

AUSTRALIAN ACCOUNTING STANDARDS BOARD

INTERPRETATIONS MODEL

(June 2006)

Objective

The AASB's objective is a streamlined interpretations function that interacts with the International Financial Reporting Interpretations Committee (IFRIC) to provide guidance to Australian constituents in the context of the formal adoption of International Financial Reporting Standards (IFRSs) in Australia for private sector, public sector and not-for-profit entities, while maintaining a capacity to deal with issues relating to purely domestic Standards. The interpretations function has a flexible structure so that it can be adapted in response to changing circumstances and the nature of the issues to be addressed.

The new model will apply from 1 July 2006.

Background

At its Strategy Meeting in March 2005, the AASB considered that it was timely to review the role, functions and composition of the Urgent Issues Group (UIG). The UIG was established in 1994 and was re-constituted as a committee of the AASB in 2000 when accounting standard-setting arrangements were restructured following amendments to the Corporations Law. While the role of the UIG has remained essentially unchanged, the financial reporting landscape in which it operates has changed considerably, including the ways in which it interacts with the activities of the IFRIC. The AASB took the view that the way in which the UIG identifies and addresses issues, particularly as they relate to the interpretation of Australian equivalents to IFRSs, was no longer appropriate because of changes such as the following:

- (a) the implementation of the Financial Reporting Council's directive on the adoption of IFRSs in Australia for reporting periods commencing on or after 1 January 2005;
- (b) the activities of the IFRIC and the relationship between it and the UIG;
- (c) the importance of achieving IFRS compliance in respect of interpretations of Australian equivalents to IFRSs;
- (d) managing the development of Interpretations in respect of a broader range of entities than those considered by the IFRIC, including public sector and not-for-profit entities, given that AASB Standards apply to a wider range of entities than those issued by the International Accounting Standards Board (IASB);
- (e) the AASB formally approving UIG Interpretations and their changed legal status as they are now given legal effect through reference in Accounting Standard AASB 1048 *Interpretation and Application of Standards*; and
- (f) the establishment of the Trans-Tasman Accounting Standards Advisory Group and the AASB's strategy of engaging more with standard-setters in the Asia-Pacific community.

In April 2005 the AASB formed a sub-committee to prepare recommendations for its consideration in developing an Invitation to Comment prior to formally seeking the views of constituents. The sub-committee consulted widely in developing its recommendations, seeking the views of selected constituents, both organisations and individuals, in writing and in a series of meetings. These included current and former AASB and UIG members. The sub-committee also met with the UIG. The AASB considered the sub-committee's recommendations at meetings in September, October and November 2005 and decided to seek comments from constituents generally on a proposed interpretations model to replace the UIG structure. During this period the AASB's discussions on the recommendations were reported in the AASB *Action Alert* and were the subject of articles in the journals of the professional bodies.

The AASB issued Invitation to Comment (ITC) *Proposed Interpretations Model for Australian Accounting Standards* in November 2005 and requested comments by 18 January 2006. When preparing the ITC the AASB focused on the main features of a concept for a model for developing Interpretations in response to the changes in the financial reporting environment rather than the details of the operation of the proposed model. The AASB received thirteen submissions, including one confidential submission, on the ITC. All non-confidential submissions are published on the AASB's website (www.aasb.com.au).

While the submissions on the ITC generally supported the need for a changed model, respondents expressed concerns about how features of the proposed model (due process, panel membership, role of agenda committee and interaction with the IFRIC) would be implemented. Respondents made a number of suggestions about the operation of the proposed model in respect of the identification of issues, the role of the Interpretations Agenda Committee (IAC) and the membership and composition of panels. Those respondents not supporting the proposal to replace the UIG considered that the UIG was operating effectively and were particularly concerned about the lack of details of the due process to be applied under the proposed interpretations model and the shift away from the representative nature of the UIG. Some considered that the current review should not be undertaken without a comprehensive review of the functions and activities of the AASB.

At its February 2006 meeting the AASB considered the submissions received, noting the concerns about the appointment of panels, particularly losing the representative nature of the UIG, and uncertainties about the due process to be adopted. The AASB addressed these concerns in outlining its expectation of how the proposed model would operate.

The Financial Reporting Council considered the AASB's proposals at its meeting in March 2006 and encouraged the AASB to consider having a public list of people with appropriate skills and experience in the different subject areas which the AASB would draw upon for the selection of advisory panels.

At its April 2006 meeting the AASB agreed to establish a public Register of Potential Advisory Panel Members and to use its best endeavours to ensure that each panel comprises a fair mix of preparers, users and other representative groups. The AASB also noted that inclusion on the register would not necessarily mean that a person will be appointed to a panel because it may be necessary to supplement the public list with additional names to cover a particular topic.

