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15 November 2005

The Chairman  
Australian Accounting Standards Board  
PO Box 204  
Melbourne Vic 8007

Via email to: [standard@asb.com.au](mailto:standard@asb.com.au)

Dear Professor Boymal

**Exposure Draft ED 143 Director and Executive Disclosures by Disclosing Entities: Removal of AASB 1046 and Addition to AASB 124**

Thank you for the opportunity to comment on the Exposure Draft ED 143 *Director and Executive Disclosures by Disclosing Entities: Removal of AASB 1046 and Addition to AASB 124*.

Our comments have been prepared in consultation with members through our Centre of Excellence – Financial Reporting and Governance.

The Preface to the ED comments "The [International Accounting Standards Board] IASB has stated it regards requirements for more detailed disclosures than the basic disclosures required by AASB 124 [*Related Party Disclosures*] as the responsibility of national standard setting bodies. The IASB does not intend to issue an [International Financial Reporting Standard] IFRS addressing the same areas covered by AASB 1046 [*Director and Executive Disclosures by Disclosing Entities*]." The inclusion of AASB 124 in the accounting literature demonstrates that corporate governance is a topic that is within the mandate of an accounting standard setter. We are of the view that, in the absence of an intention by the IASB to issue IFRSs addressing particular corporate governance issues, it is appropriate that the Australian Accounting Standards Board (AASB) issue standards that effect corporate governance. Accordingly, we consider it entirely appropriate that the AASB supplement the requirements of IAS 24 by adding disclosures that have been previously required in Australia.

We support the change to locate within one Standard:

- the disclosures necessary to ensure that an entity's financial report draws attention to the possibility that its financial position and profit or loss may have been affected by the existence of related parties and by the transactions and outstanding balances with such parties; and
- the requirement that disclosing entities disclose additional information relating to key management personnel.

However, we do have concerns with some of the proposals articulated in the ED, for example, the proposal not to relocate in the Standard the guidance that currently accompanies AASB 1046.

The Preface to the ED comments that on 7 July 2005, Corporations Regulation 2005 (No. 4) was issued aimed at resolving the considerable duplication of remuneration disclosures for listed companies, with many disclosures being required in both the Remuneration Report (as required by Corporations Regulation 2M.3.03, issued in July 2004) and the financial report. We understand that the revision proposed by the ED will cause Corporations Regulation 2005 (No. 4) to be ineffective. Should the AASB proceed with the proposals articulated by the ED, and given the adverse consequences on preparers in complying with the Remuneration Report requirements of the Corporations Act, we encourage the AASB to work with Treasury to resolve this issue as a matter of urgency.

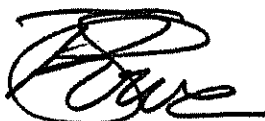
We agree with the comments articulated in the Preface to the ED that IFRS compliance requires that:

- an entity, such as some registered Managed Investment Schemes, that has no employees but there is another entity responsible for its governance that does have employees, would need to determine its key management personnel (KMP) from among the management personnel of the responsible entity or another entity that provides services to the responsible entity; and
- the indirect payment of compensation as part of a management fee falls within the meaning of compensation. This will be the case notwithstanding that the basis of the calculation of the management fee may not have any relationship to the compensation of KMP.

Our detailed comments to the specific matters identified in the ED are attached to this letter.

Should you have any queries on our comments, please contact Dr Mark Shying, CPA Australia's Financial Reporting and Governance Senior Policy Adviser at [mark.shying@cpaaustralia.com.au](mailto:mark.shying@cpaaustralia.com.au).

Yours sincerely



**Peter Lowe CPA**  
Chief Executive

cc: M Shying

**Exposure Draft ED 143 Director and Executive Disclosures by Disclosing Entities: Removal of AASB 1046 and Addition to AASB 124**

**1. Proposal to remove parent relief from AASB 124**

*Do you support the proposals to:*

- (a) remove parent relief from AASB 124; and*
- (b) rely on the definition of KMP and remove the requirement that the director and executive disclosures apply to the directors of the parent entity and at least five specified executives?*

*Do you consider that the removal of parent relief from AASB 124 is appropriate and sufficient to ensure IFRS compliance in respect of both parent and group entities?*

We support the removal of the parent relief from the current version of AASB 124. We understand that the reasons for the then AASB providing the current parent relief were the removal of what was at that time considered to be unnecessary repetition and the then held view that, in the overseas context, the primary focus of the IASB was on the development of standards for application to consolidated entities. We note that there is no relief for parent entities in IAS 24.

