

Amendments to Australian Accounting Standards – Disclosure in Special Purpose Financial Statements of Compliance with Recognition and Measurement Requirements

Comments to the AASB by 19 August 2019



Australian Government

**Australian Accounting
Standards Board**

Commenting on this AASB Exposure Draft

Comments on this Exposure Draft are requested by 19 August 2019.

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@aaasb.gov.au

Phone: (03) 9617 7600

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

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Introduction

Australian Accounting Standards

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

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

Exposure Drafts

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

Why we are making these proposals

Australia is the only jurisdiction with a 'reporting entity' concept that effectively permits entities to self-assess what type of financial reporting they do when they are required by legislation or otherwise (such as by a constitutional document) to prepare financial statements in accordance with Australian Accounting Standards issued by the AASB.¹ Accordingly, some entities may elect to prepare special purpose financial statements (SPFS) instead of general purpose financial statements (GPFS).

Users of SPFS should be able to demand any information they need. However, based on the following feedback, the AASB is particularly concerned that the quality of disclosures in a significant number of SPFS is not sufficient to enable a user to determine what additional information they might need:

- (a) responses received to user surveys indicated the key requirements of financial statement users were comparability of recognition and measurement; and
- (b) near-final research² indicates that, for 34% of for-profit non-disclosing entities lodging SPFS with the Australian Securities and Investments Commission (ASIC) and 44% of medium and large charities lodging SPFS with the Australian Charities and Not-for-profits Commission (ACNC), it was **unclear** to the academics conducting the research whether or not the entities in question complied with the recognition and measurement (R&M) requirements in Australian Accounting Standards (AAS). In addition, the academics were unable to ascertain whether or not the entities had consolidated their subsidiaries or equity accounted all their investments in associates and joint ventures.

The AASB considers it unacceptable for financial statements available on the public record to have such low levels of transparency.

While the AASB is currently undertaking a broader project which proposes to address the problems of SPFS by removing the ability for certain entities to prepare SPFS when they are required to comply with AAS and replace them with GPFS – initially for for-profit entities and, in due course, not-for-profit entities – this project will take some time.

In light of this, the AASB decided to propose, as an interim measure, amendments to AAS to require entities preparing SPFS to make an explicit statement as to whether or not the accounting policies applied in the SPFS comply with all the R&M requirements in AAS. The AASB acknowledged that disclosure of this information is not sufficient to address the problems with publicly lodged SPFS, however the AASB decided that an amendment to AAS was urgently needed to provide greater transparency to users of publicly lodged SPFS and to also improve the comparability of SPFS.

Further, understanding the alignment between an entity's accounting policies and the R&M requirements in AAS would help entities assess the impact of any future transition from SPFS to GPFS.

1 Additional discussion on this uniquely Australian concept is contained in [AASB Research Report No 7 Financial Reporting Requirements Applicable to For-Profit Private Sector Companies](#).

2 Draft AASB Research Report XX *Financial Reporting Practices of For-Profit Entities Lodging SPFSs* and draft AASB Research Report YY *Review of Special Purpose Financial Statements: Large and Medium Sized Australian Charities*. While this research has not yet been published, the findings reported in this Exposure Draft are not expected to change.

The AASB considers the proposed disclosures would require minimal effort and cost, yet result in a significant improvement in the information available for users.³

The AASB also notes it is an important part of a director's duty⁴ and an auditor's responsibility⁵ to consider and clearly identify the financial reporting framework which forms the basis for the preparation of financial statements.

What we are proposing

This Exposure Draft proposes that those entities lodging SPFS with either ASIC or the ACNC (i.e. entities currently required to comply with AASB 1054 *Australian Additional Disclosures*),⁶ shall disclose:

- (a) the basis on which the decision to prepare SPFS was made;
- (b) where the entity has subsidiaries, investments in associates or investments in joint ventures, whether or not they have been consolidated or equity accounted in a manner consistent with the requirements set out in AAS. If the entity has not consolidated its subsidiaries or equity accounted its investments in associates or joint ventures consistently with those requirements, it shall disclose that fact, and the reasons why. However, if the entity is a not-for-profit (NFP) entity, and it has not determined whether or not its interests in other entities give rise to interests in subsidiaries, associates or joint ventures, the entity shall instead disclose that fact; and
- (c) an explicit statement as to whether or not the accounting policies applied in the financial statements comply with all the R&M requirements in AAS and, if not, an indication of where they do not comply. Where an entity's accounting policies do not comply with the R&M requirements in AAS, the AASB is NOT proposing and does not expect a quantification or reconciliation of the extent of non-compliance.

Application date

It is proposed that the amendments be applicable to annual periods ending on or after 30 June 2020, with early adoption encouraged.

What happens next

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

We need your feedback

Comments are invited on any of the proposals in this Exposure Draft by 19 August 2019. Submissions play an important role in the decisions that the AASB will make in regard to a Standard. The AASB would prefer that respondents express a clear overall opinion on whether the proposals, as a whole, are supported and that this opinion be supplemented by detailed comments, whether supportive or otherwise, on the major issues. The AASB regards supportive and non-supportive comments as essential to a balanced review of the issues and will consider all submissions, whether they address some or all specific matters, additional issues or only one issue (whether an issue specifically identified below or another issue).

3 Accounting Professional and Ethical Standard APES 205 *Conformity with Accounting Standards* contains a requirement for entities to identify "the purpose for which the Special Purpose Financial Statements have been prepared". While entities within the scope of APES 205 should already be including this information in their SPFS, this information alone is not sufficient to enable financial statement users to determine whether or not the accounting policies applied in the SPFS comply with all the R&M requirements in AAS.

4 Section 295 of the *Corporations Act 2001* requires an entity's financial statements be accompanied by a directors' declaration which includes a declaration by the directors regarding whether the financial statements and notes comply with accounting standards, and give a true and fair view of the financial position and performance of the company and any consolidated entity. Section 60.15 of the *Australian Charities and Not-for-profits Commission Regulation 2013* requires a similar declaration by the entity's responsible persons (e.g. the entity's Board or Committee of Management).

5 Australian Auditing Standards contain a number of requirements for auditors in respect of the responsibilities of those charged with governance and auditors regarding the selection and application of an entity's financial reporting framework. For example, ASA 800 *Special Considerations – Audits of Financial Reports Prepared in Accordance with Special Purpose Frameworks* requires that "the auditor shall obtain an understanding of the steps undertaken by management to determine that the applicable financial reporting framework is acceptable in the circumstances" and ASA 700 *Forming an Opinion and Reporting on a Financial Report* requires for example that "the auditor shall evaluate whether the financial report adequately refers to or describes the applicable financial reporting framework".

6 Entities lodging SPFS with the ACNC are required by the *Australian Charities and Not-for-profits Commission Regulation 2013* to comply with AASB 1054.

Specific matters for comment

The AASB would particularly value comments on the following:

- 1 Do you agree that an amendment to AAS to require entities to disclose information about their SPFS, including whether or not the entity has complied with all the R&M requirements in AAS, is needed to provide more transparency to users of publicly lodged SPFS and improve the comparability of SPFS? If not, please provide reasons.
- 2 Do you agree that the proposed amendments should apply only to those entities lodging SPFS with:
 - (a) ASIC under Part 2M.3 of the *Corporations Act 2001*; or
 - (b) the ACNC?If not, please provide reasons.
- 3 Do you agree with the proposed amendments to AASB 1054 requiring disclosure of:
 - (a) the basis for the preparation of the SPFS (reflected in the proposed amendment to paragraph 9 of AASB 1054);
 - (b) information about the consolidation or non-consolidation of subsidiaries and accounting for associates and joint ventures (reflected in the proposed new paragraphs 9A(a) and (b));
 - (c) an explicit statement as to whether or not the accounting policies applied in the financial statements comply with all the R&M requirements in AAS (including the requirement to disclose an indication of where they do not comply) (reflected in the proposed new paragraph 9A(c))?If you disagree with any aspect, please provide reasons.
- 4 The proposed Amending Standard includes implementation guidance and illustrative examples illustrating the application of the proposed disclosure requirements. Do you agree it provides appropriate illustration of the application of the disclosure requirements? If not, please provide reasons.
- 5 If the Amending Standard is issued before December 2019, do you agree with the proposed effective date of annual periods ending on or after 30 June 2020 (with early adoption permitted)? If not, please explain why.
- 6 Do you agree that an entity that has no subsidiaries, investments in associates or investments in joint ventures should not be required to make an explicit statement to this effect? If not, please provide reasons.
- 7 Do you agree that a not-for-profit entity that has not determined whether or not its interests in other entities give rise to subsidiaries, associates or joint ventures should be permitted to disclose only that fact, and should not also be required to disclose the reasons why? If not, please provide reasons (refer to paragraph BC32 in the Basis for Conclusions for the AASB's consideration of this matter).
- 8 Do you have any other comments on the proposals?

