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30 November 2012

Dear Crystal

## **CONSULTATION PAPER 187: EFFECTIVE DISCLOSURE IN AN OPERATING AND FINANCIAL REVIEW**

Grant Thornton Australia Limited (Grant Thornton) is pleased to provide the Australian Securities and Investments Commission (ASIC) with its comments on Consultation Paper 187: Effective disclosure in an operating and financial review.

Grant Thornton's response reflects our position as auditors and business advisers both to listed companies and privately held companies, and public and private businesses, and this submission has benefited with input from our clients, as well as discussions with key constituents.

Whilst Grant Thornton broadly supports the proposals in the Consultation Paper for better disclosure of business strategies and future prospects as non-mandatory guidance, we believe that the 'prejudicial' exemption will remain a particularly contentious area given that the 'prejudicial' exemption from disclosing business strategies and prospects for future financial years' is a directors' opinion, and not ASIC's, as to whether it is likely to result in unreasonable prejudice to the company.

Given the demise of the Financial Reporting Panel which could have been adapted to be a much less expensive avenue for settling disputes between ASIC and companies on financial reporting issues, we question whether it is cost effective for ASIC to take Court action where it believes that directors have not properly formed their view that a prejudicial exemption is appropriate. Instead we suggest that if the Government accepts ASIC's view that there should be greater disclosure of business strategies and future prospects, this should be a matter for Corporations Law reform. We note that the 2010 Corporations Act 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.

Our comments on the specific feedback requested by ASIC is contained in the attached Appendix.

If you require any further information or comment at this time, please contact Keith Reilly at [keith.reilly@au.gt.com](mailto:keith.reilly@au.gt.com).

Yours faithfully  
GRANT THORNTON AUSTRALIA LIMITED



Keith Reilly  
National Head of Professional Standards

# Appendix: Comments on CP 187

## **CONSULTATION PAPER 187 Effective disclosure in an operating and financial review**

### **A. Overview**

Paragraph 8

### **B. The nature of an operating and financial review**

What is an operating and financial review

Proposal

B1. We propose to give guidance that an OFR should:

- a contain an analysis and narrative that explain an entity's business; and
- b provide investors with useful and meaningful information about the entity, together with its annual financial report and other market disclosures, such as continuous disclosure.

Your feedback

B1Q1. Do you agree with our view of what an OFR is, and broadly what it should contain? If not, please explain why not.

*Grant Thornton response:*

We agree

B1Q2. Do you agree with our view that an OFR should be a major source of information about an entity's business to meet the information needs of investors? If not, please explain why not

*Grant Thornton response:*

No. The OFR relates to specific disclosures which do not necessarily have more significance than other information that directors provide to the market place. We note that it is the directors' view of what they believe that readers of the financial report should be alerted to from an OFR perspective which will be company specific.

B2. We propose that disclosures made outside the OFR do not substitute for proper disclosure in the OFR as a matter of law. In addition, we consider that the OFR disclosures perform an important function that is not fulfilled by other disclosures made by the entity to investors.

**Your feedback**

B2Q1. Is there other additional guidance that would be useful about the relationship between disclosures in other documents and the disclosures made in the OFR?

**Grant Thornton response:**

No. The OFR is for a specific purpose and other market disclosures may or may not be relevant.

**Information that investors would reasonably require to make an informed assessment  
Proposal**

B3. We propose to give guidance that, while s299A contains similar wording to the prospectus disclosure requirements in s710, an OFR would very rarely contain the scope or depth of detail of a full prospectus.

Information intended to form part of an OFR must be selected with the purpose of providing insight into the matters set out in s299A.

**Your feedback**

B3Q1. Do you agree with our view on the level of disclosure required? If not, please explain why not and suggest alternatives.

