

14 December 2018

Ms Kate O'Rourke
Principal Adviser
Corporations Policy Unit
Consumer and Corporations Division
The Treasury
Level 5, 100 Market Street
SYDNEY NSW 2000

By email: reportingthresholds@treasury.gov.au

Dear Ms O'Rourke

Treasury Consultation - Reducing the financial reporting burden by increasing the thresholds for large proprietary companies

As the representatives of over 200,000 professional accountants in Australia, Chartered Accountants Australia and New Zealand (Chartered Accountants ANZ) and CPA Australia welcomes Treasury's decision to consult on increasing the thresholds that define a large proprietary company under section 45A of the *Corporations Act 2001* ("the Act").

Chartered Accountants ANZ and CPA Australia have both long held the view that these lodgement thresholds should be regularly reviewed to ensure that the regulatory framework they underpin is fit for purpose. In a joint letter to Treasury in October 2018 we called for comprehensive threshold reform and we appreciate Treasury's response to our concerns through this consultation.

Thresholds

The proposed increase in thresholds set out in the draft Regulations will help address the concerns of our members around excessive regulatory burden on smaller, but currently "large" proprietary companies. Such a revision bring these thresholds more into line with current, rather than outdated, levels of economic activity that can support "economic significance" as a basis of lodgment.

Therefore we support, in principle, the proposed doubling of the large proprietary company thresholds as set out in the draft *Corporations Amendment (Proprietary Company Thresholds) Regulations 2018*.

Representatives of the Australian Accounting Profession



cpaaustralia.com.au



charteredaccountantsanz.com

However, we suggest that Treasury release the analysis behind the numbers that have been chosen to target “larger, more economically significant companies”. This is necessary to ensure that the proposed approach is consistent with the capture of these entities using the “two out of three” test of revenue, assets and employees. Without such evidence, doubling the current levels perpetuates the arbitrary number choices that underlie the existing thresholds within the Act, and would mean any further “indexation based reviews” would be similarly flawed.

Feedback we have received indicates that while a doubling of both the thresholds for revenue and assets is consistent with an entity’s economic growth pattern, a similar doubling of employee numbers may not also occur. As Australia has moved away from a manufacturing to a service based economy over recent years, and as automation and the use of contractors has grown, it is possible that the revenue/assets generated per employee is now higher than it was when the thresholds were last raised in 2007. We therefore recommend Treasury review the doubling of employee numbers to ensure it is proportional and appropriate.

Treasury should also consider the impact of new accounting standards that begin to apply from 30 June 2019 and 30 June 2020 year ends. These standards, AASB 9 *Financial Instruments*, AASB 15 *Revenue from contracts with customers*, and AASB 16 *Leases* will impact the foundations of the revenue, income and asset numbers companies will be reporting once they are applied. In particular AASB 16 is expected to result in the inclusion of many lease assets onto balance sheets that were previously not accounted for in this way. Therefore Treasury’s analysis may need to be revised to take account of these imminent changes.

Effective date

We are not supportive of the proposal that these changes should be implemented for financial years beginning on or after 1 July 2019. This timeframe is too soon because threshold reform, while necessary and important, is just one step in a much broader reform agenda, discussed below, that still needs completion. We recommend delaying the implementation of the change in thresholds until this broader reform agenda is complete.

The broader reform agenda

This Treasury consultation is timely given the Australian Accounting Standards Board’s (AASB) current “Reporting Entity Concept” project (ITC 39). It proposes a significant overhaul of Australia’s financial reporting framework, seeking to ensure that the framework remains fit for purpose and requires the preparation of financial information that serves the information needs of investors and other stakeholders including the general public.

Since our members work in diverse roles across public practice, commerce, industry and academia throughout Australia, they have a significant interest and stake in this reform agenda, and in threshold reform, which represents a critical component of that framework.

Representatives of the Australian Accounting Profession



cpaaustralia.com.au



charteredaccountantsanz.com

While the proposal to increase the large proprietary company thresholds is a welcome step, such change is only a partial solution to a bigger question. Raising thresholds seeks to address the challenge of “who” needs to report while the AASB project mentioned above seeks to address the challenge of “what” needs to be reported. Achieving more holistic reform that meets the needs of the Australian economy and stands the test of time will require Treasury to work closely with the AASB to ensure alignment of “who” needs to report, and “what” needs to be reported.

If thresholds are revised independent of the AASB project, the reform could fail to ensure that all entities for which there exists genuine user need for publicly available audited financial reports, are adequately catered for. Our feedback suggests that such user need does exist, and could not be otherwise met, for some of the entities that would become “small” as a result of the proposed threshold change.

