Financial Reporting Standard No. 42

Prospective Financial Statements (FRS-42)

Issued December 2005 and incorporates amendments up to and including 31 August 2013

This Standard was issued by the New Zealand Accounting Standards Board of the External Reporting Board pursuant to section 24(1)(a) of the Financial Reporting Act 1993.

This Standard is a Regulation for the purposes of the Regulations (Disallowance) Act 1989.

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CONTENTS

Financial Reporting Standard No. 42 *Prospective Financial Statements* (FRS-42) is set out in paragraphs 1–73 and Appendices A and B. All the paragraphs have equal authority. Paragraphs in bold type state the main principles. Terms defined in Appendix A are in italics the first time they appear in the Standard. Definitions of other terms are given in the Glossary.

FRS-42 should be read in the context of its objective and the New Zealand Equivalent to the IASB *Conceptual Framework for Financial Reporting 2010* (NZ *Framework*). NZ IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

Introduction

General purpose prospective (future oriented or forward looking) financial statements are based on assumptions about the future and other information, and thus relate to events and actions which have not yet occurred. Although evidence may be available to support the assumptions on which the general purpose prospective financial statements are based, such evidence is itself usually future oriented and therefore speculative in nature.

Given that anticipation of the future environment is associated with considerable uncertainty, the preparation of general purpose prospective financial statements requires the exercise of significant judgement.

General purpose prospective financial statements are less amenable to objective verification than historical data. When working with, or using, general purpose prospective financial statements, it is essential to understand their inherent limitations.

Main features of the Standard

FRS-42 applies where an entity is required, or chooses, to present general purpose prospective financial information. 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.

The Standard requires that an entity use the best information that could reasonably be expected to be available in determining the assumptions and other information used in the preparation of general purpose prospective financial statements. It also requires that the prospective financial statements be understandable, relevant, reliable and comparable and that the information in the prospective financial statements be reasonable and supportable.

The assumptions used must:

(a) be based on the best information that could be reasonably expected to be available at the time prospective financial statements are prepared;

(b) be consistent among themselves;

(c) be consistent with the current plans of the entity to the extent that this is relevant;

(d) be applied consistently; and

(e) have a reasonable and supportable basis.

The Standard requires disclosure of:

(a) the entity's operations and activities;

(b) the purpose for which the prospective financial statements have been prepared;

(c) significant assumptions;

(d) any changes to the entity's existing business;

(e) the bases on which the significant assumptions have been prepared, including the principal sources of information from which they have been derived;

(f) the extent to which actual events and transactions have been reflected in the prospective financial statements;

(g) the factors that may lead to a material difference between the prospective financial statements and the actual financial results presented in historical financial statements in future reporting periods;

(h) the assumptions made in relation to those sources of uncertainty and the potential financial effect of the uncertainty on the prospective financial statements;

(i) significant accounting policies; and

(j) a cautionary note regarding possible variations in reported results.

The Standard is operative for an entity's prospective financial statements published on or after 1 June 2006. Earlier application is permitted.

Reduced Disclosure Regime

Tier 2 for-profit entities must comply with all the provisions in FRS-42.

Financial Reporting Standard 42

Prospective Financial Statements (FRS-42)

Objective

1 The objective of this Standard is to establish principles and specify minimum disclosures for entities that present *general purpose prospective financial statements* (hereafter referred to as "*prospective financial statements*" except where otherwise stated). To provide users with high quality *general purpose prospective financial information*, this Standard requires that an entity presenting general purpose prospective financial information present 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

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, or chooses, to present general purpose prospective financial information.

4 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 An entity shall apply the principles in this Standard to any prospective financial information published in conjunction with prospective financial statements.

6 Examples of prospective information to which this Standard does not apply include:

(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 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 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 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.**

11 [Deleted]

General principles

12 Prospective financial statements prepared using the principle of best information that are reasonable and supportable and that meet the qualitative characteristics outlined in paragraphs 16 and 17 of this Standard are likely to be of a high quality and assist users in forming, revising or confirming their expectations about the future.

