TA Alert 2021-11
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Technical Accounting Alert

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ASIC focus areas for 31 December 2021 financial reports

Introduction

The purpose of this Alert is to draw attention to the Australian Securities and Investments Commission's (ASIC) Media Release 21-342MR *ASIC highlights focus areas for 31 December 2021 financial reports under COVID-19 conditions*.

ASIC Commissioner Sean Hughes says, "COVID-19 conditions have continued through 2021 and companies will be affected differently depending on their industry, where they operate, how their suppliers and customers are affected, and a range of other factors".

"The changing environment in which each company operates will affect its strategies and its assumptions about the future performance of its assets and businesses. It remains more important than ever that investors and markets are properly informed through a company's financial reports and related disclosures about underlying drivers of results, key assumptions, strategies, future prospects and risks in both full-year and half-year report".

Note that this document is heavily based on 21-342MR as issued by ASIC and accessed 9 December 2021. Certain additions/amendments have been made for clarity and/or inclusion of additional guidance only.

Overview

The Media Release highlights ASIC's expectation that directors, preparers, and auditors focus on the areas of:

1 Asset values;

2 Provisions;

3 Solvency and going concern assessments;

4 Events occurring after year end and before completing the financial report; and

5 Disclosures in the financial report and Operating and Financial Review (OFR).

These items are explored in more detail in the Appendix to this document.

Specifically, ASIC has highlighted that entities may continue to face some uncertainties about future economic and market conditions, and the impact on their businesses. Assumptions underlying estimates and assessments for financial reporting purposes should be reasonable and supportable. In preparing these forecasts and setting assumptions, we recommend that directors and preparers review Grant Thornton's guide "AASB 136 Impairment and COVID-19."

Uncertainties may lead to a wider range of valid judgements on asset values and other estimates. These uncertainties may change from period to period. Disclosures in the financial report about uncertainties, key assumptions and sensitivity analysis will be important to investors.

The OFR should complement the financial report and tell the story of how the entity's businesses are impacted by both the COVID-19 pandemic and by non- COVID-19 factors. The underlying drivers of the results and financial position should be explained, as well as risks, management strategies and future prospects. Forward-looking information should have a reasonable basis and the market should be updated through continuous disclosure if circumstances change.

ASIC surveillance

ASIC will conduct its regular review of the full-year financial reports of selected larger listed entities and other public interest entities as at 31 December 2021.

The reporting process

ASIC expects appropriate experience and expertise to be applied in the reporting and audit processes, particularly in more difficult and complex areas, such as asset values and other estimates.

Directors and auditors should be given sufficient time to consider reporting issues and to challenge assumptions, estimates and assessments.

Directors should make appropriate enquiries of management to ensure that key processes and internal controls have operated effectively during periods of remote work.

The circumstances in which judgements on accounting estimates and forward-looking information have been made, and the basis for those judgements, should be properly documented at the time and disclosed as appropriate.

Further guidance on key accounting implications that directors and preparers need to consider for the 30 June reporting period when preparing accounts under COVID-19 conditions can be found in Grant Thornton's guide: Accounting implications of coronavirus (COVID-19).

Reporting deadlines

ASIC has extended the deadline for unlisted entities to lodge financial by one month for balance dates from 24 December 2021 to 7 January 2022 inclusive given possible pressures on audit firm staff resources.

Where possible, entities should continue to lodge within the statutory deadlines, having regard to the information needs of relevant stakeholders or to meet borrowing or other obligations, such as covenants.

Frequently asked questions

ASIC has published frequently asked questions on the impact of COVID-19 on financial reports and audits (see COVID-19 implications for financial reporting and audit: Frequently asked questions (FAQs)) which provides additional information on matters such as:

- focus areas and factors to consider;
- disclosures in the financial report and OFR;
- the use of non-IFRS financial information;
- half-year report disclosures;
- loan and receivable provisioning;
- non-COVID-19 focus areas
- the extensions of time for financial reporting; and

- reporting by auditors.

These FAQs are updated from time to time in response to emerging issues and changing circumstances.

Appendix: Focuses for financial reporting under COVID-19 conditions

This attachment provides further information on the focus areas for 31 December 2021 reporting. We recommend that the matters below be considered in conjunction with the Grant Thornton guide Accounting implications of coronavirus (COVID-19).

1 Factors affecting asset values, provisions and assessments to solvency and going concern

Factors to consider in relation to asset values, liabilities and assessments on solvency and going concern continue to include:

- business and domestic/international economic factors
- industry-specific factors
- impact on supply chains, customers, borrowers and lessees
- exposures to overseas operations, transactions and currencies
- short-term versus long-term conditions
- vaccination levels, responses to COVID-19 and duration of containment measures in different countries
- extent and duration of assistance and support by governments and others
- impact on short-term operating cash flows
- debt refinancing, borrowing covenants, lender forbearances, lease modifications and liquidity support
- capital raising
- management plans and response to the pandemic impacts.

These factors may also be relevant in assessing the ability of an entity's borrowers and debtors to meet their obligations to the entity, and the ability of key suppliers to continue to provide goods and services to the entity.

This list is not intended to be exhaustive and there may be other factors to consider in the circumstances of individual entities. ASIC's FAQs also discuss matters that directors and auditors may consider in assessing the solvency of an entity.

