

What directors should consider when preparing financial statements

Role of the board

Although all businesses must maintain financial records, not all are required by law to produce financial statements in accordance with the Australian accounting standards.

The law provides some relief from reporting requirements for small businesses, and every NFP organisation needs to be aware of what legislation is relevant to them in order to determine whether they must produce a financial report and have their financial statements reviewed or audited. Reporting requirements may come from the following:

- *Corporations Act 2001* (Cth)¹;
- Australian Charities and Not-for-profit Commission (ACNC);
- relevant state and territory incorporated associations legislation;
- the particular organisation's governance documents: for example, their constitution.

Section 285A of the *Corporations Act 2001* provides a very good summary of the reporting requirements and is reproduced below. These are very similar to those used by the ACNC.

Section 285A: Overview of obligations of companies limited by guarantee

The following table sets out what is involved in annual financial reporting for companies limited by guarantee:

¹ A full copy of the legislation can be found at <https://www.legislation.gov.au/>

Annual financial reporting for companies limited by guarantee

Item	Nature of company	Obligations	Sections
1	Small company limited by guarantee. ²	No obligation to do any of the following unless required to do so under a member direction or ASIC direction: <ul style="list-style-type: none"> • prepare a financial report; • prepare a directors' report; • have financial report audited; • notify members of reports. 	Sections 292, 301 and 316A
2	Company limited by guarantee with annual revenue or, if part of a consolidated entity, annual consolidated revenue of less than \$1 million.	Must prepare a financial report. Must prepare a directors' report, although less detailed than that required of other companies. Need not have financial report audited unless a Commonwealth company, or a subsidiary of a Commonwealth company or Commonwealth authority. If the company does not have financial report audited, it must have financial report reviewed. Must give reports to any member who elects to receive them.	Sections 292, 298, 300B, 301, 316A
3	Company limited by guarantee with annual revenue or, if part of a consolidated entity, annual consolidated revenue of \$1 million or more.	Must prepare a financial report. Must prepare a directors' report, although less detailed than that required of other companies. Must have financial report audited. Must give reports to any member who elects to receive them.	Sections 292, 298, 300B, 301, 316A

Financial report

For NFP's required to produce an annual financial report, s 295(1) *Corporations Act 2001* lists the content of a financial report as including the following:

- financial statements;
- notes to the financial statements;
- directors' declaration.

The format and content of the financial statements is governed by AASB 101 *Presentation of Financial Statements*.

Directors' declaration

An organisation's annual financial report not only contains the financial statements but it is also required to include a directors' declaration. This declaration is made as a resolution of the board to members.

According to s 295(4) of the *Corporations Act 2001*, the directors' declaration must state:

- whether, in the directors' opinion, the financial statements and notes to the accounts are drawn up in compliance with accounting standards;

² For the full definition of a Small Company Limited by Guarantee see s 45B *Corporations Act 2001*. An abbreviated definition is a company that has been a company limited by guarantee for the full financial year, is not a deductible gift recipient, is not required to have its financial statements consolidated into a group and has annual revenue of less than \$250,000

- b) whether, in the directors' opinion, the financial statements and notes to the accounts are drawn up so as to give a true and fair view of the financial position and performance of the company; and
- c) whether, in the directors' opinion, there are reasonable grounds to believe that the company will be able to pay its debts as and when they become due and payable.

In order for directors to be comfortable in making the above declarations, they are required to examine and interrogate the organisation's financial information.

To do this, directors must:

- look for what they expect to see;
- determine if the financial statements make sense for what they know about the organisation; and
- in instances when the information does not make sense, they must ask questions.

In this same NFP director tools series, the accompanying tool *What directors should consider before approving financial statements* provides a list of relevant questions that may be asked by directors. If an answer is not considered satisfactory, the topic should be pursued.

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