



Technical Accounting Alert

ASIC focus areas for 31 December 2013 financial reports

Introduction

The purpose of this Alert is to draw attention to the Australian Securities and Investments Commission's (ASIC) Media Release 13-297MR [Focuses for 31 December 2013 financial reports](#), which outlines ASIC's areas of focus for 31 December 2013 financial reports of listed entities and other significant economic entities.

Overview

The Media Release highlights ASIC's focus in the areas of:

1. disclosure in the operating and financial review
2. off-balance sheet arrangements and new standards
3. revenue recognition and expense deferral
4. asset values and impairment testing
5. going concern
6. financial instrument values
7. tax accounting
8. estimates and accounting policy judgements
9. non-IFRS financial information
10. related party disclosures

These areas are identical to the ASIC areas of focus for 30 June 2013 financial year ([Media Release 13-160MR](#)), except that tax accounting has been added as a new area of focus for the 31 December 2013 reporting season. It is also worth noting that amortisation of intangible assets is no longer listed as a key area of focus although it is mentioned in the context of 'asset values and impairment testing'.

Specific commentary is provided on the following areas:

1. Operating and financial review (OFR)

ASIC Regulatory Guide RG 247 (released on 27 March 2013) sets out ASIC's expectation regarding the level of disclosures that listed entities will need to provide in an OFR in order to comply with section 299A(1) of *Corporations Act 2001*. RG 247 also provides ASIC's view on when/how the 'unreasonable prejudice' exemption should be applied.

In ASIC's view, the OFR forms part of the annual report and under the law should contain information that members of the entity would reasonably require to make an informed assessment of the entity's:

- operations;
- financial position; and
- business strategies and prospects for future financial years (unless the inclusion of specific information is likely to result in unreasonable prejudice to the entity).

In light of RG 247, ASIC expects directors of listed entities to ensure that the OFR for the financial year ending 31 December 2013 provides meaningful analysis and information on the underlying drivers of the financial performance and position, including relevant analysis at a segment level. The OFR should also explain the business model and strategies of the entity, and how business strategies are expected to impact on future financial performance.

ASIC does not expect forward looking information to contain numerical forecasts or the level of disclosure appearing in a prospectus. ASIC believes that any possible risk of entities being found liable for misleading or deceptive forward looking information can be dealt with by ensuring:

- the statements are properly framed as being based on the information available at the time;
- the statements have a reasonable basis; and
- there is ongoing compliance with continuous disclosure obligations when events or results overtake forward looking statements in the OFR.

For further information on RG 247, refer to our [TA Alert 2013-04 ASIC Regulatory Guide 247: Effective disclosure in an operating and financial review](#).

2. Off-balance sheet arrangements and new standards

Accounting standards AASB 10 *Consolidated Financial Statements*, AASB 11 *Joint Arrangements*, AASB 12 *Disclosure of Interests in Other Entities* and AASB 13 *Fair Value Measurement* apply for reporting periods beginning on or after 1 January 2013 (i.e. half-years and full years ending 31 December 2013).

As AASB 10 can significantly change the identification of controlled entities, ASIC expects directors and auditors to carefully review the treatment of off-balance sheet arrangements under the new standards. AASB 11 can change the accounting for joint arrangements, AASB 12

includes disclosures on unconsolidated structured entities, and AASB 13 affects aspects of the determination of fair values of financial instruments and other assets.

We encourage directors to pay particular attention to the impact of these new standards on 31 December 2013 half-year and full year financial statements. The application of AASB 10 requires significant professional judgement having regards to the detailed application guidance in AASB 10 and the specific facts and circumstances. We strongly encourage directors to make this assessment as early as possible and discuss any issues with your audit teams to avoid any last minute surprises.

3. Revenue recognition and expense deferral

This is a reminder that directors and auditors should review an entity's revenue recognition policies to ensure that revenue is recognised in accordance with the substance of the underlying transaction. This includes:

- ensuring that services to which the revenue relates have been performed;
- ensuring that control of relevant goods has passed to the buyer;
- where revenue relates to both the sale of goods and the provision of related services, ensuring that revenue is appropriately allocated to the components and recognised accordingly;
- ensuring assets are properly classified as financial or non-financial assets; and
- recognising revenue on financial instruments on the basis appropriate for the class of instrument.

Similarly, directors and auditors should ensure that expenses are only deferred where:

- there is an asset as defined in the accounting standards;
- it is probable that future economic benefits will arise; and
- the requirements of the intangibles accounting standard are met, including expensing start-up, training, relocation and research costs, as well as ensuring that any amounts deferred meet the requirements concerning reliable measurement.