General matters for comment

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

- 9 Whether *The AASB's For-Profit Entity Standard-Setting Framework* and *The AASB's Not-for-Profit Entity Standard-Setting Framework* has been applied appropriately in developing the proposals in this Exposure Draft?
- 10 Whether there are any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals?
- 11 Whether, overall, the proposals would result in SPFS that would be more useful to users?
- 12 Whether the proposals are in the best interests of the Australian economy?
- 13 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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PREFACE

**[DRAFT] ACCOUNTING STANDARD
AASB 2019-X AMENDMENTS TO AUSTRALIAN ACCOUNTING STANDARDS – DISCLOSURE IN SPECIAL
PURPOSE FINANCIAL STATEMENTS OF COMPLIANCE WITH RECOGNITION AND MEASUREMENT
REQUIREMENTS**

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**[DRAFT] IMPLEMENTATION GUIDANCE AND ILLUSTRATIVE EXAMPLES
[DRAFT] BASIS FOR CONCLUSIONS**

[Draft] Australian Accounting Standard AASB 2019-X *Amendments to Australian Accounting Standards – Disclosure in Special Purpose Financial Statements of Compliance with Recognition and Measurement Requirements* is set out in paragraphs 1 – 8. All the paragraphs have equal authority.

Preface

Standards amended by AASB 2019-X

This [draft] Standard makes amendments to AASB 1054 *Australian Additional Disclosures* (May 2011).

Main features of this Standard

Main requirements

This [draft] Standard amends AASB 1054 *Australian Additional Disclosures* (May 2011) to require for-profit and not-for-profit entities that are required to apply AASB 1054 and are preparing special purpose financial statements to disclose information about those financial statements, including information that enables users of the financial statements to understand whether or not the accounting policies applied in the financial statements comply with all the recognition and measurement requirements in Australian Accounting Standards.

In particular, the amendments to AASB 1054 require an entity to disclose:

- (a) the basis on which the decision to prepare special purpose financial statements was made;
- (b) where the entity has subsidiaries, investments in associates or investments in joint ventures – whether or not they have been consolidated or equity accounted in a manner consistent with the requirements set out in Australian Accounting Standards. If the entity has not consolidated its subsidiaries or equity accounted its investments in associates or joint ventures consistently with those requirements, it shall disclose that fact, and the reasons why. However, if the entity is a not-for-profit entity, and it has not determined whether or not its interests in other entities give rise to interests in subsidiaries, associates or joint ventures, the entity shall instead disclose that fact; and
- (c) an explicit statement as to whether or not the accounting policies applied in the financial statements comply with all the recognition and measurement requirements in Australian Accounting Standards, and, if not, an indication of where they do not comply.

Application date

This [draft] Standard applies to reporting periods ending on or after ... [30 June 2020], with early adoption permitted.

[Draft] Accounting Standard AASB 2019-X

The Australian Accounting Standards Board makes Accounting Standard AASB 2019-X *Amendments to Australian Accounting Standards – Disclosure in Special Purpose Financial Statements of Compliance with Recognition and Measurement Requirements* under section 334 of the *Corporations Act 2001*.

Kris Peach

Dated ... [date]

Chair – AASB

[Draft] Accounting Standard AASB 2019-X Amendments to Australian Accounting Standards – Disclosure in Special Purpose Financial Statements of Compliance with Recognition and Measurement Requirements

Objective

- 1 This Standard amends AASB 1054 *Australian Additional Disclosures* (May 2011) to add requirements for for-profit and not-for-profit entities that are required to apply AASB 1054 and are preparing special purpose financial statements to disclose information about those financial statements, including information that enables users of the financial statements to understand whether or not the accounting policies applied in the financial statements comply with all the recognition and measurement requirements in Australian Accounting Standards.

Application

- 2 The amendments set out in this Standard apply to entities and financial statements in accordance with the application of AASB 1054 as set out in paragraph 7 of AASB 1057 *Application of Australian Accounting Standards* (as amended).
- 3 This Standard applies to annual periods ending on or after ... [30 June 2020]. This Standard may be applied to annual periods ending before ... [30 June 2020]. When an entity applies this Standard to such an annual period, it shall disclose that fact.
- 4 This Standard uses underlining, striking out and other typographical material to identify some of the amendments to AASB 1054, in order to make the amendments more understandable. However, the amendments made by this Standard do not include that underlining, striking out or other typographical material. Amended paragraphs are shown with deleted text struck through and new text underlined.

Amendments to AASB 1054 *Australian Additional Disclosures*

- 5 Paragraph 9 is amended as follows (new text is underlined):
- 9 An entity shall disclose in the notes whether the financial statements are general purpose financial statements or *special purpose financial statements*, and if special purpose financial statements, the basis on which the decision to prepare such statements was made.
- 6 Paragraphs 9A and 9B, and a related heading, are added as follows:

Information about special purpose financial statements

- 9A An entity that prepares special purpose financial statements shall:
- (a) where the entity has subsidiaries, investments in associates or investments in joint ventures – disclose whether or not they have been consolidated or equity accounted in a manner consistent with the requirements set out in AASB 10 *Consolidated Financial Statements* or AASB 128 *Investments in Associates and Joint Ventures*, as appropriate. If the entity has not consolidated its subsidiaries or equity accounted its investments in associates or joint ventures consistently with those requirements, it shall disclose that fact, and the reasons why;

- (b) notwithstanding paragraph (a), in respect of not-for-profit entities, if the entity has not determined whether or not its interests in other entities give rise to interests in subsidiaries, associates or joint ventures, the entity shall instead disclose that fact; and
- (c) disclose an explicit statement as to whether or not the accounting policies applied in the financial statements comply with all the recognition and measurement requirements in Australian Accounting Standards and, if not, an indication of where they do not comply.

9B *Implementation guidance and illustrative examples* accompanies this Standard. It illustrates the application of the requirements in paragraph 9A and their relationship to the requirements in AASB 101 *Presentation of Financial Statements* for the disclosure of an entity's significant accounting policies.

7 *Implementation guidance and illustrative examples* is attached to accompany AASB 1054 as set out on pages 10 to 16.

Commencement of the legislative instrument

8 For legal purposes, this legislative instrument commences on ... [date].

Implementation guidance and illustrative examples

The following implementation guidance and illustrative examples accompany, but are not part of, AASB 1054 Australian Additional Disclosures. They illustrate aspects of AASB 1054, but are not intended to provide interpretative guidance.

- IG1 The following flowcharts summarise some of the key decisions in determining how to apply the disclosure requirements in paragraph 9A of AASB 1054 in relation to special purpose financial statements.
- IG2 In disclosing the information required by paragraph 9A of AASB 1054, entities are not expected to provide quantitative information, or reconciliations, where accounting policies do not comply with all the recognition and measurement requirements in Australian Accounting Standards.

