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A&A Accounting Technical

Clarity in financial reporting

ASIC focus areas for June 2017 year ends

Talking Points

17-162MR ASIC calls on preparers to focus on the quality of financial report information

Links to ASIC media releases

[17-162MR ASIC calls on preparers to focus on the quality of financial report information]

Talking Points

- ASIC highlights that Directors are primarily responsible for the quality of the financial report and should not be simply relying on the independent auditor. They should seek explanations and advice in order to challenge estimates and accounting treatments, where appropriate.
- Companies need to provide disclosure in the notes to financial statements showing the potential impact on reported results of the three major new standards. This may mean quantification of impacts at the reporting period coinciding with the start of the first comparative period.
- Auditors of listed entities are required to issue enhanced audit reports which outline key audit matters (KAMs) that require significant auditor attention. Where KAMs relate to accounting estimates and significant accounting policy choices, preparers and directors should ensure that appropriate disclosures are provided within the financial report.
- Companies should provide information to users of the financial reports that is useful and meaningful. The seven specific areas of focus are consistent with those in December and June 2016.

17-162MR ASIC calls on preparers to focus on the quality of financial report information

ASIC has announced its focus areas for 30 June 2017 financial reports of listed entities and other entities of public interest with many stakeholders.

ASIC will continue to focus on material disclosures such as the assumptions supporting accounting estimates, significant accounting policy choices and the impact of new reporting requirements. They encourage companies to communicate information more clearly in their financial reports.

The areas of focus are the same as those for December 2016 and continue to be broadly consistent with prior periods:

- Impairment testing and asset values
- Revenue recognition
- Expense deferral
- Off-balance sheet arrangements
- Tax accounting
- Estimates and accounting policy judgements
- Impact of new revenue, financial instrument, lease and insurance standards

Further information on each of these can be found via the link to the media release above.

Further information on impairment testing can also be found in ASIC Information Sheet 203 *Impairment of non-financial assets: Materials for directors*. Reference to this document will assist in:

- performing an appropriate valuation of assets such as goodwill, intangibles and property, plant and equipment; and
- providing a sufficient level of disclosure about the assumptions and estimates made and the sensitivity of the valuation to changes in those assumptions and estimates.

The role of directors and management

Directors are primarily responsible for the quality of the financial report and should not simply be relying on the independent auditor. ASIC expects directors to seek explanation and advice to support the accounting treatments chosen and, where appropriate, to challenge those estimates and treatments. This is particularly relevant where the treatment does not reflect their understanding of the substance of the arrangement.

Directors should refer to ASIC Information Sheet 183 *Directors and financial reporting* for guidance on the duties of a director.

Enhanced audit reports

Auditors of listed entities are required to issue enhanced audit reports which include KAMs, being those matters that required significant auditor attention in performing the audit. ASIC reminds preparers and directors to be mindful that these matters may relate to accounting estimates and significant accounting policy choices which also require specific disclosures in the financial report, as well as matters relating to the business that should also be covered in the Operating and Financial Review (OFR).

Not all KAMs identified by the auditor will relate to disclosures in the financial statements. For example, a major change of IT system may result in a KAM in the year of transition. While this change may not be disclosed in the notes to the financial statements, depending on the significance of its impact on an entity's operations, it may be highlighted in the OFR.

New accounting standards

The disclosure requirements in relation to new and revised accounting pronouncements need to be considered carefully where they have not yet been adopted. AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors* requires an entity to disclose any known or reasonably estimable information about the possible impact that the new Accounting Standards will have on the entity's financial statements in the period of initial application. This requirement does not apply to entities applying Tier 2 (RDR) reporting requirements.

In December 2016 ASIC issued additional guidance in this area, 16-442MR Companies need to respond to major new accounting standards, with specific reference to the new standards on revenue, financial instruments and leasing. The International Accounting Standards Board has also subsequently issued a new accounting standard for insurance companies.

ASIC highlights various matters that should be considered in any implementation plans for new standards, including required system changes, business impacts, impacts on compliance with financial requirements, disclosures required in financial reports prior to the effective dates of the standards, possible continuous disclosure obligations, and the impact on fundraising or other transaction documents.

Our understanding from investors and analysts is that the market is keen to know how entities think these new standards will impact them and how they are progressing with implementation. We encourage directors and management to ensure that there is a robust implementation plan in place and to consider their strategy for communicating the expected impact as the application date for each new standard draws near.

Appropriate disclosures include:

- a detailed description of how key concepts will be implemented, and where relevant, the differences to the current approaches;
- an explanation of the timeline for implementation, including expected use of any of the transition practical expedients;
- if known or reasonably estimable, quantification of the possible impact; and
- when the quantitative information is not disclosed because it is unknown or not reasonably estimable, additional qualitative information enabling users to understand the magnitude of the expected impact on the financial statements of the issuer.

Contacts

Natalie Sutcliffe
Manager
Sydney
nsutcliffe@deloitte.com.au
+61 (2) 8260 4317

Rosie Ware
Director
Sydney
roware@deloitte.com.au
+61 (2) 8260 4025

Alison White
Partner
Sydney
aliswhite@deloitte.com.au
+61 (2) 9322 5304

Anna Crawford
Partner
Sydney
acrawford@deloitte.com.au
+61 (2) 9322 7177

Clive Mottershead
Partner
Melbourne
cmottershead@deloitte.com.au
+61 (3) 9671 7553