

Technical Accounting Alert

ASIC Report on its Focus Areas for 30/12/2011 financial reports

Introduction

The purpose of this alert is to draw attention to the Australian Securities and Investments Commission's (ASIC) Media Release 'Improved financial information for investors and others', which commented on the results of its reviews of financial reports for the year ended 30 June 2011 and announced its areas of focus for 31 December 2011 financial reports .

A copy of the Media Release is available at:

<http://www.asic.gov.au/asic/asic.nsf/byHeadline/11312MR%20Improved%20financial%20information%20for%20investors%20and%20others?opendocument>

Overview

ASIC's Media Release 11-312MR states that given the current difficult economic climate that confronts all companies, ASIC will focus particularly on:

- asset values and going concern assessments, including adequate disclosure of material assumptions;
- consolidation decisions and off balance sheet arrangements; and
- proper disclosure of segment information in a manner that enables useful assessment of the separate businesses.

Specific commentary is provided on the following areas:

1 Asset values

Nothing new from previous ASIC Media Releases with ASIC stating that Impairment testing of goodwill, identifiable intangibles and other assets continues to be an area requiring improvement. Particular concerns relate to:

- a ignoring indicators of possible asset impairments, such as reported net assets being significantly higher than the entity's market capitalisation.
- b use of unrealistically optimistic discount and growth rates;
- c failure to disclose carrying amounts allocated to each cash generating unit and the basis for determining recoverable amounts;
- d lack of disclosure of assumptions used in discounted cash flow calculations, particularly growth rates and discount rates; and
- e no sensitivity analysis for changes in key assumptions.

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ASIC believes that in the context of current economic conditions, some topical events that may affect asset values include: exposures to countries with economic uncertainties; the impact of exchange rate movements; the imminent carbon tax and the proposed mineral resource rent tax. Focus should also be placed on values of financial assets and investment properties measured at fair value.

2 Going concern

Again nothing new and ASIC's chief complaint seems to be where companies have failed to make adequate disclosures relating to the ability to continue as a going concern.

3 Off balance sheet arrangements

ASIC has queried a number of entities that have not consolidated entities in which they hold an ownership interest of over 50%, and this has according to ASIC, resulted in 'Many' of these entities now consolidating those interests.

Where arrangements remain off balance sheet, ASIC expects disclosure of the details of the arrangements and any exposures should be disclosed, together with the reasons why they are not on balance sheet.

4 Current vs non-current classifications

Given the Centro decision, ASIC sees the correct classification of liabilities and assets between current and non-current as important to an understanding of the financial position of an entity.

5 Estimates and accounting policy judgements

ASIC argues that some entities did not make material disclosures of significant judgements in applying accounting policies and sources of estimation uncertainty. Other entities included 'boiler plate' disclosures. These disclosures should be specific to the entity and its assets, liabilities, equity, income and expenses.

6 Non-IFRS profits

This follows up Regulatory Guide RG 230 Disclosing non-IFRS financial information (RG 230), and is covered in a separate Technical Alert TA 2011-24 which summarises the need for non-IFRS financial information to be excluded from the financial statements, but allowable elsewhere in the financial report provided the disclosure is not misleading. The banning of non-IFRS financial information in the financial statements is contentious and arguably an incorrect interpretation of the requirements of the Accounting Standards, however ASIC has stated it will be a particular focus for its surveillance activities.

7 Operating and financial review

This is a particularly contentious area given that there is a 'prejudicial' exemption from disclosing 'likely future developments' if in the directors' opinion it would result in unreasonable prejudice to the company. ASIC is not impressed with the level of exemptions, however the reality is that this is an area of Corporations Law reform as amendments to the Directors' Report for limited by guarantee companies' significantly increased detailed disclosures of objectives, strategy, and how the company measures performance, without a prejudicial let out.

8 Segment reporting

ASIC's concern is that the segmental information disclosed is at times at too high a level (less rather than more segments). It notes that in some cases, information disclosed in documents such as market announcements or the financial report suggest that there may be more segments that should be reported..

9 Financial instruments

ASIC continues to have concerns with the number of entities that do not make adequate disclosures to enable users of financial reports to understand and evaluate the nature and extent of the specific market, credit and liquidity risks associated with their use of financial instruments. Disclosures should be meaningful to users, and specific disclosures should be made rather than boilerplate disclosures.

A number of entities failed to disclose financial asset fair value information using a three level hierarchy reflecting the extent to which observable market data is used in the measurement, or failed to disclose the methods and significant assumptions used to value assets for which there was no observable market data.

Other deficiencies related to disclosing an ageing analysis of financial assets that are past due but not impaired and an analysis of impaired financial assets.

10 New accounting standards

This is a reminder of the requirement to provide disclosure of new standards issued but not yet effective, and IFRS/AASB 10 Consolidations is specifically mentioned. However ASIC is likely to be disappointed about the lack of disclosures given that most companies and auditors are still working their way through what the new requirements which apply in 2013 really mean in practice.

11 Minerals Resource Rent Tax (MRRT)

ASIC notes that the MRRT appears to be an income tax to be accounted for under AASB 112 Income Taxes (similar to the Petroleum Resource Rent Tax). Whilst the MRRT will not be considered by the Senate until 2012, ASIC states that entities should adequately plan for any valuation advice required and take care when re-measuring the tax base of their depreciable assets. Entities should assess the impact of the proposed MRRT on asset impairment and consider disclosing expected future impacts on deferred tax balances.

12 Rights to future income

Off the back of some recent ASIC litigation it is stated that ASIC is making further enquiries of some entities that have recognised a right to future income as a financial asset at fair value rather than intangible assets required to be measured at amortised cost. This is likely to also prove contentious as the accounting standards generally do allow and require recognition as a financial asset where appropriate.

13 Intangible asset revaluation

ASIC is continuing to argue that entities can only revalue identifiable intangible assets to fair value where an active market exists, but then states that it is not aware of any identifiable intangible assets for which an active market exists in Australia.

Further information

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

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