



FRA NEWS

No.4/2013

Welcome to this issue of 'TNR FRA News'. Financial Reporting and Auditing (FRA) News ('FRA News') provides partners, staff and clients with a 'heads up' of contemporary financial reporting, auditing and corporate governance developments on a monthly basis. FRA News contains items requiring immediate consideration (**Need to Know**), whereas other items are for general information (**Nice to Know**).

FRA News is prepared by Colin Parker, Principal, GAAP Consulting, and former member of the Australian Accounting Standards Board (2006-2009) with the input of staff of GAAP.com.au Pty Ltd.

In this FRA News, your attention is drawn to the following developments:

Need to know:

- Continuous disclosure guidance and listing rules updated
- ACNC ACT signs up
- Operating and financial reviews guidance
- ACNC governance standards to commence 1 July 2013
- 'Parent' identification in AASB 10
- ACNC annual information statement consultation
- Review engagements revised rules
- Terms of engagement revised rules too
- Outsourced services guidance

Nice to know:

- Loan loss provisioning proposals
- IASB/AASB work program – outputs getting closer
- NFP guidance on consolidations
- Code of ethics proposed revisions
- Risk management for responsible entities proposals
- Audit independence guide issued

Liability limited by a scheme approved under Professional Standards Legislation

Continuous disclosure guidance and listing rules updated



The ASX released its final Guidance Note on continuous disclosure that provides listed entities with clearer, more detailed information to help them understand and comply with their continuous disclosure obligations. The ASX released its 'Review of ASX Listing Rules Guidance Note 8: Consultation Response', together with the final versions of: Guidance Note 8: 'Continuous Disclosure: Listing Rules 3.1 – 3.1B'; 'Continuous Disclosure: An Abridged Guide'; and ASX's package of disclosure-related amendments to the ASX Listing Rules.

As a result of consultation process, the ASX has upgraded Guidance Note 8 in a number of key areas, including:

- What ASX means by the word "delay" when it defines "immediately" as "promptly and without delay"
- When an entity should ask for a trading halt to manage its continuous disclosure obligations
- When ASX treats media and analyst reports and market rumours as evidencing a loss of confidentiality under Listing Rule 3.1A.2; 2
- The operation of the "reasonable person" test in Listing Rule 3.1A.3
- ASX's expectations around the monitoring of social media
- The disclosure of earnings surprises, including the role played by consensus estimates in setting market expectations for earnings, and
- Refining a number of the worked examples in Annexure A.

In addition to the materials mentioned above, ASX also released updated versions of the following Listing Rule Guidance Notes: Guidance Note 1 'Applying for Admission – ASX Listings'; Guidance Note 4 'Foreign Entities Listing on ASX';

Guidance Note 12 'Significant Changes to Activities'; Guidance Note 16 'Trading Halts and Voluntary Suspensions'; and Guidance Note 17 'Waivers and In-Principle Advice'. These Guidance Notes were updated to be consistent with the new version of Guidance Note 8 and the disclosure-related Listing Rule changes. They are intended to come into operation on 1 May 2013.

Good continuous disclosure is about preparation and having the right systems in place. Companies that carefully consider the updated guidance and adopt appropriate processes with the benefit of that guidance can minimise the risk that ASIC will seek to take continuous disclosure enforcement action against them.

When confronted with potential continuous disclosure breaches ASIC can pursue a variety of enforcement remedies, including issuing infringement notices. One factor ASIC may take into account in deciding whether to take action is the nature and seriousness of the conduct of the company that contributed to the potential breach including the compliance approach of the company (refer 'Information Sheet 151 'ASIC's approach to enforcement'). [HLB](#)

ACNC ACT signs up

The Commonwealth and Australian Capital Territory (ACT) Governments announced further tangible steps to reduce red tape for the NFP sector. The ACT Government will carve out charities registered by the ACNC from regulatory requirements under relevant ACT legislation, such as the Associations Incorporation Act 1991 (ACT).

The changes will mean that charities incorporated as associations in the ACT will only need to report to the ACNC and not the ACT Office of Regulatory Services. Amendments will also be made to the Charitable Collections Act 2003 (ACT). As announced in October last year, South Australia is also progressing changes to align its regulatory framework for incorporated associations and fundraising with the ACNC. [HLB](#)

Operating and financial reviews guidance



ASIC released a regulatory guide to improve disclosure in annual reports of listed entities. The operating and financial review (OFR) forms part of a listed entity's annual report and contains information investors would reasonably require to make an informed assessment of the entity's operations, financial position, business strategies and future prospects. It is a key part of annual disclosure by a listed entity.

