

CHAPTER THREE

Issues

3.1 A number of issues were raised in evidence and submissions before the committee, including:

- the transition to the new standards;
- interpretation of the standards;
- consistency between the AASB and IASB standards;
- whether the proposed standards are genuinely principles-based; and
- whether the documentation associated with the standards is appropriate.

3.2 While the committee did not seek evidence in relation to technical aspects of the standards, evidence emerged on two technical issues which the committee wishes to note. These are:

- the impact of the new standards on co-operatives; and
- the treatment of intangible assets under the new standards.

Transition to the new standards

3.3 A number of submitters and witnesses expressed concern that the transition time between the issue of the stable platform of standards and the commencement of those standards has been insufficient, particularly for small and medium reporting entities. The Australian Institute of Company Directors (AICD), for instance, stated:

... larger companies, especially those who raise or plan to raise capital in overseas markets are well on the way to making the transition to [the new standards] on 1 January 2005. However, anecdotal evidence from AICD's membership and recent evidence from surveys conducted by the Institute of Chartered Accountants in Australia (ICAA) and the Australian Prudential Regulation Authority indicates that smaller listed companies and unlisted reporting entities are less well prepared for the transition.¹

3.4 The Institute of Chartered Accountants in Australia (ICAA) agreed, stating that "there is at least anecdotal information that the non-listed companies may be less well prepared to meet the 1 January 2005 timetable ..."²

1 Submission 14, Australian Institute of Company Directors, p. 3.

2 Submission 8, Institute of Chartered Accountants in Australia, p. 2.

3.5 Some submitters opposed any deferral of the standards' commencement. The National Institute of Accountants (NIA) stated:

Small to medium enterprises are always going to be under-resourced and will seek to delay the inevitable. In this context it is probably prudent to ensure the deadline is firmly stuck to in order to ensure companies of all sizes comply with the new body of accounting literature. It is a truism that entrepreneurs will react to emergencies rather than plan too far ahead. There is little point in delaying the implementation of IFRS at that level.³

3.6 CPA Australia provided a similar view:

We have held discussions with a range of our members and other participants in the financial reporting arena and consider that, on the whole, Australian entities will be able to prepare financial reports under the proposed standards when they are required to do so. We also understand that smaller entities usually have less complex operations (in a financial reporting sense) than larger ones, and so are likely to be impacted to a lesser degree by these changes in accounting standards.⁴

3.7 Other submitters went further, arguing that any delay to give small and medium business more time to comply would have negative consequences for Australian markets and for companies which have already complied. The Group of 100 stated:

We believe that with the promulgation of virtually all the 2005 Standards by the AASB in July 2004 and the detailed and costly preparation undertaken by our members and other entities in preparing for the implementation of the Australian equivalents to IASB Standards, delays/interruptions to this process at this stage will create confusion in the marketplace for preparers, shareholders and other users of financial reports.⁵

3.8 Mr Keith Alfredson stated:

Some commentators have also argued that the timetable for adoption of the standards should be delayed for certain entities. I do not support any such delay. In my opinion, the move to international accounting standards has been well publicised ever since the Financial Reporting Council made the strategy decision in June 2002. To now delay the process will favour those entities that have deliberately failed to take the necessary steps to make the changes. This would be a most unfortunate outcome. Further, in my opinion, the extent of change by smaller entities that do not enter into complex financial instruments has, in my opinion, been grossly exaggerated. For many such entities, there will be few changes in

3 Submission 19, National Institute of Accountants, p. 2.

4 Submission 11, CPA Australia, p. 1.

5 Submission 12, The Group of 100, p. 1.

recognition and measurement practices, with the changes in presentation and disclosure being relatively easy to cope with.⁶

3.9 In evidence before the committee, the NIA suggested a means by which small and medium reporting entities might obtain relief from some of the time pressures imposed by the commencement of the standards. The NIA stated:

We have asked the Australian Securities and Investments Commission to consider granting some lodgment relief to permit unlisted entities the opportunity to lodge a little later if the auditor finds that there are material errors in the first cut of their financial statements seen by the auditor for review, for the purposes of audit. To us, that is probably the most practical form of relief that would not conflict with any auditor independence rules...⁷

