



EXTERNAL REPORTING BOARD

*Te Kāwai Ārahi Pūrongo Mōwaho*

NZ ACCOUNTING  
STANDARDS  
BOARD

## **EXPOSURE DRAFT NZASB 2017-3**

# **PROPOSED AMENDMENTS TO THE SCOPE OF FRS-42 PROSPECTIVE FINANCIAL STATEMENTS FOR TIER 1 AND TIER 2 FOR-PROFIT ENTITIES**

**(ED NZASB 2017-3)**

**Invitation to Comment**

9 November 2017

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# Information for respondents

## Invitation to Comment

The New Zealand Accounting Standards Board (NZASB)<sup>1</sup> is seeking comments on the specific matters raised in this Invitation to Comment. We will consider all comments before finalising the *Amendments to the Scope of FRS-42*.

If you want to comment, please supplement your opinions with detailed comments, whether supportive or critical of the proposals, as both supportive and critical comments are essential to a balanced view.

Comments are most useful if they indicate the specific paragraph to which they relate, contain a clear rationale and, where applicable, provide a suggestion for an alternative. Feel free to provide comments only for those questions, or issues that are relevant to you.

Submissions should be sent to:

Chief Executive  
External Reporting Board  
PO Box 11250  
Manners St Central  
Wellington 6142  
New Zealand

Email: [submissions@xrb.govt.nz](mailto:submissions@xrb.govt.nz)  
([please include the title of the Exposure Draft in the subject line](#))

We would appreciate receiving a copy of your submission in electronic form (preferably Microsoft Word format) as that helps us to efficiently collate and analyse comments.

Please note in your submission on whose behalf the submission is being made (for example, own behalf, a group of people, or an entity).

The closing date for submissions is **28 February 2018**.

## Publication of Submissions, the Official Information Act and the Privacy Act

We intend publishing all submissions on the XRB website ([xrb.govt.nz](http://xrb.govt.nz)), unless the submission may be defamatory. If you have any objection to publication of your submission, we will not publish it on the internet. However, it will remain subject to the Official Information Act 1982 and, therefore, it may be released in part or in full. The Privacy Act 1993 also applies.

If you have an objection to the release of any information contained in your submission, we would appreciate you identifying the parts of your submission to be withheld, and the grounds under the Official Information Act 1982 for doing so (e.g. that it would be likely to unfairly prejudice the commercial position of the person providing the information).

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<sup>1</sup> The NZASB is a sub-Board of the External Reporting Board, and is responsible for setting accounting standards.

## List of abbreviations

The following abbreviations are used in this Invitation to Comment.

FRSB	Financial Reporting Standards Board
GAAP	Generally accepted accounting practice
GPFR	General purpose financial reports
NZASB	New Zealand Accounting Standards Board
XRB	External Reporting Board

## Questions for respondents

	<b>Paragraphs</b>
1. Do you agree with the proposal to remove the words "or chooses" from paragraph 3 and to delete the last sentence of paragraph 46? If you disagree, please provide reasons.	8–14
2. Do you agree with the proposal to remove most of the references to "prospective financial information", including the definition of that term in Appendix A? If you disagree, please provide reasons.	15–20
3. Do you agree with the proposal to delete paragraphs 4–9 from the Scope section of FRS-42? If you disagree, please provide reasons.	21–24
4. Do you agree with the proposal to add paragraph 3A to encourage entities that choose to prepare prospective financial statements to apply the requirements in FRS-42? If you disagree, please provide reasons.	25–27
5. Do you agree with the proposal to delete paragraphs 42, 43, 63 and 64? If you disagree, please provide reasons.	28–37
6. Do you agree with the proposed effective date of annual periods beginning on or after 1 January 2019, with early application permitted, for the proposed amendments to FRS-42? If you disagree, please provide reasons.	42–43
7. Do you have any other comments on ED NZASB 2017-3?	

# 1. Introduction

## 1.1 Background

1. FRS-42 *Prospective Financial Statements* establishes principles and specifies minimum disclosures for entities that prepare general purpose prospective financial statements. FRS-42 was developed by the Financial Reporting Standards Board (FRSB), the predecessor to the NZASB.
2. The New Zealand Accounting Standards Board (NZASB) has reviewed the scope of FRS-42 primarily due to recent changes in the regulatory environment (for example, the issuance of the Accounting Standards Framework and changes to regulations).
3. The NZASB has also become aware of concerns about the scope of FRS-42. Constituents have indicated that there is uncertainty about (i) which entities are required to comply with FRS-42; and (ii) the information to which the standard applies.

## 1.2 Purpose of this Invitation to Comment

4. The purpose of this Invitation to Comment and associated Exposure Draft is to seek comments on the NZASB's proposals to amend FRS-42, and in particular the proposals to amend the scope of the standard.

## 1.3 Timeline and next steps

5. Submissions on ED NZASB 2017-3 are due by 28 February 2018. Information on how to make submissions is provided on page 4 of this Invitation to Comment.
6. After the consultation period ends, we will consider the submissions received, and subject to the comments in those submissions, we expect to finalise these amendments soon afterwards.

## 2. Overview of ED NZASB 2017-3

### 2.1 Summary of the content

7. ED NZASB 2017-3 proposes the following amendments to FRS-42 Prospective Financial Statements.
  - (a) The scope of the standard is amended by:
    - (i) deleting the words “or chooses” from paragraph 3;
    - (ii) deleting most of the references to “prospective financial information”, including the definition of this term in Appendix A;
    - (iii) deleting public sector examples of prospective financial statements; and
    - (iv) deleting the explanation of special purpose prospective financial information.
  - (b) Application of the requirements in the standard is encouraged when an entity chooses to present prospective financial statements.
  - (c) Requirements and guidance that are not relevant in the current statutory financial reporting environment, including paragraphs of the Financial Reporting Standards Board’s Basis for Conclusions on FRS-42 that are no longer relevant, are deleted.
  - (d) Some terminology is amended for consistency with NZ IFRS.

### 2.2 Amendments to the scope of FRS-42

#### Removal of the words “or chooses”

8. FRS-42 was developed before the new Accounting Standards Framework was established.
9. An entity applies XRB A1 Application of the Accounting Standards Framework when it prepares, or when it opts under an enactment to prepare, general purpose financial reports (GPFR) in accordance with accounting standards issued by the External Reporting Board (XRB) (paragraph 2 of XRB A1).
10. The scope of XRB A1 reflects the mandate of the XRB (and hence the NZASB) established under Section 12 of the Financial Reporting Act 2013 – to issue financial reporting standards for the purpose of any enactment that requires financial statements (or a statement, report or information) to be prepared in accordance with GAAP. Any changes to FRS-42 should therefore reflect the role of the NZASB in issuing financial reporting standards for entities required by legislation or regulation to prepare prospective financial statements or prospective financial information in accordance with GAAP.
11. Paragraph 3 of FRS-42 requires both entities that are required to present general purpose prospective financial information in accordance with GAAP and entities that choose to present general purpose prospective financial information to comply with the standard.
12. The reference to “required” in paragraph 3 is generally understood to be an externally imposed financial reporting requirement established through legislation



or regulation. However, the reference to “or chooses” is open to interpretation in determining when compliance with FRS-42 is required.

13. The NZASB is proposing to delete the words “or chooses” from paragraph 3. This will align the scope of the standard with the scope of XRB A1 and the mandate of the XRB/NZASB.
14. The NZASB also proposes to delete the last sentence of paragraph 46 because it refers to entities that choose, but are not required by legislation or regulation, to publish prospective financial statements.

#### **Question for respondents**

1. Do you agree with the proposal to remove the words “or chooses” from paragraph 3 and to delete the last sentence of paragraph 46? If you disagree, please provide reasons.

