



RESEARCH NOTE

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Financial Statements of Commonwealth Commercial Entities: Disclosure of Related Party Transactions of Ministers

The Minister for Finance has in guidelines issued under the *Audit Act 1901* exempted commercial government agencies (eg. government business enterprises, business units of Department of Administrative Services) from the need to disclose transactions with Ministers as required by the accounting standard on **Related Party Disclosures - AAS 22**.

It appears that practical problems associated with the recording and disclosing of transactions was the basis for restricting the application of the accounting standard.

This research note demonstrates that the restriction in the application of this accounting standard is against the trend for enhanced disclosures introduced for public companies in recent years and suggests that in the interest of enhancing accountability -

- the disclosures required under AAS 22 by Commonwealth Authorities be available to Parliamentary Committees and Senate Estimates Committees on request; or
- the Auditor-General be empowered to disclose any unusual and material benefits where as auditor of these commercial entities the Auditor-General considers it necessary to do so in the public interest.

The guidelines for *Financial Statements of Commonwealth Authorities* (the *Guidelines*) issued by the Minister for Finance under the *Audit Act 1901* in March 1995 apply to Commonwealth Authorities in preparing financial statements for the year ended 30 June 1995. The rationale for this Research Note is the increasing significance of accountability to Parliament as more government agencies become commercialised.

Under the *Guidelines*, Commonwealth authorities are required to comply with Australian Accounting Standards issued by the **Australian Accounting Research Foundation** (AAS series) in preparing financial statements of their commercial activities. Broadly the Accounting Standard

AAS 22 on **Related Party Disclosures** governs disclosure of transactions a person has with the entity he or she controls either directly or indirectly through intermediaries. Such transactions are generally referred to as related party transactions. However the Guidelines have excluded Ministers as related parties of the commercial entities for which they have responsibility and, in consequence, transactions of Ministers with commercial entities they control do not require to be disclosed in the financial statements of Commonwealth commercial entities¹.

The object of this accounting standard is to ensure that disclosure will be a deterrent to persons who are in fiduciary positions, such as directors of public com-

panies, from making gains out of transactions with the entities they control. More specifically it is intended to deter gains which would not normally be available to others dealing with such entities. The need for law reform and disclosure was stated in the **Report of the Law Governing Corporate Financial Transactions** as follows:

Following the corporate collapses of the 1980s, it has become evident that some corporate controllers abused their positions of trust by arranging for the shifting of assets around and away from companies and corporate groups, and into their own hands.

This was made easier by the lack of any general statutory requirement that shareholders ei-

ther consent to, or be informed, of those transactions.²

The *Corporations Law* requires companies to comply with a similar standard on related party transactions.

AAS 22 has cast a wide net by its definition of 'related party'. Generally it brings in as a related party not only the members of the immediate family of each director but also companies, trusts and other entities over which a director has direct or indirect control. It also includes entities which are under the common control of the directors.

The unrestricted application of AAS 22 would entail disclosure of transactions every commercial entity of the Commonwealth has with every Minister of the Commonwealth. This is because every Minister of the Commonwealth is a member of the Federal Executive Council constituted under section 64 of the Constitution. The Federal Executive Council and Ministers are responsible for all the departments and activities carried on by them and various Commonwealth Authorities. The definition of 'related party' in AAS 22 is wide enough to bring in the Federal Executive Council and every Minister as a related party of every Commonwealth commercial entity.

It appears that the practical problems associated with the recording and disclosing of transactions was the basis for restricting

the application of AAS 22. However it is arguable that the interests of enhanced accountability to Parliament appear to have been compromised by a decision based on practical considerations. A way out may be to make such information available to Parliamentary Committees and Senate Estimates Committees on request or to empower the Auditor-General to disclose any unusual and material benefits where the Auditor-General as auditor of these commercial entities considers it necessary to do so in the public interest.

Accountability of Commonwealth commercial entities to Parliament requires that the standard of disclosure should be the same as for public companies in relation to shareholders. This is particularly so as there are limits to accountability to Parliament, given that Commonwealth authorities would plead the 'commercial-in-confidence' defence to requests for information by Parliamentary Committees and Senate Estimates Committees.

Enhanced disclosure has received emphasis in the case of public companies in recent years to address the concerns of shareholders whose right to information is limited by the identical 'commercial-in confidence' defence the board of a public company can plead at meetings of shareholders. Thus in furtherance of the policy underlying the accounting

standard on related party disclosures, the *Corporations Law* was amended in 1992 to prohibit the giving of certain financial benefits to related parties of public companies on or after 1 February 1994, without the approval of shareholders³.

It would therefore appear that the Guidelines for the disclosure of information on related party transactions of Commonwealth commercial entities are against the trend for more disclosure that has been found necessary in the 1990s in the case of public companies to prevent the abuse of fiduciary positions.

Bernard Pulle
Economics, Commerce and
Industrial Relations Group
Parliamentary Research
Service

Phone: 06 277 2469

Fax: 06 277 2475

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1. Financial Statements of Commonwealth Authorities (March 1995); subparagraphs 3(1)(c)(iv)(B) &(C); p. 9.
2. Companies and Securities Advisory Committee (July 1991); p. 2.
3. Part 3.2A, inserted into the *Corporations Law* by the *Corporations Law Reform Act 1992*.