3.10 The committee put this suggestion to the AASB, who gave the suggestion some support:

I think that has merit. One could say, 'What would one month do?' It struck me, as I heard that suggestion, that one thing that even one month would do is that when the accountants have finished with the big end of town they will then have another month to service the small end. One month is a short period of time and may not be long enough, but if lodgments with ASIC, just for the transition year, were delayed a month for that end of the market I cannot see that any great harm would be done, and it might produce a benefit. The question is: just how much of a benefit? It is a bit hard to measure, but it is a suggestion with merit.⁸

Recommendation 1

The Committee recommends that small and medium enterprises be permitted an additional month to report to ASIC for that enterprise's first reporting year under the new standards.

3.11 This recommendation immediately raises the question of what a "small or medium enterprise" actually is. This considered this issue in some depth in its *Report on Aspects of the Regulation of Proprietary Companies*, which was tabled in March 2001. In that report the committee stated as a principle that:

In applying the reporting entity test, the [Committee] believes that directors and auditors must not only consider the relationship between shareholders and management, but also whether there are existing and potential users of the accounts who may be dependent on the financial reports.⁹

6 Submission 4, Mr. Keith Alfredson, p. 2.

7 *Transcript of Evidence*, Ravlic, 7 February 2005, p. 18.

8 *Transcript of Evidence*, Boymal, 7 February 2005, p. 47.

9 Parliamentary Joint Statutory Committee on Corporations and Securities, *Report on Aspects of the Regulation of Proprietary Companies*, March 2001, p. 34.

3.12 The committee is disappointed that, nearly four years after its report, there has been no government response to its recommendations.

Reporting of comparative information

3.13 A particular concern for small and medium enterprises was the requirement to report comparative data for the reporting period immediately prior to the first reporting period under the new standards. The AICD suggested that removing this requirement for smaller reporting entities may make the task of transition more manageable:

Historically Australian companies have not been required to implement new standards in the year they are introduced – Australian companies are now faced with the dual pressure of the introduction and implementation of new standards in the same year. This is unprecedented. What is different on this occasion is that for a number of the IFRS standards the past has to be re-stated as if the new standards had always applied. It is the cost of “restatement of the past” that will fall heaviest on smaller companies.

... relief for this group could be provided by an exemption for these companies from the requirement to provide comparatives in the first year of the introduction of IFRS.

Investors will still be able to make comparisons between pre and post IFRS numbers because of AASB 1047 and AASB 1 which requires companies to make a detailed reconciliation between pre and post IFRS numbers. The AASB 1047 disclosures require companies to make estimates based on materiality whilst AASB 1 requires the detailed comparison between the two sets of financials.¹⁰

3.14 The AASB noted that the issue of comparatives is less urgent and onerous than has been claimed in other evidence and submissions:

These small companies normally will have a June year end. If they are that small they will not be listed so they will not have half-year published reporting. That means that the first set of accounts that they produce under IFRS will be for 30 June 2006. Let us say they produce them two months after that, say, 31 August 2006. At that time they will have to have restated their comparatives for 2005. Yes, everybody agrees they should be thinking about that now but they do not actually have to produce or come public with that until about August 2006. They have all of the time from now until then to continue to work on it.¹¹

3.15 The committee considers that in any major regulatory change, there will be some affected entities who delay their transition to the new regime until the last moment. Reporting entities have had sufficient notice that the new standards would be promulgated, and sufficient notice of the content of those standards. Given that the

10 Submission 14, Australian Institute of Company Directors, pp. 4-6.

11 *Transcript of Evidence*, Boymal, 7 February 2005, p. 47.

standards commenced in Europe on 1 January 2005, the committee considers that the Australian commencement date should only be amended if there are compelling reasons to do so. The evidence before this inquiry in relation to the process of transition has not suggested any such reason.

Interpretation of the standards

3.16 The proposed standards are principles-based; that is, they purport to be statements of accounting principles which can guide the accounting profession, so that any accounting treatment which accords with the principles will be regarded as compliant with the new standards. Such a system may be contrasted with the rules-based system in operation in the United States of America, where accounting requirements are spelt out in detail.

