Still large & prepare SPFS?

Reporting Update

17 April 2020, 20RU-009

Highlights

- Thresholds double
- Significant economic influence – 30 June 2020 & 2021
- Removal of SPFS – effective from 1 July 2021
- Options for 30 June 2020

Thresholds double

In April 2019 the government registered the *Corporations Amendments (Proprietary Company Thresholds) Regulations 2019*. Details of this change are discussed in 19RU-004 Proprietary company threshold: When large becomes small.

Small/large thresholds doubled

The new regulation doubles the thresholds for determining whether a company is a large or small proprietary company for a financial year. A proprietary company is large if it meets **two** of the three thresholds at the end of its financial year. Otherwise it is small. The table below outlines the three thresholds.

Threshold	Financial years beginning before 1 July 2019	Financial years beginning from 1 July 2019
Consolidated revenue for the financial year *	$25 million or more	$50 million or more
Consolidated gross assets at the end of the financial year *	$12.5 million or more	$25 million or more
Employees^ of the company and the entities it controls	50 FTE employees or more	100 FTE employees or more

*For the company and any controlled entities
^Part-time employees are counted as an appropriate fraction of the full-time equivalent (FTE)

Under the *Corporations Act 2001* (Corps Act), large proprietary companies are required to lodge an annual financial report, a director's report and an auditor's report with ASIC. Small proprietary companies have no such requirement to lodge (unless directed to by ASIC or directed by 5% or more of their shareholders).

30 June 2020?

The above change applies in relation to financial years beginning on or after 1 July 2019 – i.e. 30 June 2020 year ends.

Call to action!

Call to action!

The explanatory statement to the regulation change and subsequent commentary by both the AASB and ASIC has raised the issue around the ability of proprietary companies that remain large to continue preparing special purpose financial statements (SPFS) – before the effective date of the changes in AASB 2020-2 *Amendments to Australian Accounting Standards – Removal of Special Purpose Financial Statements for Certain For-Profit Private Sector Entities)*.
Further detail is discussed on the following pages.

Significant economic influence - 30 June 2020 & 2021

Significant economic influence

The key issue is around **large proprietary** companies and 'significant economic influence' – which is a major component in the definition of a reporting entity discussed in SAC1 *Definition of the Reporting Entity*. Further detail on the reporting entity discussion is outlined in Appendix 1.

The following are relevant extracts on large proprietary companies and 'significant economic influence'.

Explanatory statement (to regulation change)

"The requirement for large proprietary companies to lodge and audit their financial reports was introduced in 1995 to focus regulation of reporting on the financial affairs of proprietary companies which have a significant economic influence.

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 general purpose financial reports as a basis for making economic decisions.

The increased thresholds provided in the Regulations will ensure financial reporting obligations are targeted at economically significant companies, while reducing costs for smaller sized companies that will no longer be required to lodge audited financial reports with ASIC."

ASIC Commissioner – John Price

Impact large proprietary companies

"With doubling of 'large' proprietary company thresholds, directors of large proprietary companies currently preparing their SPFS will likely no longer be able to do so for years ending 30 June 2020."

AASB 2020-02 – Basis for conclusions

"BC35
The Board (AASB) 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* 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."

Thresholds reflect economic significance

KPMG comment

"For those large proprietary companies that are planning to prepare SPFS for 30 June 2020 reporting dates the directors should re-evaluate their reporting entity status in light of the above commentary.

Consult with users

The AASB has stated that it expects that the directors or those charged with governance will need to consult with their users to determine an appropriate basis of preparation (including selection of appropriate accounting policies) when next preparing financial statements. This may be consistent with the most recent SPFS.

Robust process documented

The issue is that the directors or those charged with governance will need to establish a process for the above consultation with users. This process should consider all users of the financial statements including owners, bankers, creditors, employees and any applicable regulators. The process will need to be robust and should be undergone each time the entity prepares financial statements. We would recommend that this process be appropriately documented."