#### References to “prospective financial information”

15. The NZASB understands from its outreach that it is sometimes unclear which types of prospective financial information are required to be prepared in accordance with FRS-42.
16. Although the definition of general purpose prospective financial statements is generally well understood, constituents have identified the following issues in respect of the references to prospective financial information in FRS-42.
  - (a) The definitions of *general purpose prospective financial statements* and *general purpose prospective financial information* give rise to interpretation issues as both definitions in Appendix A of FRS-42 refer to “future oriented financial statements”.
  - (b) Paragraph 3 of FRS-42 refers to *general purpose financial information*. However, the title of the standard is *Prospective Financial Statements* and the principles and requirements of the standard refer mainly to prospective financial statements. This leads to interpretation issues when considering the extent to which other forms of prospective financial information are within the scope of FRS-42 and must be accompanied by a full set of prospective financial statements.
  - (c) Paragraph 4 of FRS-42 says general purpose prospective financial information includes, but is not limited to, prospective financial statements. The wording “but is not limited to” leads to interpretation issues when determining to what extent other forms of prospective financial information are required to be prepared in compliance with FRS-42.
17. Feedback received during outreach indicates that, in practice, the term general purpose prospective financial information is not ordinarily understood to be limited to prospective financial statements or prospective financial information taken or derived from a complete set of prospective financial statements. Instead general purpose prospective financial information is commonly understood to include other forms of prospective financial information, although it is unclear to what types of prospective financial information FRS-42 should be applied (as noted above).
18. An analysis of the current legislative requirements shows that the forms of prospective financial information to be prepared in accordance with GAAP for for-profit entities comprises:

- (a) full prospective financial statements as defined in FRS-42; and
  - (b) selected items of prospective amounts or information taken or derived from full prospective financial statements prepared in accordance with FRS-42.
19. Under the proposed amendments, FRS-42 will provide the requirements and principles for the presentation of general purpose prospective financial statements. Legislation and regulations will provide the requirements and guidance for presenting selected items of prospective amounts or information extracted from full prospective financial statements prepared in accordance with GAAP.
20. The NZASB proposes to delete most of the references to prospective financial information in FRS-42, including the definition in Appendix A. This will align the scope of FRS-42 with the current regulatory environment, limit the scope of FRS-42 to reflect the mandate of the XRB/NZASB (as discussed earlier) and make it clear that the standard applies when an entity presents prospective financial statements.

**Question for respondents**

2. Do you agree with the proposal to remove most of the references to “prospective financial information”, including the definition of that term in Appendix A? If you disagree, please provide reasons.

Other amendments relating to the scope

21. Paragraphs 4–9 form part of the scope of FRS-42.
22. However, these paragraphs:
- (c) refer to prospective financial information;
  - (d) provide examples of prospective financial information that are both within and outside the scope of FRS-42; and
  - (e) explain the types of prospective financial information that are outside the scope of FRS-42 (for example, special purpose prospective financial information).
23. The NZASB proposes to delete these paragraphs because they are no longer relevant if the standard is to apply only to those entities that have a statutory obligation to present prospective financial statements in accordance with GAAP. The clarification of the scope of FRS-42 removes the need to explain what types of prospective financial statements/information are or are not within its scope.
24. In addition, the public sector examples in paragraph 4 are included in PBE FRS 42 Prospective Financial Statements, the standard applied by Tier 1 and Tier 2 public benefit entities. The placement of these examples in PBE FRS 42 is more appropriate than having them in the for-profit standard given the multi-sector, multi-standards financial reporting framework.

**Question for respondents**

3. Do you agree with the proposal to delete paragraphs 4–9 from the Scope section of FRS-42? If you disagree, please provide reasons.

## 2.3 Voluntary compliance with FRS-42

25. The proposed amendments to the scope of FRS-42 will result in the standard applying only to those entities that have a statutory obligation to present prospective financial statements in accordance with GAAP.
26. However, some entities that fall outside the amended scope of FRS-42 may elect to present general purpose prospective financial statements. The NZASB is of the view that it would be appropriate to encourage entities to apply the requirements in FRS-42 in these circumstances.
27. The NZASB, therefore, proposes to add paragraph 3A to encourage those entities that choose to present prospective financial statements to apply the requirements in FRS-42 to those statements.

### Question for respondents

4. Do you agree with the proposal to add paragraph 3A to encourage entities that choose to prepare prospective financial statements to apply the requirements in FRS-42? If you disagree, please provide reasons.

## 2.4 Alignment with the current statutory financial reporting environment

28. The NZASB proposes to make the following amendments to FRS-42 to align the requirements more closely with the current statutory financial reporting environment.

### Parent and group entities

29. Paragraph 42 includes factors to consider when an entity decides whether it should prepare both parent entity and group prospective financial statements.
30. Under the new statutory financial reporting framework as it applies to for-profit entities, a parent entity is not required to prepare both parent entity and group general purpose financial statements.
31. The NZASB therefore proposes to delete paragraph 42 as the paragraph is not relevant in the current statutory financial reporting environment.
32. The NZASB also proposes to delete paragraph 63 which requires disclosures associated with the requirements in paragraph 42.

### A subset of an entity

33. Paragraph 41 requires prospective financial statements to be prepared in accordance with the accounting policies expected to be used in the future for reporting historical general purpose financial statements.
34. Paragraph 43 is an expansion of paragraph 41 in that the requirement in respect of accounting policies applies to both an entity and/or a subset of that entity. It refers to a borrowing group as defined in the Securities Regulations 1983 as an example of a subset of an entity.
35. Although there is still a concept of "borrowing group" under the FMC Regulations, it is in relation to non-bank deposit takers (NBDTs) and there is no longer a

requirement for the preparation of prospective financial statements in respect of a borrowing group.

36. The NZASB proposes to delete paragraph 43 because it is no longer relevant and paragraph 41 is clear about the preparation of prospective financial statements in accordance with the accounting policies to be used in the future for reporting historical general purpose financial statements.
37. The NZASB also proposes to delete paragraph 64 which requires disclosures associated with the requirement in paragraph 43.

#### **Question for respondents**

5. Do you agree with the proposal to delete paragraphs 42, 43, 63 and 64? If you disagree, please provide reasons.

### **2.5 FRSB's Basis for Conclusions**

38. FRS-42 was developed by the Financial Reporting Standards Board (FRSB), the predecessor to the NZASB.
39. The FRSB's Basis for Conclusions reflects the deliberations of the FRSB during a time when the New Zealand legislative framework for financial reporting was different to what it is today. However, some of the FRSB's deliberations are still relevant to the general principles and requirements in FRS-42.
40. The NZASB proposes to delete the paragraphs in the FRSB's Basis for Conclusions that relate to the scope of the standard (paragraphs BC9–BC16). These paragraphs are no longer relevant and have been deleted to avoid the risk that they might be read out of context.

### **2.6 Changes to terminology**

41. The proposed amendments also include minor editorial corrections to align the terminology in FRS-42 with the terminology in NZ IFRS. For example, see the proposals to amend paragraphs 37 and 38.

### **2.7 Effective date and other comments**

42. An effective date of annual periods beginning on or after 1 January 2019, with early application permitted, is proposed for the amendments to FRS-42.
43. The proposed amendments might result in fewer entities applying FRS-42. There would be no additional costs for an entity that falls outside the scope of the standard.

#### **Questions for respondents**

6. Do you agree with the proposed effective date of annual periods beginning on or after 1 January 2019, with early application permitted, for the proposed amendments to FRS-42? If you disagree, please provide reasons.
7. Do you have any other comments on ED NZASB 2017-3?

## EXPOSURE DRAFT

### Amendments to the Scope of FRS-42

This [draft] Standard was issued on [Date] by the New Zealand Accounting Standards Board of the External Reporting Board pursuant to section 12(a) of the Financial Reporting Act 2013.