A more nuanced, yet simple, reporting framework could better ensure that all those with legitimate needs for assured financial information can access such information without placing a disproportionate burden on preparers. Such a framework would also ensure that all those entities enjoying the benefits of limited liability are adequately regulated in the public interest and that the necessary support infrastructure, such as a viable audit profession can be maintained. Our members are already concerned that an audit is now the principal means of regulatory oversight for many currently large proprietary companies. Removing that oversight without careful consideration, especially if it is not replaced by more active oversight by relevant regulators, may not be beneficial to these entities, the economy and the public interest in the long term.

Effective financial reporting framework reform needs detailed investigation into user needs combined with a cost/benefit analysis so that consistent and evidence-based answers exist to the questions of “who” needs to report and “why” they need to do so. This information can then support the AASB’s work to identify “what” those lodging entities need to report to best meet those user needs.

It is therefore critical that Treasury remain actively involved in the wider financial reporting framework reform project being led by the AASB.

Other important matters

The proposed increase in thresholds also ignores a number of other important related issues that still need addressing. We have highlighted these below and recommend that Treasury take them into consideration when furthering the proposals.

Entities other than large proprietary companies

The proposals fail to effectively address the information needs of users of the financial reports of small proprietary companies that currently:-

- Report under the Act as a result of direction from ASIC or from shareholders with a least 5% of the vote;

Representatives of the Australian Accounting Profession



cpaaustralia.com.au



charteredaccountantsanz.com

- Report under the Act because they are foreign controlled;
- Are subject to the *Corporations Amendment (Crowd-sourced Funding for Proprietary Companies) Act 2018* and so are required to prepare and lodge financial reports, and, if they raise more than \$3 million, have these reports audited; and
- Meet the definition of a “Significant Global Entity” and so are required to prepare and lodge audited general purpose financial statements under section 3CA of the *Taxation Administration Act 1953*.

All these entities are not necessarily economically significant, by virtue of their size, but are required to be accountable to their shareholders, and other users, including regulators, for different reasons. These different reasons, and their different circumstances, may be enough to mean that it is inappropriate to require the same level and type of financial reporting information, and associated burden of audit, that is imposed on their economically significant, large proprietary counterparts.

Raising thresholds also creates a larger number of small proprietary companies to which financial reporting, audit and lodgement requirements may no longer apply. As stated above, feedback we have received indicates that some form of potentially mandatory public reporting and assurance, as well as more active regulatory oversight may be needed to meet the needs of both their internal and external stakeholders. Such mandatory reporting may also assist entities preparing for transition to “large” given the thresholds are point in time values which can pose a risk of entities moving in and out of them, unless a more flexible system can be developed.

Public companies limited by guarantee

The current reform proposals do not address the need for a review of the thresholds for companies limited by guarantee, that are not charities registered with the Australian Charities and Not-for-profits Commission. It is important to ensure that these are also reviewed to reflect current measures of economic significance. Such reform should be performed in light of the reform of the charity reporting thresholds being contemplated in response to the legislative review of the Australian Charities and Not-for-profits Commission Act 2012 and in consultation with the AASB’s not-for-profit framework reform project. We further recommend that the thresholds for all public companies limited by guarantee be consistent and aligned with the charity thresholds, regardless of whether the companies are registered charities.

Other legislation

Other proposed legislation, such as the *Treasury Laws Amendment (Enhancing Whistleblower Protections) Bill 2018*, uses the large proprietary company definition in applying its requirements. Treasury needs to ensure that the application of such legislation, especially to those entities that will fall below the new thresholds, is reviewed and made clear if the thresholds are changed.

Representatives of the Australian Accounting Profession



cpaaustralia.com.au



charteredaccountantsanz.com

Concluding remarks

Chartered Accountants ANZ and CPA Australia believe that developing an effective financial reporting framework requires a cooperative effort by legislators, regulators and standard-setters and extensive consultation with stakeholders. Only such a framework will stand the test of time in meeting the needs of the Australian economy.

We are therefore willing to engage with Treasury to explore possible options and assist with any deliberations and have already offered to work closely with the AASB on framework reform in both the for-profit and not-for-profit sectors.

Please contact Ram Subramanian Ram.Subramanian@cpaaustralia.com.au (CPA Australia) or Jeanette Dawes Jeanette.Dawes@charteredaccountantsanz.com (Chartered Accountants ANZ) if you would like to discuss the contents of this submission.

Yours sincerely



Simon Grant FCA
Group Executive – Advocacy, Professional Standing and
International Development
Chartered Accountants Australia and New Zealand



Craig Laughton
Executive General Manager
Policy, Advocacy and Public Practice
CPA Australia

Representatives of the Australian Accounting Profession



cpaaustralia.com.au



charteredaccountantsanz.com

