report ‘Relevance of parent entity financial reports’ (2003), which was for a more limited exemption, recommending:

1. “Remove the requirement for parent entity financial reports to be published in the annual report;
2. Retain the requirement for full audited parent entity general purpose financial reports to be lodged with ASIC except for parent entities that:
  - (a) do not conduct substantive operations, including treasury operations;
  - (b) are not borrowing entities;
  - (c) are not single guarantors for the debt of one or more subsidiaries.
3. Require disclosure of the following to be published in the annual report:
  - (a) whether a full audited parent entity report has been lodged with ASIC, and, if not, a statement indicating that each of the exception criteria contained in (2) above are satisfied;
  - (b) parent entity shareholders’ funds, including dividends and franking credits, if different from the consolidated amounts;
  - (c) the manner in which the group is structured, including which entity(s) within the group conduct the major trading and treasury operations;
  - (d) in which entities the group’s borrowings and contingent liabilities reside;
  - (e) class orders, guarantees and indemnities in place, including which entities are party to the guarantee(s)....”

6. In attempting to answer these questions, the Research Report aims to cover the following topics:
- (a) Who are the primary users of a parent's separate and a subsidiary's individual financial statements?
  - (b) What is the information they are relying on within those financial statements?
  - (c) Can their needs be more cost-effectively met by the disclosure of summary financial information in the consolidated financial statements of the group (which includes the subsidiary)?

#### Project approach

7. When the Research Report was first conceived it was thought that banks in their role as lenders may be a good proxy for users. Therefore, the work to date has focused on taking feedback from major banks in Australia. So far it has indicated that:
- (a) there is information lost due to the exemption provided under the Corporations Act for parent entities; and
  - (b) there is a need for subsidiary's individual financial statements, even where the subsidiary is a wholly owned subsidiary covered by a deed of cross guarantee because bankers like to ascertain the repaying capability of the individual borrower to whom they have legal recourse.

#### Proposal to revise project approach to cover broader outreach

8. On reflection, and based on the consistent limited feedback received from banks from a lender's perspective (which stress the importance of separate and individual financial statements of parent and subsidiary entities respectively), it is proposed that a broader range of users (e.g. investors, analysts) and preparers should also be consulted to have a holistic review of user's requirements before recommending any changes to the financial reporting requirements (if any) for parent and subsidiaries, if any.
9. Additionally, as part of the outreach and briefing sessions for the Conceptual Framework project (which proposes to remove the reporting entity concept and thus restricting entities' ability to present special purpose financial statements) the relevance of the consolidated financial statements was questioned by the participants and that whether there are any users for these. Further, it was informed that individual financial statements of subsidiaries are essential especially in case of multi-national organisations.
10. Based on the above, the need to reach out to a broader range of users' requirements is considered essential (rather than a restricted focus on few major banks in Australia). Additional stakeholders identified for 'for-profit' private sector are as follows:
- Lenders: Australian Banking Association
  - Investors: Australian Shareholder's Association
  - Investors and Analysts: The Corporate Reporting Users Forum
  - Preparers: G100- CFOs
  - Liquidators: Insolvency Practitioners Association
  - Credit bureaus

Linking to AASB Strategies:

11. This project fits principally into AASB Strategy 2 and, potentially, depending on research findings, AASB Strategy 3:
- (a) Strategy 2: With the AUASB, play a leading role in reshaping the Australian external reporting framework by working with regulators to develop objective criteria on:
    - (i) who prepares external reports (including financial reports)
    - (ii) the nature and extent of assurance required on these external reports.
  - (b) Strategy 3: Actively influence IASB, IPSASB standards and other international accounting and external reporting standards and guidance, by demonstrating thought leadership and enhancing key international relationships.

**Project plan**

12. Staff have identified the following as key milestones in developing Phase 1 of the Research Report

<b>PHASE 1 (FOR-PROFIT PRIVATE SECTOR):</b>		
<b>Key dates</b>	<b>Major project milestones</b>	<b>Staff comment</b>
Oct17-Nov17	Liase with Academic Panel to identify any literature review on consolidation	Research reports shared by the Academic Panel members.
Jan 2018 – May 2018	<p>Conduct research into key issues</p> <p>Conduct targeted outreach with major banks in Australia</p>	<p>Substantively progressed</p> <p>Substantively completed (Received feedback from 3 major and 1 mid-tier bank in Australia). Additionally received feedback from one major Asian bank. Contacts at the remaining two major banks identified. Meetings are being fixed.</p>
	Prepare early version (first working draft) for review	Completed (see agenda paper 7.1)
Apr 2018	Prepare slide deck on findings to date for IFASS	Completed (presented to IFASS April meeting). IFASS members broadly emphasised the need for subsidiary's individual financial statements

