



Australian Government

Australian Accounting
Standards Board

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The General Manager
Corporations and Financial Services Division
Department of the Treasury
Langton Crescent
PARKES ACT 2600

Dear Sir/Madam

Discussion Paper: Financial Reporting by Unlisted Public Companies

The Australian Accounting Standards Board (AASB) is pleased to provide comments on the abovenamed Discussion Paper.

The AASB supports the Government's drive to reduce the reporting burden of companies, based on a cost-benefit analysis of financial reporting by such entities. In particular, the AASB welcomes the introduction of legislation that would be complementary to its current consideration of the differential reporting regime in Australia.

The attached observations on the specific questions in the Discussion Paper are based on the AASB's deliberations which led to the issue of ITC 12.

If you have queries regarding any matters in this submission, please contact Ahmad Hamidi (ahamidi@asb.com.au) or myself.

Yours sincerely

A handwritten signature in black ink that reads 'David Boymal'.

David Boymal
Chairman

Some observations on the specific questions in the Discussion Paper

Issue A Do you support the introduction of a differential reporting regime based on size for companies limited by guarantee? If so, what do you consider to be the appropriate criteria (both in terms of the indicators of size and the quantum of those indicators) for differentiating between those companies that are required to report and those companies that are exempt?

Issue B. Do you believe it is appropriate to differentiate between companies limited by guarantee by the nature of their operations rather than just size? If so, what nature of operations do you believe warrants greater transparency?

The AASB notes that small proprietary companies are exempted from preparing and lodging financial reports and supports a similar regime being introduced for companies limited by guarantee. However, the AASB also acknowledges that companies limited by guarantee have generally a not-for-profit objective¹ and there would be public interest in their activities when they receive government funds or privileged access to public assets, receive contributions directly from the public or enjoy tax concessions. A good example would be a charity that progresses its activities through a company limited by guarantee. Such public interest goes beyond the interests of members.

The public interest element makes it difficult to identify the criteria that should be used to differentiate between those companies limited by guarantee that should report and those that need not report. In its own deliberations on ITC 12, the AASB considered a number of criteria including:

- revenue thresholds
- asset thresholds
- employee thresholds
- public accountability definitions

The AASB noted that revenue and assets thresholds can achieve consistent outcomes in purely financial terms but may compromise accountability. The AASB concluded that employee numbers are unlikely to provide a robust basis for differential reporting because of the extent to which voluntary labour is used in many not-for-profit entities.

The AASB also noted that although a definition of public accountability could provide conceptually sound criteria to identify entities that should report, it would be difficult to operationalise such a concept. However, financial thresholds provide reasonable criteria from a practical point of view. In the AASB's view, accountability (and in particular its political and social forms) are directly related to public interest and accordingly it concluded that an approach based on the notion of public interest and employing size thresholds would be appropriate. The aim should be identifying thresholds that reflect various degrees of public interest.

The AASB considers that a revenue test alone would ignore accountabilities associated with managing assets, while an assets test on its own would ignore the capacity to meet reporting costs.

¹ As confirmed by the University of Melbourne's Survey quoted in the Discussion Paper.

The AASB suggests that a combination of revenue and assets thresholds holds the greatest promise as an operational test for differential reporting by companies limited by guarantee. The precise quantities of the thresholds would need to be the subject of research.

It should be pointed out that the AASB considerations were in relation to questions of differential levels of reporting requirements and not in relation to absolute exemption from reporting.

The 'nature of operations' is fundamental in assessing whether there is public interest in the activities of an entity. The AASB considers that companies engaged in activities of high public interest as indicated by their nature of operations such as charities and those involved in soliciting money from the public, whether in the form of deposits or donations, should be required to prepare financial reports, irrespective of their size.

In respect of other companies limited by guarantee, the AASB suggests that the same thresholds of revenue and assets used for small proprietary companies be applied to exempt them from financial reporting. As the companies limited by guarantee often are engaged in not-for-profit activities that may use volunteer labour, the 'employee number threshold' should not be used. Any other company that falls below both monetary thresholds should be exempted from reporting.

Issue C Do you consider that companies limited by guarantee that receive any money through grants should have financial reporting requirements? If so, can this obligation be satisfied by the company providing special purpose financial reports to the grantor rather than preparing general purpose financial reports under the Corporations Act?