2 Asset values

Examples of matters that may require the focus of directors, preparers and auditors in relation to asset values in the current environment include:

Impairment of non-financial assets

- Goodwill, indefinite useful life intangible assets and intangible assets not yet available for use must be tested for impairment annually. Entities adversely impacted in the current environment may have new or continuing indicators of impairment that require impairment testing for other non-financial assets.
- The appropriateness of key assumptions supporting the recoverable amount of non-financial assets.
- Disclosure of estimation uncertainties, changing key assumptions, and sensitivity analysis or information on probability-weighted scenarios. Key assumptions may include assumptions relating to the factors listed at the start of this attachment.

Value of property assets

- Factors that could adversely affect commercial and residential property values should be considered such as changes in office space requirements of tenants, shifts to on-line shopping, future economic or industry impacts on tenants, the financial condition of tenants and restructured lease agreements.
- The lease accounting requirements, the treatment of rental concessions by lessors and lessees, and the impairment of lessee right-of-use assets.

Expected credit losses on loans and receivables

- Whether key assumptions used in determining expected credit losses are reasonable and supportable.
- Any need for more reliable and up-to-date information about the circumstances of borrowers and debtors.
- Short-term liquidity issues, financial condition and earning capacity of borrowers and debtors.
- The extent to which past history of credit losses remains relevant in assessing expected credit losses.
- Disclosure of estimation uncertainties and key assumptions.

Value of other assets

- The net realisable value of inventories, including whether all estimated costs of completion and necessary to make the sale have been taken into account in determining net realisable value.
- Whether it is probable that deferred tax assets will be realised.
- The value of investments in unlisted entities.

3 Provisions

Consideration should be given to the need for provisions for matters such as onerous contracts, financial guarantees given and restructuring.

4 Subsequent events

Events occurring after year-end and before completing the financial report should be reviewed as to whether they affect assets, liabilities, income or expenses at year-end or relate to new conditions requiring disclosure.

5 Disclosures

Considerations on disclosure include:

General considerations

- When considering the information that should be disclosed in the financial report and OFR, directors and preparers should put themselves in the shoes of investors and consider what information investors would want to know.
- Disclosures should be specific to the circumstances of the entity and its businesses, assets, financial position and performance.
- Changes from the previous period should be considered and disclosed.

Disclosure in the financial report

- Uncertainties may lead to a wider range of valid judgements on asset values and estimates. The financial report should disclose uncertainties, changing key assumptions and sensitivities. This will assist investors in understanding the approach taken, understanding potential future impacts and making comparisons between entities. Entities should also explain where uncertainties have narrowed or changed since the previous full-year and half-year financial reports.

- The appropriate classification of assets and liabilities between current and non-current categories on the statement of financial position should be considered. That may have regard to matters such as maturity dates, payment terms and compliance with debt covenants.

Disclosure in the OFR

- The OFR should complement the financial report and tell the story of how the entity's businesses are impacted by the COVID-19 pandemic and changing circumstances. The overall picture should be clear, understandable, and be supported by information that will enable investors to understand the significant factors affecting the entity, its businesses and the value of its assets.
- The OFR should explain the underlying drivers of the results and financial position, as well as risks, management strategies and future prospects.
- Significant factors not attributable to the COVID-19 pandemic should be included and given appropriate prominence, such as changes in consumer preferences or new competitors.
- Climate change risk could have a material impact on the future prospects of entities. Directors may also consider whether to disclose information that would be relevant under the recommendations of the Task Force on Climate-related Financial Disclosures.

Assistance and support by governments and other

- Entities should appropriately account for each type of support and assistance from government, lenders, landlords and others. Both the financial report and OFR should prominently disclose material amounts, as well as the commencement date and either the end date or expected duration of support or assistance. Examples include JobKeeper, land tax relief, loan deferrals and restructuring, and rent deferrals and waivers.
- Entities should also disclose the amount of any material voluntary returns of JobKeeper or other support or assistance.
- The financial report and OFR must disclose relevant information about JobKeeper even though listed entities must also include information in a JobKeeper notice provided to a market operator (see 21-271MR ASIC issues Jobkeeper notice and guidance).

Non-IFRS financial information

- Any non-IFRS profit measures in the OFR or market announcements should not be presented in a potentially misleading manner.
- Where asset impairment losses were excluded from a non-IFRS profit measure in a prior period, any impairment reversal should also be excluded from that measure.
- Where a net tangible asset figure is presented by a lessee, there should be a prominent footnote on the same page explaining whether some, all or no lease right-of-use assets have been included.

Disclosure in half-year reports

- Disclosure will also be key for half-year financial reports and directors' reports as at 31 December 2021. These half-year reports may need to include significant disclosure about developments and continuing impacts since 30 June 2021 of COVID-19 conditions and other significant factors.

ASIC's FAQs provide more information on disclosures in the financial report, disclosures in the OFR, and the use of non-IFRS financial information.

6 Other Matters

- Cloud computing customers that did not derecognise capitalised costs of configuring or customising a supplier's application software in a Software as a Service arrangement at 30 June 2021 should do so at 31 December 2021. Further guidance on the IFRIC Agenda Decision on Configuration or Customisation Costs in a Cloud Computing Arrangement and casual workers can be found on our website.
- Whether off-balance sheet exposures should be recognised on-balance sheet, such as interests in non-consolidated entities.
- Aged care providers should review the treatment of aged care bed licenses following the Government's announcement in May 2021 that the licences will be discontinued on 1 July 2024 (see also FAQ 9D).
- The treatment of future services to be provided by a vendor in accounting for a business combination.
- The treatment of written put options over non-controlling interests in a subsidiary.

Further information

If you wish to discuss any of the information included in this Technical Accounting Alert, please get in touch with your local Grant Thornton Australia contact or a member of the National Assurance Quality Team at national.assurance.quality@au.gt.com.