# The Impact of Approved Accounting Standard AASB 1024 "Consolidated Accounts " on the Information Included in Consolidated Financial Statements

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**Abstract**

The intent of consolidated financial statements is to provide meaningful, relevant, useful, and reliable information about the operations of a group of companies. In compliance with AASB 1024 'Consolidated Accounts', and AAS 24 'Consolidated Financial Reports',a parent entity now has to include in its consolidated financial statements all controlled entities, regardless of their legal form or the ownership interest held. The new Standard also provides a new style of consolidated financial statements format, which requires an increased disclosure of outside equity interest (OEI, formerly minority interest), especially in the Balance Sheet. The purpose of this study is to determine the impact of AASB 1024 on the consolidated financial statements of effected companies. Examination of the financial statements of 52 companies reveals that: (1) the adoption of AASB 1024 (and AAS 24) did significantly alter the structure and format of the basic financial statements, especially the Balance Sheet in terms of disclosing the OEI; and (2) the adoption of AASB 1024 (and AAS 24) had no significant impact on the consolidated financial figures.

## 1. Introduction

In 1991, there was an amendment to the Corporation Act to adopt definitions used in the 'Approved Accounting Standard' prepared by the Australian Accounting Standards Board (AASB). In September 1991, following this amendment, AAS 24 was revised and reissued under AAS 24 "Consolidated Financial Reports", and the AASB also released an Approved Accounting Standard AASB 1024 "Consolidated Accounts", effective for the financial year ended on or after 31 December 1991. Both Standards apply to a parent entity which is a reporting entity; however, while AASB 1024 applies to companies, AAS 24 applies to all entities other than companies.

Based on comparison of information contained in: (1) consolidated financial statements prepared for the last financial year <u>before</u> 31 December 1991 (therefore influenced by provisions of "old" Companies Code/Corporations Act); (2) consolidated financial statements in (1) above restated according to AASB 1024 and the "new" Corporations Act; and (3) consolidated accounts prepared for the first financial year ending on or after 31 December 1991 (therefore influenced by provisions of AASB 1024 and the "new" Corporations Act); the study examines the impact the Accounting Standard on: (i ) information disclosed in financial statements; and (ii) reported financial figures.

## 2. Literature review

Before 31 December 1991, there was no `approved accounting standard` for consolidation. The preparation of financial statements for groups companies was governed by the provisions of the *Companies Act & Codes* and Schedule 7 of the Regulations to the Companies Code. These were then replaced by the *Corporations Law,* which become operative on 1 January 1991, and Schedule 5 of the Corporation Regulations respectively.

Under section 295 of the Corporations Law, the Directors of a (group) holding company were required to have made out, at the end of a financial year, before the deadline (the date where the financial statements should be signed by the Directors ) of that financial year, `group accounts` that:

> "(a) deal with:
> (i) the group's profit or loss for, and
> (ii) the group's state of affairs as at the end of;
> that financial year of the company and the corresponding financial years of the other bodies corporate in the group; and
> (b) give a true and fair view of the profit or loss and state of affairs so far as they concern members of the company".

Such group accounts are in addition to the accounts of the holding company itself.

Section 74 of the Corporations Law, however, provided relief to wholly owned `Australia ` holding companies that were incorporated in any State or Territory of Australia, from the requirement s to prepare group accounts.

however, the Corporations Law allowed only subsidiaries to be consolidated, and subsidiaries were effectively defined as *companies* in which a greater than 50% share holding was held. (Shanahan 1989, p. 75) This provision opened the way to leave assets and liabilities off the consolidated balance sheet by keeping them in (a) companies in which only 50% or less shareholding was held, or in (b) non-corporate bodies such as trusts, partnership, associations and the like.

The Corporations law also allowed four alternatives relating to `group accounts`: full consolidation, two or more sets or consolidated accounts, individual accounts, or a combination of one or more sets of consolidated accounts and one or more sets of individual accounts. Even though Schedule 5 recommended a `full consolidation`, the alternatives provided had the potential to lead to dissimilarities in practice.

Moreover, the law did not clarify the criteria and concept used in consolidating Financial statements. This led to confusion in practice, particularly in treating the `minority interest` and `inter-entity transactions.` (Shanahan 1989)

In late 1991, the Corporations Law was amended and AAS 24/AASB 1024 reissued and approved. Under the new Standards and new legislation, consolidated accounts are now compulsory. The preparation of one set of consolidated accounts is the only form allowed for an economic entity which is a reporting entity. The choices previously given by the Law with respect to alternative formats of the group financial statements have now been deleted.

