



**Australian Government**

**Department of Finance**

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Ms Kris Peach  
The Chair - Australian Accounting Standards Board  
PO Box 204  
Collins Street West  
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Dear Ms Peach

**Invitation to Comment (ITC) 40 – Financial Instruments with the Characteristics of Equity**

The Department of Finance (Finance) welcomes the opportunity to respond to ITC 40 – *Financial Instruments with the Characteristics of Equity*.

Finance does not wish to make a full submission, but has a number of issues that will need consideration in applying the principles in the Discussion Paper to not-for-profit entities in Australia, including the public sector. Our assessment is that these will impact the Australian version, but not the IASB version. We have confined our comments in this letter to the proposals in the Discussion Paper, and not extended our comments to matters already settled and codified in AASB 9 *Financial Instruments*.

The principles for distinction between liabilities and equity contained in the early parts of the Discussion Paper have limited relevance to public sector entities, both not-for-profit and for-profit. The public sector rarely has the types of liability or equity instruments on which this project is focussed. In many not-for-profit public sector entities, the equity is not even comprised of financial instruments.

The principles for presentation and disclosure in Sections 6-8 of the Discussion Paper do have relevance to the public sector, in circumstances where they are material to the preparation of financial statements, and Finance offers the comments below. References are to the sections or paragraphs of the Discussion Paper:

- We prefer valuation changes be included in Other Comprehensive Income and other income and expense items included in Profit and Loss (paragraph 6.42). This would align AAS with GFS.
- We concur that existing disclosures are adequate for assessing liquidity and cash flows (paragraph 6.49).

- We do not regard the allocation of returns across equity instruments as necessary or useful for public sector entities, particularly those that are wholly-owned (paragraph 6.57). The IASB rationalises these disclosures for better assessment of returns on equity instruments, but this is not a significant factor for public sector equity instruments. Further AASB 133 *Earnings per Share*, frequently referenced, is not applicable to the public sector.
- Our view is that changes to presentation/disclosure of instruments by type of instrument or in order of priority proposed in Sections 6 and 7 are unnecessary for the public sector:
  - Existing classification requirements, derived from existing standards including AASB 101, and from GFS standards, provide information that is adequate for users;
  - Order of priority on liquidation is usually irrelevant for public sector entities that have no separate legal identity, or those entities whose debts are guaranteed by the government. If these entities are terminated, it is usually as part of an administrative restructure, at which time equity and liabilities are re-allocated to other public sector entities, rather than crystallise and be paid;
  - Similarly, information about potential dilution of ordinary shares is mostly irrelevant; and
  - If, however, the prevailing view is that these disclosures are relevant to the public sector, we would prefer they be contained in the notes rather than on the face of the financial statements.
- We agree that under some circumstances, disclosure of contractual terms and conditions of liability and equity instruments could provide information for users. (Section 7). However:
  - Public sector users should be consulted to determine if there is a strong public sector case for this type of disclosure;
  - This should not apply to simple instruments with well-understood terms and conditions, such as trade payables; and
  - Finance agrees with the IASB's comment that if disclosures are to be instrument-by-instrument, this requirement could be challenging when there are a large number of financial instruments to aggregate, even when materiality is considered. This issue could apply to the public sector. Our view is that there should be focus on aggregating disclosures for instruments with similar terms and conditions.
- We agree in principle with Section 8, preferring disclosures based on (legal) contractual terms, over other alternatives such as economic compulsion. However, we note that this is not always the case under other existing standards, such as *AASB 119 and 137* (constructive obligations), *AASB 15* (in respect of not-for-profit amendments), and some requirements of *AASB 16*.
  - Further, current practice in the public sector in Australia is to treat "contract-like" arrangements as if they were financial instruments, even where there is not a legally enforceable contract in place. This practice should be taken into account in applying the final version of the standard to the public sector.

Finance also requests that the AASB carefully examine any final IASB standard for application of tiered reporting arrangements, such as the Reduced Disclosure Requirements.

If you have any queries regarding our comments, please contact Peter Gibson on (02) 6215 3551 or by email to [peter.gibson@finance.gov.au](mailto:peter.gibson@finance.gov.au).

Yours sincerely



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