Michael Voogt
Director, Department of Professional Practice

Removal of SPFS - effective from 1 July 2021

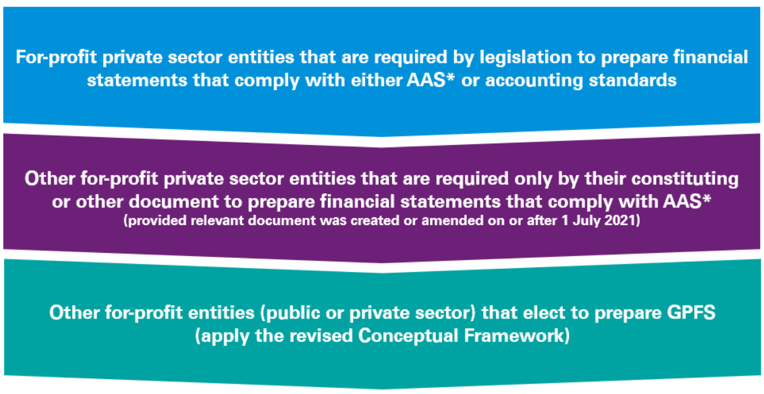
Phase Two of the Australian Accounting Standards Board (AASB) approach to adopting the revised *Conceptual Framework for Financial Reporting* (RCF) has been achieved.

The ability of certain for-profit private sector entities (which includes large proprietary companies) to prepare SPFS has been removed. These entities will be required to prepare a form of general purpose financial statements (GPFS). The amendments (set out in AASB 2020-2) were approved by the AASB in March 2020. These amendments will work in conjunction with the new GPFS-Tier 2 SD standard, AASB 1060 *General Purpose Financial Statements – Simplified Disclosures (SD) for For-Profit and Not-for-Profit Tier 2 Entities.*

Both AASB 2020-2 and AASB 1060 will apply for financial reporting periods beginning on or after 1 July 2021, with early adoption permitted. Both standards need to be applied at the same time.

Who is impacted?

AASB 2020-2 & AASB 1060



* Australian Accounting Standards

This means that for-profit entities regulated by ASIC (for example, large proprietary companies, and small foreign-owned companies) who may be currently preparing SPFS will need to prepare and lodge GPFS – either Tier 1 or Tier 2.

Appendix 2 provides a flow diagram of the Australian private sector financial reporting framework and what basis financial statements will now be required to be prepared, from annual periods beginning on or after 1 July 2021.

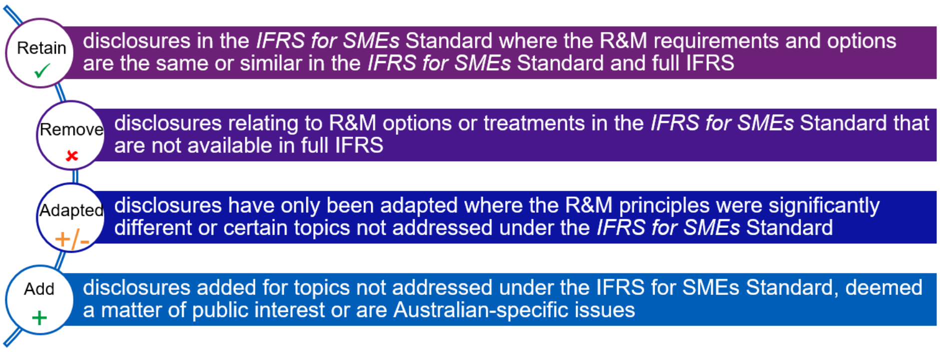
New Tier 2 reporting framework

A single SD standard to replace RDR

AASB 1060, a new single GPFS-Tier 2 SD standard, replaces the current suite of Reduced Disclosure Requirements (RDR) disclosures. It will apply to all entities preparing financial statements under Tier 2, both:

- those currently reporting under the existing RDR Framework, and
- those that will be required to stop preparing SPFS and be required to prepare GPFS and are permitted to apply the new GPFS-Tier 2 SD (as described above).

