

31 January 2012

Mr Kevin Stevenson
The Chairman
Australian Accounting Standards Board
PO Box 204
Collins Street West VIC 8007

Dear Mr Stevenson

ED 214 Extending Related Party Disclosures to the Not-for-Profit Public Sector

Attached is the Australasian Council of Auditors-General (ACAG) response to the Exposure Draft referred to above. The views expressed in this submission represent those of all Australian members of ACAG.

While ACAG supports the principle of disclosing related party information in the financial reports of not-for-profit public sector entities, ACAG believes there are a number of practical issues associated with the proposed application of AASB 124 *Related Party Disclosures* that require further consideration.

I trust you will find the attached comments useful.

Yours sincerely



Simon O'Neill
Chairman
ACAG Financial Reporting and Auditing Committee

ED 214 Extending Related Party Disclosures to the Not-for-Profit Public Sector

1. Whether extending AASB 124 (December 2009) to the NFP public sector is appropriate.

ACAG supports the principle of requiring NFP public sector entities to disclose related party information. ACAG believes, however, there are a number of issues that may arise in the proposed application of AASB 124 to NFP public sector entities.

2. Whether any amendments should be made to the proposed disclosure requirements (both Tier 1 and Tier 2) in respect of application by NFP public sector entities.

ACAG believes there are a number of practical issues that may arise on the application of AASB 124 to NFP public sector entities as proposed by the exposure draft.

The *Basis for Conclusions* section of the exposure draft discusses a number of potential issues relating to the application of the standard to Ministers. ACAG believes that this aspect of the standard would give rise to a number of significant practical application issues.

Application of Key Management Personnel definition to Ministers of Government:

If the definition of Key Management Personnel (KMP) was to include government Ministers, a number of issues arise relating to how this would be applied at an agency and Whole of Government (WhOG) level. This is particularly relevant given that Ministers will generally have direct and indirect roles with numerous government agencies (departments, statutory bodies and government owned corporations) and their related entities. Likewise, certain agencies may have more than one Minister to whom they are accountable.

Issues associated with applying AASB 124 to Ministers would include:

(a) Identification of KMP

As Ministers would appear to be KMP at the WhOG and General Government Sector (GGS) level, disclosure of their remuneration and related party transactions would be required in the financial statements prepared under AASB 1049. While ACAG believes that this information is relevant to users of the financial statements, practical issues could also arise on the disclosure of this information.

- ACAG requests clarification on whether heads of individual government agencies could also be considered as KMP for the purpose of the WhOG and or GGS financial reports.
- Clarification may also be required in relation to the definition of KMP in relation to the role of Cabinet and Executive Council which generally includes Ministers, the Governor, and in certain jurisdictions, possibly a Director-General who may act as a secretary.

These bodies can have a broad policy, planning and decision making function across all entities within WhOG. As a result of these bodies having such functions, guidance as to whether/how to include such individuals in AASB 124 disclosures would be beneficial.

(b) *KMP remuneration*

(i) Agency financial report

Ministers are generally remunerated through the Parliament via a central agency. Accordingly, where Ministers are not remunerated by individual agencies for which they are KMP, how would their remuneration be disclosed, if at all, in the financial reports of individual agencies? It is unclear how the allocation of “paid...by, or on behalf of the entity” and “includes such consideration paid on behalf of a parent of the entity” as included in the definition of compensation will affect such disclosures.

Apportionment of a Minister’s remuneration between agencies would require the application of considerable judgement and may be impractical. It would require an arbitrary apportionment of Minister’s parliamentary, party political, electorate and constituent responsibilities. Further, the inclusion of a small portion of a Minister’s salary in KMP disclosures at the agency level would provide little information to a user in interpreting the aggregate KMP compensation disclosures.

One jurisdiction remunerates Ministers through nominated agencies which report the remuneration as administered items. Again, these Ministers may have responsibility for other agencies which may give rise to apportionment issues. ACAG suggests clarification of treatment would be helpful in this circumstance.

Some jurisdictions query the need to disclose Ministerial remuneration in agencies’ financial reports where reference could be made to other published financial materials which already includes this information.

Suggested amendments that could be considered in relation to the application of the standard to Ministers of government could include:

- limiting KMP remuneration disclosures for Ministers of government to the WhOG level only; or
- exempting the disclosure of KMP remuneration for Ministers in the agency’s accounts in circumstances where the required information is publicly available and the financial report discloses where that information can be located.

ACAG Offices support limiting KMP remuneration disclosures for Ministers to the WhOG level only.