This [draft] Standard is a disallowable instrument for the purposes of the Legislation Act 2012, and pursuant to section 27(1) of the Financial Reporting Act 2013 takes effect on [Date].

Reporting entities that are subject to this [draft] Standard are required to apply it in accordance with the effective date, which is set out in Part C.

In finalising this [draft] Standard, the New Zealand Accounting Standards Board has carried out appropriate consultation in accordance with section 22(1) of the Financial Reporting Act 2013.

This [draft] Standard has been issued to amend the scope of FRS-42 *Prospective Financial Statements* and align its requirements with the current statutory financial reporting environment.

## AMENDMENTS TO THE SCOPE OF FRS-42

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ISBN

## AMENDMENTS TO THE SCOPE OF FRS-42

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## Part A

### Introduction

This [draft] Standard amends the scope of FRS-42 *Prospective Financial Statements* so that it applies only to an entity that is required by legislation or regulation to present general purpose prospective financial statements in accordance with generally accepted accounting practice (GAAP). Most references to prospective financial information have also been removed as part of clarifying the scope of FRS-42.

The amendments also align the requirements in FRS-42 with the current statutory financial reporting environment and the mandate of the XRB/NZASB to issue standards for entities with a statutory obligation to prepare, or that opt under an enactment to prepare, general purpose financial reports in accordance with accounting standards issued by the XRB.

Minor editorial corrections have also been made to align the terminology with that used in NZ IFRS.



## Scope

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This Standard applies to Tier 1 and Tier 2 for-profit entities.

## Part B: Amendments to FRS-42 *Prospective Financial Statements*

The Introduction is amended. New text is underlined and deleted text is struck through.

### Main features of the Standard

FRS-42 applies where an entity is required, ~~or chooses,~~ by legislation or regulation to present general purpose prospective financial ~~statements information that comply with generally accepted accounting practice~~. Entities applying the Standard are required to present a complete set of general purpose prospective financial statements for the reporting period for which interim or annual historical general purpose financial statements will subsequently be presented.

...

Paragraphs 1, 3 and 10 are amended, paragraph 3A is added and paragraphs 4, 5, 6, 7, 8 and 9 are deleted. Paragraph 1.1 is provided for context. New text is underlined and deleted text is struck through.

### Objective

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- 1 The objective of this Standard is to establish principles and specify minimum disclosures for entities that are required by legislation or regulation to present general purpose prospective financial statements (~~hereafter also referred to as “prospective financial statements” except where otherwise stated~~) in accordance with generally accepted accounting practice. ~~To provide users with high quality general purpose prospective financial information,~~ This Standard requires that an entity presenting general purpose prospective financial information statements presents a complete set of prospective financial statements using the best information that could reasonably be expected to be available and which meet certain qualitative characteristics.

### Scope

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- 1.1 **This Standard applies only to Tier 1 and Tier 2 for-profit entities.**
- 2 [Deleted]
- 3 **An entity shall apply this Standard where it is required by legislation or regulation, ~~or chooses,~~ to present general purpose prospective financial statements in accordance with generally accepted accounting practice information.**
- 3A An entity is encouraged to apply all the requirements in this Standard when it chooses, to present general purpose prospective financial statements.
- 4 ~~[Deleted]General purpose prospective financial information includes, but is not limited to:~~
- (a) ~~prospective financial statements required to be published by public sector entities (for example, forecast financial statements of the Crown, forecast financial statements of government departments and Crown entities, and forecast financial statements in annual plans and long term council community plans of local authorities); and~~
- (b) ~~prospective financial statements published in a prospectus, investment statement, advertisement for an offer of securities or other similar documents, including prospective financial statements published in order to satisfy the requirements of securities legislation or regulations.~~
- 5 ~~[Deleted]An entity shall apply the principles in this Standard to any prospective financial information published in conjunction with prospective financial statements.~~
- 6 ~~[Deleted]Examples of prospective information to which this Standard does not apply include:~~

## AMENDMENTS TO THE SCOPE OF FRS-42

- (a) ~~special purpose prospective financial information;~~
- (b) ~~prospective information expressed solely in general terms; and~~
- (c) ~~prospective non financial information.~~

~~Nonetheless application of the principles and requirements of this Standard to prospective financial information outside the scope of this Standard is encouraged to the extent applicable.~~

7 ~~[Deleted] Special purpose prospective financial information is prepared for external users who are able to require, or contract for, the preparation of special reports to meet their specific information needs. It may be prepared in a form agreed to by the parties.~~

8 ~~[Deleted] Prospective information which is expressed solely in general terms includes qualitative statements about future prospects. Such statements are commonly found in:~~

- (a) ~~management's discussion and analysis within an entity's financial report; and~~
- (b) ~~commentary in statements of intent provided by government departments and Crown entities and in long term council community plans provided by local authorities.~~

~~However, the above information, where presented, should be consistent with any current published prospective financial statements.~~

9 ~~[Deleted] Prospective non financial information includes forward looking disclosures about an entity's objectives, activities and performance targets. Non financial information is often provided because financial information alone is unlikely to meet all the needs of users. In the case of public sector entities, legislation may require the publication of prospective non financial information such as objectives, nature and scope of activities and performance targets in relation to objectives, outputs or outcomes. Where non financial and financial information is published together they should be consistent.~~

10 **An entity whose prospective financial statements comply with FRS-42 shall make an explicit and unreserved statement of such compliance in the notes. Prospective financial statements shall not be described as complying with FRS-42 unless they comply with all the requirements of FRS-42. An entity shall not describe prospective financial statements as complying with IFRSs. An entity wishing to assert that prospective financial statements comply with NZ-GAAP may assert compliance with FRS-42 and NZ-GAAP as it relates to prospective financial statements.**

...

Paragraphs 37, 38 and 40 are amended. New text is underlined and deleted text is struck through.
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...

37 The prospective ~~cash flow~~ statement of cash flows shall separately disclose major classes of gross cash receipts and gross cash payments arising from each of the following categories of cash flows, except to the extent that such cash flows are reported on a net basis, as permitted by the relevant standard:

- (a) ...

38 In the prospective statement of cash flows ~~statement~~:

- (a) ...

39 ...

40 Where an entity presents prospective financial information in addition to the information reported in the prospective financial statements, the relationship of that additional information to the information reported in the prospective financial statements shall be explained. For example, where an entity presents a prospective amount for earnings before interest, tax, depreciation and revaluation movements in addition to a prospective ~~income~~ statement of profit and loss and other comprehensive income that includes the minimum disclosures in paragraphs 31 to 33, the relationship of prospective earnings before interest, tax, depreciation and revaluation movements to the prospective profit or loss shall be explained. The explanation may be by way of reconciliation.

Paragraphs 45 and 46 are amended and paragraphs 42 and 43 are deleted. Paragraphs 41 and 44 are provided for context. New text is underlined and deleted text is struck through.

