



<b>Project:</b>	Franking Credit Disclosures	<b>Meeting:</b>	M196
<b>Topic:</b>	Analysis of stakeholder's feedback on franking credit disclosure requirements	<b>Agenda Item:</b>	6.1
		<b>Date:</b>	6 June 2023
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		<b>Decision-Making:</b>	High
		<b>Project Status:</b>	Decide on next steps

### Objective of this paper

- The objective of this staff paper is for the Board to:
  - consider** feedback received from targeted outreach on current franking credit disclosure requirements and the need for additional disclosures;
  - consider** staff analysis of the feedback; and
  - decide** the next steps of the project.

### Background and reasons for bringing this paper to the Board

- In response to the AASB's recent Agenda Consultation, Invitation to Comment ITC 46 *AASB Agenda Consultation 2022-2026*, some stakeholders suggested that the Board should consider developing additional disclosure requirements for franking credit disclosures.<sup>1</sup>
- There were three key areas that stakeholders suggested the Board to consider:
  - requiring a disclosure that reconciles the closing actual franking credit account balance to the adjusted franking credit account balance;
  - providing specific guidance about the disclosure of deferred franking debits under the revised Research and Development (R&D) tax offset regime;<sup>2</sup> and

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1 [Agenda Paper 8.2](#) to the June 2022 Board meeting provides a summary of the stakeholder feedback from the 2022- 2026 Agenda Consultation.

2 As presented in the [Franking Credit Disclosures draft project plan](#) to the March 2023 Board meeting, an entity's franking account may be affected by the R&D tax offset regime as entities eligible for the offset will not record any franking credits in their franking account for either future PAYG instalments, or payments of income tax until such times as those types of franking credits effectively offset any prior deferred franking debits.

- (c) requiring additional disclosures to explain the amount of franking credits available for distribution to shareholders as this information may be unclear, especially in the consolidated financial statements.
- 4 At the March 2023 Board meeting, the Board supported the draft [Franking Credits Disclosure project plan](#). The Board decided that the project’s scope should be limited to Tier 1 for-profit entities and that further evidence and stakeholder engagement was needed before it could decide on any standard-setting work.<sup>3</sup>
- 5 Staff have since performed limited targeted outreach with various stakeholders, including preparers, users, advisors, and professional accounting bodies, to understand whether there is a need to improve the current franking credit disclosure requirements under AASB 1054 *Australian Additional Disclosures* and, if so, what the best approach might be.
- 6 This paper summarises the feedback received from targeted outreach and considers whether the concerns raised are of such prevalence and magnitude that they warrant a standard-setting response.

### Structure of this paper

- 7 This paper is structured as follows:
  - (a) Amendments to Legislation on off-market share buybacks (paragraphs 8 – 12);
  - (b) Summary of feedback from limited targeted outreach and further review of financial statements (paragraphs 13 – 15);
  - (c) Staff recommendation (paragraphs 16 – 19);
  - (d) Alternative solution (paragraphs 20 – 25)
  - (e) Next steps of the project (paragraphs 26 – 27)
  - (f) **Appendix A** – Detailed summary of feedback from limited target outreach
  - (g) **Appendix B** – Further review of financial statements

### Amendments to Legislation for off-market share buybacks

- 8 In February 2023, the Federal Government introduced the [Treasury Laws Amendment \(2023 Measure No.1\) Bill 2023](#), effective from 25 October 2022.
- 9 In summary, the amendments align the tax treatment of off-market share buybacks by listed public companies with those of on-market share buybacks. Before the amendments, a listed public company that undertook an off-market share buyback could treat part of the buyback price as a dividend which was often fully franked for tax purposes. Whereas, for on-market share buybacks, no part of the purchase price is considered a dividend for shareholders. Off-market share buybacks were attractive as they were often undertaken at a discount to the market price. The Legislation now prevents any part of the buyback price from being treated as a dividend and is likely to end the practice of discounted off-market buybacks.
- 10 An integrity measure was also included in the Legislation to require listed public companies that undertake an off-market buyback to debit their franking account by an amount equal to the debit that would have arisen if the company had undertaken an on-market share buyback under the existing rules (i.e. to the extent the buyback price is not debited to the company’s share capital account). Currently, companies that undertake on-market share buybacks can choose to debit all

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3 Refer to the March 2023 Board meeting [minutes](#)

of the on-market share buyback prices against their share capital base, and it is understood that companies can continue to do this for both on-market and off-market buybacks.