AASB 1060 is principally based on the disclosures included in the *IFRS for SMEs Standard*, with some adjustment for the Australian context. From that basis, the general methodology for development of disclosures was:

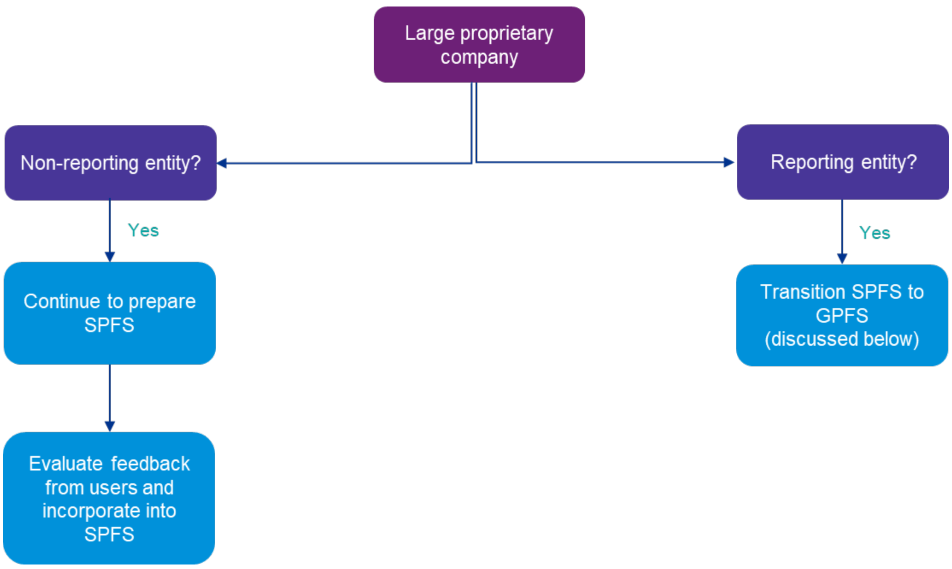


Further details on these changes are discussed in 20RU-006 Farwell SPFS … Welcome SD.

30 June 2020

Options for 30 June 2020

Large proprietary companies, that do not early adopt AASB 2020-2 and AASB 1060, may continue to self-assess whether or not they are a reporting entity – as defined in SAC 1. This is the current 'state of play' that applied for 30 June 2019.



When assessing we recommend that you:

- consult with **all** users of your financial statements to understand their needs (basis of preparation and accounting policies applied)
- document your robust processes to consider the above.

Refer to Appendix 3 for further discussion on a process to evaluate an entities reporting entities status.

Transition from SPFS to GPFS

If need to transition

AASB 1053 *Application of Tiers of Australian Accounting Standards* provides guidance when an entity needs to transition from preparing SPFS to GPFS.

When transiting the entity first needs to determine whether it will transition to:

- GPFS-Tier 1
- GPFS-Tier 2 RDR (can make this choice only for years ending before the application of AASB 1060)
- GPFS-Tier 2 SD.

GPFS-Tier 2 RDR

SPFS → GPFS-Tier 2 RDR

An overview of transitioning from SPFS to GPFS-Tier 2 RDR is provided in Appendix 4. No specific transitional relief is provided when moving from SPFS to GPFS-Tier 2 RDR.

Guidance on apply AASB 1 *First-time Adoption of Australian Accounting Standards*, for example first time consolidation can be found in KPMG's *Insights into IFRS* (Chapter 6).

KPMG comment

"Given:

- **the changes in the larger proprietary thresholds (Corps Act) – which impact years ended 30 June 2020 (and onwards), and**
- **the government/regulator discussion around larger proprietary companies having economic significance**

entities will need to reconsider whether they still qualify as a non-reporting entity in accordance with SAC 1 (refer to discussion above). Where this is not the case entities will need to prepare GPFS.

Where GPFS are required for 30 June 2020, entities will need to assess whether to apply GPFS Tier 2 RDR or GPFS Tier 2 SD. In such cases we would recommend that the entity elect to apply GPFS Tier 2 SD – otherwise they will need to transition from RDR to SD at 30 June 2022 (i.e. transition twice in two years)."