Best information

13 **An entity shall 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 information used in the preparation of the prospective financial statements.**

Reasonable and supportable

14 **The information in prospective financial statements shall be reasonable and supportable and faithfully represent the assumptions and information on which the statements are based.**

15 The information in prospective financial statements is, by definition, uncertain and its preparation requires the exercise of judgement. Events and circumstances may not occur as expected or may not have been predicted. In addition, the entity may subsequently take actions which differ from the proposed courses of action on which the prospective financial statements are based. In seeking to demonstrate that the information in the prospective financial statements is reasonable and supportable, an entity considers whether:

(a) the course of action reflected in the prospective financial statements represents the entity’s proposed course of action, or, where alternative scenarios are presented, that those scenarios are feasible;

(b) it has a reasonable and supportable basis for the determination of assumptions underlying the prospective financial statements. Ways in which an entity can demonstrate that it has a reasonable and supportable basis for the assumptions underlying the prospective financial statements are discussed in paragraphs 20 and 21; and

(c) it has used appropriate information.

Qualitative characteristics

16 **In order to meet the needs of users, prospective financial statements shall meet the qualitative characteristics outlined in the New Zealand Equivalent to the IASB *Framework for the Preparation and Presentation of Financial Statements*[1] (NZ *Framework*). Accordingly, the statements shall be understandable, relevant, reliable and comparable.**

17 In giving effect to the principle in paragraph 16, for prospective financial statements to be:

(a) **understandable**—the information in the statements should be described, aggregated, classified and presented in a format and style that is able to be clearly understood by users. For prospective financial statements to be understandable, users will need sufficient information to be able to make judgements about the assumptions employed and the risks associated with those assumptions.

[1] In February 2011 the NZ *Framework for the Preparation and Presentation of Financial Statements* was replaced with the equivalent to the IASB *Conceptual Framework for Financial Reporting*. The qualitative characteristic of reliability in the old *Framework* is the same as the qualitative characteristic of faithful representation in the *Conceptual Framework*.

(b) **relevant**—the information in 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. For prospective financial statements to be relevant they must have predictive value and be able to be confirmed, or otherwise, in future periods.

(c) **reliable**—the information in the statements should be free from material calculation error, and unbiased. The reliability of prospective financial statements is affected by the appropriateness of the assumptions and the sources of uncertainty. Users should be able to assess the reliability of prospective financial statements and identify the factors that make the statements more or less reliable.

(d) **comparable**—the statements should measure and display like items, transactions and events in a consistent manner. 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.

Assumptions

18 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.

19 An assumption is a view taken about the future for the purpose of preparing prospective financial statements. Assumptions are taken as being true for the purpose of preparing prospective financial statements but could change later. An assumption is made where some facts are not yet known or decided. In preparing prospective financial statements an entity generally needs to make assumptions regarding economic and business conditions and proposed courses of action. For example, an entity may assume that the nature of its operations and principal activities for the period of the prospective financial statements will be consistent with the operations and activities outlined in certain plans and strategies of the entity. Information used in the preparation of prospective financial statements may include the current plans and strategies of the entity, some of which may be published, market surveys, industry statistics, economic and other indicators or specialised studies.

20 A reasonable and supportable basis for an assumption may be the past performance of the entity itself, the performance of similar entities, feasibility or other studies that provide objective corroboration, and the prevailing economic or operating environment. The extent of detailed information supporting each assumption and an assessment of the degree of certainty associated with each assumption will vary according to circumstances, and will be influenced by factors such as the significance of the assumption and the availability and quality of the supporting information. The degree of reliability of assumptions is enhanced by the following:

(a) the robustness of the process to develop assumptions;

(b) use of an independent third party to review assumptions;

(c) use of specialist skills to develop assumptions;

(d) consistency with an entity's documented strategies and plans;

(e) documented analysis of related risks in relation to future actions and events;

(f) ensuring that information is complete and free from material calculation error;

(g) comparability with past performance of the entity and other similar entities; and

(h) basing assumptions on information presented in market surveys, industry statistics, economic and other indicators or specialised studies.

21 Where prospective financial statements present information on activities that have no track record and that are not subject to considerable management control and discretion, it is more difficult to establish that there is a reasonable and supportable basis for the assumptions. Ways in which an entity preparing prospective financial statements in a start-up situation can demonstrate a reasonable and supportable basis for the assumptions include:

(a) thorough research of the market opportunities and pilot testing;

(b) use of a model that has been used for similar entities or activities and which is reviewed and updated;

(c) detailed analysis by area of activity (for example, goods and services by market, product line or geography and cost by function);

(d) management plans that are consistent with the estimates;

(e) non-financial indicators of future financial results;

(f) external market surveys, general economic indicators and views of people knowledgeable in the field of activity that are consistent with the estimates; and

(g) involvement of people with appropriate experience and expertise across the full range of the entity's activities.