- 11 In addition, staff understand that there are other measures, such as distributions paid being considered unfrankable and being treated as a franking debit where they are paid as part of a selective reduction of capital. Also, distributions funded by capital raisings will now be treated as unfrankable, even if only a small portion of the dividend is funded with a capital raising or a capital raising occurs after a distribution is paid.
- 12 Staff understands that these measures could alleviate some of the concerns that prompted stakeholders to suggest that entities should be required to disclose the movements between the opening franking credit account balance and the franking credit balance available to shareholders in subsequent reporting periods.

## **Summary of feedback from limited targeted outreach and further review of financial statements**

### *Limited targeted outreach*

- 13 Staff has conducted further targeted outreach with users, Disclosure Initiative Project Advisory Panel (PAP) members, professional accounting bodies and a professional services firm. Broadly staff explained the feedback from the Agenda Consultation summarised in paragraph 3 and asked stakeholders:
  - (a) What disclosures would be useful to users of franking credits?
  - (b) Why do some entities disclose more information about franking credits than what is currently required by the Standard?
  - (c) Are there any significant barriers to disclosing the information in paragraph 14 of AASB 1054?
  - (d) Are you aware of any trans-Tasman reasons why similar disclosures in paragraph 14 of AASB 1054 should be required for New Zealand?
  - (e) Do you think staff-level guidance should be developed to help preparers consider when and what additional disclosures would be useful to users?
- 14 A detailed summary of the feedback is provided in Appendix A. However, from the feedback obtained, staff observed the following key points:
  - (a) Two users provided feedback. In principle, they both suggested additional disclosures would be of limited use because:
    - (i) User A monitors the balance of franking credits on a year-on-year basis and can make assumptions to estimate the movements in franking credits and their origin; and
    - (ii) User B considers that the Legislative changes (see paragraphs 8 – 12) will alleviate some of their concerns and therefore eliminate the need for additional disclosures reconciling the movements between the opening and closing franking credit account balance for use in subsequent reporting periods. User B did note that for dual-listed entities, it may still be difficult to determine the franking credit balance available for distribution to shareholders because there can be different classes of share capital with different dividend rights. However, they noted that there are limited instances where this is an issue;
  - (b) Disclosure Initiative PAP members suggested there is insufficient evidence to warrant standard-setting. They also did not think that staff-developed guidance about what ‘better

practice' disclosures could look like would be useful as, in their experience, entities will only disclose information that is required by the accounting standards;

- (c) Three professional accounting bodies confirmed that they had not received any feedback from their members suggesting there is an issue with the existing disclosure requirements, nor is there a need for any further disclosures; and
- (d) One professional services firm considered additional disclosures helpful. They explained that relevant, useful, and consistent information about franking credits can communicate the entity's governance and management policy to users. However, they did suggest that if users do not consider this information to be useful and there is no demand for it, there is no reason to amend the requirements of AASB 1054. Consistent with the views of Disclosure Initiative PAP members, the firm does not think staff-developed guidance would be useful. However, they suggested including the objective/rationale of why franking credit disclosures are required in the financial statements in the Basis for Conclusions may be helpful to preparers.

