



29 September 2005

Mr David Boymal  
Chairman  
Australian Accounting Standards Board  
PO Box 204  
COLLINS STREET WEST VIC 8007

By email: [standards@asb.com.au](mailto:standards@asb.com.au)

Office of the Chief Executive  
Peter Lowe, CPA

CPA Australia  
ABN 64 008 392 452

CPA Centre  
Level 28, 385 Bourke Street  
Melbourne VIC 3000 Australia  
GPO Box 2820AA  
Melbourne VIC 3001 Australia

T +61 3 9606 9689  
F +61 3 9602 1163  
W [www.cpaaustralia.com.au](http://www.cpaaustralia.com.au)  
E [peter.lowe@cpaaustralia.com.au](mailto:peter.lowe@cpaaustralia.com.au)

Dear David

**Exposure Draft 142: *Financial Reporting of General Government Sectors by Government***

Thank you for the opportunity to comment on Exposure Draft 142: *Financial Reporting of General Government Sectors by Government*. Our comments have been prepared in consultation with members through our Financial Reporting and Governance and Public Sector Centres of Excellence. One of our key methods of gathering comments has been to harness the experiences and views of users of financial reports produced by Government.

CPA Australia believes that this is a very important initiative and a fundamental change to reporting by Governments. As such, we have undertaken an extensive consultation strategy of seeking the views of key users of government financial reports. These views are expressed in part (r) of our submission.

Overall, CPA Australia supports the FRC'S directive of harmonisation of GFS and GAAP. We continue to recognise the need for our public sector to have a more robust GGS reporting framework which meets the needs of users for decision making. However, we are concerned that under the requirements of ED 142, these reports will be deemed General Purpose Financial Reports (GPFRs), even though they would not fully comply with all Australian Accounting Standards but rather certain elements as prescribed by ED 142. We are concerned that information presented will not be consistent or comparable with other GPFRs even though it will purport to be prepared within the same conceptual framework. This is consistent with feedback from our user consultation strategy.

Our members have also raised concerns about the proposed removal of AAS 27 *Financial Reporting by Local Governments*, AAS 29 *Financial Reporting by Government Departments* and AAS 31 *Financial Reporting by Governments* before the finalisation of the GAAP/GFS project. Our members have raised concerns about the potential implications for whole of government reporting which is not within the scope of ED 142.

Our detailed comments are attached.

Should you have any queries on our comments, please contact Ms Sepi Roshan our Financial Reporting and Governance Policy Adviser at [sepi.roshan@cpaaustralia.com.au](mailto:sepi.roshan@cpaaustralia.com.au) or Ms Anna D'Alessandro our Public Sector Policy Adviser at [anna.dalessandro@cpaaustralia.com.au](mailto:anna.dalessandro@cpaaustralia.com.au).

Yours sincerely

Peter Lowe CPA  
Chief Executive

cc: Sepi Roshan  
Anna D'Alessandro

## **CPA Australia's response to the issues raised in Exposure Draft 142: *Financial Reporting of General Government Sectors by Government***

### **(a) The proposal in paragraph 5 that the GGS (as defined in GFSM 2001) of a government is a reporting entity**

SAC 2 *Objective of General Purpose Financial Reporting* defines a reporting entity as "an entity (including economic entities) in respect of which it is reasonable to expect the existence of users dependent on general purpose financial reports for information which will be useful to them for making and evaluating decisions about the allocation of scarce resources" (paragraph 5). Therefore, these GPFRs are intended to meet the information needs of users.

CPA Australia agrees that the GGS can satisfy the criteria for a reporting entity and that the GAAP/GFS harmonisation process can aid in the production of GPFRs for the GGS. In fact, SAC 2 identifies government departments as entities that can potentially prepare GPFRs (paragraph 9).

SAC 1 *Definition of the Reporting Entity* "requires that to meet the "benchmark of the minimum required quality of financial reporting.....reporting entities shall prepare general purpose financial reports and that these reports comply with Statements of Accounting Concepts and Accounting Standards" (paragraph 4).

SAC 1 also states that differential reporting is not supported where there are users dependent on GPFRs (paragraph 36). It goes on to state that entities that do apply differential reporting "will not to be identified as reporting entities and thus would not be required to prepare general purpose financial reports" (SAC 1, paragraph 36). As such, it is expected that GPFRs fully comply with Statements of Accounting Concepts and all Accounting Standards.

While we do consider GGS to be a reporting entity, we do not agree that concepts such as partial consolidation required by ED 142 allow the application of accounting standards and the fundamental concept of control, as required of GPFRs by SAC 1. Given that we do not expect an amendment to the definition and requirements of reporting entity, we would urge the AASB to reconsider calling the reports produced by the GGS under the requirements of ED 142, GPFRs. This is further compounded by the decision to apply sector neutral standards as part of Australia's decision to adopt IFRS. That is, all IFRS standards should apply equally to all sectors, including government.