Some commentators assert that the most significant consequence of the removal of the parent relief is an increased cost to the preparers of financial reports (with little or no incremental improvement in the quality of the information to investors). We suggest that the issue of "the usefulness of parent entity reporting" is better examined as a separate topic.

We are concerned that, to mitigate the possible increased cost of complying with the proposed Standard, preparers might conclude that there is only one KMP group, the same for the parent and for the group. The proposal to remove the need to include at least five specified executives, and relying on the IASB's definition of KMP, means there would not be an explicit requirement to include any executives (who are not directors). This appears to make it easy for companies to claim their KMP comprises only the board of directors of the parent, the same for parent and group. We note that on page 7 of the Preface to ED 143, it is stated that "the Board expects the KMP group (or groups) for a listed company will generally include all executives identified by section 300A of the Corporations Act." In the absence of any reference to this in the proposed Standard (even if such expectations were repeated in the Preface to the new AASB 124), it is hard to see how a listed company would either be aware of these expectations or consider that the law required compliance with something that is not mentioned in the Standard. If the Board intends listed companies should be required to include such individuals, that requirement needs to be stated in the Standard (and not qualified by 'generally').

**2. Scope of AASB 124**

*Do you agree with the proposal that AASB 124 be required to be applied by non-corporate for-profit entities (and not AAS 22)?*

We support one standard for the for-profit sector and not-for-profit sector (and our support is the same for corporate or non-corporate entities). The current version of AASB 124 comments that the notes for the consolidated financial statements of a corporate or for-profit entity that comply with AASB 124 will simultaneously be in compliance with the requirements of IAS 24 for consolidated financial statements (and in the case of non-corporate for-profit entities the current version of AASB 124 relieved them of the obligation to simultaneously comply with AAS 22 *Related Party Disclosures*). The words in the proposed Standard appear to apply it to all non-corporate entities, excluding public sector entities, whether for-profit or not-for-profit, despite the comments on page 14 of the Preface to the ED that the proposals apply only to for-profit non-corporate entities. However, the proposals fail to withdraw AAS 22 or exempt non-corporate entities from compliance with AAS 22.

It is uncertain whether adequate consideration has been given to whether the principles articulated in a Standard designed to apply to for-profit corporate entities are robust enough to be applied to

non-corporate entities in general and particularly not-for-profit non-corporate entities. We suggest that the AASB field test the proposal as it relates to non-corporate entities to determine the need for any of the requirements to be specifically tailored to address differences in the structure and characteristics of such entities (e.g. by the inclusion of Aus paragraphs).

Assuming the new version of AASB 124 will apply to all non-corporate entities it would be advisable to withdraw AAS 22, to avoid any confusion as to which applies.

### **3. Amalgamation of AASB 1046 with AASB 124**

*Do you agree that the quality and quantity of disclosing entity disclosures will not be detrimentally affected by amalgamating AASB 1046 with AASB 124?*

We support the change to locate within one Standard:

- the disclosures necessary to ensure that an entity's financial report draws attention to the possibility that its financial position and profit or loss may have been affected by the existence of related parties and by the transactions and outstanding balances with such parties; and
- the requirement that disclosing entities disclose additional information relating to key management personnel.

However, we do have some concerns that the quality and quantity of disclosing entity disclosures will be detrimentally affected by some of the proposals articulated in the ED, for example:

- the proposal not to relocate in the Standard the guidance that currently accompanies AASB 1046; and
- the adverse consequences on preparers in complying with the Remuneration Report requirements of the Corporations Act.

### **4. Specified director, executive and specified executive**

*Do you agree with the proposal to use the term KMP and remove the definitions of specified director, executive and specified executive?*

We have no disagreement with the inclusion of the term KMP. However, we do not agree with the removal of the definitions of specified director, executive and specified executive.

The definition of KMP is very vague and provides little help to any entity, disclosing or otherwise, in determining the criteria it will use to decide which individuals shall be classified as KMP. Removing the definition of specified executive, and the 'floor' of at least five executives with the highest authority, means that entities will have no guidance as to how many executives might satisfy the definition of KMP.

The distinction between director and executive is fundamental to the way that companies are governed in Australia. The same distinction is important in the governance for many other bodies. Because the term KMP does not distinguish between the two, it is likely some will interpret the definition as to only include directors. Others are likely to interpret the definition as having fewer executives than the current requirements.

