

Basis for Conclusions on AASB 2020-2

This Basis for Conclusions accompanies, but is not part of, AASB 1057. The Basis for Conclusions was originally published with AASB 2020-2 Amendments to Australian Accounting Standards – Removal of Special Purpose Financial Statements for Certain For-Profit Private Sector Entities.

Introduction

- BC1 This Basis for Conclusions summarises the Australian Accounting Standards Board’s considerations in reaching the conclusions in AASB 2020-2. It sets out the reasons why the Board developed the Standard, the approach taken to developing the Standard, and the bases for key decisions made. In making decisions, individual Board members gave greater weight to some factors than to others.
- BC2 For more than a decade the Board has been undertaking work aimed at addressing the problems that arise from entities being allowed to self-assess whether to prepare special purpose financial statements (SPFS) or general purpose financial statements (GPFS) when they are required to comply with Australian Accounting Standards (AAS) (see paragraphs BC10-BC13 for details). As is evident from empirical research and feedback from stakeholders (see paragraphs BC18-BC41), there is concern that SPFS lack consistency, comparability transparency and enforceability. The Board’s research has identified that there are users of financial statements that are publicly lodged with the Australian Securities and Investments Commission (ASIC), and the Board has been informed by those users that comparability, transparency, comprehensibility and consistency are what is most important to them when reading financial statements. For example comparability of recognition and measurement (R&M) requirements in AAS was rated 88% in importance to primary users¹ and 100% in importance to other users. They also expressed concern that key information is omitted from SPFSs (see paragraphs BC37-BC41).
- BC3 Regulatory scrutiny of SPFS has also increased, for example in the Parliamentary Joint Committee on Corporations and Financial Services inquiry into the regulation of auditing, the Senate Economics References Committee Report on Tax Avoidance, and the requirement for all Significant Global Entities (SGEs) to lodge GPFS with the Australian Taxation Office (ATO) (see paragraph BC32(a)).
- BC4 Within the context of the AASB’s International Financial Reporting Standards (IFRS Standards) adoption policy, the issue of a revised *Conceptual Framework for Financial Reporting* (March 2018) (referred to throughout this Basis for Conclusions as ‘the RCF’) by the International Accounting Standards Board (IASB) provides a timely opportunity to once again consider how best to improve the quality of financial reporting in Australia by solving the so-called ‘SPFS problem’ via a broader project aimed at removing the ability of certain for-profit private sector entities to prepare SPFS when they are required to prepare financial statements that comply with AAS.² The Board is progressing with this project by considering each sector separately, in the first instance for-profit private sector entities required to comply with AAS (being the subject of this Standard – as explained in paragraphs BC68-BC93).
- BC5 The Board noted the Australian Government Treasury change in thresholds for large proprietary companies which defined the entities that are required to lodge their financial statements with ASIC (unless exempted by ASIC) in April 2019. Treasury doubled the thresholds used for determining what constitutes a large proprietary company. As set out in the Explanatory Memorandum accompanying the increase, the revised thresholds were set with the expectation of capturing entities with economic significance and noted the larger the entity, the more likely it is that there are GPFS users. These are key criteria in the AASB’s Statement of Accounting Concepts SAC 1 *Definition of the Reporting Entity* for determining whether or not an entity is a reporting entity.
- BC6 As noted in paragraph BC4, the solution to the SPFS problem provided by this Standard is to remove the ability of certain for-profit private sector entities to self-assess their financial reporting requirements and prepare SPFS when they are required to prepare financial statements that comply with AAS.³ This will

1 AASB Staff Paper *Enhancing the revised Conceptual Framework and replacing Special Purpose Financial Statements – For-profit User and Preparer Survey Results* (December 2018). ‘Primary users’ refers to users that meet the definition of primary users in AASB Practice Statement 2 *Making Materiality Judgements* (ie investors (and analysts), lenders and other creditors) and all other respondents are referred to as ‘other users’.

2 In this Basis for Conclusions, the reference to AAS in this phrase also includes accounting standards as referred to in legislation (this means legislation of a government in Australia).

3 The Australian concept of the reporting entity would be retained for entities outside the scope of this Standard (and AASB 2019-1 *Amendments to Australian Accounting Standards – References to the Conceptual Framework*). The Board will consider the financial reporting framework for these entities in the future.

improve the consistency, comparability, transparency and enforceability of financial statements, thus meeting the needs of users who are accessing these financial statements on a public register or otherwise. The Board acknowledged that these changes could not be implemented in isolation, as merely removing the ability of certain for-profit private sector entities to prepare SPFS with no other mitigating action would result in increased reporting requirements for some entities if they were required to transition from SPFS to some form of Tier 2⁴ GPFS framework. Therefore, this Standard is made in conjunction with AASB 1060 *General Purpose Financial Statements – Simplified Disclosures for For-Profit and Not-for-Profit Tier 2 Entities* (March 2020), which provides simplified Tier 2 GPFS reporting requirements for those for-profit entities that are prohibited from preparing SPFS as a result of this Standard.

BC7 The Board also decided to provide transitional relief in addition to that which is currently available via AASB 1 *First-time Adoption of Australian Accounting Standards* and AASB 1053 (see paragraphs BC122-BC135), for entities that choose to early adopt the requirements in this Standard.

BC8 The remainder of this Basis for Conclusions provides further background and explanation about the reasons for developing this Standard, including:

- (a) previous Board decisions in relation to earlier stages of the process (to provide a historical perspective, see for example paragraphs BC10-BC13);
- (b) the basis for the key decisions made, including:
 - (i) the types of entities affected by the Standard and the technical requirements (including, for context, a summary of the basis for the revised Tier 2 GPFS framework (see paragraphs BC95-BC121), which is detailed in AASB 1060);
 - (ii) transitional provisions (see paragraphs BC122-BC135); and
 - (iii) the effective date (see paragraphs BC145-BC150);
- (c) how the Board applied *The AASB's For-Profit Entity Standard-Setting Framework* when developing this Standard (see paragraphs BC154-BC156); and
- (d) the amendments necessary to implement the requirements outlined in this Standard (see paragraphs BC157-BC162).

Reasons for developing this Standard

BC9 This Standard includes:

- (a) amendments to AAS to remove the ability of certain for-profit private sector entities to prepare SPFS by removing the 'reporting entity' concept for those entities required by:
 - (i) legislation to prepare financial statements that comply with either AAS or accounting standards; or
 - (ii) their constituting document (or another document) to prepare financial statements that comply with AAS, provided the relevant document was created or amended on or after 1 July 2021; and
- (b) to provide relief from restating comparative information for entities transitioning to full R&M requirements, if the entity chooses to early adopt the requirements (see paragraphs BC122-BC135).

Board deliberations prior to the AASB's Invitation to Comment ITC 39 Consultation Paper – Applying the IASB's Revised Conceptual Framework and Solving the Reporting Entity and Special Purpose Financial Statement Problems

BC10 As noted in paragraph BC2, the Board had been aware of the problems with the application of the reporting entity concept and the consequential preparation and public lodgement of SPFS for some time. Indeed, the Board has previously publicly contemplated the removal of the ability of certain entities to self-assess and prepare SPFS when required to comply with AAS. For example:

4 Currently, Australian Accounting Standards consist of two Tiers of reporting requirements for preparing general purpose financial statements:

(a) Tier 1: Australian Accounting Standards; and

(b) Tier 2: Australian Accounting Standards – Reduced Disclosure Requirements.

(See paragraph 7 of AASB 1053 *Application of Tiers of Australian Accounting Standards*.) However, the Board is considering what the most appropriate Tier 2 GPFS framework may be – see paragraph BC95.

- (a) AASB Invitation to Comment ITC 12 *Request for Comment on a Proposed Revised Differential Reporting Regime for Australia and IASB Exposure Draft of A Proposed IFRS for Small and Medium-sized Entities* (May 2007) noted the concept of SPFS might have been misunderstood in some cases. To remove the ambiguity concerning the reporting entity concept, ITC 12 sought comment on whether all financial statements available on a public register should be required to be GPFS; and
- (b) AASB Consultation Paper (CP) *Differential Financial Reporting – Reducing Disclosure Requirements* (February 2010) and ED 192 *Revised Differential Reporting Framework* (February 2010), issued in tandem, followed ITC 12 and reaffirmed the Board’s view that the reporting entity concept which allows the public lodgement of SPFS should be removed. The Board elaborated on the issues surrounding SPFS in the CP, including noting that:
- (i) entities are asserted to be ‘abusing’ the reporting entity concept by claiming to be non-reporting entities and preparing SPFS when they should be preparing GPFS. An impetus for this is the desire to avoid the cost and exposure that would come from applying full IFRS Standards as adopted in Australia;
 - (ii) many of the regulators requiring the preparation and lodgement of financial statements may not have given sufficient consideration to the nature of the information they require and the needs of any external users of that information; and
 - (iii) preparation of SPFS by entities that are required by law to prepare financial statements in accordance with accounting standards and be lodged on a public register contradicts the legislation’s objective of providing information to a wide range of users who are not in a position to command specific information to satisfy their needs.
- BC11 However, the Board noted mixed feedback from constituents in response to these due process documents in regard to removing the ability of certain entities to self-assess and prepare SPFS when required to comply with AAS, which suggested that (as noted in paragraphs BC10-BC17 of the Basis for Conclusions to AASB 1053):
- (a) on the one hand, the reporting entity concept involves a high degree of subjectivity, is not universally understood and hence does not provide the intended result, nor does it provide a robust criterion for differential reporting purposes; and
 - (b) on the other hand, the reporting entity concept works well, and there appeared to be no evidence to the contrary, particularly from users.
- BC12 Consequently, in 2010, the Board decided to issue AASB 1053 and introduce a second tier of GPFS reporting, being Tier 2: Australian Accounting Standards – Reduced Disclosure Requirements (RDR), but delay the phase of the project addressing the reporting entity concept and the removal of SPFS until further research had been undertaken. That research would consider in more detail the impact of removing the ability of certain entities to self-assess and prepare SPFS when required to comply with AAS. The RDR requirements were designed to substantially reduce the disclosure burden when compared to the full disclosure requirements of AAS.
- BC13 Prompted by the views noted in paragraphs BC10-BC11, the Board initiated research projects, the findings of which are discussed in paragraphs BC18-BC25.

The issues with SPFS

- BC14 Australia is the only jurisdiction with a reporting entity concept that effectively permits entities to self-assess what type of financial reporting they do, when they are required by legislation or otherwise (such as by a constituting document) to prepare financial statements in accordance with AAS.⁵ Therefore, unlike other jurisdictions, in Australia two similar entities might prepare very different sets of financial statements, one preparing GPFS using a robust and consistent framework, and the other preparing SPFS with self-selected requirements. This reduces comparability for entities of similar economic circumstances and undermines the fundamental principles of trust and transparency.
- BC15 An analysis of the reporting practices of specified for-profit entities lodging financial statements with ASIC estimated that 71% of those entities prepared and publicly lodged SPFS in 2018.⁶ This same research

⁵ See AASB Research Report No. 7 *Financial Reporting Requirements Applicable to For-Profit Private Sector Companies* (May 2018) for a comparison of international financial reporting frameworks.

⁶ AASB Research Report 12 *Financial Reporting Practices of For-Profit Entities Lodging Special Purpose Financial Statements* (August 2019). Research Report 12 examines the financial reporting practices of for-profit entities, including large proprietary companies, small foreign-controlled proprietary companies, for-profit unlisted public companies and other small proprietary companies, lodging financial

estimated that 24% of these entities lodging SPFS either did not comply with the R&M requirements in AAS or did not make clear whether they did (refer to paragraphs BC20-BC22). Therefore, only 76% of the SPFS voluntarily complied with ASIC Regulatory Guide 85 *Reporting requirements for non-reporting entities* (RG 85) recommended guidance to apply all the R&M requirements in AAS (refer BC28-BC29). This suggested a strong need to improve the consistency, comparability, transparency and enforceability of financial reporting, which would also increase the usefulness and credibility of financial reporting in Australia.

- BC16 It is incumbent on the AASB to resolve the SPFS problem as, legislatively, the AASB must ensure there are appropriate accounting standards for each type of entity that must comply with accounting standards (*Australian Securities and Investments Commission Act 2001* s229(2)(c)) and facilitate comparability (s224). The ability to make the self-assessment that gives rise to the SPFS problem sits within AAS. Prior to issuing this Standard, the only AAS that explicitly apply to SPFS of for-profit private sector entities focussed on presentation and disclosure (and not R&M). As such, it was the directors' choice of accounting policies that provides the financial reporting framework. As a consequence, other regulators have attempted to fill the gap by providing additional guidance in relation to R&M. Despite this, discussions with users, including lenders and insolvency practitioners, indicated their needs for information about liquidity, solvency, cash flows, commitments and contingencies and related party disclosures were not being met in most SPFS and they were not all aware of the extent of the R&M issues. This indicated a need for minimum R&M requirements to be specified in AAS.
- BC17 Therefore, as noted in paragraph BC6, the Board decided to play its role in improving the consistency, comparability, transparency and enforceability of financial statements to meet user needs, whilst mitigating, where appropriate, the increased reporting burden for entities that would no longer be able to prepare SPFS and would instead be required to prepare GPFS in accordance with AAS.

Results of research into the reporting practices of specified for-profit entities lodging financial statements with ASIC

- BC18 The Board initiated academic research that resulted in the publication of AASB Research Report No. 1 *Application of the Reporting Entity Concept and Lodgement of Special Purpose Financial Statements* (June 2014). Research Report No. 1 analysed the application of the reporting entity concept and the adoption of special purpose financial reporting, particularly by entities lodging financial statements with ASIC and with state-based regulators of Australia's three most populous states, namely, Consumer Affairs Victoria, NSW Fair Trading and Queensland Office of Fair Trading. Research Report No. 1 showed that, based on lodgements as at 30 July 2011, approximately 66% of specified for-profit entities⁷ lodged SPFS with ASIC. The findings of Research Report No. 1 indicated to the Board that:
- (a) in light of the high incidence of SPFS being lodged with ASIC, there is doubt as to whether the reporting entity concept is being applied as intended by SAC 1;
 - (b) the reporting entity concept appears too subjective for regulators to enforce effectively and accordingly does not create a level playing field; and
 - (c) 63% of SPFS lodged with ASIC stated compliance with the R&M requirements of applicable AAS, suggesting that R&M was not always complied with despite regulatory guidance suggesting this should be the case (see paragraphs BC28-BC29).
- BC19 The Board also initiated subsequent research⁸ to understand how the reporting practices of for-profit entities lodging SPFS with ASIC may have changed since the introduction of the RDR reporting framework in 2010. An analysis of financial reports of the specified for-profit entities lodging financial statements with ASIC in 2018 confirmed that 71% of these entities were still lodging SPFS with ASIC, 13% lodged Tier 2 GPFS and 16% lodged Tier 1 GPFS. The Board also noted that those entities preparing Tier 2 GPFS (RDR) appear to have moved from Tier 1 GPFS to RDR and not from SPFS to RDR.
- BC20 In respect of compliance with the R&M requirements in AAS, the Board noted the more detailed findings of Research Report 12, which estimates that 76% of specified for-profit entities preparing and lodging SPFS with ASIC complied with the R&M requirements in AAS. In particular:
- (a) 66% explicitly stated that they followed the R&M requirements in AAS (compared with the 63% found in Research Report No.1 – see paragraph BC18(c)); and

statements with ASIC. The findings of Research Report 12 considered in this Standard are limited to those that relate to entities within the scope of the proposals in this Standard, that is large proprietary companies, small foreign-controlled proprietary companies and for-profit unlisted public companies limited by guarantee. These entities are referred to herein as the 'specified for-profit entities'.