As such, we recognise that this will produce the following options:

- Amendments to ED 142 to allow the full application of all accounting standards
- Referring to GGS financial reports as special purpose financial reports
- Referring to GGS financial reports as something between GPFRs and special purpose financial reports (eg: Government produced financial reports).

We believe that it is important to maintain the integrity of the conceptual framework through its consistent application. Consequently, our members have indicated that the AASB provide an explanation of why the GGS is of such significance that it would be considered a reporting entity.

### **(b) The proposal, implicit in paragraph 5, that a GGS financial report prepared on a partial consolidation basis is a GPFR together with the proposal in paragraph 18 that the GGS should be prohibited from consolidating controlled entities in the PNFC sector and the PFC sector;**

Further to our comments in (a), we do not believe that GGS financial reports, which are called GPFRs, should be prepared on any basis other than accounting standards. Therefore, the consolidation of controlled entities in the PNFC and PFC sectors will be required. According to SAC 1 and SAC 2, GPFRs are used to communicate information to dependent users and must apply the requirements of accounting standards. As such, GPFRs must apply the consolidation requirements in AASB 127 *Consolidated and Separate Financial Statements*, and therefore a reporting entity must fully consolidate those entities which it controls.

We have consulted with users who indicate that allowing only partial consolidation may not meet all of their information needs. The implication is that the usefulness of these GGS financial reports may be questionable and that ED 142 will not meet its desired objective.

**(c) The proposal in paragraphs 8 to 12 that, with limited significant exceptions, the GGS financial report should comply with other Australian Accounting Standards and, where it does not conflict with Australian Accounting Standards, GFSM 2001. The Board is particularly interested in comments on the proposal that where Australian Accounting Standards allow for optional treatments, only those treatments aligned with GFSM 2001 should be applied for the purposes of GGS financial reporting**

CPA Australia believes that if GGS financial reports are to be classified as GPFRs that they should comply with all Australian Accounting Standards, without exception.

We understand the rationale for requiring that where Australian Accounting Standards allow for optional treatments, only those treatments aligned with GFSM 2001 should be applied for the purposes of GGS financial reporting (ie convergent practices). However, we are concerned about the practical implications for the reporting entities within the GGS which currently apply AAS 29 *Financial Reporting by Government Departments*. That is, if current accounting policies under AAS 29 reporting are not aligned with GFS, they will either need to be changed or adjusted for the preparation of GGS reports.

As such, some of our members have expressed concerns that mandating a particular treatment may be enforcing accounting policies on the GGS and/or reporting entities within the GGS.

We suggest that Phase 1 and Phase 2 of the GAAP/GFS project be undertaken simultaneously.

**(d) The proposal in paragraphs 13 to 17 to require or allow disclosure of information in the GGS financial report that is determined in accordance with GFSM 2001 and, where it is determined in a different manner from corresponding information prepared in accordance with Australian Accounting Standards, provide a reconciliation to the GFS-related information**

When there are differences in GAAP and GFS-related information, we agree that a reconciliation showing the difference in treatment should be presented. In this way, it can be shown that GAAP requirements are applied. We agree that to add to the usefulness of the reconciliation, we suggest that a narrative explanation of the different treatments should also be provided (eg: as required by paragraph 28(b)).

**(e) The proposals in paragraphs 19 to 23 that:**

**(i) the GGS's equity investment in non-consolidated controlled entities should be measured at fair value where fair value is reliably measurable and at the government's proportional interest in the net assets of the controlled entities where fair value is not reliably measurable;**

**(ii) where net assets is used as the basis of measurement, it is determined in a manner consistent with the net assets that are consolidated into the whole of government GPFR;**

**(iii) changes in the carrying amount of the GGS's equity investment in non-consolidated controlled entities during a reporting period are treated in a manner consistent with the treatment of a change in fair value under AASB 139 even if the carrying amount is not fair value; and**

**(iv) specify the treatment of jointly controlled entities and associates**

CPA Australia believes that if GGS financial reports are to be classified as GPFRs that they should comply with all Australian Accounting Standards, without exception. Our members suggest that accounting requirements be consistently applied and any divergent practices be explained. Therefore, the treatment of non-consolidated controlled entities as required by ED 142 would not be consistent with the application of all Australian Accounting Standards.

We do agree that the carrying amount and changes in the carrying amount of all other equity investments be accounted for under the requirements of AASB 139.