Chart 1 – For-profit entities preparing special purpose financial statements

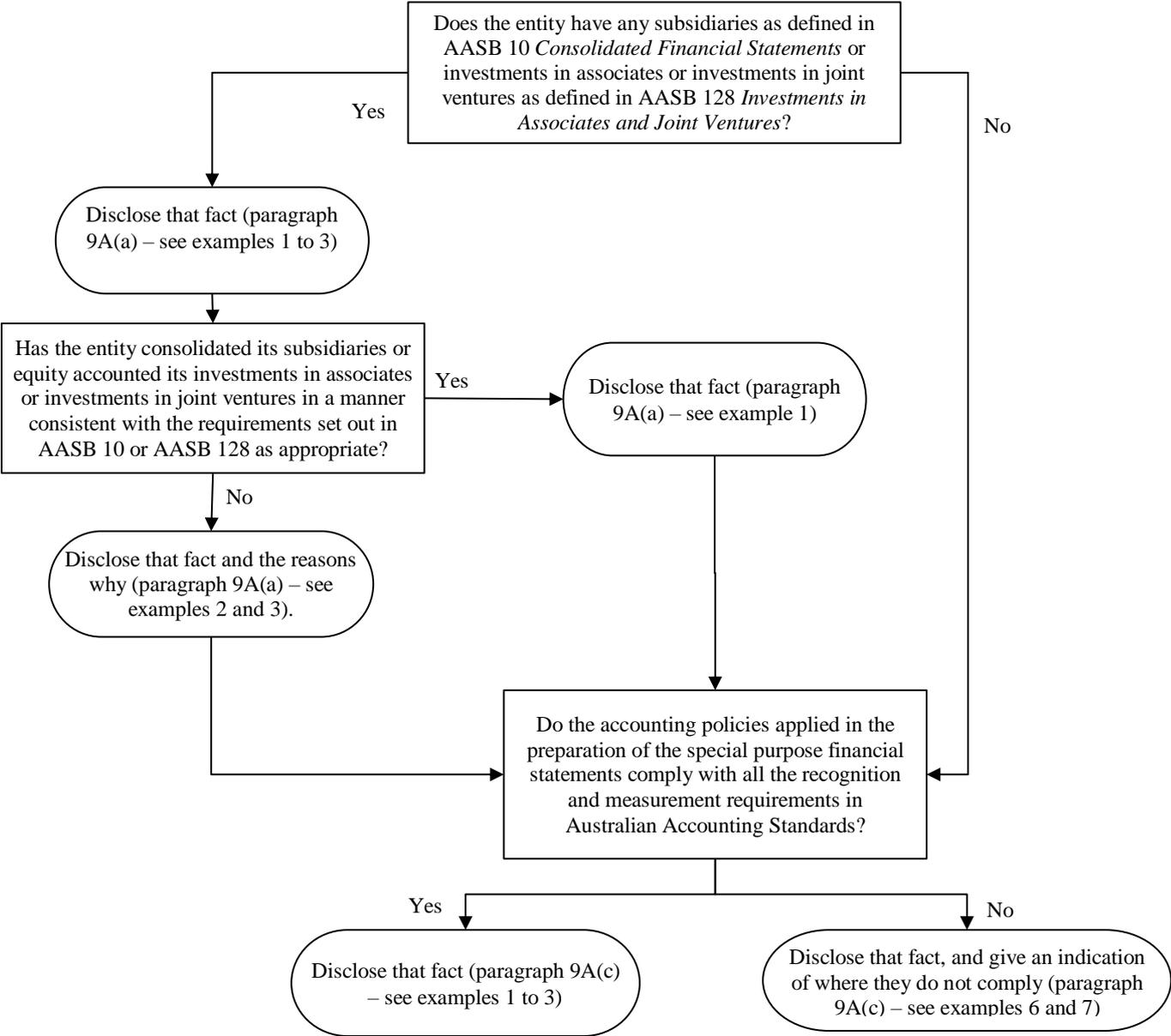
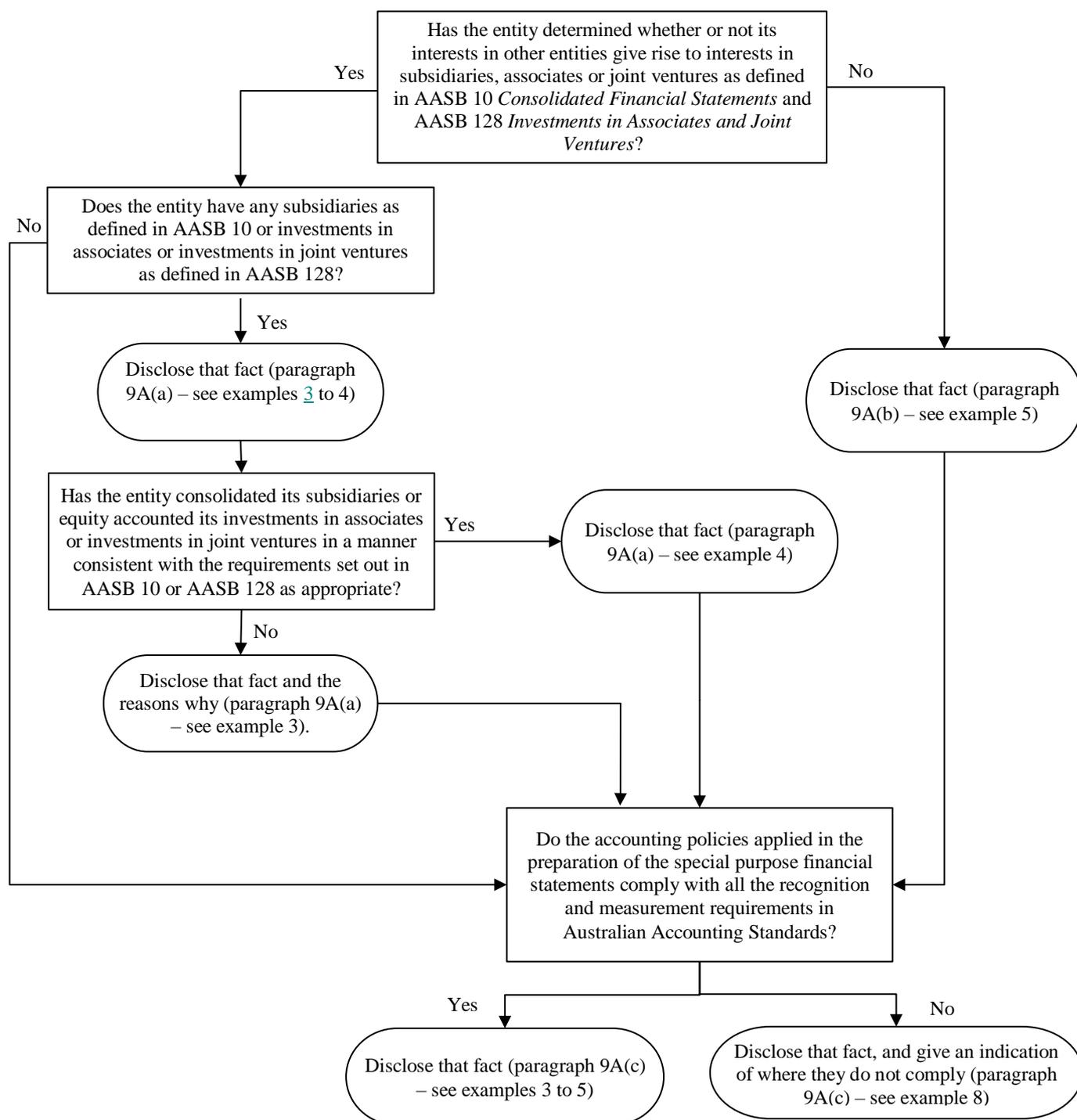


Chart 2 – Not-for-profit entities preparing special purpose financial statements



IG3 Entities required to apply AASB 1054 in their special purpose financial statements (including those lodged with the Australian Securities and Investments Commission (ASIC) or the Australian Charities and Not-for-profits Commission (ACNC)), whether consolidated or unconsolidated, are also required to apply AASB 101 *Presentation of Financial Statements* and AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*, including:

- (a) paragraph 15 of AASB 101, which requires the fair presentation of financial statements;
- (b) paragraphs 10-12 of AASB 108, which address the selection of accounting policies in the absence of an Australian Accounting Standard that specifically applies to a transaction, other event or condition; and

- (c) paragraph 117 of AASB 101, which requires disclosure of significant accounting policies comprising the measurement basis (or bases) and the other accounting policies used that are relevant to an understanding of the financial statements.

As a result, sufficient information to enable users of special purpose financial statements to obtain an understanding of the accounting policies adopted is required to be disclosed. This includes where an entity has selected and applied accounting policies that differ from the recognition and measurement requirements in Australian Accounting Standards.

IG4 In that regard, paragraph 9A(c) of AASB 1054 requires an entity to make an explicit statement as to whether or not the accounting policies applied in the financial statements comply with all the recognition and measurement requirements in Australian Accounting Standards, and if not, to provide an indication of where they differ. The nature of the disclosure providing such an indication would be expected to vary depending on the extent of non-compliance. For example an entity may choose to disclose which Australian Accounting Standards they have not complied with where the instances of non-compliance are not extensive (see Example 6 below). Alternatively where the instances of non-compliance are extensive, more meaningful information may arise from the entity choosing to disclose which Australian Accounting Standards they have complied with (see Examples 7 and 8 below).

IG5 In relation to paragraph 9A(a) of AASB 1054, information about the accounting for subsidiaries and investments in associates and investments in joint ventures is fundamental for a user's understanding of the scope of the financial statements. Exemptions from consolidation of subsidiaries are provided in AASB 10 *Consolidated Financial Statements*, paragraphs 4(a) and Aus4.1 (as modified by paragraph Aus4.2), including when the entity is a wholly-owned subsidiary and its ultimate parent produces consolidated financial statements that are available for public use and comply with accounting standards. Furthermore, an exception from consolidation under certain circumstances when a parent is an investment entity is provided in paragraph 4B of AASB 10. Directors preparing special purpose financial statements might have other reasons for non-consolidation of some or all of an entity's subsidiaries, and paragraph 9A(a) requires those reasons to be disclosed.

