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New Financial Reporting Requirements for Private Businesses

At a glance

The Federal Parliament passed tax legislation on 3 December 2015 which will create significant new disclosure requirements for many privately owned companies and other entities that are not currently subject to financial reporting requirements.

The earliest of these disclosures is expected to become effective in March 2016 when the ATO will publish the accounting income, taxable income and tax paid by Australian private companies with income greater than $200m as disclosed in their tax returns. The first round of data to be published will be for the year ended 30 June 2014. The ATO will be contacting affected companies this month to verify their 2014 tax records before publishing those details. Private companies will need to strategically consider their response, if any, on what queries this information may provoke from the media or other stakeholders. If currently outside the tax transparency rules for the 2014 year, we need to consider whether they will apply in future years and plan accordingly.

The second change will require entities with consolidated income of more than $1 billion to prepare and lodge general purpose financial statements (GPFS) with the ATO – these will be passed on to ASIC for public access.

The parliamentary debate on the second change highlighted that many large proprietary companies currently lodge special purpose financial statements with ASIC, and questioned whether some of these should be GPFS. Many private companies who already lodge financial statements will need to relook at whether they are a reporting entity or not in light of this debate.

We anticipate the highest impact will be for previously "grandfathered" exempt privately owned companies whose consolidated income exceeds the $1 billion threshold. The new requirement also affects some other types of entities that do not lodge financial statements with ASIC, for example corporate limited partnerships, corporate unit trusts and public trading trusts. These entities will need to submit GPFS on the public record for income years commencing on or after 1 July 2016. However, as the current (i.e. FY16) financial year comparatives will also likely be required, these new reporting requirements need immediate attention.

This second change is a substantial departure from the original transparency proposals and will be a significant issue for affected businesses. This reporting requirement is the subject of this Alert.

Requirement to lodge General Purpose Financial Statements

So-called 'significant global entities' (SGEs) that are taxable in Australia, including those who currently do not lodge GPFS with ASIC, will have to prepare and lodge GPFS with the ATO at the time they lodge their tax return. These may be the consolidated group financial statements of which the entity is a part. These will be forwarded to ASIC and also put on ASIC's public register.

Significant Global Entities

SGEs are broadly defined as entities or groups with consolidated global income of $1 billion or more. All entities (including subsidiaries) in such a group are also considered to be SGEs. Despite the stated intent of the legislation to combat multinational tax avoidance under the banner of 'global', Australian entities with no overseas presence and / or ownership can still be SGEs and subject to these rules.

When identifying group members, the legislation requires you to include those entities that are consolidated for accounting purposes. A greater focus on the question of 'control' from an accounting perspective is therefore likely to result.

The definition of 'global income' refers to income as shown in the latest financial statements that are prepared in accordance with accounting standards. This implies that income not only includes revenue but also other gains. An entity may therefore become an SGE for one year only by having significant one-off gains.

What are general purpose financial statements?

GPFS are required to include all disclosures required by applicable accounting standards. For some companies this means a set of financial statements similar to those prepared by listed entities is required. This would apply to companies with "public accountability" which includes those in the process of listing their debt or equity, or those that hold assets on behalf of others in a fiduciary capacity. An example of this would be if you hold customers money.

However, entities that do not have 'public accountability' may take advantage of the reduced disclosure regime to prepare 'Tier 2" financial statements, which are exempted from numerous disclosure requirements. Entities affected by the new reporting requirement should consider the requirements of AASB 1053 *Application of Tiers of Australian Accounting Standards* to determine whether they have public accountability.

We expect that many entities impacted by the new reporting requirement will not have public accountability so will be able to prepare Tier 2 financial statements. Where these entities currently prepare special purpose financial statements, this is likely to mean that additional disclosures will be needed. Some entities will also be required to prepare consolidated financial statements for the first time.

Refer to Appendix A for a comparison of the disclosure obligations of a 'tier 2' GPFS vs special purpose financial statements. For further detail please refer to our VALUE ACCOUNTS Reduced Disclosure Publication which shows with shading what information can be removed from full IFRS financial reports under the reduced disclosure regime. See PwC website for download.

Who is impacted?

The legislation applies to SGEs that are companies or other entities that are taxed as companies (e.g. corporate limited partnerships, corporate unit trusts and public trading trusts). Importantly, trusts which are treated as 'flow-through' entities for tax purposes will not be caught by this reporting requirement (e.g. discretionary trusts).

The amendments allow the lodgement of consolidated GPFS where an entity is a member of a group that prepares consolidated financial statements, rather than every single subsidiary of an SGE, as outlined in the draft legislation. The ATO has been asked to clarify if the consolidated GPFS lodged could be those of an overseas parent.

It appears the legislation will require some entities who are currently relieved from the reporting requirements of the Corporations Act to prepare and lodge GPFS with the ATO. These include:

- Australian 'grandfathered' exempt proprietary companies (privately held companies) that are SGEs. 'Grandfathered' proprietary companies are required to prepare audited financial reports but are exempt from lodging them with ASIC provided certain conditions are met. These entities may no longer be able to rely on this relief from lodging financial reports with ASIC.