3.17 One difficulty associated with principles-based standards is that companies and regulators must interpret the standards in order to assess whether their accounting practices are compliant. In the absence of authoritative interpretations, reporting entities may find that their interpretations of the standards differ from the interpretation of the regulators, exposing them to potential liability.

3.18 The IASB has established the International Financial Reporting Interpretations Committee (IFRIC) to provide authoritative interpretations of the standards. However, IFRIC's work program will focus on global aspects of the standards rather than regional or national variations. In Australia, the Urgent Issues Group (UIG) of the AASB has already been working to provide authoritative interpretations of the new standards. These interpretations are then given force under the standards, by standard AASB1048: *Interpretation and Application of Standards*. However, while these interpretations will support reporting entities, in many cases companies will still have to interpret the standards for themselves.

3.19 A number of submitters and witnesses expressed concern that the standards are not sufficiently supported by authoritative interpretations, or that there are insufficient mechanisms in place to develop those interpretations. In evidence, Mr John O'Grady from Ernst & Young expressed concern that IFRIC may be "somewhat overwhelmed."¹² Similarly, the Group of 100 stated:

there is a growing concern about the existence of appropriate mechanisms to provide timely and authoritative interpretations of the new requirements. Authoritative interpretations by the AASB and/or the IASB are essential to the Standards being applied consistently and in achieving comparability of financial reports. In the absence of such interpretations there is a risk that the major accounting firms and regulators will occupy this space and develop their own interpretations. The G100 does not believe that this would be a satisfactory outcome.¹³

12 *Transcript of Evidence*, O'Grady, 7 February 2005, p. 11.

13 Submission 12, The Group of 100, p. 2.

3.20 The NIA expressed dissatisfaction with the current arrangements whereby the UIG provides interpretations which are given force by AASB1048:

The Australian standard setter has no effective means to bring out all of the practical problems people face in practice. It does have a subcommittee that meets monthly to decide on appropriate interpretations known as the Urgent Issues Group (UIG). The UIG is fast losing relevance because most decisions relating to interpretations will now be dealt with by the IASB's interpretation body, the International Financial Reporting Issues Committee (IFRIC). There is little point for the maintenance of an Australian interpretative body that has to have its work approved formally by the domestic standard setter before it is given legal status via its incorporation into what is known as a 'service standard'. The 'service standard', known as AASB 1048, lists all of the interpretations and gives them legal force by reference. What we are in effect talking about is a system that makes a virtue out of double handling rather than dealing with interpretations with a 'one-stop shop'. Any interpretations the domestic standard setter deals with should only be in circumstances that are uniquely Australian as opposed to the taking of a different view on a technical standard that would result in substantive differences between the international and domestic bodies of literature.¹⁴

3.21 KPMG supported the NIA's view that the process of interpretation should not result in unnecessary differences between the operation of the standards in Australia and overseas:

In most cases, interpretation of IFRS is a global, not just local, issue. We agree that certain matters of interpretation remain outstanding and that shortfalls exist in the IASB based standards. However, the interpretive guidance provided by AASB, ASIC or any other regulatory body should:

- result in compliance with IFRS;
- not be mandatory; and
- not be considered the only outcome that would result in compliance with accounting standards, otherwise a rules-based system like that in the US, which has been highly criticised, may evolve.¹⁵

3.22 In evidence, the AASB indicated that concerns about interpretations are understandable, but expressed confidence that the IFRIC and the UIG will be able to provide appropriate interpretive material as the need emerges:

It is absolutely obvious that the most desirable sort of interpretation is one that would apply throughout the world. Therefore ideally IFRIC should be making the interpretation. Unfortunately IFRIC is reluctant to do that. It is a matter of resources and of the chairman of the IASB saying, 'We've introduced principles based standards; work it out for yourselves.' IFRIC is

