

AGENDA PAPER

Item Number: 8
Date of Meeting: 28 August 2020
Subject: Proposed submission on the AASB's ED regarding Special Purpose Financial Statement disclosures

Action required **For discussion** **For noting** **For information**

Purpose

To:

- update the Board on the Australian Accounting Standard Board's (AASB) proposed additional disclosure requirements in Special Purpose Financial Statements (SPFS) for certain for-profit entities; and
- seek the Board's views and comments on a draft Submission with respect to the AASB's proposals in ED 302 on Special Purpose Financial Reports.

Background

In August 2019, Technical Staff presented an [agenda paper](#) to the Board relating to the AASB's [ED 293](#) *Amendments to Australian Accounting Standards – Disclosure in Special Purpose Financial Statements of Compliance with Recognition and Measurement Requirements* (ED 293).

ED 293 proposed increased disclosures predominantly on compliance with recognition and measurement requirements for entities lodging SPFS with the Australian Securities and Investments Commission (ASIC) and the Australian Charities and Not-for-profits Commission (ACNC). ED 293 was proposed to be effective for the year ended 30 June 2020.

ED 293 proposals were approved for ACNC entities. However, the AASB determined not to proceed for ASIC entities as it was deemed that the cost of requiring these additional disclosures for just one year did not outweigh the benefits (before transitioning to General Purpose Financial Statements (GPFS) under ED 297 discussed below).

Concurrently, in August 2019, the AASB proposed removing the reporting entity concept and ability to prepare SPFS for specific entities in [ED 297](#) *Removal of Special Purpose Financial Statements for Certain For-Profit Private Sector Entities* (ED 297) for 2021 onwards.

ED 297 proposals were approved in March 2020 via [AASB 2020-2 Amendments to Australian Accounting Standards – Removal of Special Purpose Financial Statements for Certain For-Profit Private Sector Entities](#) (AASB 2020-2), however, the commencement date was delayed to 2022.

This removes the ability to prepare SPFS from 2022 for all for-profit entities required:

- under legislation to comply with Australian Accounting Standards (AAS) or accounting standards; or
- by their constituting document (or another document) to comply with AAS where the relevant document was created or amended on or after 1 July 2021.

Therefore, entities required only under their constituting document (or another document) to comply with AAS, but where this document was created or amended before 1 July 2021, remain free to continue to prepare SPFS on an ongoing basis.

However, ED 302 *Amendments to Australian Accounting Standards – Disclosures in Special Purpose Financial Statements of Certain For-Profit Private Sector Entities* ([ED 302](#)), released in June 2020 re-proposes increased disclosures predominantly on compliance with recognition and measurement requirements of AAS by for-profit entities required:

- by legislation to comply with either AAS or accounting standards, which will only apply for one period (2021) before these entities transition to GPFS under AASB 2020-2; or
- only by their constituting document (or another document) to comply with AAS, which was created or last amended before 1 July 2021.

Matters for Consideration

Entities required by constituting or other documents to comply with AAS

While some of the additional disclosures proposed under ED 302 overlap with paragraph 6.1 of APES 205 *Conformity with Accounting Standards* (APES 205), ED 302 also includes substantially more information to be disclosed.

APES 205 was first issued in 2007 and replaced Miscellaneous Professional Standard APS1 *Conformity with Accounting Standards and UIG Consensus Views*. APS 1 superseded the Institute of Chartered Accountants in Australia (ICAA) Statement K1 *Conformity with Accounting Standards* in 1979 and ICAA Statement K1 was first issued in May 1971. As such, various iterations of a professional standard on conformity with accounting standards has been in existence for almost fifty years.

ED 302 refers to Research Report No. 12 *Financial Reporting Practices of For-Profit Entities Lodging Special Purpose Financial Statements* (August 2019), which indicates that disclosures within SPFS were insufficient. However, this Research Report only focuses on entities that lodge financial statements with ASIC, being large proprietary companies, small proprietary companies, small foreign-controlled and unlisted public companies.

ED 302 does not include research findings that indicate that users of SPFS for entities required to comply with AAS by their constituting or other documents have determined that the disclosure requirements, including those required under APES 205, are insufficient. Further, APESB has not received feedback from stakeholders that the disclosure requirements in APES 205 are deficient.