22 Assumptions are frequently interdependent. An assumption may affect many items within prospective financial statements and lead to the formulation of other assumptions. Where assumptions are interdependent, the treatment of the interdependent assumptions in prospective financial statements should be consistent. For example, an entity may have a capital project that will need to be funded during the period of the prospective financial statements. As such, assumptions will be required about the source of the funding and the interest rates related to the funding. It may also be necessary to make assumptions about the related increase in depreciation charges.

23 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 in which an entity prepares prospective financial statements. Prospective financial statements reflect an entity's assumptions regarding its proposed courses of action for the period of the prospective financial statements. An entity may propose to continue its current operations and activities, make some changes to its current operations and activities, or engage in one or more alternative scenarios.

(a) To the extent that an entity intends to continue its current operations and activities for the period of the prospective financial statements, application of the best information principle requires that the assumptions and information used in the preparation of the prospective financial statements be based on and consistent with the assumptions in the entity's current plans and strategies, updated as appropriate for more recent information forecasts of economic and business conditions.

(b) Where the nature of an entity's operations and its principal activities are expected to change significantly over the period of the prospective financial statements, the assumptions will need to reflect these changes. Application of the best information principle in these circumstances requires that the assumptions and information used in the preparation of the prospective financial statements reflect the entity's proposed course(s) of action, including any alternative scenarios, and the risks and uncertainties that inevitably surround many of the events and circumstances associated with those actions or scenarios. In such circumstances the assumptions and information used in the prospective financial statements may be consistent with those in the entity's current plans and strategies, but only to the extent that those assumptions and information are relevant to the entity's planned actions or alternative scenarios. The quality of such prospective financial statements is enhanced if they are supported by an analysis of the entity's current business and the way in which that business is expected to change under the proposed course of action, including any alternative scenarios.

24 Assumptions can range from being reasonably certain to very uncertain. The degree of certainty relating to a particular assumption depends on many things, including the following:

(a) the time period the assumption relates to – the degree of uncertainty normally increases with the length of the future period covered;

(b) the complexity of the entity and the degree to which it is affected by external conditions;

(c) the stability of the entity and the ability of the entity to predict future events. For example, an entity commencing operations or venturing into a new direction is likely to have more difficulty predicting future events than an entity which has been operating for a number of years in the same business or environment;

(d) the degree of control the entity has over its future operating environment;

(e) the nature and length of the entity's operating cycle; and

(f) the number of variables associated with the assumption.

25 Full disclosure of significant assumptions is essential in order for users to determine the extent to which they wish to rely on the information in prospective financial statements. Users require information about the assumptions used so they can make an informed judgement on the degree of reliability of the information in the prospective financial statements. Users also require information which assists them in assessing the sensitivity of information in prospective financial statements to changes in assumptions and the extent to which they are subject to a high degree of uncertainty.

Prospective financial reporting

Presentation of prospective financial statements

26 **An entity that presents prospective financial statements shall present and disclose information that enables users of those statements to evaluate the entity's financial prospects and to assess actual financial results prepared in future reporting periods against the prospective financial statements.**

27 Information presented on the face of prospective financial statements is usually presented as a line item. However, additional disclosures may be used to present information on the possible range for an individual item. When a range is used the band shall not be so broad as to render the information meaningless to users and the assumptions used shall be clearly linked to the upper and lower limits of the range. Where prospective financial information has a high level of uncertainty associated with it, a range is more likely to present useful information.

28 **An entity shall present a complete set of prospective financial statements, which shall include the following:**

(a) **a prospective statement of financial position;**

(b) **a prospective statement of profit or loss and other comprehensive income;**

(c) **a prospective statement of changes in equity;**

(d) **a prospective statement of cash flows; and**

(e) **notes, comprising a summary of significant accounting policies, significant assumptions and any other relevant information underlying (a) to (d).**

29 Except as provided in paragraph 30, the prospective statement of financial position shall separately disclose:

(a) current assets;

(b) non-current assets;

(c) current liabilities;

(d) non-current liabilities; and

(e) equity, including separate disclosure of non-controlling interests.

30 All assets and liabilities shall be presented broadly in order of liquidity when a presentation based on liquidity provides information that is reliable and is more relevant and when the entity intends to present its assets and liabilities in order of liquidity in its historical financial statements.