IG6 The following illustrative examples are provided:

| Scenario/Example | | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 |
|---|-----------|---|---|---|---|--------------|-----|-----|-----|
| Reporting Framework | Corps Act | x | x | x | | | x | x | |
| | ACNC | | | | x | x | | | x |
| Subsidiaries | Yes | x | x | x | x | Not assessed | | | |
| | No | | | | | | x | x | x |
| Consolidated | Yes | x | | | x | | n/a | n/a | n/a |
| | No | | x | | | x | | | |
| | Partially | | | x | | | | | |
| Associates / Joint Ventures Equity Accounted | Yes | x | | | x | Not assessed | | | |
| | No | | x | x | | | x | x | x |
| Accounting policies comply with all the recognition and measurement requirements in Australian Accounting Standards | Yes | x | x | x | x | x | | | |
| | No | | | | | | x | x | x |

IG7 The following examples illustrate how an entity might apply the disclosure requirements in paragraph 9A of AASB 1054 within the context of the requirements in AASB 101 and AASB 108 referred to in paragraph IG4 above to the special purpose financial statements they prepare, on the basis of the limited facts presented. Although some aspects of the examples might be present in actual fact patterns, all relevant facts and circumstances of a particular fact pattern need to be evaluated when applying AASB 1054.

| # | Example | Illustrative disclosure |
|---|--|---|
| 1 | ABC Ltd, a for-profit parent, prepares consolidated special purpose financial statements that: | ABC Ltd, a for-profit entity, has prepared special purpose financial statements as, in the opinion of the directors, it is unlikely there are users of these financial statements who are not in a position to require the preparation of reports tailored to their information needs. Accordingly, these financial |

| # | Example | Illustrative disclosure |
|---|---|--|
| | <ul style="list-style-type: none"> • consolidate all of its subsidiaries in a manner consistent with the requirements set out in AASB 10; • equity account all its investments in associates and investments in joint ventures in a manner consistent with the requirements set out in AASB 128; and • apply accounting policies that comply with all the recognition and measurement requirements in Australian Accounting Standards. | <p>statements have been prepared to satisfy the directors' reporting requirements under the <i>Corporations Act 2001</i>.</p> <p>ABC Ltd has consolidated all its subsidiaries in a manner consistent with the requirements set out in AASB 10 <i>Consolidated Financial Statements</i> and equity accounted all its investments in associates and investments in joint ventures, in a manner consistent with the requirements set out in AASB 128 <i>Investments in Associates and Joint Ventures</i>. These consolidated special purpose financial statements comply with all the recognition and measurement requirements in Australian Accounting Standards. The significant accounting policies adopted in the special purpose financial statements are [set out below/in <i>Note XX</i>]¹.</p> |
| 2 | <p>EFG Ltd, a for-profit parent, prepares unconsolidated special purpose financial statements (which is consistent with AASB 10's criteria for exemption/exception from consolidation) and applies accounting policies that comply with all the recognition and measurement requirements in Australian Accounting Standards in those unconsolidated special purpose financial statements.</p> | <p>EFG Ltd, a for-profit entity, has prepared special purpose financial statements as, in the opinion of the directors, it is unlikely there are users of these financial statements who are not in a position to require the preparation of reports tailored to their information needs. Accordingly, these financial statements have been prepared to satisfy the directors' reporting requirements under the <i>Corporations Act 2001</i>.</p> <p>Consistent with the exemptions from consolidation set out in AASB 10 <i>Consolidated Financial Statements</i>, these financial statements do not consolidate EFG Ltd's subsidiaries as [EFG Ltd is a wholly-owned subsidiary and its ultimate parent HIJ Ltd produces consolidated financial statements that are available for public use and comply with Australian Accounting Standards].</p> <p>EFG Ltd's unconsolidated special purpose financial statements comply with all the recognition and measurement requirements in Australian Accounting Standards. The significant accounting policies adopted in the special purpose financial statements are [set out below/in <i>Note XX</i>].</p> |
| 3 | <p>MNO Ltd, a parent, prepares partially consolidated special purpose financial statements that:</p> <ul style="list-style-type: none"> • consolidate some but not all of its subsidiaries (and are therefore inconsistent with the requirements set out in AASB 10); • do not equity account all its investments in associates and investments in joint ventures in a manner consistent with the requirements set out in AASB 128; and • apply accounting policies to those partially consolidated financial statements that comply with all the recognition and measurement requirements in Australian Accounting Standards. | <p>MNO Ltd, a [for-profit/not-for-profit] entity, has prepared special purpose financial statements as, in the opinion of the directors, is it unlikely there are users of these financial statements who are not in a position to require the preparation of reports tailored to their information needs. Accordingly, these financial statements have been prepared to satisfy the directors' reporting requirements under [the <i>Corporations Act 2001/Australian Charities and Not-for-profits Commission Act 2012</i>].</p> <p>These financial statements do not consolidate all of MNO Ltd's subsidiaries or equity account all its investments in associates and investments in joint ventures as the directors have determined that [insert an explanation of why some subsidiaries, associates and joint ventures are not consolidated / equity accounted.]</p> <p>MNO Ltd's partially consolidated special purpose financial statements comply with all the recognition and measurement requirements in Australian Accounting Standards. The significant accounting policies adopted in the special purpose financial statements are [set out below/in <i>Note XX</i>].</p> |
| 4 | <p>Charity A Inc, a not-for-profit parent, prepares consolidated special purpose financial statements that:</p> | <p>Charity A Inc, a not-for-profit entity, has prepared special purpose financial statements as, in the opinion of the [Management Committee], it is unlikely there are users of these financial statements who are not in a position to require</p> |

¹ Text in square brackets throughout the illustrative disclosures provides examples of alternative disclosures indicating that preparers should tailor the disclosures to suit the facts and circumstances of the relevant entity preparing the special purpose financial statements.

| # | Example | Illustrative disclosure |
|---|---|--|
| | <ul style="list-style-type: none"> • consolidate all its subsidiaries in a manner consistent with the requirements set out in AASB 10; • equity account all its investments in associates and investments in joint ventures in a manner consistent with the requirements set out in AASB 128; and • apply accounting policies that comply with all the recognition and measurement requirements in Australian Accounting Standards. | <p>the preparation of reports tailored to their information needs. Accordingly, these financial statements have been prepared to satisfy the [Management Committee]’s reporting requirements under [the <i>Australian Charities and Not-for-profits Commission Act 2012</i> / insert details of the not-for-profit reporting framework under which the financial statements are prepared].</p> <p>Charity A Inc has consolidated all its subsidiaries consistent with the requirements set out in AASB 10 <i>Consolidated Financial Statements</i> and equity accounted for its investments in associates and investments in joint ventures in a manner consistent with the requirements set out in AASB 128 <i>Investments in Associates and Joint Ventures</i>.</p> <p>These consolidated special purpose financial statements comply with all the recognition and measurement requirements in Australian Accounting Standards. The significant accounting policies adopted in the special purpose financial statements are [set out below/in <i>Note XX</i>].</p> |
| 5 | <p>Charity B Inc, a not-for-profit entity, prepares special purpose financial statements that:</p> <ul style="list-style-type: none"> • do not consolidate or equity account any entities as Charity B did not determine whether its interests in other entities give rise to interests in subsidiaries, associates or joint ventures; and • apply accounting policies that comply with all the recognition and measurement requirements in Australian Accounting Standards. <p>The legislative framework in which Charity B Inc operates does not require it to identify subsidiaries, associates or joint ventures.</p> | <p>Charity B Inc, a not-for-profit entity, has prepared special purpose financial statements as, in the opinion of the [Management Committee], it is unlikely there are users of these financial statements who are not in a position to require the preparation of reports tailored to their information needs. Accordingly, these financial statements have been prepared to satisfy the [Management Committee]’s reporting requirements under [the <i>Australian Charities and Not-for-profits Commission Act 2012</i>/insert details of the not-for-profit reporting framework under which the financial statements are prepared].</p> <p>Charity B Inc has not assessed whether it has relationships with other entities which, for financial reporting purposes, might be considered subsidiaries, associates or joint ventures.</p> <p>These special purpose financial statements comply with all the recognition and measurement requirements in Australian Accounting Standards. The significant accounting policies adopted in the special purpose financial statements are [set out below/in <i>Note XX</i>].</p> |
| 6 | <p>XYZ Ltd, a for-profit entity, does not have any subsidiaries, associates or joint ventures and prepares special purpose financial statements that apply accounting policies that do not comply with all the recognition and measurement requirements in Australian Accounting Standards. The differences are not extensive.</p> | <p>XYZ Ltd, a for-profit entity, has prepared special purpose financial statements as, in the opinion of the directors, it is unlikely there are users of these financial statements who are not in a position to require the preparation of reports tailored to their information needs. Accordingly, these financial statements have been prepared to satisfy the directors’ reporting requirements under the <i>Corporations Act 2001</i>.</p> <p>These special purpose financial statements do not comply with all the recognition and measurement requirements in Australian Accounting Standards.</p> <p>The recognition and measurement requirements that have not been complied with are those specified in [AASB 112 <i>Income Taxes</i> as deferred tax has not been recognised / insert details that indicate which material recognition and measurement requirements in Australian Accounting Standards have not been complied with]. The significant accounting policies adopted in the special purpose financial statements are [set out below/in <i>Note XX</i>].</p> |
| 7 | <p>MLK Ltd, a for-profit entity, does not have any subsidiaries, associates or joint ventures and prepares special purpose financial</p> | <p>MLK Ltd, a for-profit entity, has prepared special purpose financial statements as, in the opinion of the directors, it is unlikely there are users of these financial statements who are</p> |