14 Submission 19, National Institute of Accountants, p. 2.

15 Submission 17, KPMG, pp. 8-9.

very slow and has a very drawn out process in relation to making interpretations. If international interpretations are not forthcoming then it appears to us that it would be desirable to have an Australian interpretation, because, if there is no international interpretation, we are not achieving comparability world wide. But rather than just giving up, it is better to have comparability within Australia if you cannot get it world wide. So we would defer to the international interpretations all the time—they are the most desirable—but if they are not forthcoming within a reasonable time frame then we believe there is a role for the Australian authoritative interpreter to provide interpretation.¹⁶

3.23 In the committee's view, a balance must be struck between providing reporting entities with adequate interpretative guidance on the one hand, and maintaining the flexibility of a principles-based accounting system on the other. The committee agrees that both IFRIC and the UIG should continue to work to add to the body of authoritative interpretations, but considers that the current lack of comprehensive interpretations is no reason to delay the commencement of the standards.

Consistency between the AASB and IASB standards

3.24 The international harmonisation of a regime of standards carries with it an inevitable tension between maintaining international consistency, and adapting standards to meet local requirements. While the committee received some submissions calling for changes to the proposed standards (which would differentiate them from the international standards)¹⁷, the balance of evidence was in fact critical of any deviation by the AASB away from the international standards. CPA Australia supported the international standards in the following terms:

The suite of international standards, however, is superior to the suite of existing Australian accounting standards that they propose to replace in that they are closely based on IFRSs. Further, they address financial reporting issues that are not addressed by existing Australian accounting standards. By reporting under a comprehensive international regime, Australian for-profit entities will:

- report on a well-understood and internationally recognised basis rather than being based on standards developed in Australia (that are generally not well-understood internationally). The full international suite of standards also will obviate the need for preparers to self-select accounting policies in order to report on transactions and issues that are not directly addressed by existing Australian standards;
- present reports that are able to be understood readily by international investors and comparable with the reports of entities

16 *Transcript of Evidence*, Boymal, 7 February 2005, p. 41.

17 See the discussion of co-operatives and intangible assets, below.

from many other jurisdictions. It is anticipated that the outcome will foster informed international investment that bases an entity's cost of capital on a sound understanding of the risks associated with that entity; and

- present reports that are aligned with international reports, thereby facilitating domestic and international investor confidence in the Australian economy.

Where the AASB considers that an individual Australian standard is superior to its replacement international standard, the AASB is working with the IASB to improve that international standard.¹⁸

3.25 KPMG also argued in favour of greater harmonisation, identifying a number of inconsistencies between the AASB and IASB standards and arguing that:

It is imperative for the Joint Parliamentary Committee in making its inquiries about the Australian Accounting Standards to consider its findings within the context of international developments and the need for one set of high quality globally accepted standards.

We believe that many of the issues facing Australia will be addressed at an international level. Furthermore, it is our view that working in collaboration with the international standards setters will help Australia achieve its legislative objectives and convergence with international standards.¹⁹

3.26 Finally, BHP Billiton argued for greater consistency by allowing the use of optional accounting treatments where IASB standards do so:

In all of our submissions, we have emphasised the view that harmonisation should be done in a manner that ensures Australian accounting standards are identical to those of the IASB. This means that where an IFRS contains options for the basis of accounting applied, those options should remain in the converged Australian standard to ensure that no ... differences exist.²⁰

3.27 On the latter issue, the AASB explained its reasons for withdrawing the optional accounting treatments in the following terms:

The AASB established a quite complicated policy in relation to those. I think you would understand that, if there were a country embracing the international standards that did not have rules or had very loose rules, maybe two or even three ways of doing things could well be acceptable—much better than literally dozens or hundreds of different ways. But if there were a country that had prided itself on having one approach to doing things then the idea of there being just straight out choices would not be such a good idea. The International Accounting Standards Board itself is not all that keen on choices, but some of the standards are quite old, and

18 Submission 11, CPA Australia, p. 2.

19 Submission 17, KPMG, p. 1.

20 Submission 21, BHP Billiton, p. 1.

they were written to get the UK and the US to agree, so both of their methods were included. Basically, many of the choices are rather old compromises.

