

Regulation Impact Statement

Removal of Individual Key Management Personnel Disclosures

July 2011



Australian Government

**Australian Accounting
Standards Board**

Regulation Impact Statement

Removal of Individual Key Management Personnel Disclosure Requirements

Background

Under section 227(1) of the *Australian Securities and Investments Commission Act 2001* (ASIC Act), the functions of the Australian Accounting Standards Board (AASB) are to:

- develop a conceptual framework, not having the force of an accounting standard, for the purpose of evaluating proposed accounting standards and international standards;
- make accounting standards under section 334 of the *Corporations Act* for the purposes of the corporations legislation;
- formulate accounting standards for other purposes; and
- participate in and contribute to the development of a single set of accounting standards for world-wide use having regard to the interests of Australian corporations that raise or propose to raise capital in major international financial centres.

In general, the AASB issues Australian Accounting Standards that incorporate International Financial Reporting Standards (IFRSs) issued by the International Accounting Standards Board (IASB).

The AASB issues one series of Standards applicable to both for-profit and not-for-profit entities, including public sector entities.

The AASB includes some disclosure requirements that are in addition to the IFRSs, but aims to keep these to a minimum on the basis that the IFRSs represent best international practice for general purpose financial reporting of publicly accountable for-profit entities.

Problem

- 1.1 Prior to adopting IFRSs, the AASB had on issue AASB 1046 *Director and Executive Disclosures by Disclosing Entities*, which included disclosure requirements in respect of the compensation, equity holdings and loans of individual key management personnel (KMP) of disclosing entities (as defined in the Corporations Act). When IFRSs were adopted, these requirements were largely carried forward for disclosing entities as 'Aus' paragraphs in AASB 124 *Related Party Disclosures*, which incorporates IAS 24 *Related Party Disclosures*.
- 1.2 Section 300A of the *Corporations Act 2001* and Regulation 2M.3.03 were amended in 2007 to require disclosing entities that are companies to report individual remuneration information in the directors' report.¹ The AASB responded by amending AASB 124 to relieve disclosing entities that are companies from complying with the paragraphs in AASB 124 that have been included in the Corporations Act and Regulation 2M.3.03, following a due process that involved issuing ED 162 *Proposed Amendments to Key Management Personnel Disclosures by Disclosing Entities* in April 2008 for public comment. The resulting amendment avoided requiring each disclosing entity that is a company to disclose this information twice – in its directors' report and in its financial statements.²
- 1.3 The existing AASB 124 retains individual KMP disclosure requirements on:
 - (a) remuneration in relation to disclosing entities other than companies; and
 - (b) equity holdings, loans, and other transactions and balances in relation to all disclosing entities.
- 1.4 A number of constituents who commented on ED 162 encouraged the Board to consider removing all the individual KMP disclosure requirements (Aus paragraphs) from AASB 124. Accordingly, in ED 200A *Proposals to Harmonise Australian and New Zealand Standards in Relation to Entities Applying IFRSs as Adopted in Australia and New Zealand* (issued in July 2010) the AASB specifically sought comment on whether the individual KMP

¹Corporations Act Regulation 2M.6.04 permitted listed companies to avoid making the same disclosures twice, however, the Corporations Amendment Regulations 2007 (No. 2) removed that regulation.

²AASB 2008-4 *Amendments to Australian Accounting Standard – Key Management Personnel Disclosures by Disclosing Entities*

disclosure requirements should be retained or removed. All of those who responded to this question supported their removal.

- 1.5 The views expressed by constituents on ED 162 and ED 200A highlight that the remaining individual KMP disclosure requirements:
- (a) are not part of IFRS and the AASB's Standards that incorporate IFRSs should replicate as closely as possible the content of the IFRSs as issued by the IASB;
 - (b) are a barrier to meeting the Outcome Proposals set by the Australian and New Zealand governments, which include enabling for-profit entities to use a single set of accounting standards and prepare only one set of financial statements for both jurisdictions³ and the New Zealand standards do not contain additional individual KMP disclosure requirements; and
 - (c) are a governance matter that would be most appropriately dealt with directly by the Government through the Corporations Act.

Objectives

- 2.1 The objective of removing the individual KMP disclosures (via Amending Standard AASB 2011-4 *Amendments to Australian Accounting Standards to Remove Individual Key Management Personnel Disclosure Requirements*) is to:
- (a) align the AASB's Standards that incorporate IFRSs with the content of the IFRS;
 - (b) align the AASB's Standards with New Zealand standards and meet the Outcome Proposals set by the Australian and New Zealand governments;
 - (c) leave the way open for the Government to deal with governance-type disclosure requirements.

³More information is available from the Trans-Tasman Outcomes Implementation Group website – www.treasury.gov.au/ttoig.

Options

Option 1

- 3.1 Revise AASB 124 to remove the individual KMP disclosure requirements.

Option 2

- 3.2 Status quo (do nothing).

Option considered but discounted

- 3.3 Another option that would meet two of the three objectives, would be to try and persuade the IASB and the New Zealand standards setter to also require the individual KMP disclosures currently required in AASB 124. This option has been discounted as being unrealistic and because it does not meet the third concern about disclosures of this type being more appropriately located in legislation such as the Corporations Act.