**Grant Thornton response:**

No. The CP 187 guidance is useful as is the Group of 100's guidance in this area and the IASB's Management Commentary Practice Statement, all of which are non mandatory guides that need to be tailored to the particular company circumstances

**C. Specific content of the operating and financial review**

**Operations, financial position and business strategies and prospects for future financial years  
Proposal**

C1. We propose to give guidance on the matters specified in s299A(1) to clarify :

- a the type of information that should be considered when providing an analysis and narrative on an entity's operations, financial position, business strategies and prospects; and
- b the key matters that should be addressed and principles that should be followed when preparing an OFR (rather than setting out detailed checklists of information that must be provided).

**Your feedback**

C1Q1. Do you consider that the proposed guidelines on the specified contents of an OFR (as set out in the draft regulatory guide) are appropriate? If not, please explain why not and suggest alternatives.

**Grant Thornton response:**

We believe that the prejudicial exemption needs to be considered and can apply where the directors believe it is appropriate, and that is a directors and not a regulator's decision. We see the proposed guidelines as being useful but in a non-mandatory sense.

C1Q2. Do you agree with the examples of disclosure set out in Tables 1 and 2 of the draft guide? If not, please explain why not. If you think that there is a preferable way of illustrating our guidance, please suggest alternatives.

**Grant Thornton response:**

We believe that the prejudicial exemption needs to be considered and can apply where the directors believe it is appropriate, and that is a directors and not a regulator's decision. We see the proposed guidelines as being useful but in a non-mandatory sense.

C1Q3. Do you think that there is any other key information that should be included in an OFR that has not been referred to in our draft guidance?

**Grant Thornton response:**

We believe that the prejudicial exemption needs to be considered and can apply where the directors believe it is appropriate, and that is a directors and not a regulator's decision. We see the proposed guidelines as being useful but in a non-mandatory sense.

**Operations****Proposal**

C2. Our proposed guidance outlines the key requirements in s299A(1)(a) relating to an entity's operations. We propose that an OFR should disclose the underlying drivers of an entity's performance that are relevant to understanding its performance and the factors underlying its results. This may include significant factors affecting:

- a the total income and income for major operating segments; and
- b the significant components of overall expenses and expenses for major operating segments.

**Your feedback**

C2Q1 Do you consider that our proposed guidance on disclosure about an entity's operations (as set out in the draft regulatory guide) is appropriate? If not, please explain why not and suggest alternatives.

**Grant Thornton response:**

We believe that the prejudicial exemption needs to be considered and can apply where the directors believe it is appropriate, and that is a directors and not a regulator's decision. We see the proposed guidelines as being useful but in a non-mandatory sense.

- C3. We propose that, while the guidance in Regulatory Guide 228 *Prospectuses: Effective disclosure for retail investors* (RG 228) is for disclosure in a prospectus, which is more extensive than the disclosure typically required in an OFR, RG 228 may also be useful for preparing disclosure about an entity's business model in the OFR.

**Your feedback**

- C3Q1. Do you agree that the reference to RG 228 in relation to business models is useful? If not, please explain why not and suggest alternatives.

**Grant Thornton response:**

Yes.

**Financial position**

**Proposal**

- C4. We propose that, under the requirement in s299A(1)(b), an OFR should include information that is relevant to understanding an entity's financial position. We consider that this includes:
- a disclosing the underlying drivers of the financial position of the entity;
  - b disclosing exposures that are not reflected in the financial report (e.g. off-balance sheet arrangements); and
  - c explaining the accounting information and other detail contained in the financial report (rather than simply repeating it).

**Your feedback**

- C4Q1. Do you consider that our proposed guidance on disclosure about an entity's financial position (as set out in the draft regulatory guide) is appropriate? If not, please explain why not and suggest alternatives.

**Grant Thornton response:**

Yes.

**Financial position**

**Proposal**

- C5. We propose that, under the requirement in s299A(1)(b), an OFR should include information that is relevant to understanding an entity's financial position. We consider that this includes:
- a disclosing the underlying drivers of the financial position of the entity;

- b disclosing exposures that are not reflected in the financial report (e.g. off-balance sheet arrangements); and
- c explaining the accounting information and other detail contained in the financial report (rather than simply repeating it).