<b>PHASE 1 (FOR-PROFIT PRIVATE SECTOR):</b>		
<b>Key dates</b>	<b>Major project milestones</b>	<b>Staff comment</b>
May-June 2018	<p>Provide an overview of the project to NZASB staff and request feedback on their own experience in consolidation</p> <p>Identify and scope for stakeholders that may participate in our research</p>	<p>Completed. Spoken with the NZASB. They have agreed to introduce us to relevant people at Ministry of Business, Innovation and Employment who can provide us with context about the basis for exemptions for subsidiary individual financial statements in NZ.</p> <p>Stakeholders identified for ‘for-profit’ private sector:</p> <ul style="list-style-type: none"> <li>• Lenders: Australian Banking Association</li> <li>• Investors: Australian Shareholder’s Association</li> <li>• Investors and Analysts: The Corporate Reporting Users Forum</li> <li>• Preparers: G100- CFOs</li> <li>• Liquidators: Insolvency Practitioners Association</li> <li>• Credit bureaus</li> </ul>
M165 Jun 2018	<p>AASB Board meeting – present project plan (agenda paper 7.2 – this paper) to Board</p> <p>Present first working draft of the Research Report (agenda paper 7.1) to the Board and seek broad comment</p>	<p>Staff to provide overview of project to the Board and ask the Board for feedback on the proposed direction of the project and key questions identified</p>
Jun 2018	<p>Provide an overview of the project to AUASB Staff:</p> <p>(a) identify key elements for which AUASB input will be required; and agree to timeline of document completion</p>	<p>There may be interest from the AUASB and how the issues would relate to audits of consolidated (and separate/individual financial statements).</p>
Jun 2018-Aug 2018	<ul style="list-style-type: none"> <li>• Complete pending sections for the ‘for-profit’ entities</li> <li>• Conduct more outreach</li> <li>• Collate responses out of survey and outreach</li> <li>• Finalise near final Report</li> </ul>	<p>In progress</p>
Sep 2018 (Depending on Board’s response to Q 2 below this	<p>Present near final version Report to Board</p> <p>Publication of Report</p>	<p>Not started</p> <p>Not started</p>

<b>PHASE 1 (FOR-PROFIT PRIVATE SECTOR):</b>		
<b>Key dates</b>	<b>Major project milestones</b>	<b>Staff comment</b>
timeline may get extended by 2-3 months)		
Oct 2018 (Depending on Board's response to Q 2 below this timeline may get extended by 2-3 months)	Present Report at ASAF	Not started

**PROJECT PLAN FOR NOT-FOR PROFIT PRIVATE AND PUBLIC SECTORS TO BE SUBMITTED AFTER COMPLETION OF PHASE 1**

**Project Team**

<b>Name(s)</b>	<b>Role</b>	<b>Responsibility</b>
Neha Juneja	Project Manager	Content expert; Project team leader
Robert Keys	Research Fellow	Technical review

**Key project risks**

<b>Risk</b>	<b>Impact</b>	<b>Mitigation</b>
Project milestones not met	Medium	Detailed project plan prepared, all staff on project are made aware of key dates.
Unfavourable response to project from stakeholders	High	Key stakeholders to be identified and engaged early.
Incorrect stakeholders identified or not informative	High	Engage Media/communications team early

**Communications plan**

<b>Project Milestone</b>	<b>Date</b>	<b>Communications needed</b>	<b>Lead time required</b>
Provide overview of project to AUASB staff and NZASB	Jun 18	Meeting and phone call/email	1 day
Identification of stakeholders and setting meetings	Jun 18	Online survey , with careful drafting of questions  Focus Group meetings  Personal interviews	
Present near final draft to Board	Sep 18	Formatting and styling of the Report	3 weeks

Project Milestone	Date	Communications needed	Lead time required
		Review of readability of Report and assistance with drafting of executive summary	2 weeks
Publication of Report	Sep 18  (Depending on Board's response to Q 2 below this timeline may get extended by 2-3 months)	Final formatting and styling of the Report	1 week
		Media release	2 week
		Twitter/LinkedIn/news item	2 days

#### Questions for Board members

Q1. Do Board members agree with the proposed project rationale, objective and project approach (including proposed plan to cover broader outreach) set out in paragraphs 3-10 and the proposed project plan set out in paragraph 12?

Q2. Do the Board members think the outreach relating to the for-profit sector needs to be extended to other international banks, investors and preparers such as those in the US, Europe, Asia, considering that this may strengthen the Research Report by providing international benchmarking. (This may have an impact on the proposed completion date by 2-3 months)

Q3. In relation to this project, once the 'for-profit' research is done, would the Board want us to undertake separate research in relation to not-for-profit private and public sectors, or whether the findings for the for-profit sector would be appropriate for those sectors without us undertaking further research? Additionally are there any sector specific issues relating to the not-for-profit private and public sectors that the board members identify we should start thinking about right now?