Michael Voogt
Director, Department of Professional Practice

GPFS-Tier 2 SD

SPFS → GPFS-Tier 2 SD

Details on transitioning from SPFS to GPFS-Tier 2 SD are discussed in 20RU-006 Farwell SPFS … Welcome SD. The AASB has provided some detailed transitional relief when an entity adopts AASB 2020-2 and AASB 1060 as a practical consideration to reduce costs incurred by entities when transitioning.

An overview of transitioning from SPFS to GPFS-Tier 2 SD is provided in Appendix 5.

Other entities

Grandfathered companies

Grandfathered companies (under Corps Act)

Large proprietary companies that were exempt proprietary companies under the old Corporations Law are not required to lodge their audited financial reports with ASIC, provided they met certain conditions. These companies must still prepare audited financial reports and distribute them to members.

Grandfathered companies can continue to prepare SPFS where they continue to be a non-reporting entity – before the effective date of the changes in AASB 2020-2 (financial reporting periods beginning on or after 1 July 2021).

On the adoption of AASB 2020-2 grandfathered companies will need to prepare GPFS in order to maintain their status.

Small Pty companies

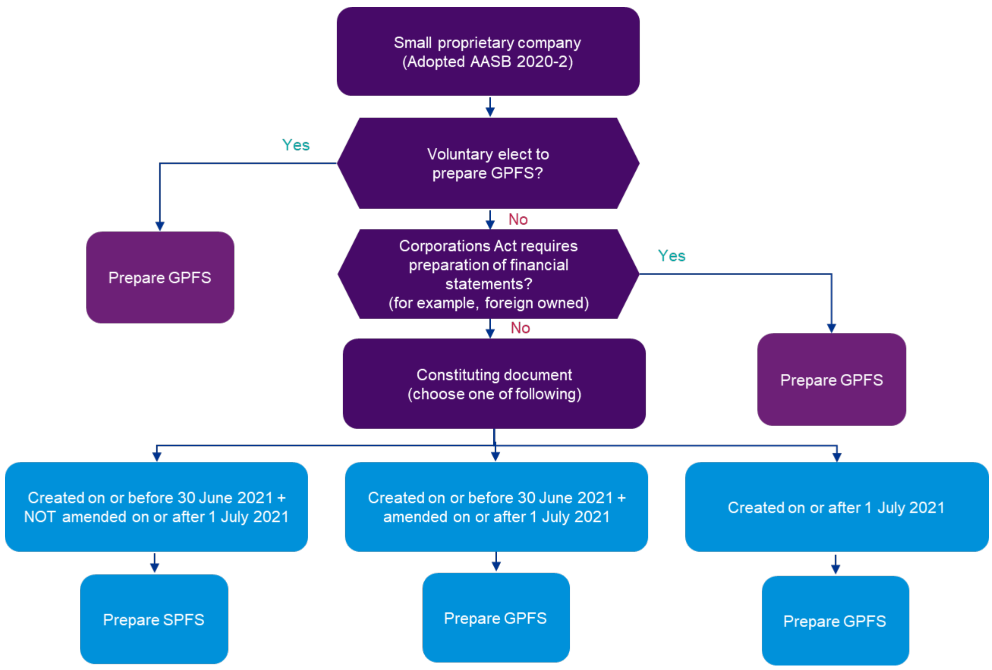
Small proprietary companies

Small proprietary companies can continue to self-assess their reporting entity status. Small proprietary companies can continue to prepare SPFS where they continue to be a non-reporting entity – before the effective date of the changes in AASB 2020-2 (financial reporting periods beginning on or after 1 July 2021).

With the introduction of AASB 2020-2, SAC 1 has been amended. For financial reporting periods beginning on or after 1 July 2021, SAC 1 cannot be applied to:

- for-profit private sector entities that are required by legislation to prepare financial statements that comply with either AAS or accounting standards
- other for-profit private sector entities that are required only by their constituting document or another document to prepare financial statements that comply with AAS provided that the relevant document was created or amended on or after 1 July 2021
- other for-profit entities (private sector or public sector) that elect to prepare GPFS.