## Accounting policies

- 41** **Prospective financial statements shall be prepared in accordance with the accounting policies expected to be used in the future for reporting historical general purpose financial statements.**
- 42 ~~[Deleted]Where an entity presents both parent entity and group financial statements for general purpose historical financial reporting, it should consider whether both parent entity and group prospective financial statements should be presented. Factors to consider include the purpose and relevance of the prospective financial statements and whether, in the absence of group prospective financial statements, the statements that are presented meet the qualitative characteristics set out in paragraphs 16 and 17 of this Standard.~~
- 43 ~~[Deleted]Where an entity presents prospective financial statements in respect of the reporting entity for general purpose financial reporting and/or a subset of that reporting entity, such as the borrowing group (as defined in the Securities Regulations 1983):~~
- ~~(a) — the prospective financial statements for the reporting entity for which general purpose financial reports will subsequently be prepared shall be prepared in accordance with the accounting policies expected to be used in the future for reporting historical general purpose financial statements;~~
  - ~~(b) — the prospective financial statements for the sub-entity such as the borrowing group shall be prepared in accordance with the accounting policies expected to be used in the future for reporting historical general purpose financial statements except where regulations otherwise require.~~

## Periods covered by prospective financial statements

- 44** **The reporting periods covered by prospective financial statements shall coincide with those for which interim or annual historical general purpose financial statements will subsequently be presented.**
- 45 When an entity presents historical general purpose financial statements for a period for which prospective financial statements have previously been presented, the comparative requirements in FRS-44 *New Zealand Additional Disclosures* (paragraphs 11.1 and 11.2) are relevant. Where legislation or regulation requires prospective financial ~~statements information~~ to be prepared for a reporting period which differs from the period for which historical general purpose financial statements ~~or information~~ will subsequently be presented, an entity is compelled to comply with such legislation or regulation. However, in such cases the entity may be able to comply with both this Standard and the relevant legislation or regulation by presenting prospective financial information for the balance of the current reporting period and for the subsequent interim or annual reporting period.
- 46 The number of reporting periods covered by prospective financial statements may vary considerably depending on the relevant legal requirements and the purpose and objective for which the prospective financial statements are prepared. In general, the greater the number of future reporting periods included in prospective financial statements, the more unreliable and uncertain the prospective financial statements become. Entities should exercise caution about publishing prospective financial statements for periods beyond that required by legislation or regulation. ~~Entities publishing prospective financial statements, other than those required to publish prospective financial information by legislation or regulation, should exercise caution in presenting prospective financial statements for more than one reporting period.~~

Paragraphs 63 and 64 are deleted. New text is underlined and deleted text is struck through.

## Disclosure of accounting policies

...

- 63 ~~[Deleted]Where an entity publishes both parent entity and group financial statements for historical financial reporting purposes but does not publish group prospective financial statements, it shall disclose the reasons for not presenting group prospective financial statements.~~
- 64 ~~[Deleted]Where an entity publishes prospective financial statements in respect of a subset of a reporting entity in accordance with paragraph 43 it shall disclose:~~
- ~~(a) — the reasons for presenting prospective financial statements for the subset; and~~

~~(b) whether the entity intends to publish historical financial statements for the subset of the reporting entity for the period or periods covered by the prospective financial statements.~~

...

Paragraph 71 is amended and the definition of general purpose prospective financial information in Appendix A is deleted. New text is underlined and deleted text is struck through. Paragraph 72G is added.

71 Comparison of prospective financial statements with actual financial results is an essential element of accountability. In the case of ~~issuers~~ FMC reporting entities a comparison of actual financial results against the originally published statements is important because it provides users with a comparison of actual performance with the projected performance at the time the entity raised funds. Some entities provide long-term prospective financial statements which are updated annually, prior to the beginning of the year. In such cases a comparison of actual financial results with the most recent prospective financial statements published prior to the beginning of the period is generally relevant. Where information is revised during the course of a year, the reasons for revising the information and an explanation of the differences between the originally published prospective financial statements and the historical financial statements should be given.

## Effective date

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72 ...

72G *Amendments to the Scope of FRS-42*, issued in [date], amended paragraphs 1, 3, 10, 37, 38, 40, 45, 46 and 71, added paragraph 3A and deleted paragraphs 4–9, 42, 43, 63 and 64, and the definition of general purpose prospective financial information in Appendix A. An entity shall apply those amendments for annual periods beginning on or after [1 January 2019]. Earlier application is permitted.

## Appendix A Defined terms

*This Appendix is an integral part of the Standard.*

<del>general purpose prospective financial information</del>	<del>One or more future-oriented financial statements prepared for external users who are unable to require, or contract for, the preparation of special reports to meet their specific information needs.</del>
<b>general purpose prospective financial statements</b>	Future-oriented financial statements prepared for external users who are unable to require, or contract for, the preparation of special reports to meet their specific information needs.

Paragraph BC1 is amended, headings are inserted above paragraphs BC1 and BC2 and paragraphs BC4–BC8 and the related heading are added. New text is underlined and deleted text is struck through.

## **NZASB Basis for Conclusions on FRS-42 *Prospective Financial Statements***

*This Basis for Conclusions accompanies, but is not part of, FRS-42.*

### **Introduction**

BC1 This Basis for Conclusions summarises the New Zealand Accounting Standards Board’s (NZASB’s) considerations in amending FRS-42 ~~in 2013~~.

### **2013 Amendments**

BC2 The NZASB noted that there was a conflict between the requirements of FRS-42 and the Securities Regulations 2009. In the case of an initial offering of equity securities by a public issuer, the Securities Regulations 2009 (Schedule 1, Clause 11) require the presentation of prospective financial statements for the balance of the current period, and the subsequent interim or annual accounting period. In contrast, FRS-42 required the presentation of prospective financial statements for the reporting period for which annual historical general purpose financial statements will subsequently be presented.

BC3 The NZASB considered that it would be desirable for the reporting period requirements in the Regulations and FRS-42 to be aligned. Having regard to the importance of comparisons between prospective and actual financial statements, the NZASB amended paragraph 44 of FRS-42 to permit the presentation of prospective financial statements for an interim period when an entity is proposing to present historical financial statements for that period. The NZASB considered that this amendment was consistent with the objectives of the Financial Reporting Standards Board (FRSB) when it originally developed FRS-42. The NZASB noted that the FRSB had sought to avoid unnecessary differences between the Securities Regulations and FRS-42, whilst highlighting the importance of being able to compare prospective financial statements with subsequent historical financial statements.

### **[Date] Amendments to the Scope**

BC4. The NZASB reviewed and made changes to the scope of FRS-42 primarily due to changes in the regulatory environment (for example, the issuance of the Accounting Standards Framework and changes to regulations).

BC5. The NZASB was also made aware of issues arising with the scope of FRS-42. There was uncertainty about to which entities the Standard applies and the prospective financial information to which it applies.

BC6. The NZASB issued *Amendments to the Scope of FRS-42* in [Date]. This amending standard amended the scope of FRS-42 so that it applies to entities that are required by legislation or regulation to present general purpose prospective financial statements in accordance with generally accepted accounting practice (GAAP). This scope reflects the fact that the NZASB issues financial reporting standards for entities that have a statutory requirement to prepare GAAP-compliant financial statements.

BC7. Most references to prospective financial information were also removed as part of clarifying the scope of FRS-42.

BC8. The NZASB also took the opportunity to align the requirements in FRS-42 with the current statutory financial reporting environment by, for example, deleting public sector examples of prospective financial statements and by deleting requirements about parent entity and group prospective financial statements.

Paragraphs BC9–BC16 and the related heading are deleted. A footnote is added to paragraph BC19 and the Appendix. New text is underlined and deleted text is struck through.

**FRSB Basis for Conclusions on  
FRS-42 *Prospective Financial Statements***

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## FRSB Basis for Conclusions on FRS-42: *Prospective Financial Statements*

*This Basis for Conclusions accompanies, but is not part of, FRS-42.*

*This Basis for Conclusions has not been revised by the NZASB, except for Paragraphs BC9–BC16 which have been deleted by the NZASB because they are no longer relevant. This also avoids the risk that they might be read out of context.*

### Introduction

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BC1 This Basis for Conclusions summarises the Financial Reporting Standards Board’s (FRSB) considerations in reaching its conclusions on FRS-42: *Prospective Financial Statements* in 2005. Individual FRSB members gave greater weight to some factors than to others.

### Background

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BC2 In March 2004 the FRSB agreed that a detailed review of FRS-29: *Prospective Financial Information* (FRS-29) (issued 1996) should be carried out with a view to improving the Standard in light of:

- (a) issues arising from an enquiry by the Securities Commission into Vertex Group Holdings Limited. As a result of the issues raised in this enquiry the review had the objective of eliminating uncertainty regarding the distinction between projections and forecasts; and
- (b) concerns raised by the Office of the Controller and Auditor-General about the appropriateness of some of the requirements and commentary in that Standard for public sector entities – in particular local authorities – preparing forecast financial statements in accordance with new legislative requirements.