⁷ Specified for-profit entities are large proprietary companies, small foreign-controlled companies and unlisted public companies.

⁸ Research Report No 12

- (b) 10% were assessed to have complied with the R&M requirements in AAS based on a qualitative review of the accounting policies, despite the absence of an explicit statement to that effect.
- BC21 For the remaining 24%:
- (a) 10% did not comply with the R&M requirements in AAS (of which only 0.5% clearly stated so); and
- (b) the extent of compliance (or otherwise) with the R&M requirements in AAS of the remaining 14% was unclear.
- BC22 In addition to it being difficult for the researchers to understand the extent of alignment between an entity’s accounting policies and the R&M requirements in AAS, the Board noted the same difficulties faced by financial statement users. This leads to fundamental issues with the transparency of information available to users of publicly lodged SPFS, consistency and the comparability of SPFS with other SPFS and GPFS. As noted in paragraph BC15, only 76% of entities preparing SPFS are voluntarily complying with RG 85 recommendations, suggesting that mandatory requirements were needed to improve the quality of financial reporting.
- BC23 In response, in July 2019, the Board issued ED 293 *Amendments to Australian Accounting Standards – Disclosure in Special Purpose Financial Statements of Compliance with Recognition and Measurement Requirements* which proposed, as an interim measure, amendments to AAS to require entities preparing SPFS to make an explicit statement as to whether or not the accounting policies applied in the SPFS comply with all the R&M requirements in AAS. The Board acknowledged that disclosure of this information was not sufficient to address the problems with publicly lodged SPFS, however the interim measure was aimed at providing some measure of transparency to users until the resolution of the SPFS problem, in the short to medium term for for-profit private sector entities and in the longer term for not-for-profit entities. After considering feedback from respondents on ED 293, the Board decided to limit the scope of the proposals to only not-for-profit (NFP) entities as respondents “were particularly concerned about the costs of the ED 293 proposals exceeding any benefits for for-profit private sector entities given the ED 293 proposals were intended to be only a short-term measure for these entities. This is because the broader project proposing to remove the ability for certain for-profit private sector entities to prepare special purpose financial statements when they are required to comply with Australian Accounting Standards is expected to be completed by 30 June 2020.”⁹
- BC24 In light of the effective date of this Standard being one year later than that proposed in ED 297, and also noting that there is likely to be a number of entities that will continue to be able to prepare SPFS (e.g. due to the exemption provided to entities with a non-legislative requirement to prepare financial statements that comply with AAS (refer paragraphs BC90-BC92)), the Board reconsidered this decision. The Board was concerned about the lack of transparency in the SPFS that continues to refer to AAS and therefore decided that these entities should also be required to disclose a statement of the entity’s compliance, or otherwise, with the R&M requirements in AAS (including requirements set out in AASB 10 *Consolidated Financial Statements* or AASB 128 *Investments in Associates and Joint Ventures*). The Board thought this was particularly important for securitisation trusts given they are listed on the ASX and other securities exchanges. The Board intends to communicate with the ASX and industry bodies to ensure they understand the implications of having SPFS on their public registers.
- BC25 In addition to the research described above, the Board also conducted significant targeted outreach prior to issuing the standard, where over 250 formal meetings were held with key stakeholders, including State, Territory and Commonwealth regulators, audit offices, large and small accounting firms, the Australian Securities Exchange (ASX), ASIC, the Australian Charities and Not-for-profits Commission (ACNC), credit rating agencies, professional bodies and users of financial statements (including analysts, investors and creditors) to help identify how implementing the RCF and removing the ability of certain for-profit private sector entities to prepare SPFS when they are required to prepare financial statements that comply with AAS, would impact Australian entities. The Board considered the feedback received, when developing the Standard.

Regulatory views and developments on SPFS

- BC26 The Board noted feedback from some stakeholders suggesting that it was the role of other regulators (rather than the AASB) to address any potential issues with SPFS. In particular, some stakeholders argued:
- (a) other regulators should specify or determine whether an entity is required to lodge GPFS,¹⁰ and

⁹ AASB 2019-4, paragraph BC43 and BC 44. At the time of making that decision, the effective date of this Standard was proposed as 1 July 2020.

¹⁰ This is consistent with the view that the AASB’s role and expertise is to determine the appropriate accounting framework and accounting standards that should apply where legislation, regulation or other authority requires the preparation of financial statements that comply with AAS.

- (b) if the reporting entity concept is not being applied correctly, this is a matter of enforcement for the appropriate regulator rather than a matter of standard-setting.
- BC27 Thus, the Board has paid particular regard to the views of other regulators, and noted the increasing regulatory interest in and concern about the use of SPFS to assess what role the Board should play in addressing the issues.
- BC28 The Board noted ASIC issued RG 85 in July 2005, which states “ASIC believes that non-reporting entities, which are required to prepare financial reports in accordance with Chapter 2M of the *Corporations Act 2001* (Act), should comply with the recognition and measurement requirements of accounting standards”¹¹ “hence, the recognition and measurement requirements of accounting standards must also be applied in order to determine the financial position and profit or loss of any entity preparing financial reports in accordance with the Act”.¹²
- BC29 RG 85 further states that “Directors of non-reporting entities must also consider carefully the need to make disclosures which are not directly prescribed by accounting standards, but which may be necessary in order for the financial statements to give a true and fair view”,¹³ and that those standards that must be applied by entities reporting under the *Corporations Act 2001* are AASB 101 *Presentation of Financial Statements*, AASB 107 *Statement of Cash Flows*, AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*, AASB 1048 *Interpretation of Standards* and AASB 1054 *Australian Additional Disclosures*. However, as noted in paragraph BC21, research into the extent of compliance with the R&M requirements in AAS by specified for-profit entities lodging SPFS with ASIC shows that at least 10% and potentially up to 24% of them do not appear to have followed the guidance outlined in RG 85. ASIC has also indicated it finds the judgements required regarding the application of the reporting entity concept in SAC 1 to be unenforceable.
- BC30 The appropriateness of SPFS have also been called into question in a number of other regulatory matters. For example, as part of the Senate Economics References Committee Report on Tax Avoidance, the Board’s Chair was asked to explain to the Committee the reporting entity concept and its role in facilitating the preparation of SPFS. The Board noted the subsequent Report, *Corporate tax avoidance Part III, Much heat, little light so far* (May 2018), outlined strong concern that multinationals operating within Australia are avoiding public scrutiny through the preparation of SPFS, which are not required to disclose corporate tax and related party transactions, and also noted the Board’s role in facilitating the public lodgement of SPFS through its reporting entity concept. The Report recommended the Government require all companies, trusts and other financial entities with income above a certain amount to lodge GPFs with ASIC. These comments, albeit with a focus on tax, reinforce the view that a problem exists in relation to the way in which the reporting entity concept is applied, as well as the information provided through the public lodgement of SPFS.
- BC31 The Board also reflected on the recommendations in the *Final Report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry* (February 2019), particularly the recommendation to remove special rules and exceptions that can create regulatory complexities. The Final Report indicated that exceptions departing from underlying principles have consequences often resulting in exploitation and that exceptions act as barriers to the simplification of regulation. The Board further considered the theme of enforceability within the Final Report, noting in particular that the subjectivity inherent in the current Australian reporting entity concept may not provide regulators with an objective basis on which to enforce financial reporting obligations.
- BC32 In addition, other regulatory developments indicated an increased need for entities to prepare GPFs instead of SPFS where they are required to prepare financial statements that comply with AAS, for example:
- (a) the requirement for SGEs¹⁴ to lodge GPFs with the ATO, which would subsequently be provided to ASIC¹⁵ (December 2015);
 - (b) questions to the Board’s Chair and the Financial Reporting Council’s (FRC) Chair on the AASB’s and FRC’s approaches to resolving the shortcomings of SPFS by the Parliamentary Joint Committee on Corporations and Financial Services as part of its inquiry into the oversight of ASIC and the Takeovers Panel (February 2018);
 - (c) the Senate Economics References Committee report *Financial and tax practices of for-profit aged care providers* (November 2018), which supported the Board’s intent to remove the ability of

11 Paragraph 2 of RG 85.

12 Paragraph 2.5 of RG 85.

13 Paragraph 2.9 of RG 85.

14 An entity is an SGE for a period if it is one of the following (as defined in Subdivision 960-U of the *Income Tax Assessment Act 1997*):

(a) a ‘global parent entity’ whose ‘annual global income’ is A\$1 billion or more; or

(b) a member of a group of entities consolidated (for accounting purposes) where the global parent entity has an annual global income of A\$1 billion or more.

15 Introduced by *Tax Laws Amendment (Combating Multinational Tax Avoidance) Act 2015*.

certain entities to prepare SPFS where they are required to prepare financial statements that comply with AAS; and

- (d) further questions to the Board's Chair on the status of the AASB's work to remove SPFS from the Parliamentary Joint Committee on Corporations and Financial Services as part of its inquiry into the regulation of auditing in Australia (November 2019). SPFS were criticised both by members of that committee as well as in several submissions from the public in relation to that inquiry.
- BC33 In light of the regulatory developments and public enquiries noted above, the Board also observed the increasing public interest and media scrutiny of the transparency and accountability of publicly available financial statements, both generally and specifically in relation to the reporting entity concept and its facilitation of publicly lodged SPFS.
- BC34 In proposing to remove the ability of certain for-profit private sector entities to prepare SPFS when they are required to prepare financial statements that comply with AAS, the Board received support from other regulators, particularly ASIC and the ATO, which conveyed the following views to the Board:
- (a) ASIC fully supports the consultation to remove SPFS for entities regulated by ASIC and remove the subjective 'reporting entity' test under SAC 1, facilitating a comparable, consistent and transparent framework for the preparation of financial statements in Australia; and
- (b) the ATO is supportive of the AASB's proposed approach to consulting on a series of principles or concepts for enhancing the transparency of entities currently preparing SPFS as part of adopting the RCF issued by the IASB and for inclusion in AAS by 2021. The ATO also noted its further support of the AASB's recommendations surrounding the timing and application of the new Tier 2 disclosures requirements during the Board's Exposure Draft process.
- BC35 The Board provided input to Treasury in considering legislative requirements that specify which types of for-profit entities should be required to prepare and, in most cases, publicly lodge financial statements with ASIC. In April 2019, Treasury announced changes to the *Corporations Regulations 2001*¹⁶ to increase (double) the thresholds used for determining whether an entity is a large proprietary company, with companies falling below the thresholds not being required to prepare or publicly lodge financial reports with ASIC. As part of the changes, the Board suggested Treasury provide objective criteria based on economic significance for determining the thresholds and noted the commentary in Treasury's Explanatory Statement, which is consistent with the Board's decision to remove the ability of certain entities to prepare SPFS when they are required to prepare financial statements that comply with AAS. In particular, the Board noted:
- (a) the requirement for large proprietary companies to prepare and in some cases lodge financial reports was first introduced to focus regulation of reporting on the financial affairs of proprietary companies that have a significant economic influence; and
- (b) the financial reports of companies that have economic significance should be publicly available because of their size and potential to affect the community and the economy. The larger the size, the more likely it is that there will exist users dependent on GPFS as a basis for making economic decisions.
- BC36 This clearly indicates the new thresholds which apply from 1 July 2019 were set to reflect the 'economic significance' of the entities captured, which is another key criterion in SAC 1 for deciding whether or not an entity is a reporting entity.

Evidence from stakeholders, including financial report users

- BC37 In addition to the above, the Board noted the general agreement amongst stakeholders that there is an SPFS problem in its outreach both prior and subsequent to the issue of ITC 39. In considering submissions received on ITC 39 the Board noted that of the 33 formal respondents (relevant to this phase of the project), 85% agreed there is a problem with SPFS that needs to be solved, with similar feedback received anecdotally through other outreach activities.
- BC38 As part of the due process, a significant amount of feedback was provided by users of financial statements. Of particular importance is the AASB Staff Paper *Enhancing the revised Conceptual Framework and replacing Special Purpose Financial Statements – For-profit User and Preparer Survey Results* (December 2018), which indicated that, from the perspective of the 37 users (analysts, investors and creditors) that responded:
- (a) there is a problem with SPFS that needs to be addressed – 78% of primary users expressed concern that SPFS do not consistently apply R&M requirements in AAS;

16 Introduced by *Corporations Amendment (Proprietary Company Thresholds) Regulations 2019*.

- (b) 93% of primary users and over 95% of other users said that comparability, transparency, comprehensibility and consistency are all paramount; and
- (c) there is dissatisfaction with SPFS that needs to be addressed, particularly around the lack of related party disclosures, lack of comparability and that the extent to which entities comply with the R&M requirements in AAS is unclear to users.
- BC39 The Board also conducted a range of meetings with users to understand their needs and received six formal submissions on ITC 39 from users of financial statements (out of the 33 responses relevant to this phase of the project). In those formal submissions, the Board noted that all of those respondents:
- (a) noted, or referred to, the lack of comparability, consistency and transparency currently caused by SPFS that needs to be resolved; and
- (b) supported public lodgement of financial statements that comply with all of the R&M requirements in AAS. Consistency, transparency and comparability were noted as important to users in their responses, with one user also noting the importance of consistent financial reporting to facilitate computer-based analysis and use of financial information.
- BC40 In addition to the information in paragraph BC38, the Board also noted other evidence that clearly indicates the existence of users who would benefit from having access to GPFS rather than SPFS. For example:
- (a) over 98,000 copies of financial statements were purchased during the year ending 30 June 2018 from ASIC. Of those financial statements purchased, 80% were of proprietary companies, 16% were of unlisted public companies and 4% were of small foreign-controlled companies;¹⁷
- (b) anecdotally, data aggregators¹⁸ rely on publicly available information to assist their clients with determining the viability, capacity and credit risk associated with a company; and
- (c) as noted in paragraph BC35, Treasury indicated in the Explanatory Statement accompanying the revision of the large proprietary company thresholds its expectation that there are users dependent on the GPFS of large proprietary companies, given their economic significance. Further, that Explanatory Statement noted that average access rates through ASIC of the revised (smaller) population of large proprietary companies was significantly higher (on average 3.6 times per company) than the proprietary companies that would no longer have an obligation to prepare and lodge financial statements with ASIC (on average 1.8 times per company).
- BC41 Despite the relatively lower access rates for small foreign-controlled companies and unlisted public companies noted in paragraph BC40(a), the Board noted its expectation that users of those financial statements would also benefit from having access to GPFS rather than SPFS given that:
- (a) small foreign-controlled companies have been specifically required to lodge financial statements with ASIC¹⁹, and are already provided with significant relief from financial reporting obligations if the company is included in the consolidated financial statements of a registered foreign company that is lodged with ASIC. Additionally, *ASIC Corporations (Foreign-Controlled Company Reports) Instrument 2017/204* provides further relief to small foreign-controlled entities – even if they are not consolidated by a registered foreign company lodging financial statements with ASIC – by requiring them to lodge financial statements with ASIC only if directed to do so by shareholders or ASIC, or if they are part of a large group in Australia. The requirement for small foreign-controlled companies to lodge financial statements where they are part of a large group is designed to prevent foreign-controlled companies disaggregating their Australian activities into smaller companies to avoid financial reporting obligations.²⁰ In light of this Australian public interest context, demonstrated also through the requirements for SGEs to lodge GPFS with the ATO and the strong public interest in seeing no avoidance of tax, there appears to be no justification for small foreign-controlled companies to be relieved from the requirement to prepare GPFS; and

17 Of these 98,000 copies of financial statements, approximately 29,000 were purchased by public users through ASIC connect and not by data aggregators.