The receipt of a grant should not automatically lead to the need for a general purpose financial report. Grants are usually offered pursuant to an agreement setting out conditions of the grant, including an acquittal process. Most acquittal processes involve accounting for the expenditure made out of the grant and providing various reports including a special purpose financial report to the grantor.

Issue D If you support some companies limited by guarantee being exempted from financial reporting, what percentage of members should be required in order to require an exempt company limited by guarantee to prepare a financial report?

We believe the 5% threshold of members used in case of small proprietary companies would be appropriate.

Issue E If you support the retention of financial reporting requirements for all companies limited by guarantee, do you consider that there is scope to reduce the amount of financial information these companies are required to report? If so, what type of financial information do users need companies limited by guarantee to report (for example, related-party disclosures)?

We do not support the retention of financial reporting requirements for the smallest of companies limited by guarantee unless they are recipients of public deposits or donations. An exemption from reporting for such companies similar to that available to small proprietary companies is preferred.

Issue F Do you consider that there is a need to harmonise the financial reporting requirements of companies limited by guarantee and incorporated associations to provide a consistent reporting framework for not-for-profit entities in Australia?

Many incorporated associations are engaged in not-for-profit activities, which in many cases would probably have been carried out through the establishment of a company limited by guarantee if the incorporated association option were not available. The harmonisation of the financial reporting requirements of the two types of entities would be helpful in creating comparability between entities engaged in similar operations and across states.

Issue G In order to assist in progressing this project, it would be useful to obtain an indication from companies limited by guarantee of the cost of preparing a directors' report and audited financial report as required by the Corporations Act

The AASB has not conducted any research on this issue.

Issue H If some companies limited by guarantee were to be exempt from financial reporting, do you consider there is value in these companies continuing to be subject to some level of non-statutory external assurance as a means of promoting good governance? If so, what should this assurance relate to and how do you think this regime should be introduced (for example, through best practice guidelines issued by the professional accounting bodies)?

The AASB does not provide a view on this issue.

Issue I For those companies limited by guarantee that are required to prepare financial statements, do you consider that there is a need to change the current audit requirements? If so, which aspects of the current requirements need to be reformed?

The AASB does not provide a view on this issue.

Issue J Do you support amending the Corporations Act so that companies limited by guarantee are specifically prohibited from distributing profits to members in the form of dividends?

The AASB does not provide a view on this issue.

Issue K Do you support the principle that all for-profit companies that have raised capital from the public should have statutory annual financial reporting obligations?

All such companies should have statutory annual financial reporting obligations. However, under the AASB's proposed revised differential reporting regime, for-profit companies that are publicly accountable or otherwise satisfy nominated size thresholds would apply Australian equivalents to IFRSs and non-publicly accountable entities that fall below the thresholds apply an SMEs Standard². The AASB notes that not all unlisted public companies limited by shares have raised capital from the public.

² See ITC 12 "Proposed Revised Differential Reporting Regime for Australia and IASB Exposure Draft of A Proposed IFRS for Small and Medium-sized Entities".

Issue L *Given a satisfactory mechanism to allow unlisted public companies limited by shares with a not-for-profit objective to convert to a company limited by guarantee is not available, would you support an equivalent differential reporting regime to that proposed for companies limited by guarantee to be established for unlisted public companies limited by shares with a not-for-profit focus? If so, do you support using the definition of not-for-profit entity in the accounting standards to determine whether a company has a not-for-profit focus?*

The AASB agrees that an equivalent differential reporting regime should be established for unlisted public companies limited by shares with a not-for-profit objective on the basis that transactions of not-for-profit entities should be accounted for similarly regardless of the legal form of the organisation in which they are conducted. However, consistent with the AASB view of issue B, only those not-for-profit unlisted public companies limited by shares that do not engage in activities where their nature of operations attracts high public interest such as charities and those with a deposit taking function should be exempted from reporting.

The AASB supports using the definition of not-for-profit entity used in accounting standards. The AASB is progressing a project to enhance the guidance provided in making use of that definition.

Issue M *In order to assist in progressing this project, it would be useful to obtain an indication from unlisted public companies limited by shares of the cost of preparing a directors' report and audited financial report as required by the Corporations Act and also the number of unlisted public companies limited by shares that have a not-for-profit objective.*

The AASB has not conducted any research on this issue.