BC3 In 2003 the FRSB proposed limited changes to FRS-29 to clarify:

- (a) the distinction between a forecast and a projection; and
- (b) the position where prospective financial information is part projection and part forecast.

The proposed amendments to the definition of “A projection” were exposed for comment on 23 July 2003, with a comment date ending on 15 September 2003. However, the FRSB subsequently decided that the adoption of New Zealand equivalents to IFRSs and changes to requirements for public sector entities justified a broader review of the Standard, and did not proceed with these limited amendments.

BC4 ED 103 *Prospective Financial Information*, which proposed a revision of FRS-29, was issued in May 2005 with a response date of 16 August 2005. Nine responses were received. In order to obtain feedback from a wider range of constituents the FRSB also sought additional feedback from constituents that had not submitted a formal response to ED 103.

BC5 The main issues raised in the context of this review, the FRSB’s proposals in ED 103, respondents’ comments and the conclusions reached in finalising FRS-42 are summarised in the following paragraphs.

### International harmonisation

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BC6 In developing the Standard the FRSB noted the desirability of harmonising with other international guidance dealing with prospective financial information. At the time of developing the Standard no jurisdiction other than Canada had issued a financial reporting standard that established requirements in respect of prospective financial information. However, a range of guidance including international audit guidance and guidance for directors was considered (refer References for a list of guidance considered in the review).

BC7 Some respondents to ED 103 expressed concerns about proceeding with a Standard based on ED 103. These respondents proposed deferring the development of a new Standard to allow for a review of existing Securities legislation and regulations and stressed the desirability of aligning New Zealand’s securities regulations with those of Australia. The FRSB decided to proceed with issuing a Standard based on ED 103. In making this decision the FRSB:

- (a) noted that the majority of respondents supported the FRSB’s proposals to revise FRS-29;
- (b) noted the imminent need for guidance for local authorities required to prepare forecast financial statements;

## AMENDMENTS TO THE SCOPE OF FRS-42

- (c) noted the practical difficulties faced by entities preparing information under FRS-29; and
- (d) agreed that although harmonisation of Securities legislation and regulations with Australia may be highly desirable, it is likely to take some time. The FRSB noted that Australia does not currently have a financial reporting standard on prospective financial statements. Current Australian guidance on prospective financial information has been issued by the securities regulator and is different in nature to a financial reporting standard.

BC8 As noted above, the FRSB considers that trans-Tasman harmonisation of financial reporting requirements for prospective financial reporting is highly desirable. The FRSB notes that the Securities Commission also shares this view. The FRSB has therefore actively sought to interest other parties in developing a trans-Tasman standard on prospective financial reporting. Current legislative differences would make it difficult to achieve complete harmonisation but possible legislative change following the forthcoming trans-Tasman mutual recognition of offers of securities may assist this process. The FRSB considers that FRS-42 would provide a good starting point for the development of harmonised requirements. In an effort to promote a harmonised standard on prospective financial reporting the FRSB has contacted or consulted the Australian Accounting Standards Board (AASB), the Australian Securities and Investment Commission (ASIC) and the Trans-Tasman Accounting Standards Advisory Group. The FRSB will continue to work with these parties and the Securities Commission with a view to developing a harmonised Standard in the future.

### Scope

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~~BC9–BC16 [Deleted by NZASB] The Standard is intended to provide guidance for all entities publishing general purpose prospective financial statements. It has been drafted in such a way that it can be applied by profit oriented and public benefit entities<sup>1</sup> both prior to, and following, the application of New Zealand equivalents to International Financial Reporting Standards (IFRSs). For example, it acknowledges the existence of current legislative requirements governing the preparation of prospective financial statements by public sector entities and uses terminology appropriate for all entities. Following the adoption of IFRSs in New Zealand the FRSB agreed that the format of the Standard should be consistent with recent IFRSs. Paragraphs are numbered sequentially and have equal authority. Paragraphs in bold type state the main principles. Definitions are included in an appendix and are in italics the first time they appear in the Standard.~~

~~BC10 The Standard applies to entities that are required, or choose, to present general purpose prospective financial information. Although the regulations or legislation giving rise to the obligation to present general purpose prospective financial information may refer to one or more prospective financial statements, (for example, a prospective cash flow statement), entities applying the Standard are required to present a complete set of prospective financial statements. They are also required to apply the principles in the Standard to any prospective financial information published in conjunction with general purpose prospective financial statements. These requirements reflect the FRSB's resolution to promote best practice in general purpose prospective financial reporting. The FRSB does not consider that the presentation of a single prospective financial statement in the context of general purpose prospective financial reporting is best practice.~~

~~BC11 The FRSB noted that pro forma information, based on alternative scenarios, is often included in a prospectus and considered the application of the Standard to such pro forma information. For example, where an acquisition is expected to occur during the period, a prospectus may include both prospective financial statements based on the assumption that the acquisition takes place on the expected date and additional information based on the assumption that the projected acquisition will occur on alternative dates. Where such additional prospective pro forma information is published together with the types of general purpose prospective financial statements outlined in paragraph 4, it would fall within the scope of the Standard. However, the Standard does not apply to:~~

- ~~(a) verbal prospective financial information disclosures or earnings guidance published by a New Zealand Exchange Limited listed issuer;~~
- ~~(b) individual items of prospective financial information, such as sales forecasts published in an annual report; or~~
- ~~(c) historical pro forma statements.~~

~~BC13 Prior to issuing ED 103 the FRSB considered whether the scope of the Standard should encompass individual items of prospective financial information published as part of an annual or other report containing general purpose financial information. However, the FRSB noted that it would be difficult to clearly establish the~~



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type of information covered by the Standard and considered that such a change would represent a significant change in market practice and would lead to higher compliance costs.

~~BC14 Some respondents to ED 103 considered that the requirements of the Standard should also apply to items (a) and (b) in paragraph BC 12. One suggestion was that the Standard should require that such prospective financial information be extracted from prospective financial statements prepared in accordance with the Standard. The FRSB considered extending the scope of the Standard to cover prospective financial information extracted from prospective financial statements. The FRSB did not agree that it was appropriate for it to extend the requirements of a financial reporting standard in this way but nevertheless considered that the requirements of the Standard could be applied more widely. For example, the FRSB considered that information extracted from prospective financial statements should be consistent with those prospective financial statements. The FRSB decided that the title of the Standard should be “Prospective Financial Statements” in order to more clearly signal the FRSB’s role in developing requirements for financial statements.~~

~~BC15 The Standard does not apply to special purpose prospective financial information (paragraph 6). That is, it does not apply to information prepared for external users who are able to require, or contract, for information to meet their special needs. Examples of prospective financial information prepared for special purposes include a cash flow forecast prepared for lenders and a pro forma consolidated financial report presented to a board to support a proposed acquisition.~~

~~BC16 The Standard does not apply to prospective information expressed solely in general terms (paragraph 6). Prospective information expressed solely in general terms includes:~~

~~(a) management’s discussion and analysis within an entity’s financial report; and~~

~~(b) commentary in statements of intent provided by government departments and Crown entities and in Long Term Council Community Plans provided by local authorities.~~

~~Although this discussion or commentary may include qualitative and quantitative statements regarding components of prospective financial statements, it does not fall within the scope of the Standard. Only prospective financial information presented on the face of a prospective financial statement or in the notes accompanying that statement falls within the scope of this Standard.~~

## Best information

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BC17 Based on feedback from respondents, the FRSB included an additional principle of best information. This principle requires that an entity use the best information that could reasonably be expected to be available at the time prospective financial statements are prepared in determining the assumptions and other information used in the preparation of the prospective financial statements. Although the information in prospective financial statements is inherently uncertain, the FRSB considered that users are entitled to prospective financial statements that are based on the best information that could reasonably be expected to be available to the entity. This principle applies regardless of whether the prospective financial statements reflect current activities or changes to an entity’s business, including alternative scenarios. The FRSB considered that application of the principle of best information was likely to result in prospective financial statements that meet the four qualitative characteristics.

