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Bruce Donald
Secretary
Financial Reporting Council
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Langton Crescent
PARKES ACT 2600

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Dear Bruce

Managing complexity in financial reporting

CPA Australia welcomes the opportunity to make a submission to the Financial Reporting Council's report *Managing complexity in financial reporting*. CPA Australia is one of the world's largest accounting bodies and represents the diverse interests of more than 139,000 members in finance, accounting and business in 114 countries throughout the world. We are committed to making CPA Australia the global professional accountancy designation for strategic business leaders. We make this submission on behalf of our members and in the broader public interest.

CPA Australia notes a number of bodies have been working on this issue, to various degrees, and their findings are likely to be relevant to any further work by the FRC on its project.[1] This month has seen the publication of discussion papers from the US Financial Accounting Standards Board *Disclosure Framework* and the European Financial Reporting Advisory Group, the Autoritie des Normes Comptables and the UK Financial Reporting Council *Towards a disclosure framework for the notes*. Each adds to the body of literature relevant to the FRC project. This is not surprising given the increasingly global nature of business and the development of the profession.

The Appendix to this letter contains our response to the questions for comment. If you require further information about our submission please contact Dr Mark Shying Senior Policy Adviser – External Reporting at CPA Australia via email at mark.shying@cpaaustralia.com.au.

Yours Sincerely

Alex Malley FCPA
Chief Executive Officer

[1] For example, the UK Financial Reporting Council discussion paper *Cutting the clutter. Combating clutter* in annual reports and the New Zealand Institute of Chartered Accountants and the Institute of Chartered Accountants in Scotland paper *Losing the excess baggage – reducing disclosures in financial statements to what's important*.

Attachment

1. **Are there any additional sources of reporting complexity which should be considered by the Task Force and the FRC, and if so, what?**
Except for developments in integrated reporting, we believe the identified sources of financial reporting complexity are the most important. We have observed the same set of issues being identified in similar studies elsewhere across the globe. This is not surprising given the increasingly global nature of business and the development of the profession.

 The Task Force's discussion of complexities in the regulatory framework notes the extent of application of IFRS in Australia in comparison to its application in other jurisdictions. However, the report does not acknowledge the Australian Accounting Standards Board's (AASB) reduced disclosure requirements (RDR) reporting framework and its effect on the general purpose financial statements of most large proprietary companies and many entities in the not-for-profit private sector whereby they are most likely to contain substantially less disclosures compared with that required by IFRS. We think the RDR framework together with the IASB's IFRS for Small and Medium-sized Entities (SMEs) standard may provide a mechanism to reducing complexity.

 We agree with the Task Force that there has been an increase in disclosure in the financial report regardless of the items materiality or importance. In part, we believe this is a consequence of a lack of clarity around materiality which forms a barrier to both preparing and auditing financial statements.

 Given that integrated reporting is still in the early phases of its development we were somewhat surprised that it has been identified as a source of complexity. The Task Force opines that Australia should monitor developments in integrated reporting with a view to encourage adoption only of that which clearly provides a pathway to simpler reporting that communicates better with stakeholders. We believe it is too early for the FRC to establish criteria to be used in making decisions about whether or not to adopt integrated reporting.

2. **Do you agree with the Task Force's conclusion that complexity is inevitable in the short-term and accordingly that efforts should be concentrated on strategies to assist stakeholders to better manage this complexity?**
In our response to Question 1 above we identified the development of the RDR framework together with the IFRS for SMEs standard as one possible approach to reducing complexity. We understand that the public sector's ability to use the RDR framework may be compromised because the framework can only be used by entities that do not have public accountability – an oxymoron for public sector entities. Exploring how this issue might be resolved may be a useful short-term activity. Currently, Australian entities without public accountability are not able to use the IFRS for SMEs standard. In some situations compliance with this standard might result in a further reduction in the complexity of reporting. Further examination of this issue might have some useful outcomes in the short term.

 Outside of work on the RDR and IFRS for SMEs frameworks, we agree that as it is not likely that complexity can be significantly reduced in the short term a concentration on strategies to assist stakeholders to better manage complexity is appropriate.

3. **Do you have any comments on the strategies to better manage complexity as suggested by the Task Force?**
Each of the six identified strategies has some relevance to the objective of managing complexity; in particular, approaches that make better use of developments in information technology and delivery and the empowerment of users through the delivery of financial information via XBRL.

 That said we make the following comments about the business judgement rule (BJR) and the need for change as a means of addressing legal impediments to preparers determining relevant material disclosures. We understand the BJR relates directly to the duty of care and diligence. This is quite deliberate as the duty is based on the law of negligence. Directors' powers of management are applied in term of an understanding of the reasonable foreseeability of harms caused by their acts and omissions. There is some validity in arguing that BJR protection could be extended to the duty of good faith (s 181 of the Corporations Act), but far less merit in suggesting application to fiduciary based duties (ss 182 and 183). We see the act of preparing and presenting financial statements falling squarely as part of powers of management governed by expectations of care, skill and diligence which directors hold themselves out as possessing. As a critical part of powers management, the associated duty falls under s 180 to which the BJR applied. The development of a broad-based defence would add no more and it is difficult to see how specific rules could be developed to provide protection in relation to financial disclosures when the overarching statutory duty is broad and quite all-embracing.

Moreover, it needs to be kept in mind that the statutory rules sit alongside general law rules which have developed to set the standards of expectation of director behaviour. These general law rules do not point to the development of any wider protections than presently exist. If the Centro case can be taken as a guide, the courts are showing little sympathy for directors who err in relation to duties around financial disclosure.

Finally, it should not be ignored that the rationale which sits behind the BJR is that courts do not wish to see themselves set up as mechanisms for reviewing management decisions which sit squarely with directors. Accordingly, we think courts would be very reluctant to determine and develop precedent about what should and should not be included in the notes to the financial statements.

4. **Do you have any suggestions for the financial reporting terms and definitions that should be encouraged for development (Suggested Strategy #4)?**
   Given the increasingly global nature of business and the development of the profession we would caution against development of financial reporting terms and definitions different from those that are used internationally.

5. **Please indicate 'quick wins' that you believe could be achieved in managed complexity, which could be delivered within the current Australian legislative framework and IFRS.**
   As described in our response to Question 2, further exploration by interested parties of whether or not Australian entities should be able to use the IFRS for SMEs standard and the ability of public sector entities to use the RDR framework may be useful. These activities may result in 'quick wins'.

6. **Are there any other issues the Task Force should consider?**
   No other issues noted.