18 Data aggregators purchase and analyse data for the purpose of providing informed credit and risk management advice, industry profiling and other analytic products and services.

19 The Explanatory Memorandum to the *Company Law Review Bill 1997* noted that “financial reporting by small proprietary companies which are foreign-controlled should, as far as possible, equate with the reporting requirements of small proprietary companies which are controlled by Australian companies. Accordingly, a small proprietary company will be required to prepare a financial report if the controlling registered foreign company does not prepare and lodge financial statements with the ASC which consolidate the affairs of the small proprietary company for the period in which it was controlled. ... An Australian company which controls a small proprietary company is required to consolidate the small proprietary company in its consolidated financial report if it comes within the scope of *AASB 1024: Consolidated Accounts*. While it would not be appropriate for the Corporations Law to generally require a registered foreign company to prepare consolidated financial statements, that company may consolidate the small proprietary company in financial statements prepared under the law of its jurisdiction of incorporation. If consolidated accounts of this kind are lodged with the ASC in accordance with the requirements in current section 349, the remainder of Chapter 2M will not apply to the small proprietary company.”

20 See the Explanatory Statement to *ASIC Corporations (Foreign-Controlled Company Reports) Instrument 2017/204*.

- (b) unlisted public companies by definition would have at least 50 non-employee shareholders (ie external users) and have the ability to offer shares to the public. As such, the Board noted it would be difficult to justify there being no external users of such entities' financial statements – and therefore GPFS are warranted. In addition, it is possible that some of the 3,102 unlisted public companies²¹ currently lodging financial statements with ASIC may be not-for-profit entities, and as such would not be affected by this Standard.

The RCF

- BC42 The IASB issued the RCF in March 2018. The RCF describes the objective and concepts for general purpose financial reporting under IFRS Standards. Its purpose is to assist standard-setters to develop Standards that are based on consistent concepts, and to help preparers develop consistent accounting policies when no Standard applies to a particular transaction or event, or when a Standard allows a choice of accounting policy.²² It also assists anyone looking to understand and interpret the Standards. However, the RCF's concept of 'reporting entity' is different from the reporting entity concept in SAC 1 and some AAS.²³
- BC43 Making the IASB's RCF applicable in Australia, modified where necessary for public sector and NFP specific issues, is consistent with the FRC's strategic direction to the Board and the Board's strategic objectives. In accordance with those strategies, the Board should:
- (a) maintain compliance with IFRS Standards for publicly accountable entities; and
- (b) use IFRS Standards as a base for determining the reporting requirements for all other entities, modified as appropriate, in accordance with *The AASB's For-Profit Entity Standard-Setting Framework* and *The AASB's Not-for-Profit Entity Standard-Setting Framework*.
- BC44 However, if the AASB's current reporting entity concept were maintained at the same time the RCF is applied, the inconsistency of the Australian reporting entity concept with the RCF could result in confusion, misinterpretation and the incorrect application of AAS and non-compliance with IFRS Standards. The likelihood of inconsistencies would also increase as and when IFRS Standards are amended or revised and more references to the term 'reporting entity' as defined in the RCF are included in IFRS Standards.
- BC45 Implementation of the RCF in Australia is challenging due to the reporting entity concept clash, that is, the reporting entity concept in the RCF determines the boundary of what needs to be reported when an entity is required to report, eg consolidation, and it does not determine who should prepare GPFS, as it is assumed that legislation requiring the preparation of financial statements in accordance with accounting standards is requiring GPFS. In contrast, the current Australian reporting entity concept allows entities to self-assess whether they should prepare:
- (a) GPFS, which requires compliance with all AAS, including recognition, measurement, presentation and disclosure requirements; or
- (b) SPFS, which only requires compliance with a small number of AAS that are more focussed on the presentation of and disclosure in financial statements and don't specify R&M requirements.
- The ability of entities to self-assess their reporting requirements under the Australian reporting entity concept has led to the more fundamental 'SPFS problem'.
- BC46 Further, the SAC 1 reporting entity concept has led to confusion and diversity in practice regarding whether consolidation and equity accounting should be applied in SPFS publicly lodged with ASIC. RG 85 notes that some "companies have failed to prepare consolidated financial statements on the grounds that the parent entity was not a reporting entity"²⁴ and that the "sole determining factor as to whether consolidated financial statements are required is whether the **group** is a reporting entity" (emphasis added).²⁵ The RCF and AASB 10 however, require consolidation if an entity is a parent, with limited exceptions.²⁶
- BC47 This reporting entity clash was addressed in ITC 39, and ITC 39 sought comment on the clash between the reporting entity concepts in the RCF and SAC 1 and the related SPFS problem. The requirements of this Standard have been informed by the Board's research and consultation undertaken prior to and since ITC 39 was issued. The results of that research and consultation, and how it influenced the Board's decisions, are outlined throughout this Basis for Conclusions.

21 Research Report 12

22 The RCF, paragraph SP1.1.

23 The term 'reporting entity' as defined by the RCF is also inconsistent with the definition of reporting entity in AASB 1057 *Application of Australian Accounting Standards*.

24 RG 85, paragraph 5.1.

25 RG 85, paragraph 5.5.

26 Paragraphs 4, Aus4.1, Aus4.2 and 4B of AASB 10 outline the exemptions and exceptions whereby a parent entity need not present consolidated financial statements.

- BC48 To address the reporting entity clash, ITC 39 considered a number of options to apply the RCF (refer to paragraphs BC52-BC57), including considering whether it would be feasible to operate with two conceptual frameworks²⁷ – the RCF for publicly accountable entities and entities that wish to claim IFRS compliance, and the current *Framework for the Preparation and Presentation of Financial Statements* (existing Conceptual Framework) for other entities (which would include maintaining SAC 1, the Australian reporting entity concept and SPFS for all entities not applying the RCF). However, the Board decided that this option was not feasible, as new and revised AAS will be based on the RCF, which includes revised definitions and recognition criteria for assets and liabilities, a new chapter on the reporting entity and a new chapter on measurement. Therefore, if entities continued to apply the existing Conceptual Framework when developing accounting policies or interpreting AAS, they are likely to develop inappropriate accounting policies or incorrectly interpret AAS. This could result in inaccurate and inconsistent financial reporting which would reduce the transparency and comparability for users of financial statements.
- BC49 Updating the existing Conceptual Framework for the changes made via the RCF other than the reporting entity concept was also not feasible given the pervasive use of ‘reporting entity’ throughout the RCF. The Board also considered an option to simply rename the reporting entity concept in SAC 1 to resolve the reporting entity clash.²⁸ The Board however decided that this approach would not meet any of the justifiable circumstances set out in *The AASB’s For-Profit Entity Standard-Setting Framework* for the AASB to have different requirements to IFRS Standards. Further, this would be inconsistent with the AASB’s legislative requirements to ensure there are appropriate accounting standards for each type of entity that must comply with accounting standards and to facilitate consistency, comparability, transparency and enforceability (refer paragraph BC16). This is because such an approach would not resolve the fundamental issues with the public lodgement of SPFS, which is addressed in the next section, or the evident inconsistency in practice and lack of transparency.

Resolving the issues

- BC50 In light of the evidence provided to the Board in paragraphs BC9-BC49, the Board decided to resolve the clash between the reporting entity concepts, as well as to improve the consistency, comparability, transparency and enforceability of the for-profit private sector financial reporting framework, it is necessary to remove the Australian reporting entity concept (by making the consequential amendments to AAS set out in this Standard). This would remove the ability of an entity to self-assess that it is not a ‘reporting entity’ as currently defined in SAC 1, and so prevent it from preparing SPFS if it is required to prepare financial statements that comply with AAS.
- BC51 The Board concluded the removal of the self-assessment of the reporting entity concept and disallowance of the preparation of SPFS for certain for-profit private sector entities would simplify the reporting framework by providing a single set of minimum requirements, facilitating the objective of a consistent, comparable, transparent and enforceable Australian financial reporting framework. In arriving at this solution the Board considered a range of alternatives through ITC 39, as noted in the next section.

ITC 39

Preferred option in ITC 39

- BC52 As noted in paragraph BC47, ITC 39 was a precursor due process document to this Standard. In ITC 39 the Board considered five different options for implementing the RCF in Australia and the benefits and barriers of each option. After considering the comments from respondents on ITC 39, the Board decided to adopt Option 1 in ITC 39, a two-phased approach to applying the RCF:
- (a) in the short term maintaining compliance with IFRS Standards for publicly accountable for-profit private sector entities required by legislation to comply with AAS and other for-profit entities voluntarily claiming compliance with IFRS Standards (Phase 1); and
 - (b) in the medium term maintaining IFRS Standards as a base by removing the Australian reporting entity concept from AAS and providing a revised Tier 2 GPFS framework (Phase 2). This would remove the ability of an entity to prepare SPFS where they are required to prepare financial statements that comply with AAS.

²⁷ Refer paragraph BC57(a).

²⁸ Refer paragraph BC57(d).

- BC53 The Board decided in favour of this two-phased approach because it:
- (a) allowed for-profit private sector entities with public accountability and entities that voluntarily report compliance with IFRS Standards to continue to do so;
 - (b) allowed all other entities to continue preparing SPFS in the short term while the Board undertook consultation and outreach activities and determined the appropriate Tier 2 GPFS framework to replace SPFS;
 - (c) maintained IFRS Standards as a base for all entities in the medium term;
 - (d) solved the reporting entity problem in the medium term;
 - (e) solved the SPFS problem in the medium term;
 - (f) allowed time for the Board to consult and determine any NFP modifications that may be necessary to the RCF in accordance with *The AASB's Not-for-Profit Entity Standard-Setting Framework*; and
 - (g) facilitated comparability and ensured there were appropriate accounting standards for each type of entity required to prepare financial statements that comply with AAS.
- BC54 Phase 1 implemented the RCF for publicly accountable for-profit private sector entities and other entities voluntarily reporting compliance with IFRS Standards so that they continue to maintain IFRS compliance when the RCF took effect internationally on 1 January 2020. Entities in Australia with public accountability must apply the full IFRS Standards as AAS incorporate IFRS Standards and therefore, the Board reconfirmed its view that for-profit private sector entities in Australia with public accountability should be required to prepare Tier 1 GPFS. The Board completed Phase 1 in May 2019 (see AASB 2019-1 *Amendments to Australian Accounting Standards – References to the Conceptual Framework*).
- BC55 ITC 39 proposed that Phase 2 would then implement the RCF for all other entities. However after considering initial feedback on ITC 39, the results of discussions with ACNC and other State and Territory regulators regarding the recommendations in the ACNC's Legislative Review 2018: *Strengthening for Purpose: Australian Charities And Not-for-profits Commission* (ACNC legislative review), research initiated by the Board and *The AASB's Not-for-Profit Entity Standard-Setting Framework*, the Board decided that the proposals in ITC 39 should only apply to for-profit private sector entities, and that it would be more appropriate to progress reform of the NFP public and private sector financial reporting framework via separate targeted consultations undertaken as part of the broader financial reporting framework project (refer to paragraphs BC73-BC75 for further discussion). The Board also decided to consider the public sector financial reporting framework separately (refer to paragraph BC80).
- BC56 Option 1 in ITC 39 contemplated that during Phase 2, the Tier 2 GPFS framework in AASB 1053 would be revised to be one of the following alternatives:
- (a) RDR – The existing Tier 2 GPFS framework as currently exists in AASB 1053, consisting of full R&M, including consolidation and equity accounting (where applicable) with reduced disclosures from each applicable AAS; or
 - (b) Specified Disclosure Requirements (SDR) – A new Tier 2 GPFS framework that would consist of full R&M including consolidation and equity accounting (where applicable), however with specified disclosures from only some AAS.
- The Board subsequently decided that neither RDR nor SDR were appropriate Tier 2 disclosure frameworks. The Board instead decided to develop another alternative, the *Simplified Disclosures Framework*, as enacted by AASB 1060 and explained further in paragraph BC98.

Other options considered in ITC 39

- BC57 ITC 39 considered four other options for implementing the RCF in Australia. However, after considering constituent comments, the Board decided not to pursue them, as explained below:
- (a) Option 2 – Operate with two conceptual frameworks. This option would implement the RCF for publicly accountable for-profit entities and other entities voluntarily reporting compliance with IFRS Standards. It would also retain the existing Conceptual Framework for all other entities. The Board decided not to pursue this option as it requires two conceptual frameworks indefinitely, which would likely lead to the development of inconsistent accounting policies between entities preparing financial statements under the existing Conceptual Framework and entities preparing financial statements under the RCF. Also this option does not solve either the clash of the reporting entity concepts or the SPFS problem.
 - (b) Option 3 – Implement the RCF for all entities when it first becomes applicable to maintain compliance with IFRS Standards and IFRS Standards as a base for Australian Accounting

Standards. This option would result in a single conceptual framework for all entities in the short term, remove the Australian reporting entity concept and the ability of an entity to prepare SPFS as a non-reporting entity when they are required to comply with AAS from 1 January 2020. Option 3 would see an increase in regulatory burden, particularly for NFP entities, as there would be a considerable step up for many entities transitioning to Tier 2 GPFS framework given the number of entities preparing SPFS and the short timeframe for transition to GPFS. The Board was concerned that this option would not provide entities with enough time for transition.

- (c) Option 4 – Retain the existing Conceptual Framework, the Australian reporting entity concept and the ability of an entity to prepare SPFS as a non-reporting entity where they are required to comply with AAS. Under this option compliance with AAS might not result in compliance with IFRS Standards after 1 January 2020.
- (d) Option 5 – Implement the RCF from 1 January 2020 when it first becomes applicable to maintain compliance with IFRS Standards and keep IFRS Standards as a base for AAS. Under Option 5, the Australian reporting entity concept would be retained but the name amended and minimum requirements for SPFS would be prescribed by the Board. The Board decided not to proceed with Option 5 as it did not consider this option to be significantly different from Option 1 (except for the phased approach) or Option 3, as the AASB would still need to prescribe minimum reporting requirements for SPFS preparers to resolve the SPFS problem.

