



New South Wales  
TREASURY

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Our Reference: T05/01897  
Doc #: X07/03743  
Your Reference: ITC 12

30 AUG 2007

Dear Professor Boymal

**Invitation to Comment 12 - Differential  
Reporting and the Proposed IFRS for SMEs**

New South Wales Treasury welcomes the opportunity to make a submission on the above Invitation to Comment.

We agree in principle with the desire to provide simplified reporting requirements for certain smaller unlisted entities. But we do not think the IFRS for SMEs proposal makes any significant contribution towards achieving this goal. We see problems with providing simpler options that conflict with accountability or cause difficulties on consolidation when a parent entity adopts the alternative full IFRS option. We would prefer the same recognition and measurement principles to apply to all entities, but with far less disclosure requirements for smaller unlisted entities.

Importantly, there are also areas where we would like to provide additional comments regarding the fundamental principles of accounting standards and accountability, in particular regarding the reporting entity concept, public accountability and general purpose financial reports.

We agree broadly with the comments of the Heads of Treasuries Accounting and Reporting Advisory Committee in response to the ITC, but there are some areas where our opinions differ:

- NSW Treasury agrees with the proposed thresholds, not higher thresholds
- NSW Treasury does not consider a third tier necessary
- NSW Treasury does not support a threshold based on number of employees

Our detailed views in relation to the specific matters raised above follow.

Yours sincerely

Robert Williams  
for Secretary

## AASB Invitation to Comment 12

New South Wales Treasury provides the following views on specific questions asked by the AASB:

**(a) do you agree with changing the application focus of Australian Accounting Standards from ‘reporting entity’ to ‘general purpose financial reports’?**

No. While the IASB does not rely on the concept of ‘reporting entity’ to determine which entities apply its standards, there is no substantive difference between the IASB definition of ‘reporting entity’ (per the IASB Framework, paragraph 8<sup>1</sup>) and the AASB definition (per AASB 3 Appendix A and SAC 1<sup>2</sup>) that would preclude the AASB referring to the concept in Australian equivalents to IFRSs.

The IASB has stated in the Draft IFRS for SMEs at paragraph BC 33 that decisions on which entities should use the IFRS for SMEs will ultimately rest with national regulatory authorities and standard-setters. At the SME roundtable in Sydney it was suggested that who should prepare general purpose financial reports should be left to the regulators. We disagree. The AASB should be clearly articulating the underlying principle. There still needs to be a principle, even if, in practice, it is the regulator applying the principle in some pragmatic matter.

The AASB proposes several reasons for changing from the reporting entity concept at page ix of the preface to ITC 12. NSW Treasury does not believe that these reasons outweigh any perceived benefits. Examples where we disagree with the reasons raised include:

- Being the only jurisdiction to use the reporting entity concept – this does not mean Australia needs to change just to be consistent with others.
- Australia has adopted IFRSs and they apply to general purpose financial reports rather than reporting entities – but Australia has amended IFRSs to suit the Australian situation.
- A focus on the entity that reports rather than the report it prepares – we support the focus on the entity because it determines which entities should prepare general purpose financial reports. A focus on the report prepared is not enough without knowing who is required to prepare the report in the first place. Who determines whether or not an entity prepares general purpose financial reports? Judgement is required. There could be many instances where entities are not preparing general purpose financial reports, but should be.

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<sup>1</sup> “An entity for which there are users who rely on the entity’s general purpose financial statements for information that will be useful to them for making decisions about the allocation of resources.....”

<sup>2</sup> “An entity in respect of which it is reasonable to expect the existence of users who rely on the entity’s general purpose financial report for information that will be useful to them for making and evaluating decisions about the allocation of resources.....”

## AASB INVITATION TO COMMENT ON SMEs

In addition, NSW Treasury agrees with the dissenting comment from Colin Parker on the AASB Proposed Invitation to Comment:

“The reporting entity concept has been applied [to these sectors] for the past 15 years. The AASB should not move away from its current differential reporting regime for such entities, without a robust analysis of the strengths and weaknesses of the reporting entity concept in practice.”

Finally, The IASB has scheduled a Discussion Paper on the Reporting Entity for the third quarter of 2007. Moreover, AASB staff will be developing a draft Consultation Paper on the reporting entity concept as a contribution to the IPSASB’s public sector conceptual framework projects. We therefore feel it is premature to abandon the reporting entity concept when there are ongoing projects on the topic.

- (c) **do you support the proposal to apply the IASB’s definition of a publicly accountable entity to differentiate between for-profit entities that apply Australian equivalents to IFRSs and for-profit entities that apply an Australian equivalent to the IFRS for SMEs?**

NSW Treasury supports the use of the concept of publicly accountable in determining who applies the IFRS for SMEs. However, we do not support the proposed definition.

We believe the IASB definition of public accountability is too narrow because of its focus on for-profit entities. Public sector entities are obviously publicly accountable as noted below; however, they do not meet the definition in the IFRS for SMEs.