So after the application of AASB 2020-2 the following will apply for small proprietary companies.



More resources

A broader understanding and more details of the Australian Financial Reporting Framework project is available on our dedicated webpage at www.kpmg.com/au/gpfs.

We will be releasing more resources to support your implementation of the new Australian Financial Reporting Framework. Watch this space!

Appendix 1 - Extract from SAC 1

Identification of Whether Dependent Users Exist

19 For the purposes of this Statement, the identification of an entity as a reporting entity is linked to the information needs of users of general purpose financial reports. In many instances, it will be readily apparent whether, in relation to an entity, there exist users who are dependent on general purpose financial reports as a basis for making and evaluating resource allocation decisions. For those entities in respect of which it is not readily apparent whether such dependent users exist, the factors outlined in paragraphs 20 to 22 are identified as the primary factors to be considered in determining whether a reporting entity exists. These factors are indicative only, and are not the only factors that will be relevant in determining whether, in a particular circumstance, an entity is a reporting entity.

Separation of management from economic interest

20 The greater the spread of ownership/membership and the greater the extent of the separation between management and owners/members or others with an economic interest in the entity, the more likely it is that there will exist users dependent on general purpose financial reports as a basis for making and evaluating resource allocation decisions.

Economic or political importance/influence

21 Economic or political importance/influence refers to the ability of an entity to make a significant impact on the welfare of external parties. The greater the economic or political importance of an entity, the more likely it is that there will exist users dependent on general purpose financial reports as a basis for making and evaluating resource allocation decisions. Reporting entities identified on the basis of this factor are likely to include organisations which enjoy dominant positions in markets and those which are concerned with balancing the interests of significant groups, for example, employer/employee associations and public sector entities which have regulatory powers.