#### *Review of financial statements*

- 15 Staff reviewed the financial statements of an additional 110 ASX-listed entities to understand better what franking credit disclosures entities make in their financial statements. A detailed summary of the financial statements review is provided in Appendix B. Consistent with the findings from the limited review of financial statements discussed with the Board at the March 2023 meeting,<sup>4</sup> staff observed there are some inconsistencies in the disclosures of franking credits in financial statements. For example:
- (a) some entities (14%) disclose a reconciliation of the opening and closing balance of franking credits adjusted by imputation debits/credits (additional disclosure **not** required by AASB 1054);
  - (b) some entities (24%) disclose the impact of franking debits arising from declared dividends not yet recognised as a liability in the financial statements (additional disclosure **not** required by AASB 1054);
  - (c) none of the entities presented information on the impact on franking debits arising from the receipt of the R&D tax offset on franking credits (this disclosure is **not** required by AASB 1054); and
  - (d) all entities presented consolidated financial statements; most (95%) indicated they had formed a tax-consolidated group.

#### **Staff recommendation**

- 16 In response to the concerns raised by stakeholders summarised in paragraph 3, the Board should consider whether the current franking credit disclosures meet the needs of users, or additional franking credit disclosures are required.
- 17 Limited targeted feedback indicated no significant issues with the current disclosure requirements. Whilst feedback in response to the Agenda Consultation suggested additional disclosures are needed, the feedback obtained from limited outreach activities does not support this. Specifically, User B, who raised concerns about the sufficiency of disclosures during the Agenda Consultation, indicated that the amended Legislation largely alleviated his concerns. Further, the professional services firm confirmed that whilst they think additional disclosures should be explored, if users do not need such information, there is no merit in proceeding.

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4 Refer to Agenda Paper [7.1 at the March 2023 Board meeting](#)

- 18 In respect to comments provided by User B about dual-listed companies (see paragraph 18 above), staff identified only one Australian dual-listed company (i.e. Rio Tinto is the only Australian dual-listed company on the Australian Securities Exchange). As such, there is insufficient evidence to demonstrate a significant or prevalent issue with the current disclosure requirements.
- 19 Therefore, in staff's view, the current franking credit disclosures required under AASB 1054 *Australian Additional Disclosures* continue meeting users' needs and no additional disclosures are warranted.

**Question 1 to the Board members:**

Do Board members agree with the staff recommendation in paragraph 19 that the current franking credit disclosures required under AASB 1054 *Australian Additional Disclosures* continue meeting users' needs and no additional disclosures are warranted?

If not, staff have presented two options on how to address the Agenda Consultation feedback discussed in paragraphs 20 – 25 below.

**Alternative solution**

- 20 If the Board disagrees with staff recommendation in paragraph 19, there are two options the Board can consider to address the Agenda Consultation feedback.

**Option 1 – Make amendments to AASB 1054 to require additional franking credits disclosures**

- 21 Under this option, additional disclosure requirements would be included in AASB 1054 requiring entities to disclose, based on the guidance in paragraph 14 of AASB 1054, how the franking credit balance available for subsequent periods is derived.
- 22 Whilst this option would address the concern raised by the limited feedback from the Agenda Consultation that additional disclosures are required, staff do not consider this option to be appropriate because:
- (a) limited targeted outreach does not support the need for additional disclosures. That is, there is insufficient evidence of a significant and widespread issue that warrants amendments to AASB 1054.
  - (b) users do not appear to value this information, which is, therefore, likely to result in boilerplate information.
  - (c) recent changes to the Legislation addressing the off-market share buyback have reduced some of the concerns raised by User B (see paragraph 14(a)(ii)).

**Option 2a – Issue staff-level paper with practical examples of current franking credit disclosures**

- 23 Under this option, there would be no changes to the current disclosure requirements. Staff would instead develop a staff-level paper to provide practical examples of when additional franking credit disclosures may be useful to users. Staff do not consider this option would address the concerns as feedback from Disclosure Initiatives PAP members indicated that entities are unlikely to adopt non-mandatory staff guidance.

**Option 2b – Include the rationale/objective for the disclosure of franking credits in the Basis of Conclusions**

- 24 Similar to option 2a above, there would be no changes to the current disclosure requirements. However, more information about the objective of the franking credit disclosures and why they are considered important could be included in the Basis for Conclusions to AASB 1054 to help preparers assess whether additional franking credit disclosures would be helpful to users. Staff acknowledge that this suggestion may have a limited effect as, in staff's experience, preparers are

unlikely to refer to the Basis for Conclusions for additional support and explanation. Further, judgement would be required about whether/when disclosures in addition to those required by AASB 1054 should be provided.