Futhermore, control rather than ownership, is the criteria which should be used to show the relationship between a parent entity and its subsidiaries. A decision must be made as to Whether entities are controlled before bringing them into the consolidation process. However, subjectivity in the definition of control may result in different opinions about a given situation. If less than 50% ownership exists and control is said to exist, the reason for decision must be disclosed in the accounts. Conversely, if more than 50% ownership exists and control is said not to exist, the reason must also be disclosed. (Commentary, para.(xix))

Under the new standards and new legislation, consolidated accounts for the parent company must now include the assets, liabilities and equities and equities of any legal entity that the company controls, including trusts, partnerships or other entities. The use of wholly owned trusts to keep projects off the balance sheet is no longer effective. (Corporations Law, Sec. 294A(5); Swindells 1991)

However, some entities which were previously required to prepare group accounts are no longer required to do so. it is the existence of users dependent upon the general purpose financial reports which constitutes a reporting entity. If there are no such users, there is no reporting entity, and no requirement to consolidate. This will be the case for many exempt proprietary holding companies. (Swindells 1991, p7)

## 3. Method

### 3.1. Sample

Companies included in the research are those that were classified as the 1991 top 100 companies ranked by the Business Review Weekly (BRW) magazine. The BRW (October 18, 1991) has ranked these Australian companies according to their reveneus. The choice of these companies as the research sample is based on the belief that they are large companies which can be expected to have subsidiaries, such that they have to prepare consolidated financial statements.

### 3.2. Time Period

The time period chosen for the research was the last period to which the 'old' legislative requirements applied, and the first period the AASB 1024 and the 'new' legislative requirements become obligatory. The 'old' legislative requirements applied until 30 December 1991, and were then replaced by the new requirement applicable from 31 December 1991. Therefore, the financial statements for these two periods were required.

### 3.3. Analysis

To fulfill the first objective of the study, the financial statements were analysed in terms of their conformity with the 'old' legislative requirement (for pre-AASB financial statements), and AASB 1024 and 'new' legislative requirements (for the post- AASB 1024 financial statements). In particular, the analysis focused on the consequences of the main differences between the two requirements.

AASB 1024 and the Corporation Law do not apply to most entities within the public sector. However, Requirements regarding consolidated accounts for public sector entities are very similar to those for private sector entities (corporation), as provided in Accounting Standard AAS 24 and respective legislative requirements. For comparison purposes, the public sector organization were also analysed.

To Fulfill the second objective of the study, the analysis was conducted by comparing financial figures of chosen companies as reported at their last pre-AASB 1024 financial report, with their equivalent figures as reported in their first post-AASB 1024 financial report. For most companies, these figures had already been restated to comply with the requirement of AASB 1024 for comparison purpose with the current year figures. Some of them, however, did not restate their last pre-AASB 1024 financial figures according to AASB requirements. If this additional information for these entities was not available, they were excluded from the analysis.

The purpose of this analysis is to examine the changes in financial figures due to application of AASB 1024. Furthermore, to measure the significance of the changes, a statistical test was applied using T-Test.

3.4. Hypotheses

*Null Hypothesis (Ho):*

The application of AASB 1024 (and AAS 24) and new legislative requirements would not significantly affect the financial figures reported in the consolidated financial statement.

*Alternate Hypothesis (Hi):*

The application of AASB 1024 (and AAS 24) and new legislative requirements would significantly affect the financial figures reported in the consolidated financial statements.

## 4. Findings-1

4.1. Characteristics of the sample

Of the top 100 companies in Australia, 48 companies have been excluded from the analysis. The reasons are that 17 did not respond and financial statements were not available, while the remaining 31 companies, branches or non-parent entities (6 companies); non-parent entity public companies (11 companies); new or reorganized companies (3 companies); and 12 companies which have not published their post-AASB 1024 financial statements. The companies included in the analysis were, therefore, 52 companies; being 46 companies which are private sector corporation and 6 which are public sector entities.