| # | Example | Illustrative disclosure |
|---|--|--|
| | <p>statements that apply accounting policies that do not comply with all the recognition and measurement requirements in Australian Accounting Standards. Although the differences have not been quantified, they are extensive.</p> | <p>not in a position to require the preparation of reports tailored to their information needs. Accordingly, these financial statements have been prepared to satisfy the directors' reporting requirements under the <i>Corporations Act 2001</i>.</p> <p>These special purpose financial statements do not comply with all the recognition and measurement requirements in Australian Accounting Standards.</p> <p>The significant accounting policies adopted in the special purpose financial statements include:</p> <ul style="list-style-type: none"> - [in accounting for income taxes, deferred tax has not been recognised, which does not comply with AASB 112 <i>Income Taxes</i>; - in accounting for property, plant and equipment, assets were not depreciated based on their useful lives and instead were [provide details of the accounting policy], which does not comply with AASB 116 <i>Property, Plant and Equipment</i>; - in accounting for impairments, the recoverable amount for impairment testing was calculated on an undiscounted basis, which does not comply with AASB 136 <i>Impairment of Assets</i>; - revenue is not recognised until control of the goods has been passed to our customers, usually upon physical delivery; and - insert further details, including an indication where material recognition and measurement requirements in Australian Accounting Standards have not been complied with]. <p>OR</p> <p>[The significant accounting policies adopted in the special purpose financial statements are set out in notes X-Y and provide an indication of where the recognition and measurement requirements in Australian Accounting Standards have not been complied with.]</p> |
| 8 | <p>Charity D Inc, a not-for-profit entity, does not have any subsidiaries, associates or joint ventures and prepares special purpose financial statements that apply accounting policies that do not comply with all the recognition and measurement requirements in Australian Accounting Standards. Although the differences have not been quantified, they are extensive.</p> | <p>Charity D Inc, a not-for-profit entity, has prepared special purpose financial statements as, in the opinion of the [Management Committee], it is unlikely there are users of these financial statements who are not in a position to require the preparation of reports tailored to their information needs. Accordingly, these financial statements have been prepared to satisfy the [Management Committee]'s reporting requirements under [the <i>Australian Charities and Not-for-profits Commission Act 2012</i>/insert details of the not-for-profit reporting framework under which the financial statements are prepared].</p> <p>These special purpose financial statements do not comply with all the recognition and measurement requirements in Australian Accounting Standards.</p> <p>The significant accounting policies adopted in the special purpose financial statements include:</p> <ul style="list-style-type: none"> - [in accounting for income, recognition of certain types of grant income has been deferred until the related expenses are incurred, which does not comply with AASB 1058 <i>Income of Not-for-Profit Entities</i>; - in accounting for employee benefits, the long term provision for long service leave was not discounted, |

| # | Example | Illustrative disclosure |
|---|---------|--|
| | | <p>which does not comply with AASB 119 <i>Employee Benefits</i>; and</p> <ul style="list-style-type: none"> - insert further details including an indication where material recognition and measurement requirements in Australian Accounting Standards have not been complied with]. <p>OR</p> <p>[The significant accounting policies adopted in the special purpose financial statements are set out in notes X-Y and provide an indication of where the recognition and measurement requirements in Australian Accounting Standards have not been complied with.]</p> |

Basis for Conclusions

This Basis for Conclusions accompanies, but is not part of, AASB 2019-X Amendments to Australian Accounting Standards – Disclosure in Special Purpose Financial Statements of Compliance with Recognition and Measurement Requirements.

Introduction

BC1 This Basis for Conclusions summarises the Australian Accounting Standards Board’s considerations in reaching the conclusions in this Exposure Draft. It sets out the reasons why the Board developed the Exposure Draft, the approach taken to developing the Exposure Draft and the bases for the key decisions made. In making decisions, individual Board members gave greater weight to some factors than to others.

Reasons for developing the Exposure Draft

BC2 Australia is the only jurisdiction with a ‘reporting entity’ concept that effectively permits entities to self-assess what type of financial reporting they do when they are required by legislation or otherwise (such as by a constitutional document) to prepare financial statements in accordance with Australian Accounting Standards (issued by the Australian Accounting Standards Board). Therefore, unlike other jurisdictions, in Australia two similar entities might prepare very different sets of financial statements, one preparing general purpose financial statements using a robust and consistent framework, and the other preparing special purpose financial statements with self-selected requirements. The Board notes that the self-selection is subject to some constraints, imposed by paragraphs 7 and 10 to 12 of AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*.

BC3 Appendix A of AASB 1053 *Application of Tiers of Australian Accounting Standards* defines what a reporting entity is,¹ and Statement of Accounting Concepts SAC 1 *Definition of the Reporting Entity* also sets out the reporting entity concept. Paragraph 41 of SAC 1 states that “Reporting entities shall prepare general purpose financial reports.”² In relation to a group, SAC 1 states in paragraph 17 that “the group, which may be termed an economic entity, will be a reporting entity where there exist users dependent on general purpose financial reports for making and evaluating resource allocation decisions regarding the collective operations of the group of entities”.

BC4 An entity that assesses itself to be a non-reporting entity can therefore prepare special purpose financial statements, which are not necessarily consistent, comparable, transparent or enforceable. In particular, special purpose financial statements do not always comply with the recognition and measurement requirements³ in Australian Accounting Standards and nor do they always disclose that fact. The Board is aware of the view of some, that this situation is acceptable because, by inference, users of special purpose financial statements can demand any information they need. However, the Board has received feedback that in practice that is often not the case. Providing users with additional information will better enable them to confidently assess an entity’s level of compliance with the recognition and measurement requirements in Australian Accounting Standards in special purpose financial statements. Clear information about the areas of difference may better support users in identifying where additional information is required.

BC5 In developing this Exposure Draft, the Board considered the responses received to its user surveys⁴ which indicated that comparability, transparency, comprehensibility and consistency are what is most important to users when they are reading financial statements. For example, comparability of the recognition and measurement requirements in Australian Accounting Standards was rated 88% in importance to primary users

1 “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.” AASB 1053, Appendix A.

2 A “ ‘general purpose financial report’ means a financial report intended to meet the information needs common to users who are unable to command the preparation of reports tailored so as to satisfy, specifically, all of their information needs”. SAC 1, paragraph 6

3 For those entities that are required to prepare and lodge financial statements with Australian Securities and Investments Commission (ASIC) by Part 2M.3 of the *Corporations Act 2001*, and who are preparing special purpose financial statements, paragraph 2 of ASIC Regulatory Guide 85 *Reporting requirements for non-reporting entities* states “... ASIC believes that non-reporting entities, which are required to prepare financial reports in accordance with Chapter 2M of the *Corporations Act 2001* (Act), should comply with the recognition and measurement requirements of accounting standards”. For those entities that are required to prepare and lodge financial statements with the Australian Charities and Not-for-profits Commission (ACNC), “section 60.10(3) of ACNC Regulations requires financial statements and notes give a ‘true and fair view’, and the determination is required by the charity as well as the auditors in their audit report.

4 AASB Staff Paper: *Enhancing the revised Conceptual Framework and replacing Special Purpose Financial Statements, For-profit User and Preparer Survey Results* (December 2018)

and 100% in importance to other users.⁵ The Board also considered two near-final research reports, the first of which considers the financial reporting practices of for-profit non-disclosing entities lodging special purpose financial statements with ASIC,⁶ and the second of which considers the reporting practices of large and medium charities lodging special purpose financial statements with the ACNC.⁷

BC6 An analysis of the reporting practices of for-profit non-disclosing entities lodging financial statements with ASIC estimated that 72% of those entities prepared and publicly lodged special purpose financial statements in 2018.