The AASB adopted the policy that, if more than one method was allowed in the international standards, and one of those methods was a method that we had already been applying in Australia, and that was the only method that we had been applying in Australia, we thought it appropriate not to introduce the alternative but to leave things as they were.²¹

Are the proposed standards genuinely principles-based?

3.28 At a number of points in this report, the committee has referred to the proposed standards as being "principles-based." The committee received a submission from Professor Graeme Dean and Professor Frank Clarke which argued that, in fact, the proposed standards simply amount to another set of rules, which may not support the underlying principle that an accounting system should give a true and fair picture of a reporting entity's financial performance and financial position:

No general principle or principles have been specified, no explanation of how the data to emerge from the [standards] will contribute to a true and fair view of an entity's financial position and performance has been made. Indeed no explanation of the dimensions of what a *true and fair view* entails has been forthcoming. For a successful transition such a specification is a prius.²²

3.29 The professors argued for a "true and fair view over-ride" to be superimposed on the standards, so that above all else, accounting reports must present a true and fair view of an entity's financial position and performance.

3.30 The committee noted standard AASB 101, *Framework for the Preparation and Presentation of Financial Statements*, which acknowledges that there is no "true and fair over-ride" but which argues that the adoption of the standards will result in the production of true and fair reports:

Financial reports are frequently described as showing a true and fair view of, or as presenting fairly, the financial position, financial performance and cash flows of an entity. Although this *Framework* does not deal directly with such concepts, the application of the principal qualitative characteristics and of appropriate accounting standards normally results in financial reports that convey what is generally understood as a true and fair view of, or as presenting fairly, such information.²³

3.31 The international equivalent of AASB 101, known as ISB 1, does however contain a "true and fair view override" in the following terms:

21 *Transcript of Evidence*, Boymal, 7 February 2005, p. 39.

22 Submission 7, Professors Dean and Clarke, p. 4.

23 AASB *Framework for the Preparation and Presentation of Financial Statements*, para 46.

In the extremely rare circumstances in which management concludes that compliance with a requirement in a Standard or an Interpretation would be so misleading that it would conflict with the objective of financial statements set out in the Framework, the entity shall depart from that requirement in the manner set out in paragraph 18 if the relevant regulatory framework requires, or otherwise does not prohibit, such a departure.²⁴

3.32 The AASB explained this departure from the international standard as follows:

Our local legislation at the present time has what you might call twin requirements, but I would say they do not relate to an override. The twin requirements, as one of the other speakers indicated, are to both comply with the accounting standards and give a true and fair view. The Corporations Law says you must comply with the accounting standards as the first initial requirement. If the directors believe that complying with the standards does not produce a true and fair view, then the directors must give as much additional information as is required in order that a true and fair view is also given. So there is an acknowledgement in the law that these are not necessarily exactly the same thing, but it is not an override.

I am afraid I cannot tell you exactly when but in previous Corporations Law in Australia we did have a true and fair view override. The law said something like, 'You must comply with the accounting standards unless this does not give a true and fair view, at which time you do not have to comply with the standards.' The companies made improper use of that, blatantly saying, 'We're not going to comply with the accounting standard because it does not give a true and fair view.' They really were not even giving good reasons; they were just saying: 'That's our view. There you are.' The law was changed to prevent that from happening, and I would fear that, if consideration were given again to a true and fair view override, we would suffer the same problems again.²⁵

3.33 The committee agrees that the presentation of a true and fair statement of a company's financial position and performance should underpin any system of accounting standards. However, the committee considers that this should be accomplished in the manner proposed by the AASB – by the presentation of additional explanatory material as necessary, to provide a clear view where the accounting standards do not. In the first instance, entities must comply with the standards.