## Reasonable and supportable

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BC18 FRS-42 requires that the information in prospective financial statements be reasonable and supportable and faithfully represent the assumptions and information on which the statements are based. This requirement was not in ED 103. The FRSB considered that this requirement was a logical extension of the requirement that assumptions be reasonable and supportable. In considering this proposal the FRSB noted a concern that had been expressed during the development of ED 103 that it would be difficult for entities in start-up mode or presenting alternative scenarios to be able to meet such a requirement. New Zealand’s securities legislation differs from that of many other jurisdictions in that New Zealand entities can seek funds from the public prior to having established operations, that is, without any historical information on which to base the prospective financial information. The FRSB addressed this concern by explicitly acknowledging in the Standard that the information in prospective financial statements is subject to uncertainty, particularly where an entity is changing the nature of its operations or presenting alternative scenarios. The FRSB considered that even in such circumstances entities should be mindful of whether the outcomes reflected in the prospective financial statements are feasible.

## Qualitative characteristics

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- BC19 The FRSB agreed that the Standard should include a discussion of the four qualitative characteristics of understandability, relevance, reliability and comparability described in the New Zealand Equivalent to the IASB *Framework for the Preparation and Presentation of Financial Statements* (NZ *Framework*) and in the *Statement of Concepts for General Purpose Financial Reporting* (*Statement of Concepts*) and their applicability to prospective financial statements (paragraphs 16 and 17).<sup>2</sup> This is based on the premise that the qualities of useful information for establishing financial reporting standards for historical financial statements are also applicable to prospective financial statements.

### Understandability

- BC20 The understandability of prospective financial statements is largely determined by the clarity of the disclosures and the way in which information in such statements is presented. Users need sufficient information to enable them to make judgements about the assumptions employed and the risks associated with those assumptions. The Standard (paragraph 55) therefore requires disclosure of:
- (a) the bases on which the significant assumptions have been prepared, including the principal sources of information from which they have been derived;
  - (b) the extent to which actual events and transactions have been reflected in the prospective financial statements;
  - (c) the factors that may lead to a material difference between information in the prospective financial statements and the actual financial results prepared in future reporting periods; and
  - (d) the assumptions made in relation to those sources of uncertainty and the potential financial effect of the uncertainty on the prospective financial statements.
- BC21 In an attempt to make prospective financial statements more understandable the Standard requires that significant assumptions be presented in a manner that makes their significance understandable to users and notes that ranking is one way of doing this.

### Relevance

- BC22 The Standard states that for prospective financial statements to be “relevant” the statements should be capable of assisting users to make economic or other decisions by helping them evaluate present or future events or correct their past evaluations. To be relevant, prospective financial statements must be provided in a timely manner and be able to be confirmed in future periods. In considering the attributes applicable to relevant prospective financial statements the FRSB agreed that prospective financial statements have value for assessing actual financial results prepared in future reporting periods.

### Reliability<sup>3</sup>

- BC23 The information in prospective financial statements is inherently uncertain. It cannot be reliable in the sense that historical financial statements are reliable. The description of reliability in the Standard (paragraph 17) is based on the requirements of the NZ *Framework* and the *Statement of Concepts*. The disclosures required by paragraph 55 are intended to allow users to assess the degree of reliability of information in prospective financial statements, including the quality of the assumptions on which the information is based.

### Comparability

- BC24 Prospective financial statements should be capable of comparison with current and subsequent information about the actual financial performance of an entity based on consistent application of accounting policies, reporting periods and presentation. Prospective financial statements should be capable of being retrospectively validated. The Standard therefore requires that prospective financial statements be prepared in accordance with the accounting policies expected to be used in the future and for the usual reporting period of the entity (paragraphs 41 and 44).

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<sup>2</sup> The references to the NZ *Framework* and the *Statement of Concepts* in this paragraph are to documents that were relevant at the time FRS-42 was first issued. They have since been superseded.

## Forecasts and projections

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- BC25 FRS-29 differentiated between forecasts and projections as follows:
- “A forecast” means prospective financial information prepared on the basis of assumptions as to future events that the governing body reasonably expects to occur associated with the actions the governing body reasonably expects to take as at the date that the information is prepared (best-estimate assumptions).
- “A projection” means prospective financial information prepared on the basis of one or more hypothetical but realistic assumptions (or “what-if” scenarios), that reflect possible courses of action for the reporting periods concerned as at the date that the information is prepared.
- BC26 The FRSB noted that these definitions had been the subject of some uncertainty. In an attempt to remove this uncertainty, in June 2003 the FRSB proposed limited changes to FRS-29 to clarify:
- (a) the distinction between a forecast and a projection; and
  - (b) the position where prospective financial information is part projection and part forecast.
- BC27 These changes were deferred pending a more detailed review of the Standard. As part of the more detailed review the FRSB reconsidered the usefulness of the distinction between forecasts and projections. In the course of its deliberations the FRSB:
- (a) noted that although a number of international documents refer to forecasts and projections, the distinction between the two is not consistent between jurisdictions. Prospective financial information may be information based on best estimates or reasonable grounds, commonly referred to as forecasts, or assumptions relating to possible alternative outcomes, commonly referred to as projections. It may also be based on a mixture of the two. The term forecast usually implies that there is reasonable assurance as to the expected operations in the forecast period and there is a reasonable degree of control over the nature and extent of those operations. A projection is subject to more uncertainty than a forecast because the quality of the evidence and assumptions available to support it may be less reliable. Some international guidance distinguishes between forecasts that preparers confidently expect to meet and other prospective financial information. However, not all jurisdictions address the issue of how to label information which includes a mix of best-estimate information and hypothetical assumptions. Nor do the international pronouncements require prospective financial information to be clearly labelled as either a projection or a forecast;
  - (b) considered the relevant requirements in Australia, in the context of trans-Tasman harmonisation. Guidance published by the Australian Securities and Investments Commission (ASIC) PS 170 Prospective Financial Information (PS 170) states that prospective financial information should not be included in a disclosure document if there are no reasonable grounds for it. PS 170 states that prospective financial information supported only by hypothetical assumptions does not, by itself, establish reasonable grounds for prospective financial information in a disclosure document (PS 170.21). The FRSB noted that this position is consistent with Australian securities legislation and regulations (see section 728(2) and Practice Note [PN 67.2]). ASIC has stated that it considers that best practice would be to refrain from including projections in a disclosure document where:
    - (i) the company is in the start-up phase;
    - (ii) the company will substantially change its operations following the capital raising; and
    - (iii) the company’s present activities constitute research and development of products and the development is not significantly advanced so as to warrant a reasonable expectation that the products will be commercialised.

By contrast, New Zealand entities in start-up phase are required to comply with the Securities Regulations 1983. Given the differences between the Australian and New Zealand legislative requirements, the opportunities for harmonisation are constrained;
  - (c) noted that most of the international material is in the form of guidance for auditors or directors or guidelines issued by securities regulators rather than financial reporting standards. The one jurisdiction that has established financial reporting requirements, Canada, does not address the issue of prospective information which is a mix of best-estimate information and hypothetical assumptions;
  - (d) noted criticism of the distinction between forecasts and projections voiced by the International Capital Markets Group (ICMG), a co-operative venture of the International Federation of Accountants, the Section on Business Law of the International Bar Association and the International Federation of Stock Exchanges (as reported in ICAEW, 2000). In 1998, the ICMG reported the results of an extensive survey of capital market participants and published the results in “Prospective Financial Information: An international perspective on the types, purposes and limitations of Prospective Financial Information”. The ICMG noted that:

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“...many respondents ... felt that making distinctions between the component parts of PFI served only to complicate further the issue and there was not general support for this distinction. Even respondents who recognised the intended distinction between forecasts and projections felt that it was not generally understood. While a technical definition of these terms can be provided, the user of PFI may not be willing to investigate the nuances of such a difference, and it sometimes may not even be necessary.