BC7 It is further estimated that of those for-profit non-disclosing entities preparing and lodging special purpose financial statements:

- (a) 66% explicitly stated that they followed the recognition and measurement requirements in Australian Accounting Standards;⁸
- (b) 10% were assessed to have complied with the recognition and measurement requirements in Australian Accounting Standards based on a qualitative review of the accounting policies, despite the absence of an explicit statement to that effect;
- (c) 10% did not comply with the recognition and measurement requirements in Australian Accounting Standards (of which only 0.5% clearly stated so); and
- (d) the extent of compliance (or otherwise) with the recognition and measurement requirements in Australian Accounting Standards of the remaining 14% was unclear.

The Board however noted, that when performing their initial assessment as to whether or not the accounting policies applied in the special purpose financial statements complied with the recognition and measurement requirements in Australian Accounting Standards, it was initially unclear to the researchers whether or not 34% of the entities in question complied with the recognition and measurement requirements in Australian Accounting Standards.

BC8 The research examining the reporting practices of large and medium charities lodging financial statements with the ACNC in 2016 estimates that approximately 36% of those charities declared that they were preparing special purpose financial statements based on data obtained from the 2016 Annual Information Statements lodged with the ACNC. It is estimated that, of those charities preparing and lodging special purpose financial statements, approximately 26% state compliance with recognition and measurement requirements of the AAS. 30% state non-compliance with the recognition and measurements requirements of the AAS. It is not clear for the remaining 44% whether or not they complied with the recognition and measurement requirements in Australian Accounting Standards.

BC9 In addition to it being difficult for the researchers to understand the extent of alignment of an entity's accounting policies to the recognition and measurement requirements in Australian Accounting Standards, the researchers were also unable to ascertain whether or not an entity had fully consolidated its subsidiaries or equity accounted all its investments in associates and investments in joint ventures.

BC10 The Board discussed the results of the research outlined above and also feedback obtained from respondents to user surveys, along with evidence supporting the existence of users of financial statements, including special purpose financial statements.⁹ The Board also discussed the feedback obtained from users in response to its Invitation to Comment ITC 39 *Applying the IASB's Revised Conceptual Framework and Solving the Reporting Entity and Special Purpose Financial Statement Problems* (May 2018), and concluded that the inability of users of special purpose financial statements to determine whether or not an entity has complied with all the recognition and measurement requirements in Australian Accounting Standards is problematic. The Board also noted the importance of consistency, comparability, transparency and enforceability in financial reporting to special purpose financial statement users, and that at times users and stakeholders alike were unaware that some special purpose financial statements (where the preparation of financial statements in compliance with Australian Accounting Standards is required by legislation or otherwise) did not comply with all the

5 Throughout the User Survey Report, 'primary users' refers to users that meet the definition of primary users in AASB Practice Statement 2 *Making Materiality Judgements* (i.e. investors (and analysts), lenders and other creditors) and all other respondents are referred to as 'other users'.

6 Draft AASB Research Report XX *Financial Reporting Practices of For-Profit Entities Lodging SPFSs*. While this research has not yet been published, the findings reported in this Exposure Draft are not expected to change.

7 Draft AASB Research Report YY *Review of Special Purpose Financial Statements: Large and Medium Sized Australian Charities*. While this research has not yet been published, the findings reported in this Exposure Draft are not expected to change.

8 To determine whether or not an entity's accounting policies complied with all the recognition and measurement requirements in Australian Accounting Standards, Research Report XX outlines a number of phrases which could be used by an entity, and which if included in an entity's financial statements resulted in the entity being deemed to have stated compliance with all the recognition and measurement requirements in Australian Accounting Standards. When determining whether or not an entity complied with all the recognition and measurement requirements in Australian Accounting Standards, the results of Research Report XX focused only on compliance with all recognition and measurement requirements and did not identify whether or not entities prepared consolidated financial statements.

9 It is understood, for example, that approximately 98,000 sets of financial statements are purchased from ASIC each year, at least some of which are special purpose financial statements.

recognition and measurement requirements in Australian Accounting Standards and consolidation. Adoption of the proposals in this Exposure Draft would help address these issues.

- BC11 The Board was also particularly concerned that the quality of disclosures in a significant number of special purpose financial statements is not adequate to enable a user to determine what additional information they might need. As noted in paragraph BC7 above research indicated that, for 34% of for-profit non-disclosing entities lodging SPFS with ASIC and 44% of medium and large charities lodging SPFS with the ACNC, it was unclear to the academics conducting the research whether or not the entities in question complied with the recognition and measurement requirements in Australian Accounting Standards. The Board considers this to be unacceptable given the feedback received from users indicated that comparability of the recognition and measurement requirements was of high importance (refer paragraph BC5 above).
- BC12 In light of the Board's current broader project proposing to remove the ability for certain entities to prepare special purpose financial statements when they are required to comply with Australian Accounting Standards,¹⁰ the Board considered whether it was necessary and timely to require an entity preparing special purpose financial statements to disclose an explicit statement as to whether or not the accounting policies applied in the financial statements comply with all the recognition and measurement requirements in Australian Accounting Standards. This is an interim measure aimed at addressing these concerns given the project proposing to remove special purpose financial statements will take some time.
- BC13 In considering whether such disclosure was necessary, the Board also considered whether any existing disclosure requirements in Australian Accounting Standards or other pronouncements required the disclosure of similar information.
- BC14 The Board noted that paragraph 117 of AASB 101 *Presentation of Financial Statements*, which applies not only to general purpose financial statements but also directly to the special purpose financial statements of entities required to prepare financial reports in accordance with the *Corporations Act 2001*,¹¹ requires an entity to disclose its significant accounting policies. The Board also noted that, where it applies, paragraph 6.1 of Accounting Professional and Ethical Standard APES 205 *Conformity with Accounting Standards* (October 2015) issued by the Accounting Professional and Ethical Standards Board (APESB) also requires that an entity's special purpose financial statements clearly identify "the significant accounting policies adopted in the preparation of the special purpose financial statements"¹². The Board however noted that while these disclosures provide information about an entity's accounting policies, they would not necessarily provide users with sufficient information about an entity's compliance with all the recognition and measurement requirements in Australian Accounting Standards.
- BC15 On the basis of the considerations outlined in paragraphs BC2 to BC14 above, the Board decided that an amendment to Australian Accounting Standards to require entities to disclose an explicit statement as to whether or not the accounting policies applied in the financial statements comply with all the recognition and measurement requirements in Australian Accounting Standards was urgently needed to provide greater transparency to users of publicly lodged special purpose financial statements and to improve the comparability of special purpose financial statements. The Board also acknowledged that disclosure of this information is not sufficient to address the problems of special purpose financial reporting, however it provides a practical interim means of improving the quality of information provided to users of special purpose financial statements.
- BC16 The Board noted that, when preparing the required disclosure, entities would need to consider how their existing accounting policies compare with all the recognition and measurement requirements in Australian Accounting Standards. While the Board confirmed that the amendment would not require an entity to change its existing accounting policies, understanding how closely the entity's existing accounting policies are aligned to the recognition and measurement requirements in Australian Accounting Standards would also help entities assess the impact of any future transition from special purpose financial statements to general purpose financial statements.
- BC17 The significant issues considered by the Board are addressed in the following section.

10 This project proposes to remove ability for certain entities to prepare special purpose financial statements when they are required to comply with Australian Accounting Standards via a phased approach, firstly in relation to for-profit entities and, in due course, in relation to not-for-profit entities.

11 And indirectly through other legislation that imposes the application of AASB 101 in the preparation of special purpose financial statements. For example, the *Australian Charities and Not-for-profits Commission Act 2012*, through section 60.30 of the *Australian Charities and Not-for-profits Commission Regulation 2013*, requires charities lodging special purpose financial statements with the ACNC to comply with AASB 101, despite the fact that the application paragraph of that Standard does not directly encompass them.