- subsidiaries of foreign groups that rely on ASIC CO 98/98 Small proprietary companies which are controlled by a foreign company but which are not part of a large group – if these entities are controlled by a foreign group that is an SGE, the Australian entity may have to lodge GPFS with the ATO regardless of the relief provided by ASIC. The lodgement of foreign consolidated accounts may be sufficient in this situation (subject to ATO views on this matter).

- wholly-owned subsidiaries that are given relief under ASIC CO 98/1418 Wholly-owned entities – these will only be able to rely on the relief if the parent company lodges GPFS.

- Australian branches of foreign companies that do not currently prepare branch accounts, and

- other entities that may not have financial reporting requirements under the Corporations Act but meet the definition of an SGE – for example, partnerships and trusts which are taxed as companies

When do these disclosure requirements apply?

The amendments become effective for income years commencing on or after 1 July 2016.

They apply to the entity's financial year that most closely corresponds to the relevant income year. For example, if an entity has a year ending 31 March for both tax and accounting purposes, the new requirement will first apply to the financial year commencing on 1 April 2017.

Next steps

The amendments raise many questions that will need to be resolved over the next few months. We will continue to update you as the answers to these questions are clarified.

However, as 2016 financial year comparatives will be required these new reporting requirements need immediate attention. The impact of this legislation on your reporting requirements should be considered now.

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Appendix A: Disclosure obligations of 'tier 2' general purpose financial statements vs special purpose financial statements

The following information is intended to be used as a guide only. The entity's directors are responsible for determining which disclosures are required in order to meet the needs of financial statement users and present a true and fair view of the business. This table highlights the significant disclosure differences between reduced disclosure general purpose financial statements and special purpose financial statements of non-reporting entities that are required to prepare financial reports under Chapter 2M of the *Corporations Act 2001*. It does not analyse the disclosures that can be removed from both sets of accounts, nor is it an exhaustive list of all differences that exist.

Financial statement note	Reference to VALUE ACCOUNTS Holdings and Reduced Disclosure (June 2015 versions)	Disclosure required in reduced disclosure general purpose financial statements (tier 2)?	Disclosure required in special purpose financial statements?
Content page/general information about the entity:			
• Domicile, legal form, country of incorporation, address of registered office and description of the nature of the entity's operations and principal activities (AASB 101(138))	Annual financial report – content page	No	Yes
Balance sheet and related notes			
• Present a third balance sheet at the beginning of the earliest comparative period in certain circumstances (AASB 101(40A))	Balance sheet and related commentary	No	Yes
Revenue			
• Breakdown of revenue by category (AASB 118(35)	Note 3	Yes	No *
Individually material items (AASB 101(97))	Note 4	Yes	Yes
Other income and expenses			
• Other items required by standards other than AASB 101	Note 5	Depending on standard	No *
• Information about expenses classified by nature where the entity has classified expenses by function in the income statement (AASB 101(104))	Note 5(b)	No	Yes
Income tax			
• Breakdown of income tax expense (AASB 112(79))	Note 6(a)	Yes	No *
• Reconciliation: income tax expense to prima facie income tax payable (AASB 112(81)(c))	Note 6(c)	Yes	No *
• Aggregate amounts recognised directly in equity (AASB 112 (81)(a))	Note 6(d)	Yes	No *
• Aggregate amounts recognised directly in OCI AASB 112 (RDR81.1)	Note 6(d)	Yes	No *
• Tax expense relating to each component of OCI (AASB 101 (90))	Note 9(b)	No	Yes
• Deferred tax assets not recognised (AASB 112 (81)(e))	Note 6(e)	Yes	No *
Financial assets and liabilities			
• Policy adopted in determining the composition of cash and cash equivalents (AASB 107(46))	Note 7(a)	No	Yes
• Transferred financial assets (whether or not derecognised in their entirety) (AASB 7(42A)-(42E))	Note 7(b)	Yes (limited disclosures)	No *
• Specific amounts recognised in profit or loss and other comprehensive income (AASB 7(20))	Note 7(c),(d) Note 12(b),(c)	Yes (with reduced disclosures)	No *
• Information that enables users of the financial statements to evaluate the significance of financial instruments (eg about debt defeasance; AASB 7(7))	Note 7(g)	Yes	No *
• Secured liabilities (AASB 7(14))	Note 7(g)	Yes	No *
• Loans payable - defaults and breaches (AASB 7(RDR18.1))	Note 7 (commentary)	Yes	No *
• Finance lease liabilities (AASB 117(31))	Note 7(g)	Yes (with reduced disclosures)	No *