The lack of a clear dividing line between the two terms “projection” and “forecast” can lead to uncertainty and a degree of inconsistency, especially in borderline cases. However, generally respondents felt that the distinction seemed to be of little relevance as, in both cases, the potential user of the information is basing an investment decision on highly subjective information.”; and

- (e) expressed concerns that requiring all entities to clearly label prospective financial information as either a forecast or a projection would lead to the majority of such information being labelled as a projection. The FRSB considered that if this occurred it would result in less useful information for users of prospective financial statements.

BC28 The FRSB also considered the comments of those who supported a distinction between forecasts and projections. Those who expressed this view considered that:

- (a) the fact that the terms are used in various international pronouncements should be considered in the context of international harmonisation;
- (b) there is no research which specifically addresses the impact of removing the distinction on prospective financial information and the assessments of users;
- (c) the labelling of prospective financial information as forecasts or projections provides useful signals to users as to the reliability of the information and is helpful from an enforcement perspective; and
- (d) if the distinction is removed, in the absence of more specific guidance, entities may continue to use such terms to convey the nature of prospective financial information to users.

BC29 After consideration of the matters outlined above, and after having regard to the available international material, the FRSB decided not to require entities to distinguish between a forecast and a projection in prospective financial statements. The FRSB considered that the Standard should require information to be disclosed about the degree of uncertainty associated with prospective financial statements (paragraphs 49 to 59). This includes an explanation of the risks that actual performance as reflected in historical financial statements may differ from prospective financial statements, and an assessment of the impact of such variations on the financial statements (for example, sensitivity analysis).

### **Assumptions underlying prospective financial information**

BC30 In view of the decision to remove the distinction between forecasts and projections the FRSB decided that the main focus of the Standard should be on the formation of assumptions and the appropriate degree of disclosure required to ensure that information in prospective financial statements is reliable and useful. The Standard states that “Assumptions shall be based on the best information that can reasonably be expected to be available to the entity, be consistent among themselves, be consistent with the current plans of the entity to the extent that this is relevant, and be applied consistently. An entity shall have a reasonable and supportable basis for the determination of assumptions underlying prospective financial statements.” (paragraph 18).

BC31 The Standard acknowledges that application of the principle of best information and the manner in which an entity demonstrates that it has a reasonable and supportable basis for assumptions will depend on the circumstances (paragraphs 19 to 23). The FRSB considered that where assumptions are uncertain, for example, where they relate to alternative possible scenarios, the entity can help users assess the degree of uncertainty by providing information on the potential range of values and the central estimate for the item. However difficulties could arise in circumstances such as the following:

- (a) an entity may be in a start-up phase;
- (b) an entity may substantially change its operations;
- (c) an entity may be reliant on research and development which is not sufficiently advanced to warrant a reasonable expectation that products will be commercialised;
- (d) the information in the prospective financial statements indicates a return significantly higher than industry competitors;
- (e) the prospective financial statements cover a long period of time; and
- (f) the information in the prospective financial statements relates to possible alternative scenarios.

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- BC32 The FRSB questioned whether it would be possible for assumptions to be considered to have a reasonable and supportable basis in such circumstances. The FRSB acknowledges that entities in a start-up phase will have more difficulty in meeting this requirement. Because some entities in start-up phase will be required to prepare prospective financial information in accordance with securities regulations the Standard includes guidance on how an entity in start-up phase can demonstrate a reasonable and supportable basis for assumptions. In other circumstances an entity will need to consider whether the information in the prospective financial statements meets the criterion of understandability. Application of the requirement that assumptions have a reasonable and supportable basis may lead to less prospective financial information being published than occurred under FRS-29.
- BC33 Users need to know the nature of the uncertainties that will affect an entity over the period of the prospective financial statements and to understand the potential impact on the prospective financial statements if assumptions are not borne out in practice.
- BC34 The FRSB noted that in some circumstances prospective financial statements may be based on assumptions that are not expected to occur, or where an entity is unsure as to which set of assumptions best reflects what will happen in the future. For example, the prospective financial statements may be based on the assumption that an acquisition will occur at the beginning of the period, when the acquisition is expected to occur at some later, but unknown date. It could be argued that such information does not have a reasonable and supportable basis. However, the FRSB considered that where such prospective financial information is presented to assist users in understanding prospective financial statements based on expected events, the purpose of the information is highlighted and the assumptions are clearly disclosed, the requirement that the information have a reasonable and supportable basis would be satisfied.
- BC35 Assumptions should not be misleading. Assumptions may frequently be interdependent and lead to the formation of other assumptions. It is important that assumptions do not overlap or result in conflicting outcomes. Where assumptions are interdependent, the treatment of the interdependent assumptions in the prospective financial statements should be consistent.
- BC36 Assumptions should be relevant and only assumptions which materially affect the prospective financial statements or would be of specific significance to users should be disclosed. Preparers should avoid duplication and inclusion of irrelevant assumptions.

## **Presentation of prospective financial statements**

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- BC37 The FRSB noted that the Office of the Controller and Auditor-General had sought clarification of the requirements in FRS-29 regarding the format of prospective financial information. The requirement in FRS-29 to present prospective financial information in the format expected to be used in the future for reporting historical information did not specify whether prospective financial information was to be presented for both a parent entity and a group if the historical financial information was presented in this manner. The FRSB considered whether this issue should be specifically addressed in this Standard. The FRSB noted that the Local Government Act 2002 requires forecast financial statements for the local authority parent entity and permits forecast financial statements for entities under the local authority's control, which would include group financial statements of the local authority. Long-term council community plans are required to cover a 10-year period and the inclusion of group prospective financial statements for the mainly profit-oriented subsidiaries can pose practicality and commercial sensitivity concerns. There are also differing views on the relevance of group prospective financial statements in a local authority context where the primary focus of users is on the proposed level of future rates. In view of this, the FRSB decided that preparers shall determine the format and content of prospective financial statements. Factors that preparers should consider include the purpose for which the prospective financial information is prepared, its relevance and whether, in the absence of an entity's group prospective financial statements, the prospective financial statements as presented meet the qualitative characteristics. The FRSB also agreed that where an entity publishes both parent entity and group financial statements for historical financial reporting purposes but does not publish group prospective financial statements, the reasons for not publishing group prospective financial statements shall be disclosed.
- BC38 The FRSB considered several issues relating to presentation of prospective financial statements, including:
- (a) whether the Standard should encourage or require entities to present a full set of prospective financial statements; and
  - (b) the level of detail required as a minimum to be shown in prospective financial statements.