AASB's deliberations on proceeding with Phase 2

BC58 The Board received 33 formal comment letters (relevant to this phase of the project) in response to ITC 39, from professional service firms, regulators, professional bodies, academics, preparers, users of financial statements and other respondents on specific and general matters for comment regarding Phase 2. The Board considered the comments received from each respondent and engaged directly with respondents to discuss any comments which required clarification. The Board also received feedback on the phase 2 proposals (targeted only to for-profit private sector entities) when they were presented at various forums, workshops and discussion groups to obtain feedback. This included roundtable sessions held in September 2018, where 106 stakeholders including regulators, professional bodies, users, preparers, auditors and academics attended. Furthermore, feedback was sought via targeted user and preparer surveys in quarter 3 of 2018, which received a total of 37 user and 49 preparer responses. The surveys were focussed on the specific matters for comment in ITC 39, and were used to get a better understanding of which of the Tier 2 GPFS frameworks proposed in ITC 39 users preferred (and why), as well as what transitional relief would be helpful to preparers. The feedback received from the formal comment letters, roundtables and surveys was consistent, indicating that

- (a) there is a SPFS problem that needs to be solved;
- (b) the Tier 2 GPFS framework should require compliance with all the R&M requirements in AAS including consolidation and equity accounting (where applicable);
- (c) comparability, transparency, comprehensibility and consistency are what users need most in financial statements;
- (d) a revised Tier 2 GPFS disclosure framework was preferred as SDR seemed to be missing some key disclosures, while RDR had too many. The Board noted the low number of entities moving from SPFS indicated that the costs of RDR were seen to outweigh the benefits for these entities. However, in comparison to Tier 1 GPFS there was some benefit as 13% had voluntarily moved to RDR. Respondents felt that something in between the RDR and SDR framework would better satisfy user needs and suggested a more balanced approach to disclosures was needed;
- (e) there is widespread uncertainty on whether AASB 1 provides enough transitional relief to facilitate the transition from SPFS to Tier 2 GPFS (in whatever form that may take);
- (f) only one Tier 2 GPFS framework is necessary for for-profit private sector entities, given the entities required to prepare and in some cases publicly lodge financial statements is such a small proportion of actively trading entities, however some respondents were concerned that the proposals were not also considering who should be publicly lodging financial statements, noting in particular that the thresholds used from determining what constitutes a large proprietary company had not been reviewed for a number of years;
- (g) there were no clear views on what additional transitional relief, is needed;
- (h) respondents were concerned about the effect of the proposals on entities with a non-legislative requirement to prepare financial statements that comply with AAS (ie entities with trust deeds and other constituting documents inadvertently requiring compliance with AAS). Respondents were also concerned about the complexities and the potential costs involved in changing such documents;

- (i) a small number of respondents wanted the AASB to further consider the *International Financial Reporting Standard for Small and Medium-sized Entities* (IFRS for SMEs Standard) as an optional Tier 2 GPFS framework alternative or as the Tier 2 GPFS framework;
 - (j) a small number of respondents asked for a financial reporting framework for those entities not required by legislation to prepare or lodge financial statements; and
 - (k) some respondents thought more evidence of user needs was required.
- BC59 Subsequent to receiving comments on ITC 39, all formal comment letters were made available to the public via the AASB website.²⁹ Summaries of feedback obtained from various outreach events, results from user and preparer surveys, and agenda papers for AASB Board meetings were also made available via the AASB website.
- BC60 The Board decided to proceed with Phase 2 and resolve the issues with SPFS after considering:
- (a) the responses from financial statement users, preparers and other stakeholders during the public consultation period, including over 200 targeted discussions;
 - (b) the findings in AASB Research Reports and commissioned academic research;
 - (c) the level of voluntary compliance with ASIC RG 85;
 - (d) the low number of entities moving from SPFS to RDR;
 - (e) the results of user and preparer surveys;
 - (f) the decision by Treasury to revise the large proprietary thresholds (and therefore answering the ‘who’ should report question) (see paragraph BC35); and
 - (g) the views of other regulators noted above, in particular the views expressed by ASIC in RG85 that, to provide a true and fair view of a company’s financial position and performance, all of the R&M requirements in AAS should be complied with (see paragraphs BC28-BC29).
- The accumulated body of evidence indicates there are users of publicly lodged SPFS and there is widespread acknowledgement, particularly from users, that the current financial reporting framework does not provide consistent, comparable, comprehensible, transparent and enforceable financial statements.
- BC61 As such, the Board developed an Exposure Draft of proposals to address the issues, as set out in the next section.

Issue of ED 297

- BC62 The Board’s proposals to implement its chosen option were exposed for public comment between August and November 2019 in two Exposure Drafts:
- (a) ED 297 *Removal of Special Purpose Financial Statements for Certain For-Profit Private Sector Entities*, which proposed the matters set out in this Standard, including the scope of the removal of SPFS and applicable transitional relief; and
 - (b) ED 295 *General Purpose Financial Statements – Simplified Disclosures for For-Profit and Not-for-Profit Tier 2 Entities*, which proposed the revised Tier 2 GPFS framework. The proposals of ED 295 are addressed in detail in AASB 1060 and its Basis for Conclusions.
- BC63 Extensive outreach was conducted on the proposals, including roundtables in Melbourne, Sydney, Brisbane, Perth and Adelaide, attended by 73 stakeholders.
- BC64 The Board received 19 formal submissions on ED 297 from stakeholders representing professional service firms, regulators, professional bodies, academics, preparers, software providers and others.
- BC65 All submissions to the Board, summaries of outreach and deliberations by the Board were made available to the public on the AASB website.
- BC66 The Board did not undertake field testing of the proposals, for reasons including the time-sensitive nature of the project and that transition from SPFS to GPFS is not a new requirement. The Board noted that many SGE entities would have transitioned shortly prior to the development of the proposals, and those entities had not shared any issues in that process with the Board.
- BC67 The next section details the matters considered by the Board in developing those proposals and this Standard, including where relevant the Board’s decisions on how to address stakeholder feedback as part of the exposure process.

²⁹ See <https://www.aasb.gov.au/DirectLink.aspx?id=2155>

Scope

- BC68 For-profit private sector entities preparing financial statements under the *Corporations Act 2001* that are affected by this Standard are principally:
- (a) large proprietary companies;³⁰
 - (b) unlisted public companies (other than companies limited by guarantee);
 - (c) small proprietary companies controlled by a foreign company;
 - (d) financial services licensees; and
 - (e) small proprietary companies with crowd-sourced funding.

These have all been identified by the Board as being likely to have users dependent on their GPFS (see paragraph BC40-BC42 and category 4 in the Summary of scope table in paragraph BC93 below).

- BC69 In addition to *Corporations Act 2001* entities covered by paragraph BC68, some other types of entities are also affected by this Standard. For example, for-profit co-operatives and incorporated associations required by state or territory legislation to prepare financial statements in accordance with AAS or accounting standards are also subject to this Standard.

- BC70 Some respondents to ED 297 questioned whether it was appropriate to include entities that are not required to publicly lodge financial statements within the scope of the Standard, such as large proprietary companies that are not required to lodge financial reports with ASIC if they meet certain conditions outlined in section 1408 of the *Corporations Act 2001* (exempt proprietary companies). However, the Board decided against such an exemption on the basis that the relevant legislation requires compliance with accounting standards for a reason, whether or not articulated by the other regulator, regardless of whether the financial statements are publicly lodged. The Board also noted a number of these entities would have been required to comply with the SGE legislation and would have benefited from the increase in the large proprietary thresholds, so the impacted number of entities is considerably reduced. Further, the Board preferred to limit any special rules or exceptions in the proposals, consistent with recommendations in the *Final Report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry*.

- BC71 Entities not subject to this Standard (or the requirements in AASB 2019-1) continue to be able to prepare SPFS if they classify themselves as non-reporting entities, and where the SPFS are prepared other than in accordance with AAS. For these entities, the financial reporting framework applied in the SPFS would continue to be determined by the accounting policies selected by the directors or those charged with governance. For example, the directors or those charged with governance could adopt a basis of preparation based on AAS, the Tier 2 GPFS framework, RG 85, the IFRS for SMEs Standard, the NZ Public Benefit Entity Simple Format Reporting – Accrual (Not-for-profit), the NZ Public Benefit Entity Simple Format Reporting – Cash (Not-for-profit), UK FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland* and other sources. Refer to paragraphs BC78, BC84, BC103 and BC106 for additional discussion.

- BC72 The Board conducted research³¹ into the number and types of specified for-profit entities lodging financial statements with ASIC and concluded there were approximately 12,797 specified for-profit entities lodging financial reports. This is based on the latest lodgements by all filing entities as at 30 July 2018, which was before the thresholds for large proprietary companies were doubled. Of these 12,797 entities, 6,763 were large proprietary companies,³² 3,102 were unlisted public companies and 2,932 were small proprietary companies controlled by a foreign company. Subsequent to the revision of the large proprietary thresholds, the Board expects there are approximately 10,500 specified for-profit entities that would be required to publicly lodge financial statements with ASIC. However, the Board was not able to obtain data on the number of other for-profit private sector entities that would be required to prepare financial statement in accordance with other types of legislation.

Not-for-profit private sector entities

- BC73 As noted in paragraph BC55, the Board decided this Standard should apply only to for-profit private sector entities and that separate later consideration of the NFP private sector was needed for the following reasons:

30 Including, for example, certain large proprietary companies that are not required to lodge financial reports with ASIC if they meet certain conditions (exempt proprietary companies).

31 Research Report 12.

32 This research was performed prior to Treasury doubling the thresholds used to determine large proprietary companies. Subsequently the Board noted that Treasury's increasing of the thresholds would reduce the number of large proprietary companies to approximately 4,500.

- (a) the removal of SPFS would have a significantly greater impact on the NFP private sector compared with the for-profit private sector. Of those NFP private sector entities that are required to prepare financial statements and lodge them with the ACNC, research estimates that of the 36% of large and medium charities preparing and lodging SPFS with the ACNC, only a small portion (26%)³³ are complying with the R&M requirements in AAS as compared to approximately 76% of specified for-profit private sector entities lodging financial statements with ASIC (see paragraph BC20). The substantially lower level of compliance in the NFP private sector would result in a much larger proportion of the NFP private sector reporting population being impacted by the proposals compared with the for-profit private sector;
- (b) specified for-profit private sector entities that are required to prepare financial statements that comply with AAS have greater levels of economic significance, size and resources compared to NFP private sector entities. Proportionately, specified for-profit private sector entities are a significantly smaller number (less than 1.5% of the population of trading entities are required to prepare financial statements in accordance with AAS – see paragraph BC101 for more details), whereas approximately 33% of charities (15,828 large and medium charities out of a total of 47,125 charities registered with ACNC)³⁴ are required to prepare financial statements in accordance with AAS. Due to the differences in characteristics, the Board consider it more appropriate to consider the merits of a third tier of general purpose financial reporting for the NFP sector, as part of a separate project; and
- (c) the unpublished Government (at the time of issuing this Standard) response to the ACNC legislative review which outlined the potential for change in reporting thresholds and obligations for affected entities. To proceed with NFP private sector financial reporting reform could be burdensome for certain NFP entities if the AASB would require them to comply with the R&M requirements in AAS, but the ACNC subsequently relieved them of any financial reporting obligations once the ACNC legislative review is finalised.

BC74 Some respondents to ITC 39 were concerned about the NFP private sector being delayed and felt that the AASB should either prioritise the NFP private sector financial reporting framework reform, or should continue to work on it concurrently with the for-profit private sector financial reporting framework reform. The basis of those respondents' concerns were mixed. Some were concerned that considering the for-profit and NFP financial reporting frameworks separately was not consistent with the objective of transaction neutrality and that the Board would develop different reporting requirements for the NFP sector compared with the for-profit private sector, which would decrease comparability and consistency of financial reports. Others were concerned the NFP private sector has specific needs that should be considered in advance or else a framework may be imposed on the NFP private sector that is fit for purpose in the for-profit private sector but not in the NFP private sector.

BC75 The Board considered this feedback and noted that *The AASB's Not-for-Profit Entity Standard-Setting Framework* provides for NFP sector specific modifications where justifiable. For this reason, notwithstanding the outcomes in the for-profit private sector, a thorough consideration of their appropriateness in accordance with *The AASB's Not-for-Profit Entity Standard-Setting Framework* would be required, and if the for-profit financial reporting framework was determined not to be suitable for NFP entities, the for-profit proposals would be modified as needed. This assessment would be required, even if the for-profit and NFP reforms were undertaken concurrently.

Legislative references to AAS and the meaning of True and Fair

BC76 The Board also conducted research (AASB Research Report No. 10 *Legislative and Regulatory Financial Reporting Requirements* (September 2019)) to identify those entities with financial reporting obligations under Federal and State/Territory legislation. The research grouped the identified financial reporting obligations into different categories, based on the nature of the financial reporting requirement (for example a requirement to prepare financial statements according to AASB accounting standards was categorised separately from a requirement to prepare financial information in accordance with AASB accounting standards, which would not require preparation of a complete set of financial statements as defined in paragraph 10 of AASB 101. This research was then used to determine which categories of for-profit private sector entities should be within the scope of this Standard.

BC77 In particular, the Board considered whether entities that are required by legislation to prepare financial statements that give a true and fair view without reference to compliance with AAS at the same time (for example small co-operatives and entities reporting under state and territory gaming legislation) should be affected by this Standard. The Board noted the *Corporations Act 2001* envisages compliance with the

33 AASB Research Report 11 *Review of Special Purpose Financial Statements: Large and Medium Sized Australian Charities* (August 2019).

34 ACNC 2017 Annual Information Statement Data, as at 24 July 2019.

accounting standards might not necessarily result in financial statements that provide a true and fair view. In addition, the UK Financial Reporting Council paper *True and Fair* from June 2014 confirmed the primacy of the true and fair requirement above compliance with accounting standards. Following consultation with other regulators responsible for the legislation referring to true and fair, the Board considered that, at this time, it should be a matter for each regulator to decide as to how to interpret the relevant legislation in relation to ‘true and fair view’ and noted that to require compliance with AAS whenever legislation required entities to give a true and fair view could possibly have significant unforeseen consequences. Accordingly, the Board decided the application paragraphs of AAS in this Standard should not explicitly refer to true and fair at this time (see category 5) in the Summary of scope table in paragraph BC93 below).

BC78 The Board also decided that for-profit private sector entities that are required under legislation to prepare financial information in accordance with AASB accounting standards (ie of which a complete set of financial statements under paragraph 10 of AASB 101 is not required) would not be within the scope of this Standard (see category 5 in the Summary of scope table in paragraph BC93 below).

BC79 In reviewing the legislative references, the Board noted that in some instances legislation referred to ‘accounting standards’, rather than ‘Australian Accounting Standards’. The Board decided that the application paragraphs of AAS should include entities that are required by legislation to comply with ‘accounting standards’ as well as ‘Australian Accounting standards’. In making this decision, the Board noted that it is reasonable to expect that legislators intended compliance with accounting standards as issued by the AASB when that term is used under Australian legislation (see category 5) in the Summary of scope table below). For these same reasons, legislative references to other similar terms such as ‘accounting principles’ or ‘generally accepted accounting practice’ are more broad, and therefore the Board did not think it was reasonable to infer they were intended to require compliance with accounting standards issued by the AASB and accordingly such references are not within the scope of this Standard. Further, the Board decided that the application paragraphs would only capture references to AAS for entities with a non-legislative requirement, as in those cases it is less clear as to whether the constituting document would have intended to refer to accounting standards as issued by the AASB, when the term ‘accounting standards’ is used (see category 7) in the Summary of scope table in paragraph BC93 below).