31 As a minimum, the prospective statement of profit or loss and other comprehensive income shall separately disclose:

(a) revenue;

(b) finance costs;

(c) depreciation and amortisation expense;

(d) share of the profit or loss of associates and joint ventures accounted for using the equity method;

(e) tax expense;

(f) a single amount comprising the total of (i) the post-tax profit or loss of discontinued operations and (ii) the post-tax gain or loss recognised on the measurement to fair value less costs to sell or on the disposal of the assets or disposal group(s) constituting the discontinued operation;

(g) profit or loss;

(h) each component of other comprehensive income classified by nature (excluding amounts in (i));

(i) share of the other comprehensive income of associates and joint ventures accounted for using the equity method; and

(j) total comprehensive income.

32 In addition to the information required by paragraph 31, an entity shall present, either on the face of the statement of profit or loss and other comprehensive income or in the notes, an analysis of expenses using a classification based on either the nature of expenses or their function within the entity, whichever provides information that is reliable and more relevant.

33 The following items shall be disclosed in the prospective statement of profit or loss and other comprehensive income as allocations of profit or loss for the period:

(a) profit or loss for the period attributable to:

(i) non-controlling interest; and

(ii) owners of the parent;

(b) total comprehensive income for the period attributable to:

(i) non-controlling interest; and

(ii) owners of the parent.

34 When an entity applies New Zealand equivalents to IFRSs, as a minimum the prospective statement of changes in equity shall separately disclose:

(a) total comprehensive income for the period showing separately the total amounts attributable to owners of the parent and to non-controlling interest;

(b) the amounts of transactions with owners in their capacity as owners, showing separately contributions by and distributions to owners; and

(c) total equity and each component of equity.

35 [Deleted]

36 [Deleted]

37 The prospective cash flow statement 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) cash flows from or used in operating activities;

(b) cash flows from or used in investing activities; and

(c) cash flows from or used in financing activities.

38 In the prospective cash flow statement:

(a) cash flows from interest and dividends received and paid shall each be disclosed separately. Each shall be classified in a consistent manner from period to period as either operating, investing or financing activities in accordance with NZ IAS 7 *Cash Flow Statements*;

(b) cash flows arising from taxes on income shall be separately disclosed and shall be classified as cash flows from operating activities unless they can be specifically identified with financing and investing activities;

(c) the aggregate cash flows arising from acquisitions and from disposals of subsidiaries or other business units shall be presented separately and classified as investing activities; and

(d) the net increase or decrease in cash and cash equivalents shall be separately disclosed.

39 This Standard specifies minimum disclosures in respect of prospective financial statements. Additional disclosures are required of any item that is of such incidence and size, or of such nature, that its disclosure is necessary to explain the prospective performance, position or cash flows of the entity. An adequate description of each item shall be given to enable its nature to be understood.

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 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.

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 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 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 require prospective financial 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.

Disclosure

Disclosure of operations and activities

47 An entity shall disclose the following, if not disclosed elsewhere in information published with the prospective financial statements:

(a) a description of the nature of the entity's current operations and its principal activities; and

(b) a description of the nature of the entity's operations and its principal activities for the period of the prospective financial statements.

Disclosure of the purpose of prospective financial statements

48 When prospective financial statements are presented, the purpose for which they have been prepared shall be disclosed together with a caution that the information in those statements may not be appropriate for purposes other than those described.

Disclosure of bases for assumptions, risks and uncertainties

49 Prospective financial statements shall contain the information necessary for a user to appreciate the degree of uncertainty attaching to the information in those statements and the impact of that uncertainty.

50 The requirement that prospective financial statements contain the information necessary for a user to appreciate the degree of uncertainty attaching to the information in those statements and the impact of that

uncertainty requires the disclosure of assumptions, the risks associated with those assumptions, and other matters and information which are of importance to users' understanding of the prospective financial statements. Disclosure of the risks surrounding assumptions and the potential impact of a change in an assumption on the prospective financial statements enables users to assess the degree of uncertainty inherent in the information in the prospective financial statements and the reliance they wish to place on the information in those statements. Such disclosure reduces the possibility that unwarranted credibility may be attached to the information. In forming a judgement on what constitutes reasonable disclosure, an entity will need to take into consideration:

(a) sources of uncertainty and the assumptions made relating to uncertainties;

(b) the factors that will affect whether assumptions will be borne out in practice; and

(c) alternative results, being the consequences of assumptions not being borne out.