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- BC39 In ED 103, the FRSB proposed to encourage, but not require, entities to present a complete set of prospective financial statements. The FRSB had noted in ED 103 that:
- (a) legislative and regulatory requirements varied. For example, securities regulations required only a cash flow statement but many public sector entities are required by legislation to prepare prospective financial statements; and
  - (b) as a minimum, FRS-29 required entities to prepare a statement of prospective financial performance (referred to in the current Standard as an income statement) and a statement of accounting policies. The FRSB considered that, as an individual statement, a prospective income statement was of limited usefulness. Rather than requiring any one prospective financial statement to be presented, the FRSB proposed in ED 103 to encourage all entities to present a complete set of prospective financial statements.
- BC40 However, the FRSB re-considered this issue based on submissions to ED 103. As a result, the FRSB agreed to require entities to present a complete set of prospective financial statements. In coming to this decision, the FRSB noted that:
- (a) a fundamental change in the Standard from FRS-29 is the requirement for prospective financial information to meet the same qualitative characteristics as historical financial information. This indicates that the same quality information and the same complete set of financial statements should be required to present historical and prospective financial information. More importantly, the FRSB agreed that an entity is able to meet the necessary qualitative characteristics only if a complete set of statements, rather than one or more individual statements, is disclosed;
  - (b) requiring individual prospective financial statements (for example, the requirement in FRS-29 for a prospective income statement or the requirement in securities regulations for a prospective statement of cash flows) was of limited usefulness. The FRSB considered that each prospective financial statement provides different but complementary information about the entity and only a complete set of prospective financial statements can give users a full picture of the future prospects of the entity; and
  - (c) entities, in drawing up prospective financial statements, will invariably need to consider aspects of all the statements whether one or all statements are published, as information in the statements is interrelated. It is therefore not unduly onerous for the information to be disclosed, compared to the benefits of disclosing the information to users.
- BC41 As far as the level of detail required to be shown in prospective financial statements was concerned, and after due deliberation, the FRSB decided that a requirement to comply with all the disclosure requirements in NZ IAS 1 *Presentation of Financial Statements* and other presentation standards would be too onerous. However, the FRSB also decided that some additional disclosures over and above those required by FRS-29 were appropriate to meet the objective of high quality financial reporting. For example, the FRSB increased the level of disclosure required in respect of income statements and cash flow statements.
- BC42 FRS-42, paragraph 32, requires that all entities present an analysis of expenses using a classification based on either the nature of expenses or their function within the entity. This requirement mirrors that in NZ IAS 1 in respect of general purpose historical financial statements. From 2007 all entities will be required to comply with NZ IAS 1. The FRSB initially proposed (ED 103 paragraph 27) that only public benefit entities be required to present an analysis of expenses. However, following consideration of comments by respondents, the FRSB decided that an entity preparing prospective financial statements should be required to present information on expenses in a manner consistent with that required in its historical financial statements.

### **Periods covered by prospective financial statements**

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- BC43 Three issues were identified as being important in relation to periods covered by prospective financial statements. These were:
- (a) the length of the reporting period, for example, quarterly, six monthly or annually;
  - (b) consistency of the reporting period with the usual annual reporting period of the entity; and
  - (c) the number of future reporting periods, for example, 2 years, 5 years or 10 years.
- BC44 The FRSB concluded that, except as otherwise required by legislation or regulations, the reporting period should be the same as for historical financial statements (paragraph 44). For example, if the company

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presented financial statements half yearly and annually then prospective financial statements could be presented half yearly and annually.<sup>4</sup>

- BC45 The Standard requires that the reporting periods covered by prospective financial statements coincide with those for which annual historical general purpose financial statements will subsequently be presented (paragraph 44). ED 103 proposed that entities complying with legislation or regulation which requires prospective financial information to be prepared for a reporting period which differs from the usual reporting period of the entity, be permitted to prepare prospective financial information for only the period required by legislation or regulation. However, based on feedback from respondents, the FRSB agreed to require the use of a consistent reporting period. This requirement enhances comparability between prospective financial statements and subsequent historical financial statements. The FRSB noted that respondents referred to the emerging practice of seeking Securities Commission approval to present prospective financial information for the balance of the current reporting period and for the subsequent reporting period.
- BC46 The FRSB noted that, in general, the greater the time period covered by prospective financial statements, the more unreliable and uncertain the prospective financial statements would become. The FRSB noted that in some cases the number of periods required to be included in prospective financial statements is specified in legislation. In other situations the time period may be dependent on the circumstances and the associated risks. Factors affecting the time period include:
- (a) the operating cycle, for example in the case of a major construction project the time required to complete the project may dictate the period covered;
  - (b) the degree of reliability of the assumptions, for example, if an entity is introducing a new product the prospective period may be relatively short. Alternatively if the entity's business is owning property under long-term lease, a relatively long prospective period might be reasonable; and
  - (c) the needs of users, and/or legislative requirements, for example long-term council community plans are required for 10 years.

### **Disclosure of bases for assumptions, risks and uncertainties**

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- BC47 Disclosure of the assumptions underlying prospective financial statements were considered by the FRSB to be the most important factor in providing prospective financial information that would be consistent with the four qualitative characteristics (paragraphs 49 to 59). The main issues which were considered to be important in relation to the disclosure of assumptions were the following:
- (a) the bases on which the significant assumptions have been prepared, including the principal sources of information from which they have been derived;
  - (b) the extent to which actual events and transactions have been reflected in the prospective financial statements;
  - (c) the factors that may lead to a material difference between information in the prospective financial statements and the actual financial results prepared in future reporting periods; and
  - (d) the assumptions made in relation to those sources of uncertainty and the potential financial effect of the uncertainty on the prospective financial statements.
- BC48 The Standard notes that additional disclosures may be used to present information on the possible range for an individual item. Presenting prospective financial information as a range may reduce the risk that investors will place undue weight on it. However, a range must be small enough to give meaningful information about an entity's prospects. If a range is given, the link between the assumptions and the upper and lower ends of the range should be clear and a more favourable figure or fact should not be given undue prominence.
- BC49 The FRSB noted that as well as disclosure of the assumptions relating to prospective financial statements it would also be necessary to disclose the risks in relation to these assumptions and the likelihood that the results in the prospective financial statements might not be achieved. In general it was considered that assumptions and risks go hand in hand. The higher the degree of uncertainty surrounding an assumption the greater the risk that the information in the prospective financial statements would be unreliable or misleading.
- BC50 The FRSB considered that due to the risks and uncertainties relating to prospective financial statements it would be prudent to include a warning to readers regarding the predictive character of prospective financial statements and the risks in placing undue reliance on information in those statements.

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### References<sup>5</sup>

ICAEW Guidance	Institute of Chartered Accountants in England and Wales, 2003, <i>Prospective Financial Information—Guidance for UK Directors</i>
ICAEW Guidance	Institute of Chartered Accountants in England and Wales, 2000, <i>Discussion Paper Prospective Financial Information—Challenging the Assumptions</i>
AUS 804	Auditing and Assurance Standards Board of the Australian Accounting Research Foundation, revised 2002, <i>Auditing Standard AUS 804—The Audit of Prospective Financial Information</i>
AGS 1062	Auditing and Assurance Standards Board of the Australian Accounting Research Foundation, 2002, <i>Auditing and Assurance Guidance Statement AGS 1062—Reporting in Connection with Proposed Fundraisings</i>
CICA AuG 6	Canadian Institute of Chartered Accountants, 1989, <i>Assurance and Related Services Guideline—The Examination of a Financial Forecast or Projections Included in a Prospectus or Public Offering Document</i>
CICA – Section 4250	Canadian Institute of Chartered Accountants, <i>Section 4250 Future-oriented Financial Information</i>
ISAE 3400	International Auditing and Assurance Standards Board, International Standard on Assurance Engagements 3400— <i>The Examination of Prospective Financial Information, IFAC Handbook of International Auditing, Assurance, and Ethics Pronouncements</i> ; 2005 Edition
ASIC PS 170	Australian Securities and Investments Commission (ASIC), 2002, <i>PS 170 Prospective financial information</i>
ASIC	Draft ASIC Guide, July 2005, <i>Disclosing pro forma financial information</i>

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<sup>5</sup> This Appendix refers to documents that were relevant at the time FRS-42 was first issued. Some of these documents have since been superseded.



## **Part C**

### **Effective Date**

This [draft] Standard is effective for annual periods beginning on or after [1 January 2019]. Earlier application is permitted.