(ii) WhOG/GGS financial report

At the WhOG/GGS level, is there a need to give KMP disclosures for both the WhOG financial report and the GGS financial report? This would create another level of complexity in the compilation and readability of the disclosures and the apportionment issues noted above remain.

If the AASB does not consider it appropriate to change the proposed application of AASB 124 to Ministers, ACAG recommends that further clarity be provided in the standard relating to:

- the definition of KMP as applicable to NFP public sector entities, specifically taking into account the role of Ministers at both WhOG/GGS level and at an agency level. For example, if it is the AASB's intention that Ministers are always KMP of the Government, it would be helpful to state this.
- allocation of remuneration where the Minister is responsible for a number of entities within their portfolio e.g. whether apportionment of remuneration should be made based on services rendered regardless of who paid the remuneration.

(c) *Transactions with KMP of the entity or entity's parent*

Since the nature of transactions vary greatly e.g. purchases/sales of various types of goods or property, rendering and receiving of various types of services, lease or rent income/expense, ACAG suggests guidance be included on the level of detail required. This may also be of relevance to non-Ministerial KMP/related parties. Where there is a transition of Government, guidance would be useful on what transactions should be disclosed.

Related Party Transactions

Ministers as related parties

Even where a Minister is not KMP of a particular agency, it appears that they (and potentially their family members) would be captured as a related party (assuming the Minister is a KMP of the Government). The broader nature of activities undertaken by the government sector will likely involve more transactions between government entities and related parties than in a typical private sector context. The time taken to prepare disclosures may be significant and may pose difficulties in agencies meeting their statutory obligations to prepare financial statements by a given date.

Most ACAG Offices would like transactions with Ministers disclosed at the agency level, however, there are other Offices which are of the view that related party transactions should be aggregated at the WhOG level only.

WhOG and GGS financial reports

ACAG seeks clarification as to whether related party disclosures are required in both the WhOG financial report and the GGS financial report. To reduce complexity and duplication, ACAG recommends exempting the GGS financial report from complying with AASB 124.

Transactions between government entities

By virtue of the definition of related party (b)(i), all government entities will be related parties of each other. Although such entities are provided with exemption from application of paragraph 18, paragraph 26 requires disclosure of specific significant inter-government entity transactions and significant aggregate information. The costs of compliance with paragraph 26 are likely to be significant in the time and resources taken to compile the information given agency reporting timeframes.

General application of AASB 124 to NFP public sector entities

ACAG also recommends that consideration be given to including a public sector perspective for the section titled "Purpose of Related Party disclosures" within AASB 124 (paragraphs 5 to 8). Similarly, paragraph 27 of AASB 124 identifies that in assessing the significance of a related party transaction, consideration would be given as to whether they are carried out on "non-market terms." Since many government agency transactions are non-commercial (particularly those classified as NFP), ACAG suggests a broader sector neutral approach would be to refer to "transactions outside the normal course of business or on terms not available to non-related parties" as in Australian Auditing Standard ASA 550 *Related Parties*.

ACAG acknowledge the examples in AASB 124 at IE1-IE3, however, it is suggested additional guidance be considered for other types of transactions, e.g.:

- various types of fees/charges
- appropriations
- tax equivalent amounts
- amounts collected on behalf of another agency (as an agent).

In relation to these matters, ACAG believes that further consideration is required as to the exact nature and extent of the intended disclosures from the application of AASB 124 to NFP public sector entities. The application of AASB 124 to NFP public sector entities should provide for disclosure of information relevant to users of the report in a manner that does not significantly increase the cost of gathering the information required and is not so extensive that it potentially reduces the overall readability and usefulness of the financial report. This also avoids unnecessary duplication of information.

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

ACAG is not aware of any regulatory or other issues.

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

Subject to the points raised above, ACAG believes that related party information is useful to the users of the financial reports of NFP public sector entities. The proposals, with some adjustment, have the potential to help promote standardisation and comparability of related party disclosures across jurisdictions.

5. Whether the proposals are in the best interests of the Australian economy.

ACAG supports the disclosure of related party information on the basis of sector neutrality. ACAG does not believe there are significant economic impacts, positive or negative, associated with the proposed requirements.

6. Unless already provided in response to specific matters for comment 1–5 above, the costs and benefits of the proposals relative to the current requirements, whether quantitative (financial or non-financial) or qualitative.

ACAG believes significant additional costs may occur in the understanding and capture of relevant information. However, in some instances, these may be offset by the benefits of accountability and transparency in the long term.