Instead, we support preliminary view 3.2 of the 2004 IASB Discussion Paper on SMEs, where an entity has public accountability if:

- There is a high degree of outside interest in the entity from non-management investors or other stakeholders, and those stakeholders depend primarily on external financial reporting as their means of obtaining financial information about the entity; or
- The entity has an essential public service responsibility because of the nature of its operations.

Because we believe that all public sector entities would be regarded as publicly accountable under the preliminary view above, the IASB definition of the term needs to be broadened to include this perspective.

We strongly argue that public sector accountability is also about achievement of community desired outcomes; eg improvements in health, education, etc and that these require additional or separate non-financial reporting accountability. But we believe that this is separate and/or additional information, not a substitute for financial reporting.

## AASB INVITATION TO COMMENT ON SMEs

Clearly, the public wants to know whether those outcomes and services have been achieved effectively and efficiently and that there is accountability for the expenditure of funds provided by taxpayers. This is similar to the increased focus in the private sector on corporate social responsibility being additional to and/or separate from financial responsibility (ie information that's found in annual reports).

- (i) **do you agree that, consistent with the IASB's view of a general purpose financial report, under a revised Australian differential reporting regime:**
- (i) **all financial reports that are available on a public register, such as those prepared and lodged with the ASIC under the Corporations Act, should be regarded as general purpose financial reports; and**
  - (ii) **all financial reports that are made available to the public at large, such as those tabled in a Parliament, also should be regarded as general purpose financial reports?**

**If you do not agree, explain why.**

We disagree. Although the IASB proposed changing the definition of 'general purpose financial reports' to incorporate the wording above, the most recent amendments (IAS 1 Near Final Draft) did not include any change.

We understand that many respondents were concerned that the proposed wording could capture documents other than annual reports and could affect some entities required by law to place their financial statements on a public file even if they were not general purpose financial statements. Not all reports tabled in Parliament are general purpose financial reports. Therefore, the question above does not reflect the current status of the IASB definition of general purpose financial reports at paragraph 7 of the Near Final Draft:

*"General purpose financial statements (referred to as 'financial statements') are those intended to meet the needs of users who are not in a position to require an entity to prepare reports tailored to their particular information needs."*

- (k) **the Corporations Act includes three size thresholds respectively for revenue, assets and the number of employees to distinguish between small and large proprietary companies. The AASB's proposed size thresholds only include the monetary thresholds of revenue and assets. Do you think that, except for the case of for-profit entities that are not publicly accountable but are important from a public interest perspective, a further size threshold for the number of employees would be appropriate under the proposed differential reporting for not-for-profit private sector entities and public sector entities?**

## AASB INVITATION TO COMMENT ON SMEs

No, we feel that a further size threshold – number of employees – is not necessary. We agree with the comment in the AASB Basis for Conclusions at paragraph BC41 related to the number of employees in the not-for-profit private sector. Regarding the public sector, the number of employees is not relevant to the public accountability or reporting entity concept which is what we prefer to use to determine who applies the proposed IFRS for SMEs.

**(n) do you think Australia and New Zealand should seek to achieve harmonisation in their reporting requirements regarding SMEs?**

No. New Zealand's definition of publicly accountable is more restrictive than the current understanding of public accountability in Australia. New Zealand's SMEs' reporting also has more concessions regarding financial reporting than Australia or the IASB. New Zealand doesn't require a cash flow statement, nor will it require a Statement of Changes in Equity in its proposed NZ IAS 1 if total recognised gains and losses are shown in a comprehensive income statement and there are no transactions with equity holders.

**(p) do you think that the overall benefits that would arise from the proposals would exceed the overall costs? If you are an entity that prepares a general purpose financial report or would need to do so under the proposals, please advise us of any increased costs or any savings that would result from the proposals, and if possible, quantify them.**

We do not think the overall benefits of entities switching from full AEIFRS to the proposed IFRS for SMEs would exceed the costs. In Australia, the adoption of AEIFRS proceeded fairly smoothly. If entities who qualify under the proposals adopt the IFRS for SMEs, they must explain how the transition affected their financial report, as well as provide reconciliations of equity and profit or loss. They must also present full comparatives as at the transition date. Australian entities have already done this exercise when they adopted AEIFRS. They may not wish to go through another transitional period again so soon. If the proposals are adopted, some entities may switch to the IFRS for SMEs but then be forced to switch back again to full AEIFRS if circumstances change in the future; eg they no longer meet the size threshold requirements or they become publicly accountable. There could also be increased costs where entities using the IFRS for SMEs are consolidated by a parent using full AEIFRS. The AASB voiced similar comments at paragraph BC46 in its Basis for Conclusions.

We would prefer the same recognition and measurement principles to apply to all entities, but with far less disclosure requirements for smaller unlisted entities. Reduced disclosures by a smaller unconsolidated entity could result in the benefits outweighing the costs if the entity adopts the IFRS for SMEs.