Principal Features of the Interpretations Model

Under the new Interpretations model the AASB will have direct responsibility for developing and approving Interpretations and thus will replace the UIG. The new model will have the following principal features:

- (a) an Interpretations Agenda Committee (IAC) comprising the Chairman and two other AASB members, with the role of considering issue proposals, IFRIC Draft Interpretations and IFRIC Interpretations and recommending a course of action to the AASB. On the basis that it is the primary regulator in respect of the Corporations Act, the Australian Securities and Investments Commission (ASIC) has been invited to accept observer status on the IAC;
- (b) forming Advisory Panels, constituted as a committee of the AASB, as required on a topic-by-topic basis. The role of panels will be limited to preparing alternative views and, where appropriate, recommendations for consideration by the AASB. Each panel will normally comprise 4-8 members, including the Chairman and at least one AASB member. Members will be appointed on the basis of their professional competence and practical experience in the topic area. The AASB agrees that it is important that panels have a balanced composition to ensure that both a depth of knowledge and breadth of perspective are achieved. The AASB will seek to ensure that the perspectives represented include those of preparers, users, auditors and regulators;
- (c) a public Register of Potential Advisory Panel Members on the AASB website. It is expected that members of panels will be drawn from the register. However, depending on the issue to be addressed, the AASB may decide to draw panel members from other sources to achieve an appropriate balance of expertise and experience. Inclusion on the register does not necessarily mean that a person will be appointed to an advisory panel;
- (d) issues relating to interpreting Australian equivalents to IASB requirements that the AASB considers warrant further guidance will, in the first instance, be forwarded to the IFRIC for consideration for inclusion on the IFRIC work program. **The AASB considers that a unique domestic interpretation of Australian equivalents to IASB requirements will be required only in rare and exceptional circumstances.** In addition, the AASB will deal directly with the adoption of IFRIC Interpretations in Australia; and
- (e) the due process will include publishing the recommendations of a panel on the AASB's website for an appropriate period, depending on the nature of the issue, before an AASB meeting. Where the AASB proposes to issue an Interpretation, the Proposed Interpretation will be further exposed by publication on the website for an appropriate period, depending on the nature of the issue, before the AASB considers it for formal adoption. Due process will also include documentation, on public record, of the composition of each panel and the background and experience of each panel member.

The AASB acknowledges that its workload will increase with the additional responsibilities and considers that this can be managed by streamlining its practices to ensure the more efficient use of meeting time and that of the members.

Operation of the Interpretations Model

The AASB expects that the new model will operate as follows:

1 Identification of Issues and Role of Interpretations Agenda Committee

The process for identifying issues for consideration for inclusion on the work program will include the following features:

- (a) issue proposals will be submitted by constituents;
- (b) staff (often in consultation with the proposer) will develop the issue proposal for consideration by the Interpretations Agenda Committee (IAC);
- (c) the IAC will review issue proposals and recommend a course of action to the AASB, giving its reasons. Similar to IFRIC processes, the IAC will, in making recommendations to the AASB, assess issue proposals against the following criteria:
 - (i) the issue is widespread and has practical relevance;
 - (ii) the issue indicates that there are significantly divergent interpretations (either emerging or already existing in practice);
 - (iii) financial reporting would be improved through the elimination of or reduction in diverse reporting methods;
 - (iv) the issue is a narrow implementation or application issue that can be resolved efficiently within the confines of existing IFRSs or Australian Standards;
 - (v) it is probable that the IFRIC or AASB (as relevant) will be able to reach a consensus on a timely basis; and
 - (vi) if the issue relates to a current or planned IASB or AASB project, there is a pressing need to provide guidance on a more timely basis than would be expected from that project; and
- (d) the IAC will meet at a convenient time before each AASB meeting, as appropriate.

IAC Recommendations

It is anticipated that the IAC will structure its recommendations to the AASB as follows:

- (a) *if an issue proposal relates to an Australian equivalent to IFRS* — either:
 - recommend that the AASB take no action and give reasons; or
 - recommend to the AASB that the issue be referred to the IFRIC for consideration for inclusion on its work program.

Decisions by the AASB in respect of all rejected issue proposals relating to Australian equivalents to IFRSs will be sent to the IFRIC for information and published on the AASB's website.

Where the AASB refers an issue proposal to the IFRIC:

- (i) if the IFRIC adds the issue to its work program, the AASB will adopt the IFRIC decisions in respect of including the issue on the IFRIC work program; and
 - (ii) if the IFRIC does not add the issue to its work program, the AASB will assess the reasons for its rejection and, depending on the significance of the issue in Australia and before publishing an agenda rejection statement on the AASB website, decide whether further action, if any, should be taken by the AASB. The AASB may decide to add the issue to its work program and establish an advisory panel. However, the AASB considers that a unique domestic interpretation of an Australian equivalent to IASB requirements will be required only in rare and exceptional circumstances.
- (b) *if the issue proposal relates to domestic requirements that relate only to not-for-profit entities in the public and/or private sectors — either:*
- recommend that the AASB take no action and give reasons; or
 - recommend that the issue be added to the work program and, if required, a panel be established to prepare recommendations for consideration by the AASB.