51 All significant assumptions underlying prospective financial statements shall be disclosed separately and clearly identified in a manner that makes their significance understandable to users. Where possible, assumptions shall be quantified.

52 A significant assumption is one that materially affects one or more financial estimates. One way of highlighting the significance of assumptions is to rank assumptions in order of importance in relation to their impact on the prospective financial statements. For example, the most significant risks may be uncertainty regarding the level of demand for a new product, exposure to future price changes (inflation), exposure to movements in foreign currency exchange rates or interest rates, and increased demand for services caused by shifts in population growth. If the level of expected demand for the new product is the most important assumption it should be disclosed as such and the risk of demand being significantly less than assumed should be disclosed as a key risk.

53 Where prospective financial statements are not based on the entity's existing business, this fact shall be disclosed together with a description of the changes proposed.

54 Where prospective financial statements reflect planned actions or alternative scenarios that do not represent the entity's existing business, this fact shall be disclosed to enable users to understand the nature of the changes proposed and the possible future direction that the business may take.

55 An entity shall disclose:

(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.

56 The purpose of disclosure of the bases for the assumptions is to provide users with information to determine the extent to which they can rely on the information in the prospective financial statements. Disclosure about the bases of the preparation of the significant assumptions may include discussion of the process used to develop assumptions, including the use of documents such as plans, surveys and reports. The factors outlined in paragraph 20 and, where applicable, paragraph 21, are examples of items that could have formed the bases of assumptions.

57 Items disclosed as the bases for the assumptions should be described in specific rather than general terms. For example, reference to an expert's report should include the name of the report and the author and the date of the report. As another example, reference to an entity's business or marketing plan should include the date on which it was approved by the entity and the period that it covers.

58 Examples of factors that may lead to a material difference between prospective financial statements and actual financial results include macroeconomic exposures, political changes, market volatility, competitor action and risks associated with the entity's own processes for producing goods and services. One way in which information on the effect of such uncertainties on prospective financial statements may be presented is a sensitivity analysis. Where a sensitivity analysis using positive or optimistic variables is presented, it should generally be accompanied by a corresponding analysis based on negative or pessimistic variables.

59 Prospective financial statements shall include a cautionary note to the effect that actual financial results achieved for the period covered are likely to vary from the information presented, and that the variations may be material.

Disclosure of accounting policies

60 Significant accounting policies used as a basis for the preparation of prospective financial statements shall be disclosed in accordance with NZ IAS 1.

61 Where prospective financial statements give effect to a change in accounting policy, this change shall be disclosed, including the reason for the change and its effect on the prospective financial statements.

62 The changes in accounting policies referred to in paragraph 61 include changes from the accounting policies used in the prior period historical general purpose financial statements and changes from the accounting policies used in prior period prospective financial statements where prospective financial statements are presented for more than one year.

63 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 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.

Other disclosures

65 When an entity presents prospective financial statements, it shall disclose:

(a) the date when the prospective financial statements were authorised for issue and who authorised the issue of the prospective financial statements;

(b) a statement that the person or body that authorised the issue of the prospective financial statements by the entity is responsible for the prospective financial statements presented, including the appropriateness of the assumptions underlying the prospective financial statements and all other required disclosures;

(c) the extent to which actual financial results are incorporated and the period covered by those results; and

(d) whether or not it is intended to update the prospective financial statements subsequent to presentation and, if so, when.

66 The process involved in authorising the prospective financial statements for issue will vary depending upon the management structure, statutory requirements and procedures followed in preparing and finalising the prospective financial statements. It is important for users to know when the prospective financial statements were authorised for issue because this is the date of adoption of the underlying assumptions. The prospective financial statements do not reflect events or knowledge obtained after this date.

67 The authorising body is responsible for ensuring that the entity has a robust process for developing assumptions and that the assumptions developed are appropriate in the circumstances. The responsibility of the authorising body extends beyond ensuring that individual assumptions used to prepare the prospective financial statements are appropriate in the circumstances, to ensuring that the assumptions taken as a whole are appropriate and that there is adequate disclosure of all significant risks.