ASIC believes OFRs can be improved and released Regulatory Guide 247 'Effective disclosure in an operating and financial review; with the purpose of lifting the standard of disclosure. The guide aims to: promote better communication of useful and meaningful information to shareholders; and assist directors in understanding the OFR requirements.

RG 247 also includes guidance on:

- Appropriate standards of disclosure through the inclusion of worked examples
- The use of the 'unreasonable prejudice' exemption from disclosing specific business strategies and prospects, and
- Presentation of the analysis and narrative relating to operations and financial position.

ASIC's proposed guidance is not intended to add unnecessary length to annual reports, but rather is intended to promote more meaningful information and analysis for investors. The focus is on quality not quantity. HLB

ACNC governance standards to commence 1 July 2013

The governance standards for charities registered with the ACNC have been tabled of Parliament. The ACNC governance standards cover: the purposes and NFP nature of charities; accountability to members; compliance with Australian laws; the suitability of those who govern charities; the duties of those who govern charities; they are not intended to reflect best practice governance, but rather a minimum standard of governance that would be expected by the Australian community. The ACNC governance standards are proposed to commence on 1 July 2013.

A number of changes were made to the governance standards as result of consultation process, including:

- Inserting references that the governance standards must be interpreted in a manner that is consistent with the objects of the Act and the requirements of section 15-10 of the Act; in particular, the principles of regulatory necessity, reflecting risk and proportionate regulation, as well as the unique nature and diversity of NFP entities and the distinctive role that they play in Australia
- Removing the governance standard proposed in consultation that specifically covered responsible management of financial affairs – this standard has now been incorporated as part of the governance standard that deals with duties of those who govern charities
- Clarifying that the governance standard about compliance with Australian law is necessary to trigger the ACNC Commissioner's enforcement powers in the event of a serious breach of the law, and that compliance with the law sets a minimum benchmark by which all entities should govern themselves
- Clarifying that the governance standard dealing with accountability to members does not mandate annual general meetings, and does not add to the financial reporting requirements that already exist in the ACNC Act, and
- Introducing transitional arrangements that apply until 1 July 2017 and will allow incorporated associations to comply with duties under their State or Territory laws, instead of ACNC governance standard 5, which deals with duties of those who govern charities. HLB

Parent identification in AASB 10

It is time to determine 'parent' status under AASB 10 'Consolidated financial statements'. AASB 10 introduces a new approach to identifying entities that are controlled and also an exemption from consolidation for an 'investment entity'.

Control exists when the investor has 'power over investee', 'exposure to variable returns' and 'the ability to use that power to affect its returns from the investee'. These are new concepts through which all existing 'involvements' by an investor with entities must be viewed and determined. Such determinations need to be supported by evidence which complies with the processes inherent in AASB 10.

AASB 10 'Consolidated financial statements' is operative for annual reporting periods beginning on or after 1 January 2013 and applies to 30 June 2013 half-year financial statements under AASB 134 'Interim Financial Reporting'. Not-for-profit entities cannot apply AASB 10 before annual reporting periods beginning on or after 1 January 2014. The investment entity exemption does not apply until annual reporting periods beginning on or after 1 January 2014 but can be early adopted.

An investor, regardless of the nature of its involvement with an entity (the investee) must determine whether it is a parent by assessing whether it controls the investee. Power is the starting point; it arises from rights. Such rights can be straightforward (e.g. through voting rights) or be complex (e.g. embedded in contractual arrangements). An investor that holds only protective rights does not have power over an investee and so cannot control an investee.

An investor is required to consider all facts and circumstances when assessing whether it controls an investee. AASB 10 contains extensive guidance on the following issues when determining who has control:

- Assessment of the purpose and design of an investee
- Nature of rights – substantive or protective in nature
- Assessment of existing and potential voting rights
- Whether an investor is a principal or agent when exercising its controlling power
- Relationships between investors and how they affect control, and
- Existence of power over specified assets only.

Where control does not exist other standards may apply to the investor's involvement with the entity, such as AASB 11 'Joint Arrangements' and AASB 128 'Investments in Associates and Joint Ventures'.