**(f) The proposals in paragraphs 26 to 31 relating to the format and content of the balance sheet and the treatment of convergence differences**

CPA Australia believes that this is an important initiative in government financial reporting and as such has embarked on an extensive user consultation strategy. We targeted the four Public Accounts Committees, academics of GFS and GAAP and ratings agencies. Our primary aim was to gauge whether the proposed content and form of the Financial Statements would assist users in decision-making.

Our consultation of key users indicates that the format and content of the balance sheet and the treatment of convergence differences is satisfactory. However, our members suggest that ED 142 should explain why the liquidity format provides a more relevant and reliable format.

**(g) The proposals in paragraphs 32 to 40 relating to the format and content of the operating statement and the treatment of convergence differences, including the proposal:**

**(i) to mandate the classification of income and expenses by nature on the face of the operating statement, with the classification aligned with the GFSM 2001 classification scheme to the extent appropriate;**

**(ii) to mandate a comprehensive income approach whereby all non-owner movements in equity are recognised in a single operating statement; and**

**(iii) that the option in AASB 119 Employee Benefits (December 2004) of partially deferring actuarial gains and losses on defined benefit superannuation plans using a “corridor approach” should be prohibited, and that the remaining options of recognising them in operating result or in the other non-owner movements in equity section of the operating statement should be allowed. The Board is particularly interested in comments on whether the Standard should remove options entirely, and in so doing, prohibit recognition directly in other non-owner movements in equity**

CPA Australia believes that the application of sector neutral standards means that except in limited circumstances, accounting standards will apply equally to all reporting entities – including options within those standards

Consultation of key users has identified that the format and content of the operating statement is satisfactory.

However, there were concerns raised by members who use GFS information about including all non-owner movements in equity in a single operating statement as they felt that it distorted the true economic flows which resulted from the policy decisions of the GGS. Based on feedback from our members and our concern of the AASB in part (iii) of this question, we ask the AASB to revisit its decision to include all non-owner movements in equity in a single operating statement.

**(h) The proposals in paragraphs 41 to 43 relating to the format and content of the cash flow statement. The Board is particularly interested in comments on whether the Standard should also require a distinction between cash flows relating to investing in financial assets for “policy” and “liquidity management” purposes on the face of the cash flow statement and whether such a distinction would be useful and could be made with sufficient rigour for GPFR purposes**

Our consultation of users has determined that the format and content of the cash flow statement is satisfactory.

Some of our members who use GFS information have suggested the distinguishing between cash flows relating to investing in financial assets for “policy” and “liquidity management” purposes on the face of the cash flow statement would provide useful information.

**(i) The proposals in paragraphs 44 and 45 relating to additional information to be provided in the note containing the summary of significant accounting policies, illustrated in Appendix C. In particular, the Board is interested in comments on whether the proposed disclosures provide sufficient information to minimise the risk that users might perceive the GGS financial report as being a substitute for the whole of government GPFR**

We agree that the additional disclosures would be useful to users in reading the context in which GGS financial reports are prepared. Our members however, are concerned that these inconsistent treatments might mislead users.

**(j) The proposals in paragraphs 46 to 48 relating to additional disclosures. The Board is particularly interested in comments on whether the proposal in paragraph 46(d) to require disclosure of explanations of key technical terms used in the financial report is useful**

We agree that the additional disclosures would be useful to users in reading the context in which GGS financial reports are prepared. Specifically, key technical terms may be useful for those who are not familiar with all technical terms under GAAP or GFS.

**(k) The proposals in paragraphs 49 to 52 relating to disclosures that provide disaggregated information about GAAP and GFS amounts on a functional basis, whereby functions are determined in accordance with GFSM 2001**

Our members question the stability of these functional definitions. If these definitions are amended there may be implications for comparability.

**(l) The proposals in paragraphs 53 to 56 to specify principles for the presentation of performance indicators**

We agree that the additional disclosures should be useful to users. As such, we believe that all information presented should satisfy the qualitative characteristics in the *Framework For the Preparation and Presentation of Financial Statements*.

**(m) The proposals in paragraphs 57 to 62 to require disclosure of:**

**(i) the original budget, restated if necessary so that it is presented on a basis that aligns with the basis on which the financial statements and notes have been prepared (in accordance with the Standard); and**

**(ii) an explanation of major variances between the original GGS budget and actual amounts;**

CPA Australia believe that this will provide useful information, as long as budgeted and actual information is prepared on the same basis and are comparable and this would also facilitate major variances to be explained. Our members are concerned that amendments to the "original budget" would not be reflected and hence distort the basis on which variances occur. Therefore, we suggest that a flexible (variable) budgeting approach be appropriate under ED 142, whereby changes in the original budget are incorporated.