*Your feedback*

C5Q1. Do you consider that our proposed guidance on disclosure about an entity's financial position (as set out in the draft regulatory guide) is appropriate? If not, please explain why not and suggest alternatives.

*Grant Thornton response:*

Yes.

**Business strategies and prospects for future financial years**

**Proposal**

C6. We propose that the information required under s299A(1)(c) on business strategies and prospects for future financial years should focus on the areas that are likely to affect the future financial performance and position of the entity. We consider that the OFR should usually include:

- a an outline of the entity's key business strategies, and its plans that are a significant part of those strategies; and
- b disclosure of the main risks that could adversely affect the successful fulfilment of the business strategies of the entity.

*Your feedback*

C6Q1. Do you consider that our proposed guidance on disclosure about an entity's business strategies and prospects (as set out in the draft regulatory guide) is appropriate? If not, please explain why not and suggest alternatives.

*Grant Thornton response:*

Yes.

**Use of the unreasonable prejudice exemption**

**Proposal**

C7. We propose to provide guidance on how to determine whether the exemption in s299A(3) applies, including whether there is 'unreasonable prejudice' and whether it is likely to occur.

C8. We also propose that, if information has been omitted in reliance on the exemption (in addition to stating in the OFR that information has been omitted, as required by s299A(3)):

- a a summary of the type of information omitted and the reasons for the omission should be disclosed in the directors' report, where possible; and

- b because ASIC may ask for the reasons why information has been excluded, directors may find it helpful to keep an internal record which:
  - i identifies the information that has not been disclosed; and
  - ii explains how disclosure of the excluded information would be likely to result in unreasonable prejudice.

**Your feedback**

C8Q1. Do you agree with our interpretation of the exemption requirement? If not, please explain why not.

**Grant Thornton response:**

No. The Corporations Act is quite clear that it is the directors' opinion and not anyone else's. If the Government wishes to remove or modify this exemption, then it is a legislative issue and not a regulators.

C8Q2. Do you agree that, when information has been omitted in reliance on the exemption, a summary of the type of information omitted and the reasons for the omission should be disclosed, where possible? If not, please explain why not.

**Grant Thornton response:**

No. The exemption is a matter for the directors to determine.

C8Q3. Do you agree with the final example of disclosure (relating to the use of the unreasonable prejudice exemption), which is set out in Table 2 of the draft regulatory guide? If not, please explain why not.

**Grant Thornton response:**

No. we see this is useful but non-mandatory guidance.

C8Q4. Are there other matters of practical guidance that should be included? If so, please describe these matters and explain why you think they should be included.

**Grant Thornton response:**

No.

C8Q5. Do you agree with our suggestion for internal record keeping? If not, please explain why not.

**Grant Thornton response:**

No. We see this as useful but non-mandatory guidance.

#### Presentation of analysis and narrative

##### Proposal

C9. We propose to set out some good disclosure practices to assist directors in preparing a high-quality OFR.

##### Your feedback

C9Q1. Do you consider that the proposed good disclosure practices in Table 3 of the draft regulatory guide are appropriate? If not, please explain why not and suggest alternatives.

##### Grant Thornton response:

Yes.

#### Integrated reporting

##### Proposal

C10. At this stage, we do not propose to include any guidance on integrated reporting.

##### Your feedback

C10Q1. Do you agree that it is not appropriate to include guidance on integrated reporting at this stage? If you think guidance should be included, please explain why.

##### Grant Thornton response:

Yes. Whilst Grant Thornton is a passionate supporter of integrated reporting, we see it as quite separate to the Financial Report.

### **D. Regulatory and financial impact**

##### *Grant Thornton response:*

Given that CP 187 states that ASIC has carefully considered the regulatory and financial impact of these proposals, we find it odd that no detail is given, instead respondents are asked to provide details of likely compliance costs; the likely effect on competition; and any other impacts, costs and benefits.