Where an entity meets the definition of an 'investment entity' it does not consolidate its subsidiaries, or apply AASB 3 'Business Combinations' when it obtains control of another entity. An investment entity: obtains funds from one or more investors for the purpose of providing those investor(s) with investment management services; commits to its investor(s) that its business purpose is to invest funds solely for returns from capital appreciation, investment income, or both; and measures and evaluates the performance of substantially all of its investments on a fair value basis. Examples of investment entities in the Australian context are: listed investment companies and managed investment schemes.

An entity is required to consider all facts and circumstances when assessing whether it is an investment entity, including its purpose and design. AASB 10 provides that an investment entity should have the following typical characteristics: more than one investment; more than one investor; has investors that are not related parties of the entity; it has ownership interests in the form of equity or similar interests.

An investment entity is required to measure an investment in a subsidiary at fair value through profit or loss in accordance with AASB 9 'Financial Instruments' or AASB 139 'Financial Instruments: Recognition and Measurement'.

There should be a structured process for the identification of existing 'involvements' by an investor with entities, and for investment entities. The results of this process should be communicated to governance. The documentation and conclusion will also assist in future determinations as to whether facts and circumstances have changed regarding the control of an investee or the application of investment entity definition. 



ACNC annual information statement consultation



The ACNC opened a public consultation on the 2014 Annual Information Statement (AIS) and released a preview of the 2013 AIS. Charities will use the AIS as the primary method of reporting to the ACNC. The information the ACNC receives from all 56,600 charities through the AIS will be published on the ACNC Register.

Charities do not need to begin completing the first AIS, known as the 2013 AIS, until after 1 July 2013. This will be due six months after the end of the charity's 2012–13 reporting period, which will be 31 December 2013 for most charities. To assist charities in preparing for the 2013 AIS, the ACNC created a sample and guidance notes available at acnc.gov.au/reporting.

Registered charities do not need to provide any financial information to the ACNC for the 2013 reporting period. From 2014 onwards the amount of financial information charities will need to provide the ACNC depends on the size and type of the charity.

For example small charities, with annual revenue of less than \$250,000, will not have to provide the same type of information as large charities. HLB

Review engagements revised rules

ASRE 2400 'Review of a Financial Report Performed by an Assurance Practitioner Who is Not the Auditor of the Entity' is a completely revised standard. It replaces the existing ASRE 2400 (August 2008) of the same name. The standard is effective for financial reporting periods commencing on or after 1 July 2013; early adoption is permitted.

The form and content of the new standard is in line with the "clarity" versions of the Auditing Standards. The revised standard now includes requirements and guidance that were, in some cases, previously contained in other pronouncements or were implicit within the existing standard, ASRE 2400.

A compiled standard ASRE 2415 'Review of a Financial Report: Company Limited by Guarantee or an Entity Reporting under the ACNC or Other Applicable Legislation or Regulation' has been issued.

There is an expansion of the scope of ASRE 2415 to incorporate entities reporting under the ACNC Act and other applicable legislation or regulation.

As the purpose of ASRE 2415 is to direct auditors and assurance practitioners to the relevant review standard (ASRE 2400 or ASRE 2410), it is the appropriate standard to direct reviews under the ACNC Act and other applicable legislation or regulation.

ASRE 2415 is a legislative instrument made under section 336 of the Corporations Act 2001. Accordingly, changes made to that standard need to be made through an amending standard. The result is a "compiled" standard which, in this case, comprises the original standard (i.e. ASRE 2415 issued in June 2010) together with the changes contained ASA 2013-1 'Amending Standard to ASRE 'Review of a Financial Report – Company Limited by Guarantee'.

The changes made to ASRE 2415 are editorial in nature and deal mainly with broadening the scope of the standard (to accommodate entities reviewed under the ACNC Act and other applicable legislation or regulation); and acknowledging the issuance of the revised ASRE 2400. HLB