We note that generally, directors and other non-director executives do not operate as a single group, that is, there is no single key management personnel group. There is usually a director grouping, and an executive management grouping, with executive directors being in both.

Therefore, there should be a separation between disclosures of directors and non-director executives – in particular, aggregates.

## **5. Subtotals for compensation and loans for directors and non-director KMP**

*Do you agree with the deletion of the requirement to disclose subtotals for compensation and loans for directors and non-director KMP (i.e. requiring only one KMP total)?*

We disagree with the deletion of the requirements to require subtotals for compensation and loans for directors and non-director KMP. Removal would seem to result in both a reduction:

- in the quantity of disclosures by disclosing entities; and
- in the quality of disclosures.

Given the present requirement to disclose the number of KMP included in each aggregate of loans, it is possible to calculate an average for directors and an average for executives, and this has some use in providing for a quick comparison between different companies. An average for all KMP is likely to be much less useful as a comparator.

We note that the compensation disclosures required by paragraph 16 require only one aggregate for KMP. Even accepting this is sufficient for non-disclosing entities, proposing to reduce the other disclosures of disclosing entities to the same level seems contrary to the general principle of requiring more detailed disclosures from disclosing entities.

## **6. Former KMP**

*Do you agree with the proposal to delete the requirement for separate disclosure of transactions or balances with former KMP?*

We disagree with the proposal. The proposed disclosures appear to be only for current key management personnel. Accordingly, it appears that the remuneration of a (former) key management person who retires, resigns or is terminated prior to year end will not be required to be disclosed.

## **7. Prescribed benefits**

*Do you agree with the proposal to delete the AASB 1046 requirement for separate disclosure of prescribed benefits in each component of the five categories of compensation?*

We disagree with the proposal. We see no merit in removing the requirement for disclosing entities to provide separate disclosure, within a component of compensation, of amounts arising from benefits that are prescribed under the Corporations Act.

Items that are prescribed by the Corporations Act have been prescribed because the law considers them significant.

## **8. Entities that have to disclose details of KMP**

*Do you agree with the proposal that all entities covered by AASB 124, not only disclosing entities, be required to disclose certain minimum descriptive information in respect of each key management person (refer to paragraph Aus16.1) and information on changes that occur in the period after the reporting date and prior to the date when the financial report is authorised for issue (refer to paragraph Aus16.2)?*

We agree with the proposal to require all entities to name each individual included as a key management person, and provide the other details.

The removal of the current parent entity relief means it is possible for there to be two sets of KMP when a parent entity within a group presents, in its financial report, its financial statements together with the consolidated financial statements. We suggest it would be helpful to require identification of the composition of each set. Otherwise, a simple listing of all KMP would not enable users to readily identify which individuals are included in each (or both) of the sets.

We suggest that it be made clear the requirements of AASB 101 *Presentation of Financial Statements* to provide comparative information for the prior year do not apply to this addition.

**9. Incorporation of section 300A(1)(ba) into AASB 124 paragraph Aus25.3**

*Do you agree with the Board's proposal to incorporate section 300A(1)(ba) of the Corporations Act into AASB 124?*

The reasons for incorporating part (but not all) of Section 300A are not explained. The consequences, whether intended or not, are uncertain.

Given the provisions of the Standard will apply to all disclosing entities, the only advantage that appears to result from incorporation is that it will contribute to greater consistency between disclosures of listed companies and other disclosing entities. However, because not all the requirements of Section 300A for listed companies are replicated, differences will still exist. Incorporation does not reduce the current problems with reconciling differences between pronouncements in this area from a variety of authoritative sources (Parliament, ASIC and the ASX).

**10. Disclosures of 'other transactions'**

*Do you agree that the "other transaction" disclosures in paragraphs Aus25.5.3 to Aus25.7 should be by individual director when the disclosures in paragraph 18 are disaggregated into "key management personnel of the entity or its parent" and "other related parties"?*

We agree that disclosures of the 'other transactions' of the KMP with the disclosing entity (paragraphs Aus25.5.3 to Aus25.7) should be made on an individual basis and not aggregated together.

**11. No Appendices to final revised AASB 124**

*Do you agree with the Board's proposal to delete all the Appendices to this ED when issuing the final revised AASB 124?*

We disagree with the proposed deletion of Appendices. The removal of the Appendices will significantly affect the ability of preparers to comply with the standard, and affect users' ability to understand and compare the remuneration and other disclosures.