- 25 On balance, if the Board wish to further continue with the project, staff recommend that the Board proceed with Option 2a, i.e. not to proceed with amending the current disclosure requirements in AASB 1054. Instead, staff will look at developing staff-level paper to provide practical examples, as an educative avenue, to provide preparers on what additional disclosures may be useful to users. While there was some feedback from stakeholders that staff-level guidance may not be relied upon by preparers, however staff think this option would not impose any additional cost to preparers and one accounting professional body supported the development of education material to address the Agenda Consultation feedback.

**Question 2 to Board members:**

If the Board wishes to continue with the project, do the Board members agree with the staff recommendation in paragraph 25 to proceed with Option 2a, that is:

- (a) not to make any amendments to the existing accounting standards; and
- (b) staff will start developing a staff-level paper providing practical examples to preparers on the additional franking credit disclosure that may be considered useful to users.

If not, what do Board members suggest?

**Next steps of the project**

- 26 If the Board agrees with the staff recommendation in paragraph 19 above, then the project will be closed and removed from the AASB Work Program. To formally close the project, the Board could explain the reasons for closing the project by:
- (a) documenting them in the Action Alert and minutes of this meeting; or
  - (b) issuing a Board Agenda Decision (sometimes called “items not taken onto the agenda” or “agenda rejection statement”) providing the Board’s reasons for rejecting the issue. Board Agenda Decisions are generally prepared where there may be mixed views from stakeholders on an issue, and the Board, after consideration, decides not to add or remove the issue from the agenda, and it is decided that an Interpretation will not be issued.
- 27 Staff consider that documenting the reasons for rejecting the introduction of additional disclosures for franking credits in the Action Alert and minutes of this meeting would be sufficient given the majority of the limited targeted feedback consider the current disclosures adequate.

**Question 3 to Board members:**

Do Board members agree with the staff recommendation in paragraph 27 to document its reasons for closing the project in the Action Alert and meeting minutes?

If not, what do Board members suggest?

## Appendix A – Detailed summary of feedback from limited target outreach

- 1 As noted in paragraph 13, staff have conducted further limited targeted outreach with various stakeholders, including users, preparers and representatives of professional accounting bodies. Stakeholders were asked for their views on the following matters:
  - (a) What disclosures would be useful to users of franking credits?
    - (i) Two users have mixed views on what disclosures would be useful, but they suggested additional disclosures would be of limited use. In particular:
      - (A) User A, who invests mainly in Australian listed equities, does not consider additional disclosures necessary as they monitor franking account balances from year to year rather than the movements during the year. They suggest assumptions can be made to determine the impact on franking credits from dividends declared but not yet recognised if the dividends are fully franked, so there is no need to provide additional disclosure. Whilst an increase in disclosures in the financial statements means an increase in information, User A suggests that additional disclosures may be useful only where there are large differences in balances from year to year, and in their view, additional franking credit disclosures are not of key importance; and
      - (B) Conversely, User B, who invests in Australian and multinational listed equities, initially considered that additional disclosures are useful to investors to see how the entity has derived and utilised their franking credits, given that they are not recognised on the balance sheet. User B noted that where multinational groups exist, it is difficult to determine from the financial statements the amount of Australian tax paid to understand the impact on the franking credit account balance unless the tax transparency report or similar is considered. However, User B considers the legislative amendments concerning off-market share buybacks (see paragraphs 8 – 12 above) would enable an investor to determine the impact of the franking account because no part of off-market share buyback proceeds can be taken as dividends. In their view, this provides greater transparency about the impact of off-market share buybacks on the franking account. Finally, User B also noted that for dual-listed entities, it might be difficult to determine the franking credit balance available for use for shareholders because there can be different classes of share capital having different dividend rights, which can add to the complexity. However, they noted limited instances where this is an issue.
    - (ii) Disclosure Initiatives PAP members suggested there is insufficient evidence to warrant standard-setting. In particular:
      - (A) whilst disclosing the movements of franking debits/credits during the reporting period would not be overly burdensome as the information is already available because it is used to derive the closing franking credit balance, Disclosure Initiatives PAP members did not consider the information would provide additional value to users. One Disclosure Initiatives PAP member observed that in their experience, franking credits is not something that is raised as an issue by audit teams, which suggests that it is not a discussion point with preparers; and
      - (B) one PAP member suggested that if an entity's franking account is in deficit at a point in time and it was an unusual event that caused the deficit in the franking credit, it may be useful for users if the entity disclosed specific information.