Financial statement note	Reference to VALUE ACCOUNTS Holdings and Reduced Disclosure (June 2015 versions)	Disclosure required in reduced disclosure general purpose financial statements (tier 2)?	Disclosure required in special purpose financial statements?
Non-financial assets and liabilities			
• Amount of inventory recognised as an expense and amount of any write down of inventory to net realisable value (AASB 102(36)(d))	Note 8(a)	Yes	No *
• Description of assets held for sale (AASB 5(41)(a)-(c))	Note 8(b)	Yes	No *
• Reconciliations from opening to closing balance (PPE, intangibles, investment property, provisions retirement benefit obligations)	Notes 8(c),(d),(f) (g),(h)	Yes (but only current year)	No *
• Net carrying amount of leased assets (AASB 117(31)(a)	Note 8(c)	Yes	No *
• Investment property (other disclosures) (AASB 140)	Note 8(d)	Yes (with reduced disclosures)	No *
• Finance and operating leases of lessors (AASB 117(47),(56))	Note 8(d)	Yes	No *
• Breakdown of deferred tax balances by type of temporary differences (AASB 112(81)(g))	Note 8(e)	Yes	No *
• Nature of provisions (AASB 137(85)(a))	Note 8(g)	Yes	No *
• Retirement benefit obligations (other disclosures) (AASB 119)	Note 8(h)	Yes (with reduced disclosures)	No *
• Amounts expected to be recovered/settled within and after 12 months (AASB 101 (61))	Notes 8(e),(g)	No	Yes
Impairment			
• Impairment losses and reversals for each class of asset (AASB 136(126); if not disclosed as part of the reconciliation from opening to closing balances)	Note 4	Yes	No *
• The recoverable amount of the individual asset or CGU for which an impairment loss has been recognised or reversed (AASB 136(130)(c) as amended by AASB 2013-3)	Note 4	Yes	No *
Fair value measurements			
• If financial and non-financial assets and liabilities are recognised at fair value, disclose valuation techniques and inputs used (AASB 13(91)(a))	Notes 7 and 8	Yes	No *
Cash flow information			
• Reconciliation of profit after tax to cash flow from operating activities (AASB 1054(16))	Note 10	No	Yes
Financial risk management			
• Derivatives: information about hedges entered into by the entity (AASB 7(22)-(24))	Note 12(a),(b)	Yes	No *
• Credit risk: Reconciliation of movement in impairment provision (AASB 7(16))	Note 12(c)	Yes	No *
Capital management: dividends			
• Dividends per share (AASB 101(107))	Note 13(b)	No	Yes
• Dividends not recognised at the end of the reporting period (AASB 101(137))	Note 13(b)	No	Yes
• Franked dividends available for subsequent financial years (AASB 1054(13)-(15))	Note 13(b)	No	Yes
Business combination			
• Purchase consideration & breakdown of assets/liabilities acquired (AASB 107(40))	Note 14(a)	No	Yes
• Other information about the acquired entity/operation (AASB 3)	Note 14(a)	Yes (with reduced disclosures)	No *
• Cash flow information (AASB 107 (40))	Note 14(b)	No	Yes

Financial statement note	Reference to VALUE ACCOUNTS Holdings and Reduced Disclosure (June 2015 versions)	Disclosure required in reduced disclosure general purpose financial statements (tier 2)?	Disclosure required in special purpose financial statements?
Discontinued operations			
• description of discontinued operation (AASB 5(41)(a))	Note 15(a)	Yes	No *
• financial performance of discontinued operation (AASB 5(33), AASB 112(81)(h))	Note 15(b)	No (except tax amounts)	No *
• cash flows of discontinued operations (AASB 5(33)(c))	Note 15(b)	Yes	No *
• details of the sale of the subsidiary or other business: disposal consideration and carrying amount of assets/liabilities sold (AASB 107(40))	Note 15(c)	No	Yes
Interests in other entities (AASB 12)		Applies to all:	Applies to all:
• Judgements and assumptions made in relation to non-control and agency/principal relationship	Note 16(a)	Yes (with reduced disclosures)	No *
• Composition of the group	Note 16(a)		
• Significant restrictions	Note 16(a)		
• Information about interests in joint arrangements and associates	Note 16(d),(e)		
Contingencies (AASB 137(86),(89))	Note 17	Yes	No (but often necessary to provide a true and fair view)
Commitments			
• Lease commitments (AASB 117(31)(b) and (35)(a))	Note 18(b)	Yes (with reduced disclosures)	No *
• Commitments re property, plant and equipment, intangible assets, investment property (AASB 116(74)(c), AASB 138(122)(e), AASB 140(75)(h))	Note 18(a)	Yes	No *
Related party transactions			
• Name of parent and ultimate parent (AASB 124(13) and AASB 101(138)(c))	Note 20 (a)	Yes	Yes
• Key management personnel (AASB 124(17))	Note 20 (c)	Yes (with reduced disclosures)	No *
• Other related party disclosures (AASB 124)	Note 20(d)-(g)	Yes	No *
Share-based payments (AASB 2)	Note 21	Yes (with reduced disclosures)	No *
Remuneration of auditors (AASB 1054(10),(11))	Note 22	No	Yes
Assets pledged as security (various standards)	Note 25	Yes	No *
Summary of significant accounting policies			
• New accounting standards and interpretations issued but not yet applicable (AASB 108(30))	Note 28(ae)	No	Yes

* While non-reporting entities do not need to comply with the relevant standards, they may need to disclose similar information where the amounts are material and the information is relevant to an understanding of the financial statements, or to provide a true and fair view. References: AASB 101 paragraphs 97 and 112(c) and section 297 of the *Corporations Act 2001.*