Public sector entities

BC80 The Board decided that separate consideration of the public sector was needed because, unlike in the for-profit private sector and NFP private sector, public sector financial reporting is arguably too extensive and not targeted enough to enable public sector entities to be held sufficiently to account. For example, government departments are effectively administrative constructs, and requiring Tier 1 GPFS for all such departments when they are also included in Whole of Government (WoG) GPFS means users might not be directed to the key budget versus actual and service performance reporting information that would enable genuine accountability. Therefore, the Board decided it would pursue financial reporting reform in the public sector via consultation based on the AASB Discussion Paper *Improving Financial Reporting for Australian Public Sector*, which was issued in June 2018, rather than as part of Phase 2 of ITC 39 (see categories 2, 3 and 8) in the summary of scope table in paragraph BC93 below).

Trusts and other entities with a non-legislative requirement to comply with AAS

BC81 When deciding on the scope of Phase 1 of ITC 39 the Board’s intention was to allow entities to maintain compliance with IFRS Standards, not to extend the requirement for entities to prepare GPFS if they were not currently required by legislation to do so. Respondents to ITC 39 identified some entities that may be affected by the amendments proposed in Phase 1, such as trusts required by their constitutional document (rather than legislation) to prepare financial statements that comply with AAS. They do not have any legislative requirement to prepare such financial statements and may be currently preparing SPFS. Therefore, transitioning to GPFS could be burdensome for those trusts.

BC82 Consequently, the Board decided to limit Phase 1 to for-profit private sector entities that have public accountability and are required by legislation to comply with AAS, however it noted that the appropriateness of this limitation would be reconsidered as part of Phase 2 after additional research and outreach was performed.

BC83 When reconsidering the appropriateness of this limitation the Board considered entities with a non-legislative requirement to prepare financial statements that comply with AAS more broadly than just those affected by Phase 1, noting there were likely to be a significant number of additional trusts possibly affected by Phase 2.

BC84 Based on discussions with legal advisors and additional targeted outreach, it is expected that the constituting documents of most trusts contain a requirement for them to prepare financial statements in compliance with

AAS (albeit they might refer to ‘accounting standards’). These financial statements are prepared for a specific purpose and a specific user (eg the beneficiaries of a trust). It is also understood that many such entities, particularly ‘non-corporate’ trusts, prepare SPFS.

- BC85 The Board noted that:
- (a) as the financial statements are prepared for specific users, those users have the ability to command whatever information they require from the entity;
 - (b) there is no external regulator of financial reporting for trusts; and
 - (c) the financial statements of trusts are not lodged on public record.
- BC86 For these reasons, the Board considered whether it was appropriate to provide some form of relief to them, as the Board noted that while changing constitutional documents to remove the requirement to comply with AAS is possible, it can be onerous and if not done correctly can have tax consequences.
- BC87 Targeted outreach was undertaken to understand the number of trusts that may be affected by this Standard, including their size (with reference to income and assets). This was to determine whether it was possible to develop objective criteria related to economic significance for distinguishing between those trusts that should be required to comply with this Standard and those that should be exempted. The Board considered whether the thresholds used for determining what constitutes a large proprietary company could be an appropriate benchmark for this purpose.
- BC88 While there are a large number of trusts undertaking business activities and therefore lodging tax returns with the ATO, data provided by the ATO indicates that a small minority of them would meet the increased income and assets thresholds used for determining what constitutes a large proprietary company.
- BC89 The Board also noted there are entities other than trusts that may currently have a requirement to prepare financial statements in accordance with AAS in their compliance documents but are not required to do so by legislation, such as partnerships, joint arrangements and self-managed superannuation funds, as well as entities subject to other requirements such as lending agreements. As these entities also have specific users, the Board decided that the issues identified above would be equally relevant to such entities.
- BC90 The Board therefore decided that existing for-profit private sector entities should be provided with an exemption from the requirement to prepare GPFS where they do not have a legislative requirement to prepare financial statements that comply with AAS. However, the Board decided this exemption should only apply where their constituting document (or another document) requiring them to comply with AAS was created or amended before 1 July 2021 (the effective date of the Standard) – ie any amendments to or creation of such documents on or after 1 July 2021 would require the entity to prepare GPFS where it referred to the preparation of financial statements that comply with AAS (see category 6) in the Summary of scope table below). If an entity were required to make any amendment to the constituting document for any reason after the effective date of this Standard, then the trustee for example could at the same time amend the financial reporting requirements, subject to the agreement of the beneficiaries. Further, the relief should not be available to an entity whose constituting document was created after the effective date of the amendments, as when drafting the constituting document, the beneficiaries should have determined their information needs including whether or not they required GPFS.
- BC91 Respondents to ED 297 expressed mixed views on such an exception. Whilst a minority considered no exemption was necessary, others supported providing relief in other ways. For example:
- (a) specifying a ‘sunset’ date on the exemption, or in other words, providing an extended transition period for such entities compared to entities required by legislation to prepare financial statements in accordance with AAS; or
 - (b) providing a permanent exemption for such entities.
- BC92 The Board considered this feedback and decided that providing a ‘sunset’ date on the exemption would not meet the objective of providing the exception, because instead of alleviating entities of the potential consequences of changing a trust deed noted in paragraphs BC86 for example, it would only defer such consequences until a later date. Further, the Board reconsidered providing a permanent exemption, and confirmed it would not be appropriate, as providing a permanent exemption would perpetuate the SPFS issue, and cause further interpretative confusion as to whether such a reference is or is not intended to require GPFS. The Board therefore decided to retain exemption for only limited circumstances, consistent with the proposals in ED 297.

Summary of scope

- BC93 The examples in the table below illustrate the types of entities that would be generally covered in the category but some entities may have different specific requirements:

	Entity	In scope/ out of scope of the project
1	Not-for-profit private sector entities including NFP entities that are companies limited by guarantee and lodging financial statements with ASIC under the <i>Corporations Act 2001</i>	Not in scope
2	Not-for-profit public sector entities	Not in scope
3	For-profit public sector entities³⁵	Not in scope
	For-profit private sector entities	
4	Companies required to prepare financial statements under the <i>Corporations Act 2001</i> principally: <ul style="list-style-type: none"> - large proprietary companies (including those with relief from lodging with ASIC); - unlisted public companies other than small companies limited by guarantee; - small proprietary companies controlled by a foreign company; - financial services licensees; and - small proprietary companies with crowd-sourced funding. 	In scope
	Companies preparing financial statements under the <i>Corporations Act 2001</i> because they are directed by ASIC or shareholders to prepare financial reports.	This will depend on what the direction requires ³⁶
5	Entities with financial reporting obligations under Federal or State/Territory legislation (ie required by legislation) to:	
	- prepare financial statements in accordance with AAS or accounting standards (eg co-operatives, incorporated associations and higher education providers)	In scope
	- prepare financial statements that give a true and fair view without reference to compliance with AAS or accounting standards (eg gaming venue operators, internet gaming licensees)	Not in scope – each regulator to interpret the reference to ‘true and fair view’
	- prepare financial information in accordance with AAS or accounting standards but are not required to prepare financial statements as defined in paragraph 10 of AASB 101 (eg friendly societies, superannuation funds, retirement villages)	Not in scope
	- prepare financial information that gives a true and fair view but not to prepare financial statements as defined in paragraph 10 of AASB 101 (eg incorporated associations or housing societies)	Not in scope
	- prepare financial information without reference to AAS or accounting standards (eg for provision to a regulator)	Not in scope
	- keep financial records (but not prepare financial statements) (eg small proprietary companies not required by the <i>Corporations Act 2001</i> to prepare financial statements)	Not in scope
6	Entities required only by their constituting or another document (not by legislation) to prepare financial statements that comply with AAS (eg trusts, partnerships, joint arrangements and self-managed superannuation funds):	
	- existing entities – constituting or other document not created or amended on or after 1 July 2021	Not in scope
	- existing entities – constituting or other document amended on or after 1 July 2021	In scope
	- new entities – constituting or other document created on or after 1 July 2021	In scope
7	Entities required only by their constituting or other document (not by legislation) to prepare financial statements that comply with “accounting standards” (rather than AAS) (eg trusts, partnerships, joint arrangements and self-managed superannuation funds).	Not in scope

35 For-profit public sector entities can elect (voluntarily) to prepare GPFS and apply the revised Conceptual Framework.

36 These companies will be in scope when the direction requires financial statements to be prepared in accordance with AAS or accounting standards.

	Entity	In scope/ out of scope of the project
8	Entities that elect (ie voluntarily) to prepare GPFS (eg for-profit public sector entities or other for-profit private sector entities)	In scope

BC94 Having determined the entities to be caught within the scope of this Standard, the Board considered how best to revise the Tier 2 GPFS framework to appropriately balance the costs and benefits of this Standard. The following section summarises the Board’s deliberations on revising the Tier 2 GPFS disclosure framework (that is detailed in the separate, but related Standard, AASB 1060).

Tier 2 GPFS Framework

BC95 As noted in paragraph BC6, the Board acknowledges that it would be inappropriate to remove the ability of certain for-profit private sector entities to prepare SPFS where they are required to prepare financial statements that comply with AAS, and replace them with GPFS, without reconsidering the Tier 2 GPFS framework, because the current Tier 2 GPFS framework is considered too onerous. The Phase 2 approach in ITC 39 contemplated revising the Tier 2 GPFS framework in AASB 1053 to include one of two alternatives as noted in paragraph BC56:

- (a) RDR – The existing Tier 2 GPFS framework as currently exists in AASB 1053, consisting of full R&M, including consolidation and equity accounting (where applicable) with reduced disclosures from each applicable AAS; and
- (b) SDR – A new Tier 2 GPFS framework that would consist of full R&M including consolidation and equity accounting (where applicable), however with specified disclosures from some AAS. Those standards are those that are currently mandatory for entities required to prepare financial statements in accordance with Chapter 2M of the *Corporations Act 2001*, being AASB 101, AASB 107, AASB 108, AASB 1048 and AASB 1054, plus the disclosures required by AASB 124 *Related Party Disclosures*, AASB 136 *Impairment of Assets*, AASB 15 *Revenue from Contracts with Customers* and AASB 112 *Income Taxes*.

BC96 As noted in paragraph BC58, the feedback from the roundtables, user and preparer surveys and submissions on Phase 2 of ITC 39 indicated that:

- (a) RDR has too many disclosure requirements; and
- (b) SDR was too much in some ways but fell short in many other ways. For example, the feedback received from roundtables, user and preparer surveys and submissions on Phase 2 of ITC 39 was that whilst the disclosures in SDR are important, requiring all disclosures from those nine Standards was too much. Most participants further suggested that SDR might not be appropriate for all industry sectors and is missing some critical disclosures to help predict the viability of an entity such as liquidity, contingent liabilities, subsequent events and commitments.

BC97 As a consequence, the Board decided to propose a third alternative to replace the current disclosure aspects of Tier 2 GPFS disclosure framework, being a new and separate disclosure standard for entities reporting under the Tier 2 GPFS framework, termed ‘Simplified Disclosures’. It would be based on the disclosure requirements of the IFRS for SMEs Standard, but retain the R&M requirements in AAS.

BC98 The disclosures required by the Simplified Disclosures Standard are set out in a separate but related Standard, AASB 1060, and have been developed via a ‘bottom-up’ approach based on the disclosures in the IFRS for SMEs Standard, without reference to the full IFRS disclosures (ie no shading). The Board’s decisions on the content of the Simplified Disclosures Standard are set out in the Basis for Conclusions to AASB 1060.

One Tier 2 GPFS Framework

BC99 Some respondents to Phase 2 of ITC 39 suggested that more than one Tier 2 GPFS framework was necessary, as having only one Tier 2 GPFS framework is too limited.

BC100 The Board noted transition costs, and the ongoing costs of training and maintenance of either two Tier 2 GPFS frameworks or even three tiers of GPFS reporting for users, preparers, auditors and regulators for only 1.3%³⁷ of actively trading entities outweighed any potential benefits.

BC101 As noted in paragraph BC73, the Board observed that of the 2.5 million companies registered with ASIC in 2016-2017, only approximately 840,000 were actively trading, and of those there were only approximately

37 This is subsequent to Treasury increasing the thresholds used for determining what constitutes a large proprietary company.

12,797 specified for-profit private sector entities that were required to prepare and lodge financial statements (at July 2018). This represents approximately only 1.5% of the total population of trading entities. The Board further noted that Treasury's increase of the large proprietary company thresholds would further reduce this number to 1.3% of the population of trading entities. The Board noted that this is a very small proportion of the total number of trading entities and having one Tier 2 GPFS framework for this population was sufficient.

- BC102 The Board also noted the results of a survey conducted by an accounting firm in Australia that asked respondents to answer a polling question regarding whether additional tier(s) of GPFS reporting should be considered. In response, 52% (118 of the 228 respondents) stated no, 18% (41 of the 228 respondents) stated yes and 30% (69 of the 228 respondents) weren't sure. The Board however noted that of those respondents who answered 'yes' to this question, a number of them provided suggestions specific to the NFP sector.
- BC103 Some respondents felt that additional tiers of GPFS reporting with varying degrees of disclosure may be useful, as entities preparing financial statements range in size and complexity. The Board emphasised that entities without a statutory requirement to comply with AAS, such as those below the now doubled large proprietary company thresholds in the *Corporations Act 2001*, would be able to continue to tailor their financial statements to the needs of their specific users and therefore additional tiers of GPFS reporting were not required. Further, there are only an estimated maximum of approximately 4,500 entities (subsequent to Treasury increasing the thresholds used for determining what constitutes a large proprietary company) that may be required to prepare financial statements under Part 2M.3 of the *Corporations Act 2001* who would be able to use a Tier 2 GPFS framework (including those currently preparing Tier 1 and Tier 2 GPFS).
- BC104 Further, separating this already small proportion of the total population (ie 1.3% or approximately 10,500 entities) into more than one tier would require objective criteria on which to make this separation. Treasury's consultation on its proposals to increase the thresholds used for determining what constitutes a large proprietary company considered this, and determined there should only be a large, small distinction.
- BC105 As noted in paragraph BC71, entities not subject to this Standard (or the requirements in AASB 2019-1) would continue to be able to prepare SPFS if they classify themselves as non-reporting entities.
- BC106 Further, as noted in paragraph BC45(b), the few AAS that are mandatory for SPFS are focussed on the presentation of and disclosure in financial statements, rather than R&M requirements, and cannot be considered an appropriate financial reporting framework. For this reason, when preparing SPFS, directors and those charged with governance are responsible for determining the financial reporting framework of the entity by specifying the accounting policies (ie R&M requirements). The directors and those charged with governance are also responsible for ensuring the financial reporting framework is appropriate to meet the needs of the users of their SPFS.
- BC107 A key theme noted through submissions and outreach on Phase 2 of ITC 39 was the need for comparability across publicly lodged financial statements, particularly in relation to R&M requirements (see paragraphs BC108-BC113). As such, the Board decided that creating additional tiers of GPFS reporting for such a small proportion of the total population of trading entities would not adequately meet the objective of creating a consistent and comparable financial reporting framework, and could lead to unnecessary complexity for financial statement users of such a small proportion of the population when trying to determine which tier of GPFS reporting requirements have been applied to the financial statements. Further, separating this population into two separate tiers would require objective criteria on which to make this separation. As noted in paragraph BC104 above Treasury had consulted on the thresholds used for determining what constitutes a large proprietary company and determined there should only be a large, small distinction. Also, small foreign-controlled entities would likely be required to use the R&M requirements of their parent entities that are unlikely to be using the IFRS for SMEs Standard, and finally, approximately 90%³⁸ of unlisted public companies preparing and lodging financial statements with ASIC already comply with the R&M requirements in AAS.