Documentation associated with the standards

3.34 During the Senate Economics Legislation Committee's estimates hearings in June 2004, Senators raised with the AASB the fact that some supporting materials required in order to implement the new standards were only available to the public if

24 IASB *IAS1: Presentation of Financial Statements*, para IN7

25 *Transcript of Evidence*, Boymal, 7 February 2005, p. 43.

an annual subscription fee of \$44 is paid. The AASB International Standards Support Materials service continues to charge this annual fee. According to evidence presented before both this committee and the Senate Economics Legislation Committee, this is because the material is owned by the IASB, which insists upon the fee.²⁶

3.35 This committee agrees with views expressed by members of the Senate Economics Legislation Committee that, as a matter of basic principle, such materials should be available free of charge. It is unreasonable to expect reporting entities to report on their financial positions in accordance with supporting material which is not freely available. The committee wishes to express its disappointment that the IASB has not acceded to the request to provide this information free of charge.

3.36 A submission before the committee raised further concerns about the syntax of the standards themselves. Mr Ian Langfield-Smith from Monash University stated:

The standards also fail to satisfy the requirements of s. 224(a)(vi) of the *Australian Securities and Investments Commission Act 2001* (ASIC Act) that standards be “readily understandable”. In particular, the inclusion of editorial comments (or implementation guidance) makes the standards extremely difficult to read, navigate, and interpret. The drafting can only reasonably be described as an exemplar of the worst drafting practice possible...

The absence of definitions of key terms makes the standards unnecessarily difficult to interpret. The reader has to decide if the term is intended to have a technical meaning or an every day meaning. If it is the former, is that meaning the one generally understood in Australia before the making of the 2005 AASB standards, or is it to be found in one or more other 2005 standards? What do we do when the usage differs in those other standards? I find it hard to understand how competent, skilled professionals could think that the standards are easier to understand without defining key terms. The AASB cannot excuse its failure to do so merely because the IASB has not done so. That is not what the community is entitled to expect from the AASB. Having accepted the task, it should be done properly.²⁷

3.37 The AASB in response noted that the drafting was undertaken by the IASB and not the AASB, and that in any event such a comment was "a gross overstatement ... I don't think others have really been complaining along those lines."²⁸

3.38 The committee is, however, satisfied that the standards do not contravene the requirements of the ASIC Act. Section 224 of the ASIC Act outlines the objects of Part 12 of that Act, which relate to the Australian Financial Reporting System. The facilitation of "readily understandable" standards is clearly an object of Part 12, but it

26 *Transcript of Evidence*, Boymal, 7 February 2005, pp. 44-45. See also Senate Economics Legislation Committee, *Transcript of Evidence*, Boymal, 2 June 2004, p. E104.

27 Submission 15, Langfield-Smith, p. 3.

28 *Trasncript of Evidence*, Boymal, 7 February 2005, p. 44.

is not a legal requirement. Consequently, while the committee would encourage the AASB, along with all Commonwealth agencies, to pursue plain English wherever possible, criticism of the syntax of the standards cannot in this case call into question the compliance of those standards with relevant legislation.

3.39 In relation to the definition of terms in the standards, the committee notes that almost all of the standards contain definitions, typically as a section at the beginning of the standard, though a number of them (AASB 1, 2, 3, 4, 5, 6, 1004, 1031) contain definitions in appendices, and a number (AASB 1023, 1038, 1039, 1045, 1046) contain definitional sections towards the end of the standard. Only standards AASB 129: *Financial Reporting in Hyperinflationary Economies*, AASB 130: *Disclosure in the Financial Statements of Banks and Similar Financial Institutions* and AASB 1048: *Interpretation and Application of Standards* do not contain definitional sections. The committee is therefore satisfied that sufficient definitional guidance is in place.

Issues relating to the content of the standards

3.40 In establishing this inquiry, the committee took the view that its objective should not be to focus on the technical content of the standards. The IASB and AASB have conducted extensive consultation in designing the standards, and it would be unproductive for the committee to throw those standards open for additional debate at this time, within the relatively short timeframe of this inquiry. However, two matters relating to the technical content of the standards emerged in evidence before the committee. The committee does not propose to make recommendations in relation to these issues, but will set out the evidence received.