Impact Analysis

Impact assessment methodology

- 4.1 The expected impacts of removing the individual KMP disclosure requirements can be considered as relating to three groups – preparers, users and the accounting profession (including auditors).
- 4.2 The assessment of impacts in this RIS is based on a three-point scale of positive, neutral or negative impacts. The impacts of each option are compared with the equivalent impact of the status quo option. If an impact on a particular group would, relative to the status quo, benefit the group, the impact is allocated a positive rating. On the other hand, if the impact on the group would result in a cost to the group, the impact is allocated a negative rating. If the impact is assessed to be the same as that imposed under the status quo option, a neutral rating is given.
- 4.3 The ratings for each type of impact compared with the status quo are aggregated to arrive at an overall effect at the option level. If the overall effect at the option level is positive, it indicates that the option is more likely to produce a favourable cost-benefit outcome than the status quo. If the overall effect at the option level is negative, it indicates that the option would be more likely to provide a less favourable cost-benefit outcome than the status quo. If the

rating at the option level is neutral, it indicates that there would be no overall benefit or cost from the option relative to the status quo.

Option 1 – Revise AASB 124 to remove the individual KMP disclosure requirements

Preparers

Impact	Assessment	Analysis
Preparation costs	Positive	Amending Standard AASB 2011-4 <i>Amendments to Australian Accounting Standards to Remove Individual Key Management Disclosure Requirements</i> has the potential to decrease preparation costs, particularly for those affected disclosing entities with complex remuneration and other arrangements with their KMP. The cost savings are likely arise because: * fewer disclosures would be required; and * preparers would have fewer places to look in order to find the requirements with which they need to comply. These cost savings may be mitigated if the Government decides to require disclosures through the Corporations Act that are similar to those being removed.
NZ conformity	Positive	AASB 2011-4 will allow the AASB to align its Standards with New Zealand standards and meet the Outcome Proposals set by the Australian and New Zealand governments. This will help lower costs of preparation because the Outcome Proposals are expected to facilitate mutual recognition of financial statements across the Tasman, which will save Australian entities with New Zealand branches or subsidiaries from preparing both Australian and New Zealand financial statements.

Users

Impact	Assessment	Analysis
Availability of information	Neutral	AASB 2011-4 has the potential to make information used by users unavailable and thereby impair their decision making, although generally only in relation to the accountability of particular individual KMP rather than the accountability of the entity as a whole. This concern is mitigated by: * the fact that other governance-type disclosures are required by the Corporations Act;⁴ and * the fact that KMP are within the definition of ‘related party’ and, accordingly, disclosures would still be required about any loans or other transactions between the entity and KMP, although without necessarily identifying the names of the individual KMP involved. In the context of general purpose financial reporting about an entity as a whole, the loss of information about individual KMP should not adversely impact on users’ decision making.
IFRS conformity	Positive	AASB 2011-4 will bring Australian Accounting Standards closer to IFRSs and generally enhance the acceptance of financial statements prepared in accordance with Australian Accounting Standards, particularly among non-Australian users.

⁴Note, at some stage, the Government may consider modifying the existing disclosures required by the Corporations Act as a result of the individual KMP disclosure requirements being removed from Australian Accounting Standards.

Accounting profession (including auditors)

Impact	Assessment	Analysis
Costs of education and professional development	Positive	On the basis that AASB 2011-4 will result in Australian Accounting Standards that are better aligned with IFRSs and New Zealand standards, the costs of training staff across mutli-national accounting firms will be reduced and the knowledge gained in one part of the world will be more readily transportable across national boundaries. The benefits would be of less significance to mid-tier accounting firms and probably of little consequence to smaller firms.

Option 2 – The status quo

- 4.4 The analysis above considers the benefits and costs of adopting Option 1 relative to Option 2 and, therefore, also reflects the benefits and costs of maintaining the status quo. It demonstrates that Option 1 is likely to yield a better cost-benefit outcome than Option 2.

5. Consultation

- 5.1 The AASB issued ED 162 *Proposed Amendments to Key Management Personnel Disclosures by Disclosing Entities* in April 2008 for public comment. As part of the AASB's efforts to converge with New Zealand standards, the AASB issued ED 200A *Proposals to Harmonise Australian and New Zealand Standards in Relation to Entities Applying IFRSs as Adopted in Australia and New Zealand* in July 2010 for public comment. All of those who responded to these Exposure Drafts expressed support for removing the remaining individual KMP disclosure requirements from AASB 124. In total, over the two Exposure Drafts, this would represent more than 25 respondents, which included a number of users of general purpose financial statements.
- 5.2 Constituents responding on the issue, including users, noted that having all the individual KMP disclosure requirements located in the Corporations Act would be a welcome simplification and that aggregate disclosure requirements in Standards about transactions involving KMP would generally satisfy their needs for information about the accountability of entities as a whole in relation to their dealings with KMP.

- 5.3 The AASB has had ongoing consultation with the Australian Treasury and New Zealand Ministry of Economic Development and they are aware that the legislative requirements regarding individual KMP disclosures may need to be changed in order to align them across the two jurisdictions.

6. Conclusion and Recommendation

- 6.1 As demonstrated in section 4 above:

- * Option 1 offers a greater level of benefits to preparers of financial statements and the accounting profession more generally than Option 2 (the status quo); and
- * users would be no worse off under Option 1 than they are under Option 2 in terms of the availability of relevant information, and better off in the context of IFRS compliance.

Accordingly the AASB concluded that Option 1 is the most appropriate course of action.

- 6.2 Option 2, which would keep the status quo, is seen as inappropriate as reflected in constituents' comments on ED 162 and ED 200A.

7. Implementation and Review

- 7.1 The impacts of AASB 2011-4 will be subject to review taking account of the experience of constituents and developments in other regulation affecting disclosing entities. However, the AASB doubts there would be a need to reinstate any of the disclosure requirements being removed via AASB 2011-4.