- (iii) the professional accounting bodies have not received any feedback from members expressing concerns about the existing disclosure requirements.<sup>5</sup> When asked about whether the information disclosed at the tax consolidated group level was useful to financial statement users, one professional accounting body considered that there might be merit in providing further disclosures (such as tax paid amongst the group members and the impact it has on the franking credit balance of the tax consolidated group) given the franking credit balance represents the single balance for the tax consolidated group. In their view, a reconciliation of the movement of how the franking credit balance available for subsequent reporting periods was derived based on the activities of the group members, including the impact of receipt of the R&D tax offset, may be useful in that regard. However, they emphasised that information provided in general purpose financial statements should be useful to a broad range of users and that there is a need to consider the prevalence of any possible issues to determine whether they warrant any changes to the existing requirements.
  - (iv) A preparer considers the consolidated financial statements sufficient to meet their needs, given a tax consolidated group is often formed in which one single franking credit account is maintained for the group. As such, the franking credit balance disclosed in the consolidated financial statement does not change the fact that these franking credits would be available to shareholders in subsequent reporting periods.
  - (v) A professional services firm considers that it would be useful for users to obtain more information about the franking credits available for distribution, given it is an area of political debate and can attract media attention. They have developed better practice disclosure guidance showing the opening franking credit balance at the start of the reporting period, adjusted by movements during the reporting period and the impact on future franking credits (e.g. the impact of R&D tax offsets). They consider the additional disclosures useful to users of the financial statements as they would communicate the entity's governance and management policy for franking credits. In their view, users are looking at the franking credits that can be distributed or 'locked up' to shareholders. As such, they question whether the current disclosure requirements to only disclose the franking credits balance meet the objective of providing useful information to users. However, they suggest that if users do not consider this information to be useful and there is no demand for it, there is no reason to amend the requirements of AASB 1054.
- (b) Why do some entities disclose more information about franking credits than what is currently required by the Standard?
- (i) Disclosure Initiatives PAP members suggested that entities that provide additional disclosures of the movements of franking credits/debits during the year voluntarily may do so because it is their view of how the existing disclosure requirements should be applied rather than them providing additional disclosures for specific reasons.
  - (ii) While they are unsure of the reasons, the professional services firm considers there is a lot of diversity in how entities calculate the amount of franking credit disclosed and that there are inconsistencies in the disclosures too. They noted that in most cases, entities would only disclose information that complies with the minimum requirements in the accounting standards.

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5 CPA Australia's written submission on ITC 46 noted that they conducted a survey with members and the results of the survey did not indicate any support for further work to be conducted on franking credit disclosure requirements. As part of this outreach, CPA Australia re-confirmed this view.