2 Formation of Panels

An advisory panel for an issue will comprise the AASB Chairman, at least one other AASB member and other persons with a range of skills and experience to reflect different perspectives. In this regard the AASB is cognisant of the views expressed in some submissions on the ITC that in forming panels care should be taken to achieve a balanced composition of members. The formation of panels will be achieved as follows:

- (a) the AASB Chairman, in conjunction with the AASB member(s) allocated to a panel, determines the number of members, membership and the Chair of a panel. The Chair of a panel will be the AASB Chairman or another AASB member;
- (b) membership of a panel will be determined on an issue-by-issue basis. In forming a panel the AASB will use the Register of Potential Advisory Panel Members and, where appropriate, identify other persons to invite for appointment to the panel.

Depending on the issue being addressed, members of a panel will be drawn from preparer and user groups, accounting firms, the accounting bodies, relevant public sector and not-for-profit organisations and academia. For example, a person drawn from an accounting body need not be its technical director or advisor. Likewise, a person from an accounting firm need not be a technical partner as the relevant expertise and experience may reside elsewhere in the firm. This approach is consistent with the objective of forming a panel on a particular issue to marshal the best available combination of technical expertise and diversity of business and market experience while seeking to maintain a balance of views and perspectives on the issue.

This will provide flexibility in accessing the skills and experience relevant to a particular issue. However, the AASB considers transparency in the appointment of panels is essential to good governance, accountability to constituents and the

acceptance of the outputs from the process. The identity and affiliation of panel members will be published on the website. Records will also be kept to briefly explain the skills, expertise or other reasons for appointment of each panel member; and

- (c) panel members will be entitled to reimbursement of reasonable out-of-pocket costs.

3 Due Process

The due process will normally include:

- (a) consideration of issue proposals by the IAC;
- (b) IAC recommendations (including the wording of any proposed rejection statements), reasons, and issue proposals will be published on the website for an appropriate period, depending on the nature of the issue, prior to AASB meetings so that constituents have adequate opportunity to participate in the process by informing the AASB within a short time period whether they support an IAC recommendation. The AASB will discuss the IAC recommendations in public and publish its proposed action in the *AASB Action Alert* and on the website;
- (c) where an advisory panel is formed, it will consider the issue and make recommendations to the AASB. The panel's recommendations and draft Interpretation (if any) will be posted on the website for an appropriate period, depending on the nature of the issue, before being considered at an AASB meeting to enable constituents to make submissions on the proposals. Where the AASB proposes to issue an Interpretation, the Proposed Interpretation will be published on the website for an appropriate period, depending on the nature of the issue, before the AASB meeting at which the AASB considers whether to formally approve an Interpretation;
- (d) consistent with the IASB's *Statement of Best Practice: Working Relationships between the IASB and other Accounting Standard-Setters*, the AASB should liaise with the IFRIC/IFRIC staff on an issue being addressed nationally. Although some constituents have suggested the desirability of obtaining assurance from the IFRIC in some way, the IFRIC has stated that it will not give assurance that a national Interpretation is either consistent or inconsistent with IFRSs; and
- (e) the AASB will consider and vote on the approval of Interpretations in public. As with the making of an Accounting Standard, the approval of an Interpretation will require nine votes in favour.

4 IFRIC Interpretations and Draft Interpretations

Under the model the AASB will be responsible for making submissions on IFRIC Draft Interpretations and considering IFRIC Interpretations for adoption in Australia. As part of this process the IAC will also have the task of recommending to the AASB whether:

- (a) a panel should be formed to develop a draft submission on an IFRIC Draft Interpretation for consideration by the AASB or whether a draft submission should be prepared by staff; and

- (b) the AASB should deal directly with adopting an IFRIC Interpretation in Australia or a panel should be formed to prepare recommendations for the AASB's consideration. It is envisaged that the formation of a panel would occur only where it may be necessary to add Australian material, for example to accommodate specific requirements in respect of public sector entities or to acknowledge Australian legal requirements.

5 Australian Interpretations

The AASB anticipates that from time to time guidance will be required in respect of applying domestic Standards, for example specific requirements that apply only to not-for-profit entities including those in the public sector, such as AASB 1004 *Contributions* and AAS 27 *Financial Reporting by Local Governments*.

The AASB considers that the format and structure of Australian Interpretations should, to the extent feasible, mirror IFRIC Interpretations, with a Basis for Conclusions attached.

6 Secretariat

A member of the AASB technical staff will be responsible for coordinating the work of the IAC. Technical staff will also be assigned to assist advisory panels.