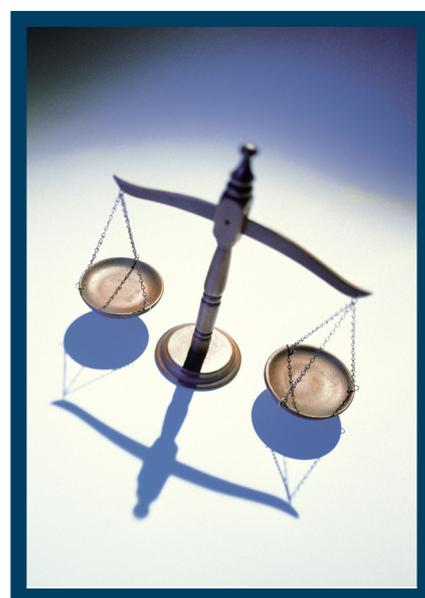
Terms of engagement revised rules too

The APESB issued a revised APES 305 'Terms of Engagement' (APES 305) to update the existing APES 305 (June 2009) of the same title. The pertinent details to be included in the scope of the engagement have been expanded; the features of recurring engagement have been described; and additional factors have been identified for determining the need to reissue or amend an engagement document for a recurring engagement. The revised APES 305 is effective for engagements commencing on or after 1 July 2013.

The changes are:

- The scope of the engagement now has a specific reference to "accounting or auditing and assurance standards" that may be relevant to the engagement; limitations on the conduct of the engagement now specifically include scope limitations and limitations arising from legal or professional and ethical requirements
- The practitioner should now consider the implications of the scope requirements in recurring engagement when documenting the required details
- In certain circumstances, a practitioner will have to determine whether an engagement is a recurring engagement. The features of a recurring engagement are now specified: unchanged terms of engagement under which the professional services are provided; the same or similar professional service provided by the member in each period; defined or identifiable commencement and completion dates each time the engagement is performed; and performance of the engagement is on a regular periodic basis as agreed with the client, for example annually, and
- When determining the need to reissue or amend an engagement document for a recurring engagement, a practitioner should now consider the following factors additional factors: any significant

changes to professional standards or applicable accounting or auditing and assurance standards; and any changes to regulatory requirements. [HLB](#)



The APESB released guidelines to assist professional accountants manage risks associated with providing or utilising outsourced services. APES GN 30 'Outsourced Services' was developed in response to the rapid growth of outsourcing professional services.

The guidance includes:

- In providing an outsourced services, the risk to the fundamental principles in APES 110 'Code of Ethics for Professional Accountants' needs to be assessed. Develop and document an outsourcing policy framework to effectively manage the risks associated with outsourcing
- When considering utilising outsourced services, a practitioner should take reasonable steps to determine that the outsourced service provider has the required professional competence, skills, capacity, policies and procedures to conduct the outsourced services and to manage the risks associated with outsourcing. Appropriate due diligence should be conducted prior to entering into any outsourcing agreement
- When utilising outsourced services, a practitioner should develop and document an outsourcing policy framework together with policies and procedures and communicate this framework to all relevant personnel of the member's firm, and
- In providing or utilising outsourced services, a practitioner should manage the risks of transition and implementation by using appropriate project management skills and discipline.

Guidance is also provided on: monitoring and managing performance, renewal, renegotiation and termination; and documentation. [HLB](#)

Loan loss provisioning proposals



The AASB issued ED 237 'Financial Instruments: Expected Credit Losses', incorporating IASB ED/2013/3. ED 237 contains IASB proposals that would require earlier recognition of credit losses to replace the current incurred loss impairment requirement in AASB 139 'Financial Instruments: Recognition and Measurement'. The proposals build upon previous work to develop a more forward-looking provisioning model, which recognises expected credit losses on a timelier basis.

Expected credit losses are recognised on all financial instruments within the scope of the proposals from when they are originated or purchased. Full lifetime expected credit losses are recognised when a financial instrument deteriorates significantly in credit quality. This is a significantly lower threshold than under the incurred loss model today which in practice has resulted in provisioning only when financial assets are close to default.

Financial reporting requirements both internationally and in the US currently use an incurred loss model to determine when impairment is recognised on financial instruments. The incurred loss model requires that a loss event occurs before a provision can be made and was introduced to avoid the use of so-called 'big bath' general provisions that distorted the accurate reporting of financial performance to investors. However, during the financial crisis the incurred loss model was criticised for delaying the recognition of losses and for not reflecting accurately credit losses that were expected to occur.

Consistent with requests from the G20, the Financial Crisis Advisory Group and others, the IASB and the US FASB have been working jointly to develop a more forward-looking impairment model that reflects expected credit losses. The proposals build upon the expected credit loss model previously agreed between the IASB and the FASB, but it has been simplified to reflect feedback received from interested parties. The FASB has published separately for public comment an alternative expected credit loss model and the two sets of proposals have overlapping comment periods.