Financial characteristics

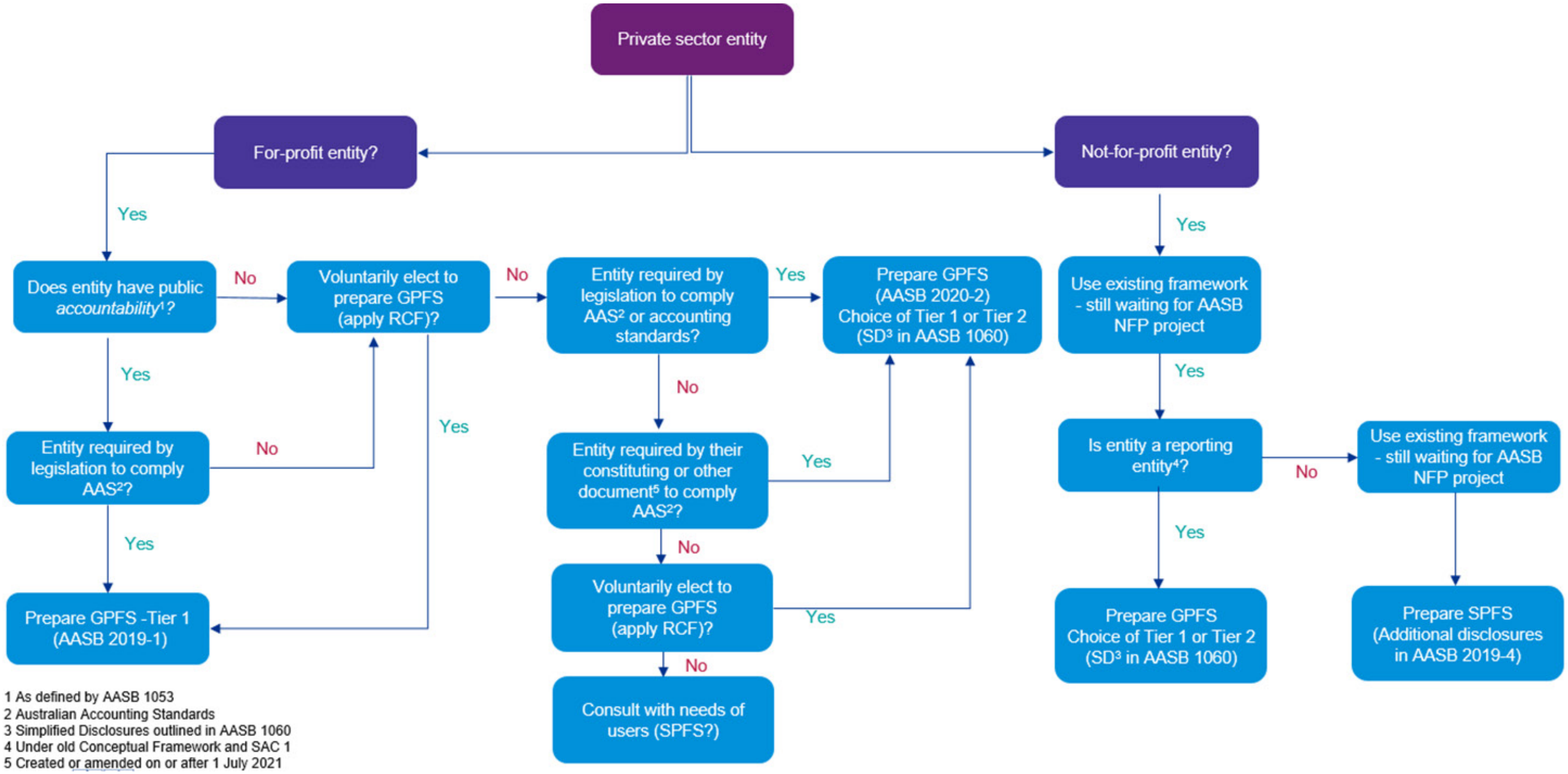
22 Financial characteristics that should be considered include the size (for example, value of sales or assets, or number of employees or customers) or indebtedness of an entity. In the case of non-business entities in particular, the amount of resources provided or allocated by governments or other parties to the activities conducted by the entities should be considered. The larger the size or the greater the indebtedness or resources allocated, the more likely it is that there will exist users dependent on general purpose financial reports as a basis for making and evaluating resource allocation decisions.

KPMG comment

"All of these factors need to be considered. The fact that there is little separation between the management and ownership of an entity does not mean that the company is not a reporting entity. The other factors need to be given equal consideration."

Michael Voogt
Director, Department of Professional Practice

Appendix 2 - Australian Private Sector Financial Reporting Framework



1 As defined by AASB 1053
2 Australian Accounting Standards
3 Simplified Disclosures outlined in AASB 1060
4 Under old Conceptual Framework and SAC 1
5 Created or amended on or after 1 July 2021