12 Paragraph 6.1(c) of APES 205.

Significant issues

Scope

- BC18 In deciding who should be required to make the disclosures proposed in this Exposure Draft, the Board considered *The AASB's For-Profit Entity Standard-Setting Framework* and *The AASB's Not-for-Profit Entity Standard-Setting Framework*, and decided the proposals would be consistent with both frameworks and therefore should apply to for-profit and not-for-profit entities.
- BC19 In making this decision, the Board had particular regard to the following factors:
- (a) the uncertainty about whether or not the accounting policies applied in the financial statements comply with all the recognition and measurement requirements in Australian Accounting Standards described in paragraphs BC7 and BC8 above significantly adversely impacts financial statement users in both the for-profit and not-for-profit sectors;
 - (b) financial statement users have noted during AASB outreach to date¹³ the lack of, and need to improve, comparability, consistency, transparency and enforceability in special purpose financial statements;
 - (c) the evidence of diversity in the application of, and compliance with, the recognition and measurement requirements in Australian Accounting Standards in special purpose financial statements noted in Research Report XX and Research Report YY (as referred to in paragraphs BC7 and BC8 above);
 - (d) the significant number of charities preparing special purpose financial statements and the low levels of explicit statements of compliance with recognition and measurement requirements in Australian Accounting Standards therein (refer paragraph BC8 above); and
 - (e) the requirements of Australian Auditing Standards as they relate to special purpose financial statements (refer to paragraph BC27 below).
- BC20 When deciding which for-profit and not-for-profit entities should be required to make the disclosures, the Board considered whether the disclosures should be required by:
- (a) all entities preparing special purpose financial statements (including those preparing financial statements voluntarily); or
 - (b) all entities preparing special purpose financial statements that are required by legislation or otherwise to comply with Australian Accounting Standards; or
 - (c) only those entities preparing special purpose financial statements that are directly subject to AASB 101 and AASB 1054 *Australian Additional Disclosures*¹⁴, as set out in paragraph 2 of AASB 1054 and paragraph 7 of AASB 1057 *Application of Australian Accounting Standards*, (and, indirectly, any entities required through legislation to comply with AASB 101 and AASB 1054, such as entities lodging special purpose financial statements with the ACNC as they are required by legislation to comply with AASB 101 and AASB 1054 (as noted in footnote 11 to paragraph BC14 above)).
- BC21 As one objective of the disclosures proposed in this Exposure Draft is to provide information to users of special purpose financial statements about whether or not the entity has complied with all the recognition and measurement requirements in Australian Accounting Standards, the Board considered that while there was merit in requiring all entities required by legislation or otherwise to comply with Australian Accounting Standards preparing special purpose financial statements to make the disclosure, to do so was not warranted. This is consistent with the current scope of Australian Accounting Standards and the Board's role and expertise, which is to determine the appropriate accounting framework and accounting standards that should apply where legislation, regulation or other authority requires the preparation of financial statements that comply with Australian Accounting Standards.
- BC22 The Board did acknowledge that if the disclosures were required only by entities subject to AASB 101 and AASB 1054, there may be a large number of entities preparing special purpose financial statements when required to comply with Australian Accounting Standards that would not be required to make the disclosures (e.g. entities outside the scope of the *Corporations Act 2001* and entities not regulated by the ACNC). The Board however made the observation that many of these entities are expected to fall within the scope of APES 205, as the intention of APES 205 is to set requirements for members¹⁵ who are involved in the preparation, presentation, audit, review or compilation of financial statements for entities that are outside the

¹³ Such outreach included responses received on ITC 39, user surveys and participation of stakeholders at ITC 39 roundtable events.

¹⁴ And AASB 107 *Cash Flow Statements*, AASB 108 and AASB 1048 *Interpretation of Standards*, although they were not considered appropriate candidates to give effect to the proposed amendments, as noted in paragraph BC24 below.

¹⁵ APES 205 defines a member as "a member of a professional body that has adopted this Standard as applicable to their membership as defined by that professional body". APES 205 is therefore applicable, to and mandatory for, accounting professionals who are members of CPA Australia, Chartered Accountants Australia and New Zealand or the Institute of Public Accountants. This includes accountants working in accounting firms (of all sizes), the corporate sector and in government. Therefore, although its reach is limited, it is broader than that of AASB 1054.

scope of the *Corporations Act 2001*. Therefore, to possibly mitigate (albeit not eliminate) concerns about entities outside the scope of AASB 101 and AASB 1054 not being required to make the disclosures, the matter was raised with staff of the APESB as to whether the APESB might consider, following its own due process, making any consequential amendments to APES 205 consistent with the amendments to the affected Australian Accounting Standard proposed in this Exposure Draft. The Board will monitor any work the APESB might undertake and continue to liaise with staff of the APESB on this matter, keeping them informed of the outcome of this Exposure Draft. The Board will also inform other regulators of the outcome of this Exposure Draft, which will help them consider whether there are any regulatory consequences of the proposed disclosure requirements.

BC23 For the reasons outlined in paragraph BC21 and BC22 above, the Board decided it was not necessary to broaden the application paragraphs of AASB 101 or AASB 1054, and therefore the amendment should apply in the manner described in paragraph BC20(c) above.

BC24 The Board then considered whether the disclosure requirement should be effected through AASB 101 or AASB 1054. They were identified as the only two reasonable candidates as vehicles for housing the requirements because they already have related requirements: AASB 101 includes requirements relating to the disclosure of accounting policies and compliance with Standards, and AASB 1054 includes requirements relating to compliance with Australian Accounting Standards and explicitly refers to special purpose financial statements. The Board’s preferred approach was to amend AASB 1054 because the amendment is Australian-specific, specifically relates to special purpose financial statements, and is consistent with the objective of AASB 1054 “... to set out Australian-specific disclosure requirements that are in addition to the disclosure requirements of International Financial Reporting Standards”.

Disclosures regarding the basis for the decision to prepare special purpose financial statements

BC25 Paragraph 9 of AASB 1054 requires an entity to disclose whether the financial statements are general purpose or special purpose. The Board decided that entities should also be required to disclose the reasons why the preparation of special purpose financial statements was considered appropriate.

BC26 In making this decision, the Board noted that APES 205 contains a requirement for entities to identify “the purpose for which the Special Purpose Financial Statements have been prepared”¹⁶ and therefore entities within the scope of APES 205 should already be including this information in special purpose financial statements, however mandating it in an Australian Accounting Standard would help ensure users are provided with useful information.

BC27 The Board also noted the requirements of Australian Auditing Standards and the existing responsibilities of those charged with governance and auditors with respect to the selection and application of an entity’s financial reporting framework. In particular, the Board noted the requirements in ASA 800 *Special Considerations-Audits of Financial Reports Prepared in Accordance with Special Purpose Frameworks* which for example require that “the auditor shall obtain an understanding of the steps undertaken by management to determine that the applicable financial reporting framework is acceptable in the circumstances”¹⁷ and also ASA 700 *Forming an Opinion and Reporting on a Financial Report* which for example requires that “the auditor shall evaluate whether the financial report adequately refers to or describes the applicable financial reporting framework”.¹⁸

Disclosures regarding compliance with all the recognition and measurement requirements in Australian Accounting Standards

BC28 When deciding what information about compliance with all the recognition and measurement requirements in Australian Accounting Standards should be disclosed, the Board considered the following alternatives:

| Option | Information to be disclosed |
|----------|--|
| Option 1 | <p>Contextual information about the entity, being where the entity has subsidiaries, investments in associates or investments in joint ventures, and whether or not they have been consolidated or equity accounted in a manner consistent with the requirements set out in Australian Accounting Standards.</p> <p>If the entity has not consolidated its subsidiaries or equity accounted its investments in associates or joint ventures in accordance with the requirements set out in Australian Accounting Standards, the entity shall disclose that fact and the reasons why. If the entity is a not-for-profit entity, and it has not determined whether or not its interests in other entities give rise to interests in subsidiaries, associates or joint ventures, the entity shall instead disclose that fact.</p> |

16 Paragraph 6.1(c) of APES 205.
 17 Paragraph 8 of ASA 800.
 18 Paragraph 15 of ASA 700.

| Option | Information to be disclosed |
|----------|--|
| Option 2 | An explicit statement as to whether or not the financial statements comply with all the recognition and measurement requirements in Australian Accounting Standards and, if not, an indication of where they do not comply. |
| Option 3 | Merely a binary statement regarding compliance or non-compliance with all the recognition and measurement requirements in Australian Accounting Standards, for example either that “the entity has complied with all the recognition and measurement requirements in Australian Accounting Standards” or “the entity has not complied with all the recognition and measurement requirements in Australian Accounting Standards”. |
| Option 4 | Merely a statement of compliance with all the recognition and measurement requirements in Australian Accounting Standards that is, no statement would be required if an entity did not comply with all the recognition and measurement requirements in Australian Accounting Standards. |