The major proposals by the IASB are:

- **Objective:** To recognise expected credit losses (shortfall in contractual cash flows) for all financial instruments within the scope. An entity should estimate expected credit losses considering past events, current conditions and reasonable and supportable forecasts
- **Scope:** Financial instruments within the scope are: all financial assets measured at amortised cost; all debt instruments measured at fair value through other comprehensive income under the new proposal issued in December 2012; all trade and lease receivables;

and other financial instruments subject to credit risk (e.g., written loan commitments and written financial guarantee contracts provided they are not measured at FVTPL)

- **Impairment amount:** Its recognition depends on whether or not the financial instrument has significantly deteriorated since their initial recognition. Three stages are being distinguished: Stage 1: Financial instruments whose credit quality has not significantly deteriorated since their initial recognition; Stage 2: Financial instruments whose credit quality has significantly deteriorated since their initial recognition; and Stage 3: Financial instruments for which there is objective evidence of an impairment as at the reporting date. For stage 1 financial instruments, the present value of 12-month expected credit losses are recognised which are the expected shortfalls in contractual cash flows over the life of a financial instrument that will result if a default occurs in the 12 months after the reporting date ('12 months expected credit losses'). In contrast, an impairment is recognised for financial instruments classified as stage 2 or 3 at the present value of expected credit shortfalls over their remaining life ('lifetime expected credit loss')
- **Impairment recognition:** For financial assets, recognise a loss allowance. For commitments to extend credit a provision is established to recognise expected credit losses
- **Interest:** For stage 1 and 2 instruments interest revenue is calculated on their gross carrying amounts. Interest revenue for stage 3 financial instruments is recognised on a net basis (i.e. after deducting expected credit losses from their carrying amount)
- **Purchased or originated credit-impaired financial assets:** Rather than apply the two-stage approach, changes in lifetime expected credit losses in the estimate of lifetime losses since initial recognition are recognised directly in profit or loss
- **Simplified approach for trade and lease receivables:** There is an accounting policy choice to always measure the impairment at the present value of expected cash shortfalls over the remaining life of the receivables instead of applying the two-class model, and
- **New disclosures.** These include: a reconciliation; a description of inputs and assumptions used to measure expected credit losses; and information about the effects of the deterioration and improvement in the credit risk of financial instruments. 

IASB/AASB work program – outputs getting closer

Following its March meeting, the IASB updated its work plan. A timing of expected milestones in a number of projects has been changed, and a number of new expected project steps and narrow scope projects have been added. As the AASB draws down on these, we should expect to see the Australian outputs in similar time frames.

Projects where EDs are expected in the second quarter include insurance contracts, leases, and rate-regulated activities. In addition, the IFRS on revenue recognition is expected to be finalised by the end of June 2013, and a discussion paper on the IASB's conceptual framework project is also expected then.

The status other projects are:

- Financial instruments (limited consideration of IFRS 9): Redeliberations expected in the second and third quarters of 2013 (previously second quarter)
- Financial instruments (impairment): Redeliberations expected in the third quarter
- Financial instruments (general hedge accounting): Finalisation of this chapter of IFRS 9 expected in the second or third quarter (previously second quarter)

- Financial Instruments (macro hedge accounting): Discussion paper expected in the second or third quarter (previously first or second quarter)
- Rate regulated industries: Expected timing of a request for information expected in the first quarter of 2013 (previously second quarter)
- Going concern disclosures (IAS 1): A new project following with an ED expected in the second or third quarters
- Discount rate (IAS 19): A new project with an ED expected in the third quarter
- Unit of account (IFRS 13): A new project with an ED expected in the second quarter
- Employee contributions to defined benefit plans (IAS 19): Expected date for the finalisation of the amendments of the fourth quarter
- Reflecting other asset changes when applying the equity method of accounting (IAS 28): Finalised amendments are expected in the fourth quarter of 2013 (previously third quarter)

- Put options written over NClS (IAS 32): Target date for an ED of amendments of the third or fourth quarters
- Novation of OTC derivatives and continuing designation of hedge accounting (IAS 39/IFRS 9): Target date for finalisation of the amendments in the second or third quarter of 2013, and
- Sale or contributions of assets between an investor and its associate/JV: Finalised amendments expected in the fourth quarter of 2013 (previously third quarter). [HLB](#)