Appendix 3 - Evaluation of reporting entity status

Process

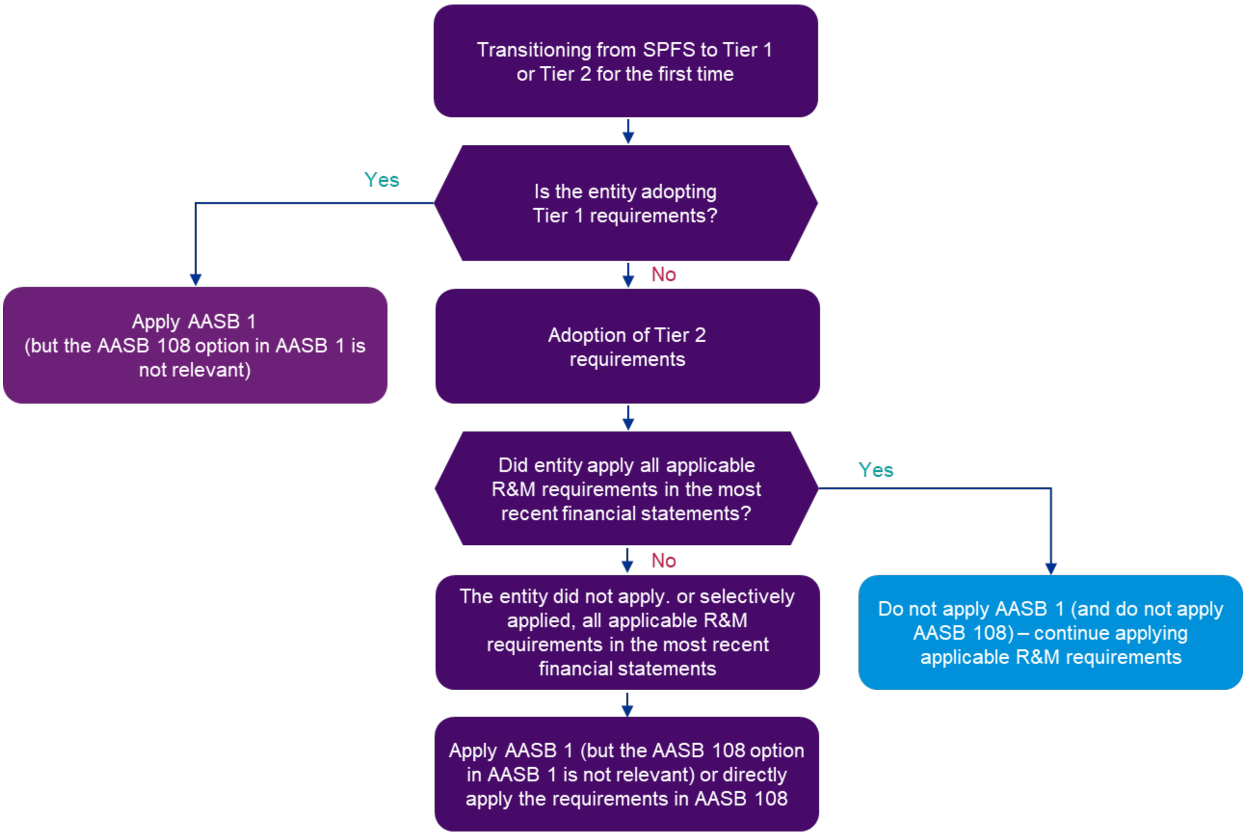
There can never be a definitive checklist developed in deciding whether an entity is a reporting entity or not – judgement is required – each entity will need to be considered on a case-by-case basis.

The following process may assist:

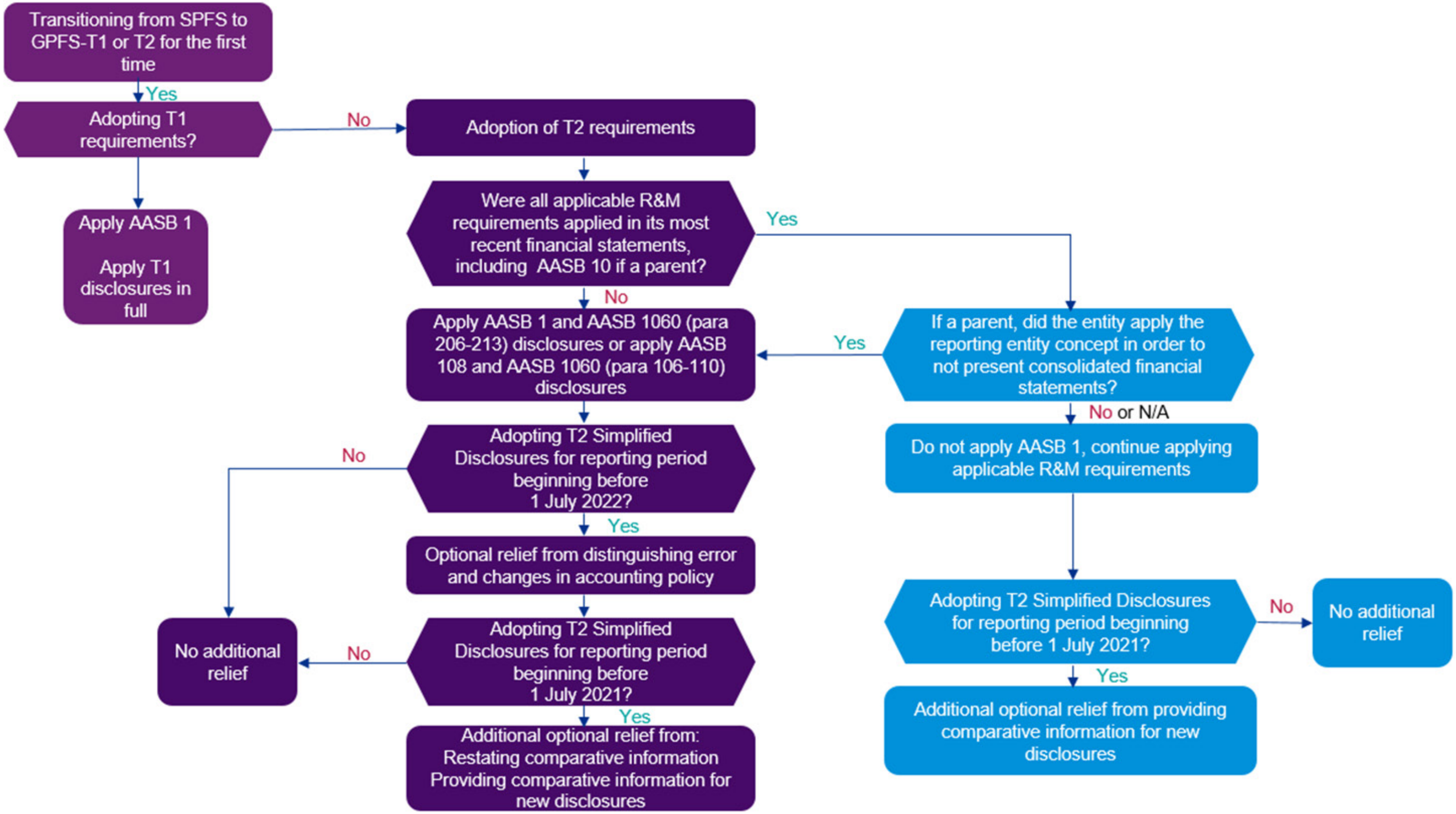
- Identify all financial statement users – consider shareholders, management, customers, creditors, employees, lending institutions, and any others unique to your entity.
- For each group of user identified consider if they are likely to rely on general purpose financial information – or do they obtain information about the entity they control/deal with in other forms. For example:
  - those who can demand specific information to suit their needs (lending institutions, majority shareholders)
  - those who may perform credit checks from external information providers (for example creditors)
  - those who may obtain information for other parties – for example – superannuation plans are required to mail out certain financial information to all fund members
  - those who may obtain general purpose financial information of a parent entity.
- Consider the nature of the clients operations and whether they have a high level of economic or political importance/influence.
- Consider the ASIC explanatory statement to the *Corporations Amendment (Proprietary Company Thresholds) Regulations 2019* and subsequent commentary by both the AASB and ASIC has raised the issue around the ability of proprietary companies that remain large to continue preparing special purpose financial statements (SPFS) – before the effective date of the changes in AASB 2020-2 *Amendments to Australian Accounting Standards – Removal of Special Purpose Financial Statements for Certain For-Profit Private Sector Entities*).
- If an entity was to present a special purpose financial report, identify what information would not be disclosed in the report.
- For the (non) disclosures identified above assess what the impact of non-disclosure of this information would have on the identified financial statement users. For example if the entity has a large number of transactions with a foreign parent at other than "fair value" and is proposing not to include AASB 124 disclosures relating to transactions with the ultimate parent.

Documentation should focus on those disclosures being omitted to assess their impact on the information required by users.

Appendix 4 - Overview transition from SPFS to GPFS-Tier 2 RDR



Appendix 5 - Overview transition from SPFS to GPFS-Tier 2 SD



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