**12. Transitional provisions**

*Do you consider that transitional provisions should be included in AASB 124 in respect of paragraphs Aus25.1 to Aus25.7.3, since it is the first time that disclosing entities are required to make the disclosures required by paragraphs Aus25.1 to Aus25.7.3 in respect of KMP rather than specified directors and specified executives?*

We agree it would be desirable to include transitional provisions in AASB 124 for all entities (for paragraphs 1 to 22) and for disclosing entities (for paragraphs Aus25.1 to Aus25.7.3).

We do not understand why no suggestions are provided as to what sort of transitional provisions are contemplated or how it will be possible, on first-time adoption, to overcome the override in AASB 1 *First-time Adoption of Australian Equivalents to International Financial Reporting Standards* (paragraph 9) that invalidates transitional provisions in all other Australian equivalents to IFRSs.

**13. Application to managed schemes (including MIS)**

*(a) Do you agree that when a managed scheme (including a MIS) pays a management fee to its responsible entity, the managed scheme indirectly provides the compensation of the KMP for managing the MIS for the purposes of paragraph 16?*

*(b) Do you agree that the KMP of managed schemes that are disclosing entities (including MIS) should be subject to the same disclosure regime as all other disclosing entities in paragraphs Aus25.1 to Aus25.7.3 or should be required to make fewer disclosures, and perhaps only those required by paragraphs 1 to 22 of AASB 124?*

*(c) Do you agree that the KMP of a managed scheme are among the individuals paid by the responsible entity (or by another entity that provides services to the responsible entity)?*

We agree that a MIS that pays a management fee to its Responsible Entity (RE) is thereby obligating the RE to pay compensation, on its behalf, to those individuals responsible for its governance. Accordingly, that indirect payment of compensation as part of a management fee falls within the meaning of compensation.

We agree that MIS should be required to make the same disclosures as other disclosing entities.

We agree that the KMP of a managed scheme are among the individuals paid by the responsible entity (or by another entity that provides services to the responsible entity).

**14. Are there any other disclosure requirements you believe should be:**

*(a) added*

No.

*(b) deleted*

No.

**15. Are the proposals in the best interest of the Australian economy?**

We do not believe the proposals are in the best interests of the Australian economy as they will reduce comparability between financial reports.

**OTHER CONCERNS**

**Director related transactions – Non-disclosing entities**

It appears that the deemed materiality of all director related transactions has been removed from the former AASB 1017 *Related Party Disclosures* for non-disclosing reporting entities.

These disclosures should be retained, as transactions with directors are important information.

**Totals - remuneration**

Separate totals for compensation for each individual key management personnel should be disclosed (i.e. for disclosing entities that require this detail). It appears that paragraph Aus16.1 only requires a grand total for KMP. We consider it inappropriate to require disclosure of the components (paragraph Aus25.2), and then require users to manually add up the sub-totals.

**Totals – loans - KMP**

The total of all loans to KMP should be shown, not just total of directors and loans > \$100,000 to other KMP.

## **Determination of Compensation**

### **Accruals method**

The definition of compensation refers to "paid" annual leave. AASB 1046 referred to accrued benefits. How is this perennial issue in remuneration disclosures going to work under the proposed Standard? Is it just paid benefits, or accrued benefits? For example, if someone works for 11 months and takes 1 month leave (paid 12 months, accrued 12 months), do they have the same remuneration as someone who works for 12 months and does not take leave (paid 12 months, accrued 13 months)?

### **Non-monetary benefits**

We consider that retention of the guidance articulated in UIG 14 *Directors' Remuneration* as to what to include as remuneration (and which was also included in AASB 1046) to be useful to determine amounts attributable to non-monetary benefits, including reduced rate housing and reduced rate loans.

The lack of guidance in the proposed Standard is likely to cause interpretation issues and lack of comparability (and a possible referral to the Urgent Issues Group for clarification).

### **Difficulties with using AASB 124 definitions**

The term "domestic partner" may be broader than the current definition of spouse. It is common for a non-married couple to be considered the equivalent of a spouse if they have lived together for 2 years. "Domestic Spouse" may include couples that have lived together for less than 2 years.

The term "children" may include adult non-dependent children. It is often very difficult for a parent to know what holdings their adult children have in a company.

Paragraph Aus16.2. Why is the change of a key management person (other than a director or chief executive officer) only required on "retirement". What about termination, and resignation?