



Technical Accounting Alert

TA 2020-14

ASIC findings from review of 31 December 2019 financial reports

Introduction

The purpose of this Alert is to draw attention to the Australian Securities and Investments Commission's (ASIC) Media Release 20-173MR [Findings from 31 December 2019 financial reports](#), announcing the results of ASIC's inspections of 90 listed entities and other public interest entities with many stakeholders.

This is a timely reminder for entities and their auditors who are currently in the process of finalising 30 June 2020 financial statements.

Overview

ASIC's findings categories are largely in line with its focus areas for 31 December 2019 financial reports (refer to TA [2019-14](#)). Due to the COVID-19 pandemic ASIC has provided further guidance on Focus areas for financial reporting under COVID-19 conditions (refer TA [2020-13](#)). The findings are divided into eight broad categories, with specific commentary below on each:

- 1 Asset values and impairment testing
- 2 Revenue recognition
- 3 Tax accounting
- 4 Consolidation accounting
- 5 New accounting standards
- 6 Non-IFRS financial information
- 7 Operating and financial review
- 8 Estimates and accounting policy judgements



Accounting estimates

1 Revenue Recognition

ASIC identified 10 items concerning the recognition of revenue, in particular, contracts that involve multiple performance obligations (e.g. sale of goods and provision of services) where one or more obligation is still to be met.

ASIC also identified instances where the accounting policy for revenue recognition needed to be more clearly described.

2 Asset values

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

Reasonableness of cash flows and assumptions

There continue to be cases where the cash flows and assumptions used by entities to determine recoverable amounts are not reasonable or supportable in light of historical cash flows, economic and market conditions, and funding costs.

In particular, ASIC found cases where:

- assumptions derived from external sources were not assessed for consistency and relevance, and
- the entity's forecast cash flows did not appear reasonable and had exceeded actual cash flow achieved for a number of reporting periods.

Determining the carrying amount of cash generating units

There are cases where entities appear to have:

- identified cash generating units (CGUs) at too high a level despite cash inflows being largely independent, resulting in cash flows from one asset or part of the business being incorrectly used to support the carrying values of other assets;
- not included all assets that generate the cash inflows in the carrying amount of a CGU, such as inventories, trade receivables, and tax balances, and/or
- incorrectly deducted liabilities from the carrying amount of a CGU.

Use of fair value

ASIC still sees entities using discounted cash flow techniques to estimate fair value where the calculations are dependent on a large number of management inputs. Where it is not possible to reliably estimate the value that would be received to sell an asset in an orderly transaction between market participants, the entity may need to use the asset's value in use as its recoverable amount.

Impairment indicators

Some entities are not paying sufficient attention to impairment indicators, including significant adverse changes in market conditions, and reported net assets exceeding market capitalisation.



Disclosures

ASIC still finds a number of entities not making necessary disclosure of:

- sources of estimation uncertainty and key assumptions, including discount rates and growth rates;
- sensitivity analysis;
- instances where a reasonably foreseeable change in one or more assumptions could lead to impairment, and/or
- for fair values, the valuation techniques and inputs used.

ASIC notes that these disclosures are important to investors and other users of financial reports given the estimation uncertainty associated with many assets valuations. They enable user to make their own assessments about an entity's carrying values and risk of impairment.

The disclosures will be particularly important for 30 June 2020 reports because of the wider range of asset value judgements caused by the uncertainties of the COVID-19 pandemic (refer: [20-157MR](#)).

The findings listed above on asset values and impairment include findings arising from the finalisation of matters identified in ASICs reviews of 30 June 2019 financial reports.

3 Tax accounting

ASIC asked four entities about their accounting for income tax, including the adequacy of tax expense and whether it is probable that future taxable income will be sufficient to enable the recovery of deferred tax assets relating to tax losses. For further information, we recommend reading [TA 2019-12 Guidance on Recognition of Tax Operating Losses](#).

4 Provisions

ASIC inquired of four entities about the adequacy of provisions for rehabilitation, warranty claims and employee benefits.

5 Financial instruments

ASIC questioned four entities about the treatment of certain financial instruments, including the fair value of equity instruments and an arrangement where a fair value gain arose from the forgiveness of debt.

6 Consolidation and equity accounting

ASIC approached four entities about the non-consolidation of other entities or not applying equity-method accounting an interest in other entities where there were indicators of possible significant influence.

7 New lease accounting standard

Some entities could have provided a clearer explanation of the impact of adopting the new accounting standard on leases. This includes the nature and cause of any changes.

In one instance, ASIC made inquiries about a sale and leaseback of property.



Material changes

ASIC's risk based surveillance of the financial reports of public interest entities for reporting periods ended 30 June 2010 to 30 June 2019 has led to material changes to about 5 per cent of the reviewed financial reports. The main changes were to impairment of assets, revenue recognition and expense deferral.

When a company makes material changes to information previously provided to the market following inquiries made by ASIC, ASIC makes a public announcement. In addition to improving the level of market transparency, these announcements are intended to make directors and auditors of other companies aware of ASIC's concerns so they can avoid similar issues.

Other matters

Given the impact of COVID-19 asset values and related disclosures are important areas for the focus of the directors, prepares and auditors for financial reports at 30 June 2020, ASIC reminds directors and auditors need to focus on impairment of non-financial assets in financial reports to ensure the market is properly informed about asset values and expected future performance implied by those values.



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.