68 Disclosure of the date of adoption of the underlying assumptions alerts users to the possibility that events occurring subsequent to this date may affect the usefulness of the information presented. Disclosure of the extent to which actual financial results are incorporated and the period covered by those results provides an indication of the degree of reliability that can be attached to the information in the prospective financial statements. Further disclosure of whether or not it is intended to update the prospective financial statements subsequent to presentation may alert the user to the extent of the intention to communicate such updated information.

Disclosure of reasons for revising prospective financial statements

69 Where revised prospective financial statements are issued, the following shall be disclosed:

(a) the reasons for revising the prospective financial statements;

(b) an explanation of the changes made to the prospective financial statements most recently issued, including a reconciliation of material differences between the previously reported prospective financial statements and the revised prospective financial statements; and

(c) the date as at which the statements were revised.

Subsequent reporting

70 Where an entity has published prospective financial statements that are within the scope of this Standard the entity is required, in accordance with FRS-44, to present a comparison of the prospective financial statements with the actual financial results when reported. Explanations for material variations shall be given.

71 Comparison of prospective financial statements with actual financial results is an essential element of accountability. In the case of issuers 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

72 This Standard becomes operative for an entity's prospective financial statements published on or after 1 June 2006. Earlier application is permitted.

72A NZ IAS 1 (as revised in 2007) amended the terminology used throughout New Zealand equivalents to IFRSs. In addition it amended paragraphs 31, 33, 34 and 45 and deleted paragraph 35 of this Standard. An entity applying New Zealand equivalents to IFRSs shall apply those amendments for annual periods beginning on or after 1 January 2009. If an entity applies NZ IAS 1 (revised 2007) for an earlier period, the amendments shall be applied for that earlier period.

72B The *Omnibus Amendments* (2009-1) amended paragraph 10. An entity shall apply that amendment for annual periods beginning on or after 1 July 2009. Early application is permitted. If an entity applies the amendment for an earlier period it shall disclose that fact.

72C *Presentation of Items of Other Comprehensive Income* (Amendments to NZ IAS 1), issued in August 2011, amended paragraphs 28(b), and 31–33 and added paragraph 2.1. An entity shall apply those amendments when it applies NZ IAS 1 as amended in August 2011.

72D *Framework: Tier 1 and Tier 2 For-profit Entities*, issued in November 2012, amended extant NZ IFRSs by deleting any public benefit entity paragraphs, deleting any differential reporting concessions, adding scope paragraphs for Tier 1 and Tier 2 for-profit entities and adding disclosure concessions for Tier 2 entities. It made no changes to the requirements for Tier 1 entities. A Tier 2 entity may elect to apply the disclosure concessions for annual periods beginning on or after 1 December 2012. Early application is permitted.

72E *Amendments to Prospective Financial Statements* (Amendments to FRS-42), issued in August 2013, amended paragraphs 44 and 45. An entity shall apply those amendments for interim or annual periods beginning on or after 1 January 2014. Earlier application is permitted.

Withdrawal of FRS-29 (1996)

73 This Standard supersedes FRS-29 *Prospective Financial Information* (issued 1996).

Appendix A

Defined terms

This Appendix is an integral part of the Standard.

general purpose prospective financial information	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.
general purpose prospective financial statements	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.

Appendix B

Amendments to other standards

The amendments in this appendix shall be applied for prospective financial statements published on or after 1 June 2006. If an entity applies this Standard for an earlier period, these amendments shall be applied for that earlier period.

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The amendments contained in this appendix have been incorporated into the relevant pronouncements.

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

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

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

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.

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

CONTENTS

FRSB 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 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

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

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;

(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

BC9 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[2] 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 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.

[2] In [date] separate suits of standards for for-profit entities and PBEs were established.

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

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

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

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). 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[3]

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).

[3] In February 2011 the NZ *Framework for the Preparation and Presentation of Financial Statements* was replaced with the equivalent to the IASB *Conceptual Framework for Financial Reporting*. The qualitative characteristic of reliability in the old *Framework* is the same as the qualitative characteristic of faithful representation in the *Conceptual Framework*.

Forecasts and projections

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:

"...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.

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

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.

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 N 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

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 presented financial statements half yearly and annually then prospective financial statements could be presented half yearly and annually.[4]

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

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.

[4] In 2013 the New Zealand Accounting Standards Board (NZASB) amended paragraph 44 to permit an entity to present prospective financial statements in respect of a reporting period for which interim or annual historical general purpose financial statements will subsequently be presented. The NZASB's reasons for amending paragraph 44 are set out in the NZASB's Basis for Conclusions on FRS-42.