4.2. Subsidiaries

Analysis the two potential differences in this area, there are 14 entities specifically affected by the changed definition in AASB 1024 and new legislation requirements, of which one is a public sector entity. These companies, 13 private companies and one public companies, had to include some subsidiaries excluded in their original pre-AASB 1024 financial statements in their restated pre-AASB 1024 financial statements, as many as 41 entities for the private sector companies and 81 entities for the public sector entities. The reasons for inclusion of these subsidiaries for the private companies are shown in the Table 1:

Table 1. Reasons for including originally excluded subsidiaries in the restated pre AASB 1024 financial statements among private companies.

| Reason for inclusion (numbers of subsidiaries) | Number of parent entity |
|---|---|
| 1. Others (Not mentioned) (13) | 3 |
| 2. Control more than 50% of the voting shares (10) | 2 |
| 3. Non corporations (trusts, partnerships, etc.) in which more than 50% of their shares are held by other companies (3) | 2 |
| 4. Control the appointment of Board of Directors (10) | 2 |
| 5. Control through profit share agreement (10) | 1 |
| 6. Agreement that, in substances, gives the parent entity the capacity to enjoy the majority of the benefits and to be exposed to the majority of the risks of subsidiaries (2) | 1 |
| 7. Control over the allocation of financial resources (3) | 1 |

Three of these 13 private sector companies, and also the one public sector entity, did not mention the reasons for including their originally excluded subsidiaries from their pre-AASB 1024 (or pre-AAS 24 for the public company) financial statements. This does not comply with one of the disclosure requirements of AASB 1024 and AAS 24, that is, "the identity of any subsidiary in which the parent entity hold an ownership[ interest and/or voting rights of 50 per cent or less, together with an explanation of how control exists," [emphasis added].

In addition, one private sector company held more than 50% ownership interest in a subsidiary without having any control over that subsidiary. The reason is that the parent entity cannot exercise a majority of the voting rights at meetings of members or directors. Another private sector company, on the other hand, has control over 9 entities though the right to appoint the Board of Directors, even though it did not hold any ownership interest in the controlled entities.

4.3. Outside Equity Interest **(OEI)**

There are two main points to be considered in relation to disclosure requirements for OEI: the nature of disclosure in the Profit and Loss Statement, and in the Balance Sheet. The Pre-AASB 1024 basic format for financial statements were provided in Schedule 5 to the Corporation Regulations, and also AASB 1018: Profit and Loss Account. The financial statements format according to AASB 1024 is provided in Appendix 3 of the standard. However, the basic format according to Schedule 5 and AASB 1018 have not yet been amended, even though the Standards have come into effect. Summary of the two requirements regarding this issue is shown in Table 2

Table 2. Outside Equity Interest Location (Pre- and Post-AASB).

| Location: | Pre-AASB 1024: | AASB 1024: |
|---|---|---|
| Profit & Loss Statement | Deduction in determining 'Operating profit or loss and extra ordinary items after income tax attributable to members of the holding company' | Allocatio of consolidated operating profit |
| Balance Sheet | Part of Equity, shown in its total amount | Part of share capital, retained profits ( or accumulated loss) and reserves |

Analysing these two main points, the findings have been summarised as shown in Table 3. In order to fulfil both Schedule 5 and AASB 1024 requirements, some companies combined these two different format requirements -- showing total amount in the Balance Sheet an Profit an Loss Statement, and provide the detail in from of Notes.

Table 3. Outside Equity Interests Location Distribution -- Private Companies

| Location of Outside Equity Interest in: | Number of companies Pre-AASB Reports | Number of companies Post-AASB Reports |
|---|---|---|
| **Balance Sheet:** | | |
| 1. Does not appear. | 12 | 10 |
| 2. Total amount (Schedule 5) | 27 | 6 |
| 3. Total amount and Notes | 7 | 24 |
| 4. Detail (AASB 1024 ) | 0 | 6 |
| Total | 46 | 46 |
| **Profit & Loss Statement:** | | |
| 1. Does not appear | 11 | 11 |
| 2. Deduction (Schedule 5) | 34 | 34 |
| 3. Allocation (AASB 1024) | 0 | 0 |
| Total | 46 | 46 |

In addition to the information given in Table 3, in the private sector sample four companies had 'wholly owned subsidiaries and hence they did not show any OEI in their financial statements. The Remaining two companies show OEI in their Profit and Loss Account on a one line basis, Without giving any additional notes. However, they show OEI in detailed amount according to the AAS 24 format requirements in their Balance Sheet.

## 4.4. Eliminations

The 'Old' legislation did not indicate whether all the affects of inter-entity transaction should be eliminated partially or totally. AASB 1024, however, clearly requires that all effects of inter-entity transactions be eliminated fully. Analysis of both pre-and post-AASB 1024 financial statements, in both private and public companies, leads to the conclusion that all companies eliminated the effect of inter-entity transaction totally.