ASIC believes that in order to assist users of financial reports to understand the results of an entity, it is important to ensure that items of income and expense are appropriately allocated between the profit and other comprehensive income.

4. Asset values and impairment testing

ASIC continues to identify concerns regarding assessments of the recoverability of the carrying values of assets, including goodwill, other intangibles and property, plant and equipment.

Directors and auditors are urged to exercise professional scepticism and challenge the appropriateness of asset values and assumptions underlying impairment calculations, particularly

in the context of current economic conditions and where prior period financial forecasts have not been met.

In particular, ASIC stresses the importance of ensuing:

- (a) cash flows used are matched to carrying values of all assets that generate those cash flows, including inventories, receivables and tax balances;
- (b) cash flows and assumptions are reasonable having regard to matters such as historical cash flows, how an entity is funded, and market conditions. Significant variances between prior period cash flow projections and actual results may raise doubt whether assumptions are reasonable and supportable;
- (c) cash generating units (CGUs) are not identified at too high a level, including where cash inflows for individual assets are not largely independent. CGUs must not be at a higher level than the operating segments; and
- (d) disclosure of key assumptions and sensitivity analysis, which enable users of the financial report to make their own assessments about the carrying values of the entity's assets and risk of impairment given the estimation uncertainty associated with many asset valuations.

ASIC will continue to focus on entities with substantial assets held in emerging economies. Entities should also take into account any impact of the carbon tax when performing impairment testing of non-current assets.

Directors and auditors should also review the amortisation periods and methods applied for intangible assets, including amortising of intangible assets available for use even if they have not yet generated revenue.

5. Going concern

Directors need to be realistic with their assumptions about an entity's future prospects, particularly in the current environment or where the entity has continuing losses. Where an entity is assessed to be a going concern, but significant uncertainty exists, the financial report must adequately disclose the uncertainty and why the directors consider the entity to be a going concern. Directors should continue to review their entity's ability to refinance maturing debt and ongoing compliance with loan covenants.

6. Financial instrument values

ASIC expects directors and auditors to focus on the valuation of financial instruments, particularly where the value relies on assumptions that are not based on quoted prices or observable market data. Regard should also be given to [AASB 13 Fair Value Measurement](#), which is mandatory for the first time to financial reporting periods beginning on or after 1 January 2013.

Furthermore, the methods and significant assumptions used to value financial instruments should be adequately disclosed. Directors should also focus on the classification of assets and liabilities between current and non-current.

7. Tax accounting

ASIC notes that tax effect accounting can be complex and preparers of financial reports should ensure that:

- (a) there is a proper understanding of both the tax and accounting treatments, and how differences between the two affect tax assets, liabilities and expenses;
- (b) the impact of any recent changes in legislation are considered; and
- (c) the recoverability of any deferred tax asset is appropriately reviewed.

8. Estimates and accounting policy judgements

ASIC continues to identify inadequate disclosures regarding sources of estimation uncertainty and significant judgements in applying accounting policies.

In ASIC's view, disclosures in this area are important to allow users of the financial report to assess the reported financial position and performance of an entity with all relevant and necessary information. Accordingly, directors and auditors should review the disclosures in 31 December 2013 financial reports to ensure the necessary disclosures are made and are specific to the assets, liabilities, income and expenses of the entity.

9. Non-IFRS financial information

ASIC advises directors to continue to review their use of non-IFRS financial information against [RG 230](#) *Disclosing non-IFRS financial information*.

Non-IFRS financial information should not appear in the financial statements, except that the management basis of accounting is used in segment disclosures.

To ensure non-IFRS financial information in other documents (e.g. market announcements, investor and analyst presentations, and related media releases) is not potentially misleading, it should not be given more prominence than corresponding IFRS measures. It should be presented on a consistent basis between reporting periods, and items of expense should not be described as 'one-off' or 'non-recurring' where they are inherent to the entity's business or can be reasonably expected to recur.

10. Related party disclosures

ASIC expects directors and auditors to ensure that related party disclosures are made in accordance with [AASB 124](#) *Related Party Disclosures*. This information can assist investors in understanding the impact of related party transactions on the entity's financial performance and

financial position, as well as the accountability of directors and management. This includes disclosing any relevant information on whether the transactions are on an arm's length basis, and any terms and conditions.

Further information

For further information on any of the information included in this TA alert, please contact your local Grant Thornton Australia contact or a member of the National Audit Support team at NAS@grantthornton.com.au.