Co-operatives

3.41 The committee received a number of submissions from co-operative entities concerned about the likely impact of the new standards on their operations. Currently, when a new member joins the co-operative they purchase a share in the co-operative, which is then counted as equity. However these "shares" differ from listed, traded shares because the co-operative must refund the value of the share to a Member when that member leaves the co-operative. This obligation to pay leads to difficulties under AASB 132, which states:

A financial liability is any liability that is:

(a) a contractual obligation:

(i) to deliver cash or another financial asset to another entity...²⁹

3.42 Because the co-operative has an obligation to repay its members' initial investment essentially on demand, AASB would classify those member funds as debt rather than as equity. This will result in a substantial shift in the debt to equity ratios of these co-operatives without any actual change in their circumstances or operations.

29 AASB 132, *Financial Instruments: Disclosure and Presentation*, s. 11.

3.43 Submissions from the co-operatives outlined the possible consequences of this change as follows:

There are a number of potentially significant negative consequences of reclassifying member shares from equity to debt:

- it would disrupt the financial ratios and complicate access to finance;
- many co-operatives would find themselves in technical default on their loan agreements which require particular levels of equity;
- a balance sheet that reflected zero equity would make it difficult for co-operatives to secure new debt financing;
- vendors and suppliers who utilise the balance sheet to assess credit worthiness would be confused over the lack of equity and may withhold credit arrangements or force onto co-operatives added credit compliance costs;
- the classification may result in the preparation of misleading financial statements for co-operative companies that will confuse rather than assist members' understanding of those financial statements.³⁰

3.44 The AASB recognised that this is an issue for co-operatives and similarly structured entities, but regarded this challenge as manageable:

... the earth is not going to fall in. Those entities are exactly the same entities they were before. There is going to need to be an educational program so that this is understood by all, but they are identical to the organisations that they were before.

We have been warning them about debt covenants or other contracts that are inappropriately worded for a while and they had better get on with fixing them. Yes, their accounts will look different, but the earth will not fall in. I think the sooner they get on with it and realise that as entities they are completely the same as they were before, the better.³¹

Intangible assets

3.45 The new standards provide rules for the valuation of internally generated intangible assets. In most cases, where there is not an external market to facilitate a market-equivalent evaluation of the value of those assets, they will no longer be given a value. This is a substantial change from current regulatory arrangements, which do not provide specific rules in relation to the valuation of internally generated intangible assets.

30 This point was made in identical terms by the Co-operative Federation of Western Australia (Submission 6), Norco Co-operative Limited (Submission 10), the Co-operative Federation of NSW (Submission 13),.

31 *Trasncript of Evidence*, Boymal, 7 February 2005, pp. 47-48.

3.46 While this was a source of some contention during the development of the standards, there was little evidence on this issue before the committee.³² However, the committee notes the final rationale presented by the Financial Reporting Council for agreeing to the IASB's treatment of internally generated intangible assets:

Australia has been the only significant country, in terms of accounting standards, that has allowed an accounting treatment for the recognition and valuation of internally generated intangible assets. This aspect of Australia's former accounting standards was not highly regarded internationally.³³

Conclusions

3.47 Submissions and evidence received by the committee make it clear that the transitions to the new accounting standards is a major regulatory change which will no doubt bring transitional challenges to large, medium and small reporting entities. The committee was reassured by the AASB's evidence that, in managing this transition process it has established it will maintain, strong communication links with enforcement agencies, including ASIC. While some members of the committee had the view that this relationship might be formalised by a Memorandum of Understanding or similar instrument, the committee's primary concern is that sufficient communication takes place in order for the transition to proceed smoothly.

3.48 The committee is satisfied that this transition is being managed effectively, and that any costs associated with the transition will be more than offset by the benefits of operating under an internationally harmonised set of accounting standards. The committee considers that the standards are in accordance with their governing provisions in the *Corporations Act 2001*, and that they will act in furtherance of the objectives of that Act.

Recommendation 2

The committee recommends that the Senate and House of Representatives do not disallow the Australian Accounting Standards tabled on 30 August 2004 and 16 November 2004.

Senator Grant Chapman

Chairman

32 Intangibles were dealt with by Mr Keith Alfredson (submission 4), the Financial Reporting Council (submission 18) and PricewaterhouseCoopers (submission 22).

33 Submission 18, Financial Reporting Council, p. 3.