R&M requirements of Tier 2

- BC108 The Board noted the strong preference expressed by respondents to Phase 2 of ITC 39 for a framework that includes the full R&M requirements in AAS as it would enhance the comparability, consistency and transparency of the financial statements. Feedback from targeted outreach emphasised that users agreed that the usefulness of information within financial statements for decision making is adversely affected where entities have not consistently applied the R&M requirements in AAS.
- BC109 The findings noted in Research Report 12 estimates that 76% of specified for-profit entities that are lodging SPFS with ASIC are complying with the R&M requirements in AAS (see paragraph BC20). Therefore, the Board considered that moving to a Tier 2 GPFS framework that is not based on the full R&M requirements

38 Research Report 12.

in AAS is counter-intuitive when trying to improve the consistency, comparability, usefulness and credibility of financial reporting in Australia.

BC110 The Board did however re-evaluate the suitability of the IFRS for SMEs Standard as the Tier 2 GPFS framework in Australia and reconfirmed that the full IFRS for SMEs Standard continues not to be a preferred option for the for-profit private sector in Australia for the following reasons:

- (a) users specifically identified the comparability of the R&M requirements in AAS as a key concern. The IFRS for SMEs Standard has different R&M requirements compared to AAS, and to meet user needs for comparability, all for-profit private sector entities within the scope of this Standard would need to apply the IFRS for SMEs Standard (with it being the only Tier 2 GPFS framework), or a third tier of GPFS reporting would need to be created;
- (b) to achieve a consistent Tier 2 GPFS framework, additional transitional costs would be expected to arise because based on the data in paragraph BC20, it is estimated that a majority of ASIC regulated entities currently lodging SPFS are already complying with the R&M requirements in AAS. To achieve a consistent Tier 2 GPFS framework and implement the IFRS for SMEs Standard, all of these entities, approximately 8,800 of the 10,500 specified for-profit entities lodging financial statements with ASIC (subsequent to Treasury increasing the thresholds used from determining what constitutes a large proprietary company) would need to change their accounting policies to adjust for the different R&M requirements contained in the IFRS for SMEs Standard. That is, all of the specified for-profit entities preparing Tier 1 GPFS, Tier 2 GPFS or SPFS which comply with the R&M requirements in AAS.

In comparison only the 10% that currently don't comply with the R&M requirements in AAS and potentially the 14% where it's unclear whether or not they have complied with the R&M requirements in AAS (approximately up to 1,700 entities in total) would be required to change their accounting policies to align with the R&M requirements in AAS. Therefore, a larger population of preparers would see an increase in the costs associated with the transition from SPFS to GPFS if the Tier 2 GPFS framework were based on different R&M requirements; and

- (c) having different R&M requirements is not consistent with ASIC and other regulators' views that the full R&M requirements of accounting standards should be applied in order to give a 'true and fair view' of the financial position and performance of an entity.³⁹
- (d) there is no need for a third tier of GPFS reporting as approximately 98.7% of the 840,000 trading entities only have an obligation to prepare and lodge a tax return with the ATO. Further, creating a third tier would require objective criteria on which to make this separation, and Treasury has just consulted on the thresholds used for determining what constitutes a large proprietary company and determined there should only be a large, small distinction. Also, small foreign-controlled entities would likely be required to use the R&M requirements of their parent entities that are unlikely to be using the IFRS for SMEs Standard, and finally, approximately 90%⁴⁰ of unlisted public companies preparing and lodging financial statements with ASIC already comply with the R&M requirements in AAS. Subsidiaries would also need to provide additional information to be compliant with IFRS Standards for the purpose of consolidating into their parent's consolidated financial statements where the parent applies Tier 1 AAS or IFRS Standards;
- (e) the IFRS for SMEs Standard would result in reduced comparability between entities preparing full IFRS Standards compliant financial statements because of different accounting policy alternatives due to different R&M requirements;
- (f) in the event an entity moves to, or from, preparing financial statements applying full IFRS Standards, there would be costs involved in transitioning from the R&M requirements of one tier of reporting to another. Transition costs, and the ongoing costs of training and maintaining either two Tier 2 GPFS frameworks or even three tiers of GPFS reporting for users, preparers, auditors and regulators for only 1.3%⁴¹ of actively trading entities would also outweigh any potential benefits;
- (g) the feedback received on Phase 2 of ITC 39 suggested that applying the consolidation and equity accounting requirements for the first time would be the most difficult aspect of transitioning from SPFS to GPFS, however consolidation and equity accounting are both required under the IFRS for SMEs Standard. As such, it does not appear that adopting the IFRS for SMEs Standard would mitigate these concerns;
- (h) using a single basis for the R&M requirements in AAS would support efficiency in the education of accountants and financial statement users;

³⁹ See, for example, section 2 of RG85.

⁴⁰ Research Report 12.

⁴¹ This is subsequent to Treasury increasing the thresholds used for determining what constitutes a large proprietary company.

- (i) the use of the IFRS for SMEs Standard would decrease harmonisation with New Zealand further than the requirements in this Standard, as the New Zealand financial reporting framework for for-profit entities has only two tiers and does not use the IFRS for SMEs Standard; and
 - (j) despite the issues noted above that would be faced if the IFRS for SMEs Standard were to be adopted, the IFRS for SMEs Standard is based on full IFRS Standards, and does not appear to depart significantly from the IFRS Standards (see AASB Staff Paper *Comparison of Standards for Smaller Entities* (April 2018)). This is acknowledged by the IASB in the Basis for Conclusions to the IFRS for SMEs Standard, which also notes that the needs of users of financial statements of small and medium sized entities are similar in many ways to the needs of users of publicly accountable entities.⁴² As such, it appears unlikely that the benefits of moving to the IFRS for SMEs Standard would outweigh the costs noted above.
- BC111 The Board also noted that any possible reduction in on-going compliance costs or alleviation of concerns that the R&M requirements of IFRS Standards are too complex which may arise from having the IFRS for SMEs Standard as the Tier 2 GPFS framework, would not be significant enough to outweigh the loss of benefit to users (ie the loss of consistency and comparability of R&M requirements in AAS), because as noted above, the IFRS for SMEs Standard still requires consolidated financial statements and equity accounting, along with deferred tax accounting, lease accounting, fair valuing of derivatives and other complex financial instruments and related party disclosures that are not substantively different from the full requirements in AAS.
- BC112 The Board further noted that 65% of respondents to Phase 2 of ITC 39 did not agree with having the IFRS for SMEs Standard as the Tier 2 GPFS framework in Australia.
- BC113 In light of the above, as noted in paragraph BC98, the Board decided to create a new and separate Tier 2 GPFS framework that would have the R&M requirements of Tier 1 (including consolidation and equity accounting) and the disclosure requirements of the IFRS for SMEs Standard.
- BC114 The new Tier 2 GPFS framework replaces the existing Tier 2 GPFS RDR framework and is available for application by for-profit private sector entities that do not have public accountability, NFP private sector entities and public sector entities other than the Australian Government and State, Territory and Local Governments.

Consolidation requirements of Tier 2 GPFS framework

- BC115 Anecdotally, the Board is aware that some entities preparing SPFS are parent entities but do not prepare consolidated financial statements, and some of those entities are also not providing an explanation as to why they have not prepared consolidated financial statements.
- BC116 While considering how best to revise the Tier 2 GPFS framework, the Board also contemplated whether it was possible to provide financial information about subsidiaries in a more cost effective way, such as by providing summary financial information in the consolidated financial statements of the parent instead of a complete set of financial statements for the subsidiary. The Board undertook research (AASB Research Report No. 13 *Parent, Subsidiary and Group Financial Reporting*) to assess the suitability of current reporting requirements where the views of different lending institutions were sought. The feedback received showed there is a need for both a full set of subsidiary financial statements and the consolidated financial statements of the group. Feedback received from users in response the AASB's user survey and submissions to ITC 39 also highlighted the need for consolidated financial statements.
- BC117 The majority of the lending institutions interviewed mentioned that in the case of group structures, they require the consolidated financial statements of the group to make their lending decisions and that these are particularly important when:
- (a) there is structural subordination within group structures;
 - (b) there is a deed of cross guarantee;
 - (c) banks have legal recourse to the assets of the consolidated group;
 - (d) lending to a subsidiary is in the form of a credit enhancement to the whole group; and
 - (e) lending to a subsidiary that does not have substantial operations and it is a financing vehicle.
- BC118 Similarly, feedback from users mentioned that in order to make decisions, they require:
- (a) consolidated financial statements including note disclosures (which include all assets, liabilities, revenues and expenses of the parent and all subsidiaries); and / or

⁴² IFRS for SMEs Standard, Basis for Conclusions, paragraph BC96.

- (b) consolidated financial statements including note disclosures plus some parent entity information to understand their dividend paying capacity.
- BC119 The feedback noted in paragraphs BC117-BC118 provided further support to the Board's view that consolidated financial statements are essential to provide users with transparent and complete information about the financial position and financial performance of the group and the entities in the group.
- BC120 Further information on the Board's decisions in relation to the revised Tier 2 GPFS framework is available in the Basis for Conclusions to AASB 1060.
- BC121 Although the Board decided that a revised Tier 2 GPFS framework would help facilitate the removal of SPFS, it also decided that transitional relief in addition to what is currently available in AASB 1 was warranted to further assist entities with transition from SPFS to Tier 2 GPFS where they choose to early adopt this Standard, as noted in paragraphs BC122-BC135.

Transition

Feedback from ITC 39

- BC122 In developing this Standard, the Board acknowledged that some entities might incur additional costs, particularly on transition from SPFS to Tier 2 GPFS. As such, the Board included specific matters for comment in ITC 39 seeking feedback on what transitional relief should be provided, in addition to that already available in AASB 1. Feedback on transitional relief was also sought by the Board in its roundtable discussions, surveys, webinar and individual meetings with stakeholders.
- BC123 Feedback from outreach activities related to Phase 2 of ITC 39 and specifically on transitional matters was mixed. Whilst some constituents agreed that AASB 1 would be sufficient to facilitate transition, others were either unclear on whether AASB 1 would be sufficient, or argued that more transitional relief was necessary. The Board noted two common areas of suggestion for transitional relief:
- (a) relief from consolidation and equity accounting, particularly in relation to the retrospective application of AASB 3 *Business Combinations*; and
- (b) relief from the requirement to restate the comparative period on transition from SPFS to Tier 2 GPFS.

However, despite requesting more information, stakeholders did not articulate the specific aspects of the above-mentioned transitional issues that would be particularly costly or onerous.

Options considered

- BC124 In deliberating the options for transitional relief, the Board noted AASB 1053 requires an entity to either apply all the relevant requirements in AASB 1 or the requirements in AASB 108 to transition from SPFS to Tier 2 GPFS, if that entity had not applied or had only selectively applied the R&M requirements in AASB.
- BC125 In light of constituent feedback that consolidation and equity accounting would be the most challenging aspects of transition, the Board considered the relief provided by AASB 1 from the need to retrospectively account for past business combinations (a specific challenge noted for consolidation and equity accounting). The Board concluded that the application of AASB 1 provides significant and sufficient relief to address the stakeholder concerns noted in paragraph BC123(a).
- BC126 The Board also noted:
- (a) **Doubling of thresholds for large proprietary companies:** As noted in paragraph BC35, Treasury doubled the thresholds used for determining what constitutes a large proprietary company. Based on the data available from a data aggregator for the latest lodgements by all filing entities as at 30 June 2018 (being before the doubling of the thresholds), as noted in paragraph BC72, there were a total of 6,763 large proprietary companies that had lodged financial statements with ASIC, out of which 5,500 entities filed SPFS. The doubling of the thresholds reduced the total population of large proprietary companies by approximately one third. Based on the revised thresholds, the same data from a data aggregator indicates that a maximum of approximately 3,666 large proprietary companies would be required by this Standard to transition from SPFS to Tier 2 GPFS.
- In addition, the Board noted the Explanatory Statement accompanying the revision of the thresholds that had outlined the expectation that larger entities are more likely to have users that are dependent on the entity's GPFS. Further, the Explanatory Statement also noted that the average access rates for financial reports through ASIC for the remaining population of large proprietary companies is

significantly higher than for those entities that would now be small proprietary companies (see paragraph BC40(c)).

The Board considered that such economically significant companies are expected to have sufficient skills and resources to cope with any transitional challenges within the current requirements.

- (b) **Findings from Research Report 12:** One of the key findings of this research is that overall it is estimated that 76% of specified for-profit entities lodging SPFS with ASIC comply with the R&M requirements in AAS; 10% did not comply with the R&M requirements in AAS, while for the remaining 14% it was unclear whether or not they complied with the R&M requirements in AAS. As noted in paragraph BC124, entities already applying all of the R&M requirements of AAS would not require transitional relief.

While the Board noted that these results focused only on compliance with R&M requirements in their lodged SPFS and therefore did not identify whether entities prepared consolidated financial statements, the results show that out of approximately 7,295⁴³ for-profit entities lodging SPFS with ASIC following the revision of the large proprietary company thresholds, only 10% to 24% (approximately 600 to 1,700 entities) are expected to be affected by this Standard. This is because 76% of the specified for-profit entities lodging SPFS with ASIC are already complying with the R&M requirements in AAS. The Board also noted that this number may be further reduced as the research showed a clear correlation between entity size and compliance with the R&M requirements in AAS, with the level of compliance increasing with company size.

Further, the Board noted that the primary reason for 6% of entities that did not comply with the R&M requirements in AAS was due to not applying AASB 112 in full, however constituents have not raised AASB 112 as being problematic for the purpose of transition.