The proposals in ED 302 for entities required by their constituting or other documents to comply with AAS would capture a wide range and size of entities, including large trading trusts, small family trusts, partnerships and SMSFs. Technical Staff anticipate that a significant proportion of these entities, in particular the smaller entities, would either have no external users or external users that can demand specific reports or disclosures (for example, banks) and could do so on an ad hoc basis if required.

The AASB have not provided details in ED 302 of the number and breakdown of entities affected by the proposals and the likely users and those users' needs. An [AASB staff paper in April 2020](#) estimated that this may be in excess of 359,000 but is likely to be significantly higher as this does not appear to include entities such as self-managed superannuation funds (of which there are almost 600,000 in Australia).

Therefore, there are potentially a significant number of smaller entities that would be captured under these requirements, where empirical evidence has not been provided as to whether it is required by users or the anticipated benefits of the proposals.

ED 302's proposals leave limited options for smaller entities. These entities could potentially amend their constituting document to not require adherence to AAS. However, this could result in significant legal/accounting fees and potentially unintended consequences such as capital gains tax. Alternatively, they would be required to produce these increased disclosures, which would also result in additional accounting fees on an ongoing annual basis.

The AASB has not presented information with respect to the anticipated costs for either amending constituting documents or providing the additional disclosures. However, if you extrapolate potential costs over the number of entities affected, the regulatory impact is significant. For example, if the additional annual cost was \$400, and 700,000 entities were affected, the yearly regulatory impact would be \$280m.

Further, ED 302 does not apply to 'small proprietary companies' with less than \$50m consolidated gross revenue, \$25m consolidated gross assets, and 100 employees. Whereas ED 302 applies to all entities required by their constituting or other document to comply with AAS regardless of size. This would include, for example, a family trust with \$200,000 revenue, \$100,000 assets and no employees. Technical Staff are concerned that it appears inequitable to impose additional requirements on such an entity, that could be less than 1% of the size of a small proprietary company where these requirements would not apply.

Technical Staff are also concerned that the enforceability of these requirements has not been established where these SPFS are not lodged with a regulator.

Technical Staff recommend that the AASB:

- *in respect of entities only required by their constituting or other documents to comply with AAS, undertake research and gather empirical evidence in respect of whether there is a deficiency for users of these SPFS to inform the standard-setting process in this non-legislated environment, including a cost-benefit analysis of these proposals.*
- *should the research and analysis listed above not identify issues in respect of these entities, maintain this non-legislated environment subject to the requirements in APES 205 as no reports of deficiencies have been reported*

ED 302 notes that the AASB considered a proposal to place a threshold on the entities that the proposed disclosures applies to in order to exclude entities that would not be classified as large proprietary companies under the *Corporations Act 2001*, which was ultimately decided against. However, if after the above research and analysis, the AASB believes additional disclosures are required, a threshold could be reconsidered.

Technical Staff recommend that if after the above research and analysis of these entities, the AASB believes additional disclosures are required, then it is strongly recommended that a an appropriate threshold be determined. This approach will then mean that only entities above the threshold will provide the additional disclosures.

Entities required by legislation to comply with AAS

Technical Staff are also concerned that the costs of the proposals for entities required by legislation to comply with AAS or accounting standards for only a one-year period (2021) will outweigh the benefits due to the temporary nature of the changes.

Technical Staff recommend that the AASB reconsider the temporary one-year requirement to produce the proposed additional disclosures for entities required under legislation to comply with AAS or accounting standards.

Way Forward

APESB Technical Staff have discussed these concerns with the AASB Technical Staff as well as the financial reporting policy advisers of the professional accounting bodies.

AASB is holding a stakeholder webinar on the 1st of September 2020 and APESB Technical Staff will attend this webinar to gather further information and insights.

Technical Staff propose making a submission to the AASB on ED 302, noting the above concerns. A draft submission on ED 302 is attached as Agenda Item 8(a) for the Board's consideration.

Recommendations

The Board:

- note the update on the AASB's proposed additional disclosure requirements in SPFS for certain for-profit entities; and
- provide the Board's observations, review, and editorial comments, in respect of APESB's proposed submission on ED 302.

Materials presented

Agenda Item 8 (a) APESB Draft Submission to the AASB on ED 302

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