NFP guidance on consolidations

The AASB issued ED 238 'Consolidated Financial Statements – Australian Implementation Guidance for Not-for-Profit Entities'. The ED proposes implementation guidance to assist NFP entities in the private and public sectors to apply AASB 10 'Consolidated Financial Statements and AASB 12 Disclosure of Interests in Other Entities'. Those Standards apply mandatorily to NFP entities for periods beginning on or after 1 January 2014, following amendments by the AASB in December 2012. Comments to the AASB on ED 238 are requested by 30 June. [HLB](#)

Code of ethics proposed revisions

The APESB issued an exposure draft on proposed revisions to the existing APES 110 'Code of Ethics for Professional Accountants' (the Code). The proposed revisions are: definition of immediate family; new AUST paragraph to address circumstances where auditors may be receiving multiple referrals from a single source. This revision addresses risks identified in the SMSF context. Comments are sought by 19 April. Once finalised, the proposed revisions to the Code will be operative from 1 July 2013. [HLB](#)

Risk management for responsible entities proposals

ASIC released a consultation paper and proposed regulatory guidance on risk management practices for responsible entities in the managed funds sector. Consultation Paper 204 'Risk management systems of responsible entities' and the proposed guidance are based on many current practices of responsible entities. ASIC's proposals also reflect international standards and developments in risk management.

The proposed guidance includes:

- Ensuring risk management systems comprise processes to identify, assess and treat risks
- Ensuring these processes are suitable for individual business objectives and operations
- Ensuring that risk management systems address all material risks, including strategic, governance, operational, investment and liquidity risks, and
- Reviewing risk management systems regularly, and no less than annually, for appropriateness, effectiveness and relevance to individual businesses.

Responsible entities, as Australian financial services (AFS) licence holders, have an ongoing obligation under s912A(1) (h) of the Corporations Act 2001 to have adequate risk management systems, unless they are regulated by APRA. ASIC's existing guidance on meeting this obligation is limited and is contained in Regulatory Guide 104 'Licensing: Meeting the general obligations' and applies across all AFS licensees.

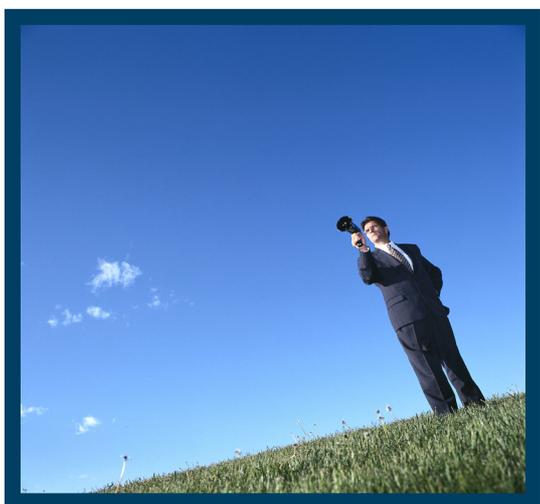
In September 2012 ASIC released Report 298 'Adequacy of risk management systems of responsible entities'. The report reviewed the risk management systems of a selected cross-section of responsible entities of diverse size and complexity to assess the adequacy of their risk management systems. The report found responsible entities that are part of APRA-regulated groups appeared to have more sophisticated risk management systems. ASIC's review also found most responsible entities indicated that their risk management system did not change as a result of the global financial crisis. As a result of the review, ASIC indicated its intention to develop good practice guidance on risk management systems for responsible entities. [HLB](#)



Audit independence guide issued

A new edition of 'The Independence Guide' has been released for members in public practice. It provides an explanation of the conceptual approach to independence set out in Sections 290 and 291 of APES 110 'Code of Ethics for Professional Accountants', together with guidance on application and practical examples.

Major changes in the 2013 version include updating material in relation to public interest entity definitions, rotation requirements, and other legislative changes, and introducing guidance on the key audit partner concept and application of SMSF independence requirements. The Guide is a joint publication of the Institute of Chartered Accountants Australia, CPA Australia and the Institute of Public Accountants. 



Internet

Copies of 'FRA NEWS' are available on the internet at www.tnr.com.au

Queries

For further information or assistance, please contact your TNR Audit & Assurance Partner or Manager.

The information provided in this publication was provided by Colin Parker FCA, former member of the AASB.

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