- (c) **Insufficient compelling evidence from extensive outreach:** The Board performed extensive outreach and asked for specific information on transitional relief that might be needed through formal comments on ITC 39, roundtables in capital cities and over 200 meetings with individual stakeholders, and did not receive compelling evidence or suggestions identifying specific issues that needed transitional relief. Further, no specific feedback was received from small foreign-controlled proprietary companies or unlisted public companies not limited by guarantee.
- (d) **The AASB's For-Profit Entity Standard-Setting Framework:** The Board noted the presumption that IFRS Standards are appropriate as a base for all entities, with particular regard to the fact that AASB 1, which incorporates IFRS 1 *First-Time Adoption of International Financial Reporting Standards*, had been developed by the IASB to reduce the cost of first-time adoption of IFRS Standards, so that it does not outweigh the benefits of adoption. The Board also observed that the application of AASB 1 has been an appropriate base for entities transitioning to AAS since 2005, including a large number of SGEs that were required to transition from SPFS to GPFS for reporting periods ending on or after 30 June 2017. Paragraphs BC154-BC156 provide further discussion on how the Board applied *The AASB's For-Profit Entity Standard-Setting Framework* in arriving at the requirements in this Standard.
- (e) **No adverse feedback from entities that transition as a result of the SGE requirements:** Despite specifically requesting feedback, the Board was not made aware of any significant transitional issues faced by the SGEs that were required to begin lodging GPFS with the ATO. These entities would have transitioned using the current requirements of AASB 1. The Board has also not heard any adverse feedback from the ATO on the quality of the financial reports that have been lodged.

Further, the Board noted that many of the entities that have already transitioned to preparing GPFS as required by the SGE legislation, are entities expected to be within the scope of this Standard (ie they are required to prepare financial statements under Part 2M.3 of the *Corporations Act 2001* and are now preparing GPFS). As a result, there are likely to be fewer entities required to transition from SPFS to GPFS as a result of this Standard. Further the Board does not expect the reporting requirements for these SGE entities to be any more onerous as a result of this Standard (ie they will continue to prepare GPFS as required by SGE legislation).

BC127 Nevertheless the Board considered three possible options to provide transitional relief in addition to what is available under AASB 1, as follows:

⁴³ 3,666 large proprietary companies, 1,252 unlisted public companies not limited by guarantee and 2,377 small foreign-controlled proprietary companies

Option	Nature of the relief considered	Key factors considered
<p>‘Push-down accounting’ for entities that are subsidiaries of an IFRS Standards and / or AAS compliant parent</p>	<p>To allow subsidiaries that are consolidating into the financial statements of an AAS or IFRS Standards compliant parent to recognise amounts reported in their reporting / consolidation pack (which would have been derived from acquisition date fair values) to be deemed cost in their individual financial statements (subject to requiring them to recognise only those assets and liabilities that qualify for recognition under AAS in the subsidiary’s own financial statements).</p>	<p>The Board noted that advantages of this relief would include:</p> <ul style="list-style-type: none"> (a) no need to keep two sets of parallel accounting records (ie one set for group reporting purposes and another set for its own mandatory Tier 2 GPFS); and (b) opening balances would still be based on AAS principles, albeit measured at a different point in time. <p>However, the Board decided not to provide this relief:</p> <ul style="list-style-type: none"> (a) for the reasons noted in paragraph BC126; (b) because this relief would have been inconsistent with <i>The AASB’s For-Profit Entity Standard-Setting Framework’s</i> presumption that IFRS Standards are an appropriate base; (c) because anecdotally, adjusting balances to be consistent with AAS is not the most difficult area of transition, rather it is more difficult to restate prior periods; (d) because the relief would only be available for a limited number of entities, which would likely be foreign-controlled and hence subject to public interest. It was not clear to the Board, the number of entities that would be able to utilise this relief in any case; and (e) because such relief would reduce comparability with other entities that are transitioning from SPFS to GPFS. <p>The Board considered whether AASB 1 effectively provided such relief through other exemptions (such as event driven fair values), but did not form a view on this matter.</p>
<p>Relief from recognising ‘deemed goodwill’ if applying paragraph C4(j) of AASB 1.</p>	<p>Provide a parent entity applying the relief in AASB 1 Appendix C in relation to previously unconsolidated subsidiaries with an option to write off ‘deemed goodwill’ immediately in retained earnings, rather than recognise it and then be required to undertake day 1 and annual impairment testing.</p>	<p>The Board noted that advantages of this relief would include:</p> <ul style="list-style-type: none"> (a) the potential to reduce the cost of undertaking an impairment test at the date of transition and ongoing annually; and (b) that it would provide relief for entities consolidating for the first time, a key concern of respondents to Phase 2 of ITC 39. <p>However, the Board decided not to provide this relief:</p> <ul style="list-style-type: none"> (a) for the reasons noted in paragraph BC126; (b) because this relief would have been inconsistent with <i>The AASB’s For-Profit Entity Standard-Setting Framework’s</i> presumption that IFRS Standards are an appropriate base. In particular, the Board noted that this amendment would fundamentally change the R&M requirements of AASB 1; and (c) because this relief could lead to significant loss of information about impairment for users and regulators.

Option	Nature of the relief considered	Key factors considered
Relief from restating comparative information as required by AAS	To amend AASB 1 to specify that entities need not restate or present comparative information as required by AAS. This would mean the date of transition is the beginning of the reporting period (rather than the beginning of the comparative period).	<p>The Board decided to propose this relief in ED 297, noting the advantages include:</p> <ul style="list-style-type: none"> (a) the relief would facilitate the transition to GPFS in a more timely manner – for periods beginning on or after 1 July 2020 (on the assumption the Standard would be issued as an amending standard prior to 30 June 2020). This would also mean that, effectively, the RCF and the removal of the ability of certain entities to prepare SPFS when they are required to prepare financial statements that comply with AAS would become effective for the first time in the same reporting period; (b) the relief was not expected to have implications for the R&M requirements in AAS, except to the extent that the change in the date of transition would lead to differences in opening balances based on a different date of transition; and (c) the relief would reduce costs to all entities required to transition from SPFS to GPFS. <p>However, the Board did note some disadvantages, including:</p> <ul style="list-style-type: none"> (a) reduced information for users – particularly in making trend analyses; and (b) the approach would require divergence from the presumption in <i>The AASB's For-Profit Entity Standard-Setting Framework</i> that IFRS Standards are appropriate as a base, albeit it would not a major deviation.

BC128 For the reasons noted in the table in paragraph BC127, the Board decided against providing additional transitional relief in the form of 'push-down accounting' or immediate write-off of deemed goodwill against retained earnings. The Board sought specific feedback through ED 297 on whether it should re-consider any of the rejected options noted above but did not receive any further compelling reasons to do so.

Relief from restating and presenting comparative information

BC129 As noted in the table in paragraph BC127, the Board concluded that relief from the restatement and presentation of comparative information in accordance with current AAS would be beneficial as it could reduce preparation costs whilst providing a consistent, enforceable and transparent reporting framework (despite a lack of comparability in the year of transition). Thus the Board proposed in ED 297 that an entity would not be required to provide restated comparative information as per current AAS in the year the Standard first becomes effective, on the premise that the Standard would be issued by 30 June 2020, effective for periods beginning on or after 1 July 2020 (see paragraphs BC145-BC148 for further discussion on effective date).

BC130 However, the Board noted the particular importance for users:

- (a) to understand the effect of an entity's transition from SPFS to Tier 2 GPFS on its assets, liabilities and equity; and
- (b) to have comparative information in the statement of profit or loss and other comprehensive income to facilitate trend analysis.

BC131 To balance the needs of users and the costs to preparers, the Board proposed in ED 297 that a pragmatic approach would be to require an entity to:

- (a) present two statements of financial position ie as at the reporting date and at the beginning of the reporting period, with a comparative statement of financial position as presented in the entity's last SPFS disclosed in the notes to the financial statements. This would be supplemented with a description of the main adjustments that were required to make the opening statement of financial

position compliant with AAS. To reduce costs, the Board proposed an entity need not quantify those adjustments; and

- (b) present its statement of profit or loss and other comprehensive income as presented in its last SPFS as comparative information, but clearly labelled, where applicable, that such comparative information is not AAS compliant. This would be supplemented with disclosure in the notes to the financial statements describing the main adjustments that would have been required to make the comparative information compliant with AAS. Also to reduce costs, the Board proposed an entity need not quantify those adjustments.

BC132 Respondents to ED 297 agreed in principle with the transitional relief, however some respondents raised concern that the comparative information in the statement of financial position (being the adjusted opening balances – AAS compliant) would not be comparable to the comparative information in the statement of profit or loss and other comprehensive income (which would not necessarily be AAS compliant). Those respondents argued that this would not be helpful for users of financial statements. Further, some software providers provided feedback that having comparative information presented on different bases could be difficult from both a software development and financial statement user perspective.

BC133 In response, the Board decided a pragmatic approach would be to require the statement of financial position as presented in the entity's last SPFS to be presented on the face of the statement of financial position, and to require the opening statement of financial position (compliant with AAS) to be disclosed in the notes. However, given the comparative information on the face of the financial statements would be less comparable under this approach, the Board decided to require entities to disclose a quantified reconciliation of the entity's equity in the notes. The Board considered whether to require a reconciliation of the entity's statement of financial position, however noted that a reconciliation of equity should provide sufficient detail to understand the changes to the statement of financial position, and providing a reconciliation to equity would be more consistent with the general first-time disclosure requirements of AASB 1060. The Board noted this requirement should not be too onerous for preparers, as they would be required to calculate these amounts in any case.

BC134 Some respondents to ED 297 questioned whether not restating comparative information would mean that an entity would be required to disclose two sets of accounting policies (ie one set to explain the basis of preparation of the comparative information and one set to explain the information for the reporting period). The Board decided not to provide specific requirements on the basis that the disclosure requirements of AASB 1060 and those contained within the relief required by the Board would provide sufficient information about the previous accounting policies in explaining the effect of the transition from SPFS to GPFS.

BC135 Because the purpose of this relief is to facilitate transition from SPFS to Tier 2 GPFS in a timely manner, rather than a general first-time adoption of GPFS, the Board decided to propose in ED 297 that the additional transitional relief from restatement of comparative information should not be available beyond the first year in which the Standard becomes effective. That is, on the assumption that the Board would have issued the Standard by 30 June 2020 with an effective date of 1 July 2020, the Board proposed the transitional relief in respect of comparative information would only be available for annual reporting periods beginning on or after 1 July 2020 but before 1 July 2021.

BC136 However, for the reasons set out in paragraph BC145-BC151, the Board decided to defer the effective date of the Standard by 12 months to 1 July 2021. Because the transitional relief from restating comparative information is intended to facilitate a timely transition from SPFS to GPFS, the Board decided that an extended effective date would remove the need for transitional relief. However, the Board decided to retain the transitional relief for entities that choose to adopt the requirements of this Standard and AASB 1060 prior to the effective date (ie that choose to early adopt). That Board decided that retaining this option would incentivise a timely transition to GPFS, helping to solve the SPFS problem sooner.

BC137 The Board also decided for pragmatic reasons that the transitional relief from restating comparatives will be available regardless of whether an entity had a legislative or other requirement to comply with AAS in prior periods.

Correction of errors in year of transition

BC138 With an objective to facilitate a timely transition to better quality financial reporting, the Board decided to also provide relief to entities from distinguishing errors from changes in accounting policies on transition from SPFS to GPFS-Tier 2. The Board noted this relief could be particularly relevant where an entity had claimed compliance with applicable R&M requirements in error. In such a case, there were diverse views as to whether an entity would be permitted to apply the transitional relief in AASB 1 based on the requirements of AASB 1053. As such, the Board decided to clarify in AASB 1053 that the applicability of AASB 1 (or AASB 108) relies on whether or not the entity complied with applicable R&M requirements, rather than whether the entity stated compliance with applicable R&M requirements. As such, an entity that discovered

an error in its previous SPFS would still be permitted to apply the transitional relief in AASB 1 (or elect to apply AASB 108).

- BC139 The Board also noted that the first-time adoption disclosures in AASB 1060 would generally require an entity to distinguish the correction of errors and changes in accounting policies in the notes. As such, to provide relief for preparers and facilitate a more timely transition to a GPFS framework, the Board decided not to require an entity to distinguish errors and accounting policies in the year of transition, noting that in any case all adjustments would be disclosed in the financial statements regardless of their nature. The Board considered whether such an amendment would affect any other obligations of those charged with governance with respect to prior period errors, however noted that such obligations would not be overridden. In making that decision, the Board noted that not distinguishing prior period errors from accounting policy changes may not meet the Conceptual Framework's qualitative characteristic of faithful representation, however the Board decided to make a trade-off with faithful representation to meet the Board's objective in these limited circumstances.

Scope of transitional relief

- BC140 In developing ED 297, the Board noted that entities already complying with the R&M requirements in AASB would not need transitional relief, given that such entities are required to continue applying the applicable R&M requirements in accordance with AASB 1053. However, many respondents to ED 297 considered that the transitional relief should be available to all entities impacted, regardless of whether the SPFS previously issued complied with all R&M requirements. Respondents noted that providing comparative information for disclosures that had not previously been made in an entity's most recent SPFS could be difficult, in particular when gathering information and preparing disclosures about related parties (including key management personnel) and income tax. The Board considered this feedback and decided that extending the relief to such disclosures would be reasonable to address stakeholder feedback and facilitate timely transition to GPFS. The Board decided to limit the relief only to instances where the comparative information had not previously been disclosed, on the basis that the entity would have all other comparative information available to them.
- BC141 The Board also decided that it would be appropriate to amend the requirements in AASB 1053 for the transition from SPFS to Tier 2 GPFS generally, as the Board was aware there were mixed views amongst stakeholders as to whether or not consolidation was to be considered a R&M requirement. The Board decided to make amendments to paragraph 18A to explicitly state that entities would be able to apply either AASB 1 (including the relief for preparing consolidated financial statements in Appendix C) or AASB 108 for first-time adoption of GPFS where a parent entity either:
- (a) did not apply the requirements of AASB 10 and hence did not prepare consolidated financial statements; or
 - (b) did not prepare consolidated financial statements on the basis that neither the entity nor the consolidated entity was not a reporting entity, and hence was not required by paragraph Aus4.2 to prepare consolidated financial statements where the entity was an ultimate Australian parent.
- BC142 In respect of BC141(b), the Board decided that even though such an entity would have technically complied with the R&M requirements of AASB 10 (because it was not required to consolidate), because the amendments in this Standard mean that the reference to a reporting entity in AASB 10 paragraph Aus4.2 is removed, the Board considered it appropriate to make available the same transitional relief as would be available for entities previously not complying with AASB 10. The Board considered whether to also extend such relief to entities preparing separate GPFS on the same basis (ie applying AASB 10 paragraph Aus4.2), however decided this would not be appropriate at this time as the extent of the entities impacted is currently unknown, but is expected to be limited, and as:
- (a) the Board expects that such entities should already have comprehensive IFRS-compliant information available to help produce consolidated financial statements, as the entity would be reporting that information to its parent; and
 - (b) entities currently preparing SPFS would also be required to provide new additional disclosure as well as potentially changes to R&M, hence it could be argued that not having such other challenges would mean entities already preparing GPFS would have enough resources to retrospectively consolidate.
- BC143 The Board considered whether to explicitly refer also to the equity method of accounting for investments in associates and joint ventures, and concluded that this was not necessary. As the equity method of accounting affects the measurement of the investments and the presentation in the statement of profit or loss and other comprehensive income, it is clear that the existing references in paragraph 18A to the R&M requirements of AAS cover application of the equity method. In any case, paragraph 9 of AASB 1053 now states that the R&M requirements include both consolidation and the equity method of accounting. The explicit references to consolidated financial statements added to paragraph 18A therefore emphasise their coverage.