- BC29 The Board decided that Options 1 and 2 together were most appropriate, as they best inform financial statement users about the special purpose financial statements and best address the issues identified in paragraphs BC2 to BC14 above.
- BC30 In considering the application of Australian Accounting Standards to special purpose financial statements, the Board noted that section 45A of the *Corporations Act 2001* requires the assessment of thresholds for small and large proprietary companies to be determined on a consolidated basis (i.e. the parent and the entities it controls (subsidiaries)) in accordance with the accounting standards even if the standards do not otherwise apply to some or all of the companies concerned. For the purposes of this section, the question of whether a proprietary company controls another entity is to be decided in accordance with the requirements of Australian Accounting Standards (i.e. AASB 10 *Consolidated Financial Statements*) even if the standards do not otherwise apply to the company.
- BC31 The Board considered whether an explicit statement that an entity does not have subsidiaries, or investments in associates and joint ventures was required. The Board noted that entities preparing either Tier 1 or Tier 2 general purpose financial statements¹⁹ are not required to make these statements and accordingly an explicit statement in these circumstances should not be required.
- BC32 The Board decided that in situations where an entity’s financial statements do not consolidate some or all of its subsidiaries, information about the consolidated financial statements of the entity’s parent is likely to be useful to enable financial statement users to at least be able to know if and where they can access some consolidated information, even if it is incorporated into a wider group. While this requirement arguably improves transparency in financial reporting, the Board decided not to mandatorily require disclosure of this information as such information is currently not required to be provided by entities preparing Tier 2 general purpose financial statements. The Board also considered whether to require these entities to identify those subsidiaries that have not been consolidated. Whilst the Board acknowledged that this information might be useful to users of financial statement, the Board noted that for some entities, particularly those in the not-for-profit sector, this disclosure might be unduly burdensome, such as where entities are not required to determine whether they have subsidiaries in accordance with AASB 10. Thus, on balance, the Board decided not to require entities to disclose the identity of subsidiaries that have not been consolidated.
- BC33 The Board noted the general requirement in paragraph 117 of AASB 101 to disclose accounting policies provides financial statement users with an explanation of the basis upon which the financial statements have been prepared, but does not provide information regarding how those accounting policies compare with all the recognition and measurement requirements in Australian Accounting Standards. Accordingly, the transparency of special purpose financial reporting is compromised. The Board therefore decided that it was necessary for an entity to explicitly disclose whether or not it complied with all the recognition and measurement requirements in Australian Accounting Standards and to supplement that disclosure with an indication of where they do not comply.
- BC34 In relation to the requirement to provide an indication of where non-compliance exists (for example, where the entity has not provided for employee entitlements in a manner consistent with the requirements set out in AASB 119 *Employee Benefits*), the Board decided to express a broad principle (i.e. an indication of where the non-compliance exists) rather than take a more prescriptive approach (e.g. a description of the extent of non-compliance). This was because, in the Board’s view, the explanation of that disclosure requirement in paragraph IG4 of the *Implementation guidance and illustrative examples* and the implementation guidance and illustrative examples themselves attached to AASB 1054 as non-mandatory material (see paragraph BC36 below) provide sufficient guidance for preparers to understand the nature of the information that is to be

19 “Australian Accounting Standards consist of two Tiers of reporting requirements for preparing general purpose financial statements:
(a) Tier 1: Australian Accounting Standards; and
(b) Tier 2: Australian Accounting Standards – Reduced Disclosure Requirements.” Paragraph 7 of AASB 1053.

disclosed. As illustrated in the *Implementation guidance and illustrative examples*, the approach taken by the Board also leaves discretion for entities to determine how best to make the disclosure having regard to their particular circumstances and the needs of their users.

- BC35 The Board did however confirm, that in disclosing the required information, the Board did not expect entities to provide quantitative information or reconciliations where their accounting policies do not comply with all the recognition and measurement requirements in Australian Accounting Standards.
- BC36 The Board noted the view of some that, if the differences between an entity's accounting policies and the recognition and measurement requirements in Australian Accounting Standards are extensive, the preparation of the required disclosure could be onerous. To help address this concern, as referred to in paragraph BC34 above, the Board prepared a number of illustrative examples and flowcharts. The *Implementation guidance and illustrative examples* is designed to provide examples of how the required information might be disclosed having regard to the existing variation and diversity to compliance with all the recognition and measurement requirements in Australian Accounting Standards in special purpose financial statements currently seen in practice.
- BC37 The Board further noted the view that, depending on the current level of expertise, some entities might find it burdensome to determine whether their accounting policies comply with the recognition and measurement requirements in Australian Accounting Standards. The Board also made the observation that understanding whether or not the entity has complied with all the recognition and measurement requirements in Australian Accounting Standards is a part of good governance and therefore it is reasonable to expect the necessary level of expertise is available, and any costs of acquiring that expertise would be reasonably expected to be outweighed by the benefits. Furthermore, the Board confirmed that the amendment would not require an entity to change its existing accounting policies and therefore is not onerous.
- BC38 While Options 3 and 4 in the table in paragraph BC28 above were not without their advantages, the Board decided they were not the most appropriate alternatives for a number of reasons including:
- (a) A binary disclosure stating only 'non-compliance' as suggested in Option 3 would not be useful as users would not be able to discern an indication of the extent of recognition and measurement compliance or non-compliance; and
 - (b) Option 4 was not appropriate as if an entity did not make the disclosure, users would also not be able to discern the reason for non-compliance, that is, whether it was a recognition and measurement non-compliance or the omission of a disclosure requirement for example.

Accordingly, any costs that would be saved by adopting Options 3 or 4 relative to Option 2, including that they would result in less voluminous disclosure, would be clearly outweighed by the benefits to users of Option 2.

Other issues

- BC39 Both *The AASB's For-Profit Entity Standard-Setting Framework* and *The AASB's Not-for-Profit Entity Standard-Setting Framework* state that the Board does not currently set standards for special purpose financial statements, as such financial statements should only be prepared where users can tailor them to their own information needs, and therefore do not need a standard-setter or regulator to require the information on their behalf. Accordingly, the Board noted the view that those responsible for the preparation of special purpose financial statements should determine the extent to which they conform with Australian Accounting Standards and therefore it is not necessary for the Board to specify the disclosures proposed in this Exposure Draft.
- BC40 Notwithstanding this, "as part of moving legacy regulations out of legislation and into Australian Accounting Standards ...",²⁰ and as noted in paragraph BC20(c) above, Australian Accounting Standards AASB 101, AASB 107, AASB 108, AASB 1048 and AASB 1054 apply to special purpose financial statements. The Board considered that this, especially the requirement in paragraph 9 of AASB 1054,²¹ together with the needs of users noted in paragraph BC19 above, provided a sufficient basis for requiring the disclosures in special purpose financial statements proposed in this Exposure Draft. The Board was particularly concerned that a significant number of special purpose financial statements do not provide adequate disclosures to enable a user to determine whether they do need additional information to meet their needs.

20 Paragraph 14 of both *The AASB's For-Profit Entity Standard-Setting Framework* and *The AASB's Not-for-Profit Entity Standard-Setting Framework*.

21 Paragraph 9 of AASB 1054 requires an entity to disclose whether the financial statements are general purpose financial statements or special purpose financial statements.

Trans-Tasman convergence

- BC41 *The AASB's For-Profit Entity Standard-Setting Framework* requires that, wherever possible, differences between accounting standards issued in Australia and New Zealand should be minimised to reduce costs for entities operating trans-Tasman.
- BC42 The Board noted that the New Zealand equivalent of AASB 1054, Financial Reporting Standard No. 44 *New Zealand Additional Disclosures* would not be amended to require the disclosures in this Exposure Draft. This is because in New Zealand, entities that apply accounting standards issued by the External Reporting Board have a statutory obligation (or alternatively choose) to prepare general purpose financial statements. In New Zealand, entities that have a statutory obligation to prepare financial statements cannot prepare special purpose financial statements.

Effective date

- BC43 The Board confirmed that the narrow scope amendment proposed in this Exposure Draft is an interim measure, until the broader project proposing to remove the ability for certain entities to prepare special purpose financial statements is completed (an Exposure Draft relating to which is planned for Quarter 3 of 2019 and expected to be mandatory for annual periods beginning on or after 1 July 2020 for for-profit entities and a later, yet to be determined date, for not-for-profit entities), and confirmed, on the basis outlined in this Basis for Conclusions, that the amendment is urgently needed to provide more transparency to the users of publicly lodged special purpose financial statements and to increase the comparability of special purpose financial statements with other special purpose financial statements and general purpose financial statements.
- BC44 As noted in paragraph BC37 above, the amendments do not require entities to change their existing accounting policies, and therefore the information required to be disclosed is based on an entity's existing financial reporting policies and practices. Accordingly, it is not necessary to provide an extended operative date.
- BC45 As such, in the expectation the Amending Standard proposed in this Exposure Draft is issued prior to 31 December 2019, the Board decided the amendment should be effective for annual periods ending on or after 30 June 2020. However, early voluntary disclosure is allowed, and indeed encouraged.