## 5. Findings-2:

This section discusses the comparison of the 1991 pre-AASB 1024 consolidated financial figures with the post-AASB 1024 restated consolidated figures to determine whether the application of AASB 1024 and the new legislative requirements had a significant impact on the reported financial figures.The financial figures in the Balance Sheets analysed were: Current Assets, Total Assets, Current Liabilities, Total Liabilities, and Net Assets. Financial figures from the Profit and Loss Statements used for the analysis were Revenues and Operating Profit After Tax (OPAT). Table 4., summarises the financial figures as reported in the Balance Sheets and Profit & Loss Statements.

Table 4. Financial Figures in Balance Sheets and Profit & Loss Statements ($ 000)

| No | Description | Private Companies | | Public Entities | |
|---|---|---|---|---|---|
| | Descriptions | MEAN | STDEV | MEAN | STDEV |
| 1 | **Current Assets** | | | | |
| | Original | 1,088.555 | 899,455 | 1,283,630 | 1,165,675 |
| | Restated | 1.088.456 | 899,559 | 1,283,630 | 1,165,675 |
| 2 | **Total Assets** | | | | |
| | Original | 7.222.878 | 16.536,090 | 24,471,624 | 32,797.026 |
| | Restated | 7.219,013 | 16,592,371 | 24,471.344 | 32.797,056 |
| 3 | **Current Liabilities** | | | | |
| | Original | 1.191,027 | 1.431.881 | 1,860.040 | 1.494.150 |
| | Restated | 1.186,601 | 1,428,579 | 1,860,040 | 1,494,150 |
| 4 | **Total Liabilities** | | | | |
| | Original | 4,390.024 | 13.638,200 | 22,654,322 | 30.551,048 |
| | Restated | 4.419.081 | 13.738,897 | 22,660,212 | 30,550,494 |
| 5 | **Net Assets** | | | | |

| | | | | | |
|---|---|---|---|---|---|
| | Original | 2,881.725 | 8.045.681 | 1.817,304 | 2,409,584 |
| | Restated | 2,799.931 | 7.937.788 | 1.811,135 | 2,409.584 |
| 6 | **Revenues** | | | | |
| | Original | 3,745.848 | 3.793.962 | 2,834,784 | 925,550 |
| | Restated | 3,735,876 | 3.789.183 | 2.831.739 | 921.531 |
| 7 | **OPAT** | | | | |
| | Originial | 51.516 | 533.024 | 275.922 | 448,029 |
| | Restated | 49,264 | 527.104 | 273.215 | 449,922 |

Applying a T-Test, the T-value and P-value for each elements of the Balance Sheet and Profit & Loss Statement are reported in Table 5. The result means that there is no significant difference between pre-AASB and restated post-AASB financial figures reported in the consolidated financial statements.

Table 5. T-Test Result for Changes in Balance Sheet and Profit & Loss Statements Figures.

| | | Private | Companies | Public | Entities |
|---|---|---|---|---|---|
| No | Changes in: | T Value | P-Value | T Value | P-Value |
| 1. | Current Assets | 0.08 | 0.93 | ** | ** |
| 2. | Total Assets | 0.22 | 0.83 | 1.00 | 0.36 |
| 3. | Current Liab's | 1.56 | 0.13 | ** | ** |
| 4. | Total Liabilities | -1.20 | 0.24 | -1.00 | 0.36 |
| 5. | Net Assets | 1.01 | 0.32 | 1.00 | 0.36 |
| 6. | Revenues | 1.37 | 0.18 | 1.23 | 0.27 |
| 7. | Opat | 0.32 | 0.32 | 1.00 | 0.36 |

** No Changes -- no T-test

## 6. Conclusions

From analysing the consolidated financial statements of 52 companies, of which 48 of them are private sector companies, it may concluded that:

(1) AASB 1024, AAS 24 and the 'new' legislative requirements did affect companies in preparing their financial statements, particularly the Balance Sheet. Most of the affected companies applied, for the first time, the format of the Balance Sheet recommended by the Standard.

(2) The Application of AASB 1024 (and AAS 24), did affect the financial figures, and financial ratios derived from these figures, reported in the consolidated financial statements. However, applying T-Test statistics, it can be conclude that such changes were not significant. This conclusion, therefore, rejects the hypothesis that the application of AASB 1024 (and AAS 24) and new legislative requirements would significantly affect the financial figures and ratios reported in the consolidated financial statement.

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