**(n) The proposals in paragraphs 63 to 67 relating to transitional requirements. In particular, the Board is interested in assessments of the costs and benefits of the approach proposed, compared with alternative approaches, including remaining silent in the Standard about transitional requirements, and thereby effectively requiring AASB 108 Accounting Policies, Changes in Accounting Estimates and Errors to operate in its own right**

Our members' main concern is that an application date of 1 July 2006 is not feasible, given the need for further debate on the GAAP/GFS issue. There are concerns that such an application date may result in a framework that is underpinned by pragmatism rather than the conceptual framework.

**(o) The illustrated acceptable format for the financial statements and notes related to convergence differences in Appendix B. The Board is particularly interested in comments on:**

- (i) the columnar approach illustrated for the balance sheet and operating statement. In addition to any criticisms of the columnar approach, respondents are invited to provide an alternative that is consistent with the Exposure Draft's proposals for the Board's consideration; and**
- (ii) whether the illustration provides guidance that is helpful in implementing the proposals in the Exposure Draft, particularly those that adopt the requirements in AASB 101 as effectively amended by the proposals**

The columnar approach is useful when it clearly illustrates the reconciliation between GFS and GAAP.

**(p) Whether it is appropriate for the Standard to cross-reference to GFSM 2001, given that GFSM 2001 is not prepared by the AASB and that there is a need for the AASB to consider whether amendments to the Standard are necessary each time GFSM 2001 is amended. The Board is also interested in comments on whether instead of GFSM 2001 the Standard should cross-reference to the GFS Manual published by the Australian Bureau of Statistics (ABS)**

Given the trend to international harmonisation, CPA Australia believes that it is appropriate to cross-reference only to the GFSM 2001 because of Australia's commitment to international harmonisation. We also believe that the AASB has the obligation to consider amendments made to the GFSM.

**(q) Whether there are any aspects of GFSM 2001 that you consider should be prohibited from forming part of the basis upon which the GGS's financial report is prepared**

No part of the GFSM 2001 has come to our attention that would require prohibition from forming part of the basis upon which the GGS's financial report is prepared.

**(r) Whether, overall, the proposals result in financial reports that are useful to users.**

Our consultation process has indicated that users want simple, consistent and comparable information which will reflect the substance of transactions and the Government's financial position. Providing more information that adds little incremental value may in fact lower the quality of financial information currently being presented.

#### Outcomes from user consultation

CPA Australia has undertaken an extensive consultation strategy as part of developing its response to this Exposure Draft, given the importance of this initiative for government financial reporting. Consultation involved the following key stakeholders; four Public Accounts Committees, a Finance and Estimates Committee, a Ratings Agency, GFS and GAAP academics and Access Economics.

From the varied feedback received, several key issues were identified:

- The most resounding message was agreement that GAAP and GFS should be harmonised. The current regime of having two sets of financial reports seems to add to the confusion and one set of converged financial reports may increase government transparency and accountability. Comparability, consistency and uniformity were the key requirements from users.
- The second key issue was why Australia was insisting on leading the way with GAAP/GFS harmonisation. Our user groups suggested that Australia should at least wait for the IPSASB and the IMF review of the System of National Accounts, due in 2008. There were concerns that there may be significant changes which would make the work undertaken in Australia dated.

- The issue of “partial” consolidation was a major concern. Users believed that the approach advocated by ED142 would exclude relevant information about the effects of all controlled interests. There was also concern about the financial reports being prepared on a basis contrary to the conceptual framework but being held out to be GPFRs.
- Users acknowledged that the financial report will not meet many of their information needs and that they would still need to consult with preparers on other specific requirements.
- Questions were also raised as to why we were converging with the existing GAAP framework. Statements prepared under GAAP were already complex and difficult to understand and it was perceived that introducing another, different, framework would add to the complexity. Therefore, there were suggestions that we investigate the GAAP requirements for government reporting first, before converging with GFS.
- There was a common view that the converged statements would benefit the preparers more than the users.
- In terms of financial statement presentation the following comments were made:
  - Most of our consultative group liked the proposed format of ED142 financial statements (as presented in Appendix B) as they provided a streamlined approach in providing most information.
  - Why is there no Statement of Equity in the proposed statements, as is the GAAP requirement?
  - Some users did not like the convergence column and expected this to disappear over time, or when the IMF review of GFS was completed
  - Users generally liked the disaggregated information as appeared in Note 23 (Appendix B)
  - Detailed tax information should be presented in the Operating Statement to be useful for analysis purposes.

Some of those consulted were concerned about the future of whole-of-government reporting, especially in the light of the revision of AAS31. They would not want GGS statements to be prepared in lieu of whole-of-government statements. However, they were in favour of a financial report to be prepared for all three sectors of government, with a whole of government report that consolidates all sectors sitting on top of these – consistent with the AASB’s intended phased approach to the GAAP/GFS convergence project.