- (c) Are there any significant barriers to disclosing the information in paragraph 14 of AASB 1054?
- (i) A preparer considers any additional disclosures would add to the cost of preparing financial statements, with entities already subject to many other disclosures, such as Environmental, Social, and Governance (ESG) disclosures.
  - (ii) One Disclosure Initiatives PAP member highlighted that a possible barrier to disclosing additional information is that the disclosure of tax paid, which impacts franking credits, is a narrow subset of the tax paid across the group and disclosing that information could be misleading or provide a narrow view of the tax contribution across the group. They also suggested it could be challenging to disclose the movements of the franking credits/debits of tax paid across groups.
  - (iii) In general, Disclosure Initiatives PAP members consider that any additional disclosures would add to the cost of preparation, even if only in a small way and would increase clutter in the financial statements.
  - (iv) The professional services firm is unaware of any barriers to disclosing the information. In their view, the information is already available to derive the franking credit balance, and they consider that if the information is material, especially if the entity has a franking credits distribution policy, then the information should already be disclosed.
- (d) Are you aware of any trans-Tasman reasons why similar disclosures in paragraph 14 of AASB 1054 should be required for New Zealand?
- (i) One user and the professional services firm did not indicate any trans-Tasman reasons other than if additional disclosures are required in the Australian Accounting Standards, similar disclosures should also be considered for New Zealand because of the trans-Tasman harmonisation policy in standard-setting; and
  - (ii) Disclosure Initiatives PAP members were not aware of any specific trans-Tasman need for additional disclosures by New Zealand entities. They suggested the concerns in Australia appear to be a jurisdictional issue.
- (e) Do you think staff-level guidance should be developed to help preparers consider when and what additional disclosures would be useful to users?
- (i) Disclosure Initiatives PAP members did not consider staff-level guidance helpful because entities would apply the requirements of Australian Accounting Standards rather than referring to the staff-level guidance. They also consider that unless there is more research and outreach to understand the pervasiveness of the issue as to why further franking credit disclosures should be required, they do not consider any amendments to Australian Accounting Standards should be made.
  - (ii) Like the feedback from Disclosure Initiatives PAP members, the professional services firm did not consider staff-level guidance useful since preparers rarely apply guidance unless it is mandated. However, they suggested it may be helpful if the objective/rationale of why franking credit disclosures are required in the financial statements was explained in the Basis for Conclusions.
  - (iii) However, one professional accounting body considered that staff-level guidance might address the initial concerns raised by stakeholders from the Agenda Consultation.

## Appendix B: Further review of financial statements

- 1 As noted in paragraph 15, in addition to the limited review of financial statements discussed with the Board in March 2023 and literature review,<sup>6</sup> staff expanded the sample of financial statements of listed entities in Australia it reviewed to better understand the disclosures made by entities in their financial statements relating to franking credits. Staff have presented the initial observations and findings in Table 1 below. Staff expect to conduct further analysis, such as industry effects, and is expected to publish further research findings in the future.
- 2 In reviewing an additional 110 sets of financial statements, staff noted that 25 entities did not disclose any franking credit balance because they were a foreign listed entity or paid unfranked dividends. Of the remaining 85 entities, staff make the following observations:

*Table 1 Staff observations from the review of financial statements of listed companies*

Disclosures	Number of entities	Required by AASB 1054?
Australian franking credit balance available for use in subsequent periods	85	Yes
Disclosure at tax consolidated group level only	81	
Disclosure at the consolidated group level (no information if and whether disclosures relate to tax consolidated group) only	4	
New Zealand franking credit balance available for use in subsequent reporting periods	8	
Reconciliation of opening and closing balance of franking account adjusted by imputation debits/credits	12	No
Impact of franking debits arising from declared dividends not yet recognised as a liability in the financial statements	20	No
Potential impact on future franking credits from the receipt of the R&D tax offset	0	No

- 3 Based on the observations above:
  - (a) while all entities disclosed franking credit balances available for use in subsequent reporting periods as per AASB 1054, there are some inconsistencies in the level of disclosures made by entities;
  - (b) Only some entities have disclosed the impact of franking debits for dividends declared but not yet recognised as a liability in the financial statements; and
  - (c) 14 entities disclosed R&D refundable tax offset in their profit or loss statement, but no further disclosures were made, including the potential impact on future franking credits from the receipt of R&D refundable tax offset.

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<sup>6</sup> Refer to Agenda Paper [7.1](#) for findings from the initial limited review of financial statements and Agenda Paper [7.2](#) for the literature review on franking credit disclosures.