BC144 The Board noted that paragraph 18A(a) and 18A(b) of AASB 1053 as amended would permit an entity to apply the transition relief available under AASB 1, and thus potentially restate recognised amounts, even if the previous SPFS applied all the applicable R&M requirements of AAS, except for the consolidation requirements in AASB 10.

Effective date

- BC145 In proposing an effective date in ED 297, the Board considered available policies and precedent, including:
- (a) the amendments to the tax law requiring SGEs to lodge GPFS with the ATO were issued in December 2015, and required lodgement to the ATO for ‘income years’ commencing on or after 1 July 2016. However, the ATO provided transitional concessions in the first year, whereby it allowed entities with reporting periods ending on 30 June 2017 additional time to lodge those financial statements, with lodgement due by 31 March 2018. It also permitted foreign-controlled entities to lodge financial statements in accordance with another set of Generally Accepted Accounting Principles (GAAP) other than AAS (eg US GAAP);
 - (b) the AASB issued the first principal version of AASB 1 in July 2004, prior to the effective date of full adoption of the Australian-equivalents to IFRS Standards of annual periods beginning on or after 1 January 2005. The FRC provided the AASB with the directive to adopt IFRS Standards in 2002. Given that all entities would have applied AASB 1 on Australia’s transition to IFRS Standards, this length of time is arguably indicative of how much time might need to be provided for a transition from SPFS to GPFS; and
 - (c) the now superseded AASB *Policies and Processes* outlines in paragraph 32 that “when determining the effective date of Standards the AASB seeks to ensure that constituents have adequate time to prepare for their implementation. In normal circumstances the AASB will issue a Standard a significant time before its effective date, say, during the previous annual reporting period and generally permits entities to apply those requirements early should they wish to do so”.
- BC146 The Board also noted that a timely effective date would be welcomed by users of financial statements, and may also be preferred by preparers. This is because:
- (a) the regulations in relation to the doubling of the thresholds used for determining what constitutes a large proprietary company are applicable to financial years beginning on or after 1 July 2019. The Board noted that the commentary contained in the Explanatory Statement to those regulations may be persuasive in an entity reconsidering its status as a non-reporting entity. As such, if entities were to reassess and determine that they were in fact a reporting entity, it would be preferable for the revised Tier 2 GPFS framework and the RCF to be applicable at the same time as for other publicly accountable for-profit private sector entities (annual periods beginning on or after 1 January 2020); and
 - (b) a large proportion of affected entities (76% - refer paragraph BC20) are already complying with the R&M requirements in AAS.
- BC147 As noted in the table in paragraph BC127, the Board also concluded that providing relief from restating comparative information in the year of transition would be particularly beneficial as it could allow for an earlier effective date. As such, with regard to the above considerations, the Board decided to propose an effective date of annual periods beginning on or after 1 July 2020 in ED 297. The Board noted this would effectively align with the effective date of the RCF, given most Australian for-profit private sector entities would have reporting dates of 30 June.
- BC148 Further, the Board noted the timeliness of completing this project, in order to provide an option for large proprietary companies to early adopt the RCF, applicable transitional relief and Tier 2 GPFS framework for periods beginning on or after 1 July 2019 (ie aligned with the doubling of the thresholds used for determining what constitutes a large proprietary company).
- BC149 Respondents to ED 297 expressed mixed views on the proposed effective date, with many recommending the Board defer the effective date by 1-2 years. Reasons for deferral suggested by respondents include:
- (a) to provide time for education, software and process changes;
 - (b) challenges caused by first-time consolidation, for example gathering AAS-compliant information from subsidiaries;
 - (c) deferring the effective date would dismiss the need for transitional relief;
 - (d) the *AASB Due Process Framework for Setting Standards* (September 2019) (Due Process Framework) suggests an implementation period of 2 years in typical cases; and

- (e) whilst the effective date appeared appropriate for entities that should have been complying with RG 85 (ie entities required to prepare financial statements in accordance with the *Corporations Act 2001*), it may be too soon for other for-profit entities within the scope that had not previously had RG 85 to guide their financial reporting framework.

BC150 In addition, because ED 297 and ED 295 are complementary – that is, the revised Tier 2 framework is an integral piece of the removal of SPFS – the Board also considered the comments to ED 295 addressing the effective date, which included in addition to the responses noted above:

- (a) that the revised Tier 2 framework should be delayed until the direction of the IASB’s *Subsidiaries that are SMEs* project is finalised, due to the multiple framework changes that could occur if the AASB were to adopt the IASB’s solution shortly after implementing its own simplified disclosure standard; and
- (b) to give time for the NZASB to decide the direction for its own Tier 2 framework in an attempt to retain trans-Tasman convergence for for-profit entities.

BC151 The Board considered a range of options to determine the most appropriate solution to balance the urgency of solving the SPFS problem whilst providing sufficient time for stakeholders to transition:

Option	Advantages	Disadvantages
<p>Option 1</p> <ul style="list-style-type: none"> Effective date of 1 July 2021 Transitional relief available to all entities (R&M compliant and non-compliant) <u>which elect to early adopt</u> No transitional relief to entities adopting from 1 July 2021 	<ul style="list-style-type: none"> Stakeholders will have more time to prepare for the significant change to the financial reporting framework including education and collation of historical information Transitional relief may incentivise voluntarily early adoption The effective date would be consistent with the AASB’s Due Process Framework that suggest an implementation period of 2 years Retaining transitional relief for those that early adopt provides an incentive to transition in a timely manner Software providers have expressed concerns about their ability to create templates in a timely manner and also the presentation of ‘mixed’ comparatives 	<ul style="list-style-type: none"> Effective date would not be aligned with the change in proprietary company thresholds. Large proprietary companies would likely need to prepare GPFS prior to the effective date to be consistent with Treasury’s expectations regarding GPFS financial report by large proprietary companies There is a strong desire for transparent and high-quality financial statements. The recent parliamentary inquiry highlighted even more the need for change in financial reporting. Delaying the effective date is inconsistent with this
<p>Option 2</p> <p>No change to transitional relief and effective date</p>	<ul style="list-style-type: none"> Effective date would be aligned with the change in proprietary company thresholds The project will be completed more quickly, therefore responding to the strong desire for transparent and high-quality financial statements and recent parliamentary inquiry There are only a maximum of 7,295 entities expected to be effected, and with the effect for the majority of these entities (5,589) expected to be limited to providing additional disclosures only coupled with the 	<ul style="list-style-type: none"> Stakeholders are concerned they do not have sufficient time to prepare for such a significant change to the financial reporting framework including education and collation of historical information. However, research strongly suggests that deferring the effective date of new standards does not necessarily result in entities using the extended lead time to better prepare for the new requirements, instead it is often used to delay starting to prepare.⁴⁴ Software providers have expressed concerns about their ability to create templates in a timely manner and

44 Davern, M., Gyles, N., Potter, B. and Yang, V. (2019), "Implementing AASB 15 revenue from contracts with customers: the preparer perspective", *Accounting Research Journal*, Vol. 32 No. 1, pp. 50-67. <https://doi.org/10.1108/ARJ-03-2018-0055>.

Option	Advantages	Disadvantages
	transitional relief an earlier effective date was considered reasonable	also the presentation of 'mixed' comparatives <ul style="list-style-type: none"> The effective date is not consistent with the AASB's Due Process Framework that suggest an implementation period of 2 years
Option 3 <ul style="list-style-type: none"> Effective date of 1 July 2021 No transitional relief 	<ul style="list-style-type: none"> Similar as those for Option 1 above Transition requirements would be consistent with those applied by SGEs 	<ul style="list-style-type: none"> Similar as those for Option 1 above There is no incentive for entities to early adopt
Option 4 <ul style="list-style-type: none"> Extend the effective date of both standards to 1 July 2021 with the transitional relief applicable only to entities' first time consolidation 	<ul style="list-style-type: none"> Similar as those for Option 1 above Research Report 12 does not address the number of financial reports which were presented on a consolidated or separate basis, it is difficult to quantify the number of affected entities. As such the entities preparing first time consolidation would be given extra time to prepare for any changes that might be required 	<ul style="list-style-type: none"> Disadvantages of deferred effective date similar as for Option 1 above
Option 5 Staggered implementation <ul style="list-style-type: none"> Corporations Act entities to apply the requirements in year one Effective date deferred by a further year for all other entities in scope 	<ul style="list-style-type: none"> Effective date would be aligned with the change in proprietary company thresholds. All entities regulated by Corporations Act, which are in the scope of this Standard would comply with R&M requirements of AAS in a timely manner It is expected that entities required to prepare financial reports in accordance with the <i>Corporations Act 2001</i> should already be complying with the R&M requirements in AAS - as there are only a maximum of 7,295 entities expected to be effected, this option is not expected to be too onerous for Corporations Act entities. As the population of other entities is unknown, and they do not have a RG 85 equivalent, an additional year to prepare would be beneficial 	<ul style="list-style-type: none"> The resolution of the problems with SPFS reporting would take an additional year for entities not regulated by the Corporations Act

BC152 The Board ultimately decided that Option 1 provided the most appropriate solution, for the reasons set out in paragraph BC151 above.

BC153 In respect of the issues raised in respect of the revised Tier 2 framework (see paragraph BC150), the Board decided that the need to remove SPFS for the entities within the scope of this Standard in a timely manner would mean that waiting for the IASB and retaining trans-Tasman convergence (in the short term) would not meet the objective of the project (see the Basis for Conclusions to AASB 1060 for the Board's considerations on these matters).

Application of The AASB's For-Profit Entity Standard-Setting Framework

- BC154 In developing the Standard the Board considered the principles in *The AASB's For-Profit Entity Standard-Setting Framework*, which outlines the matters the Board must consider when determining whether or not to make amendments to IFRS Standards or develop Australian-specific guidance.
- BC155 *The AASB's For-Profit Entity Standard-Setting Framework* states that, when developing accounting standards for non-publicly accountable for-profit entities, the AASB's objective is to use IFRS Standards and transaction neutrality as a starting point, with modifications where justified to address:
- (a) Australian-specific legislation, user needs, or public interest issues relevant to financial reporting or beyond financial reporting;
 - (b) issues specific to the (for-profit) public sector of such prevalence and magnitude that users are likely to make inappropriate decisions based on the financial statements;
 - (c) where the objectives and qualitative characteristics of financial reporting as set out in the existing Conceptual Framework would not be met; and/or
 - (d) undue cost or effort considerations.
- BC156 Consistent with this, the Board decided standard-setting activities as reflected in this Standard were necessary after undertaking the following (as already noted throughout this Standard):
- (a) extensive public consultation and outreach including ITC 39 and ED 297, research into the needs of financial statement users (eg public surveys and targeted outreach), feedback obtained from stakeholders (including users) who participated in roundtable events, along with other general and targeted outreach with stakeholders;
 - (b) engaging with Treasury and assessing the impact of regulatory changes to large proprietary companies, including understanding the number of entities expected to be affected by the increase in the large proprietary company thresholds from this Standard;
 - (c) the preparation and review of various research reports, including Research Report No. 1, AASB Research Report No. 4 *Review of Adoption of International Financial Reporting Standards in Australia* (March 2017), AASB Research Report No. 7 and Research Report 12 to understand the current application of the reporting entity concept, as well as to understand the degree of non-compliance with the R&M requirements in AAS. The objective of these research activities was to better understand the cost implications of disallowing entities required to prepare financial statements that comply with AAS to prepare SPFS and require them to prepare GPFS instead;
 - (d) considering whether it was necessary to provide transitional relief in addition to that currently available under AASB 1 and AASB 108 with the objective of minimising any undue costs in relation to both the transition from SPFS to GPFS and the associated disclosure requirements; and
 - (e) a consideration of matters relevant to Regulation Impact Statement (RIS) requirements.

Amendments required to implement Phase 2

- BC157 As noted in paragraph BC54, in May 2019 the Board made AASB 2019-1 to implement Phase 1 of the Board's phased approach to implementing the IASB's RCF in Australia, limiting the application of the Board's *Conceptual Framework for Financial Reporting (Conceptual Framework)* to for-profit private sector entities with public accountability that are required by legislation to prepare financial statements that comply with AAS.
- BC158 In this Standard, to facilitate the implementation of Phase 2, the following amendments are made:
- (a) the applicability of the *Conceptual Framework* is extended so that it applies to:
 - (i) for profit-private sector entities that are required by legislation to comply with either Australian Accounting Standards or accounting standards (with the previous limitation to entities with public accountability removed);
 - (ii) other for-profit private sector entities that are required only by their constituting document or another document to comply with Australian Accounting Standards (and so excluding requirements to comply merely with 'accounting standards'), provided that the relevant document was created or amended on or after 1 July 2021; and
 - (iii) other for-profit entities (including for-profit public sector entities) that elect to prepare GPFS; and

- (b) the existing Conceptual Framework and SAC 1 are also amended so that they do not apply to all for-profit entities that are applying the *Conceptual Framework*. Consequential amendments are made to the applicability of the reporting entity definition in AASB 1057, which is not relevant to entities applying the *Conceptual Framework*.
- BC159 Therefore, with these amendments, an entity that is required to apply the *Conceptual Framework* cannot identify as a non-reporting entity under SAC 1 or AASB 1057. As a consequence, the ability of such an entity to prepare SPFS is removed and the entity will be required to prepare GPFS that comply with AAS (or accounting standards under legislative requirements). For the avoidance of doubt, an entity applying the *Conceptual Framework* cannot apply the definition of reporting entity outlined in SAC 1 or AASB 1057.
- BC160 The application paragraph of AASB 1057 is extended to state that it will apply to for-profit private sector entities that are required by legislation to comply with either AAS or accounting standards, and other for-profit private sector entities that are required only by their constituting document or another document to comply with AAS (provided that the relevant document was created or amended on or after 1 July 2021). The application paragraphs of the other Standards and Interpretations, as set out in AASB 1057, are extended similarly.
- BC161 In respect of entities that voluntarily choose to prepare GPFS, the Board proposed in ED 297 to permit such entities to apply either the revised *Conceptual Framework* or the *Framework for the Preparation and Presentation of Financial Statements*. However, many respondents disagreed with this proposal, and preferred that voluntary GPFS preparers are restricted to applying only the revised *Conceptual Framework*. In response, the Board decided to require entities that voluntarily prepare GPFS to apply the revised *Conceptual Framework* once it becomes applicable. The Board considered that allowing either framework for voluntary GPFS preparation could perpetuate problems that this Standard intended to resolve, such as maintaining two conceptual frameworks (which will anyway occur in the medium term due to other exemptions), creating confusion about what compliance with AAS means, and two entities preparing GPFS may adopt different accounting policies for like transactions. Allowing either framework also means that preparing GPFS would not necessarily lead to IFRS compliance.
- BC162 The AusCF paragraphs in AAS that were introduced in AASB 2019-1 do not need to be amended in this Standard. The definition of AusCF entities as NFP entities and for-profit entities that are not applying the *Conceptual Framework*, as introduced in AASB 2019-1, will continue to apply, but with a limited scope such that those paragraphs would only be relevant to FP entities not within the scope of this Standard. The phase 2 amendments reduce the set of for-profit entities that are not applying the *Conceptual Framework*.