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.

Subsequent reporting

BC51 The Standard notes that NZ IAS 1 and FRS-9 *Information to be Disclosed in Financial Statements* establish requirements for the comparison of prospective financial statements or information with historical statements or information. However, these standards do not specify whether the comparison is to be against the originally published information, the most recent information or some other information.

BC52 The FRSB agreed that the Standard should highlight that comparisons of prospective financial statements with historical financial statements is important in demonstrating accountability – for a range of entities. The FRSB also noted that focusing on accountability will assist an entity to determine the most relevant information to provide as a comparative. Issuers should provide investors with a comparison of historical financial statements against the originally published prospective financial statements because the originally published statements were used to raise funds from the investors. The FRSB noted that public sector entities frequently prepare long-term prospective financial statements. In the case of a 10-year forecast a comparison with the originally published prospective financial statements may lose relevance after a year or so. The Standard suggests that a comparison with the most recent prospective financial statements published prior to the beginning of the period is relevant. However, legislation may also require a comparison with the originally published statements or information. Entities may provide additional comparatives if they wish.

References

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

HISTORY OF AMENDMENTS

Table of Pronouncements – FRS-42: *Prospective Financial Statements*

This table lists the pronouncements establishing and substantially amending FRS-42. The table is based on amendments approved as at 31 August 2013.

Pronouncements	**Date approved**	**Early operative date**	**Effective date (prospective financial statements published… on or after …)**
FRS-42: *Prospective Financial Statements*	Dec 2005	Early application permitted	March 2006 for Local Authorities, June 2006 for other entities
NZ IAS 1 *Presentation of Financial Statements* (revised 2007)	Nov 2007	Early application permitted	1 Jan 2009
NZ IAS 27 *Consolidated and Separate Financial Statements* (amended 2008)	Feb 2008	Early application permitted	1 July 2009
Omnibus Amendments (2009-1)	May 2009	Early application permitted	1 July 2009
Presentation of Items of Other Comprehensive Income (Amendments to NZ IAS 1)	Aug 2011	Early application permitted	1 July 2012
Framework: Tier 1 and Tier 2 For-profit Entities[1]	Nov 2012	Early application permitted	1 Dec 2012
Amendments to Prospective Financial Statements (Amendments to FRS-42)	Aug 2013	Early application permitted	1 Jan 2014

Table of Amended Paragraphs in FRS 42		
Paragraph affected	**How affected**	**By … [date]**
Paragraph 2.1	Inserted	*Presentation of Items of Other Comprehensive Income* [Aug 2011]
Paragraph 10	Amended	*Omnibus Amendments* (2009-1) [May 2009]
Paragraph 28	Amended	*Presentation of Items of Other Comprehensive Income* [Aug 2011]
Paragraph 31	Amended	NZ IAS 1 [Nov 2007]
Paragraph 31	Amended	*Presentation of Items of Other Comprehensive Income* [Aug 2011]
Paragraph 32	Amended	*Presentation of Items of Other Comprehensive Income* [Aug 2011]
Paragraph 33	Amended	NZ IAS 1 [Nov 2007]
Paragraph 33	Amended	*Presentation of Items of Other Comprehensive Income* [Aug 2011]
Paragraph 34	Amended	NZ IAS 1 [Nov 2007]
Paragraph 35	Deleted	NZ IAS 1 [Nov 2007]
Paragraph 44	Amended	*Amendments to Prospective Financial Statements* [Aug 2013]
Paragraph 45	Amended	*Amendments to Prospective Financial Statements* [Aug 2013]
Paragraph 72A	Inserted	NZ IAS 1 [Nov 2007]
Paragraph 72B	Inserted	*Omnibus Amendments* (2009-1) [May 2009]
Paragraph 72C	Amended	*Presentation of Items of Other Comprehensive Income* [Aug 2011]
Paragraph 72D	Inserted	*Framework: Tier 1 and Tier 2 For-profit Entities* [Nov 2012]
Paragraph 72E	Inserted	*Amendments to Prospective Financial Statements* [Aug 2013]

[1] This pronouncement amended extant NZ IFRSs by (i) deleting any public benefit entity paragraphs, (ii) deleting any differential reporting paragraphs, (iii) adding scope paragraphs for Tier 1 and Tier 2 for-profit entities, and (iv) adding RDR disclosure concessions.