



COLIN'S

CORNER

Why I dislike models

As we head towards another 30 June reporting date, are preparers and auditors going to be trapped again into using model financial statements?

Some jurisdictions, mainly involving the public sector, have mandated a particular model. This does a great disservice to those involved in the financial-reporting supply-chain by not allowing preparers to tell their own unique stories.

Central authorities are deeply misguided when they rate the consistency of financial statements as more important than their relevance.

Model financial statements can be a useful reference for preparers, but they must not be blindly followed. Financial reporting is about the provision of information for user decision-making. It is a thinking person's process; it must not be about mere compliance.

Accounting standards contain many disclosure rules that require entity-specific consideration, such as related-party disclosures, capital management and financial-instrument risk disclosures. Model financial statements cannot address all the permutations.

Judgements and estimates disclosures under AASB 101 *Presentation of Financial Statements* are also entity specific. Not to mention disclosures about going concern.

Transactions and events, such as a new financial instrument, discontinued operations, or a business combination, can arise during a financial year but are not well catered for in model financial statements.

A model's summary of accounting policies might include several that are irrelevant for a particular entity. The inclusion of these (and related disclosures) contributes to financial-statement 'clutter', key messages obscured. An opportunity is lost to explain how specific policies have been applied.

Some eligible entities apply the reduced-disclosure regime (RDR). In the main they're not-for-profits. Important disclosures may be missed by a certain 'compliance' mindset by preparers and auditors. The challenge with RDR is to add relevant disclosures to those removed by arbitrary rules.

Congratulations to the increasing number of entities that have thought through and improved their financial reporting. They have articulated their business models and revised the financial report structure to reflect it, removing clutter through the thoughtful application of materiality and begun a journey towards plain English reporting. Informative, well-written integrated reports benefit stakeholders.

Contrast this to mindless adherence to a model set of financial statements.

Show leadership. Use the time between now and 30 June to start the journey towards improved financial reporting.

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Financial reporting

Write-downs follow ASIC enquiries

The Australian Securities and Investments Commission has noted MMA Offshore Limited's decision to write down property, plant and equipment by \$254 million in its financial report for the half-year to 31 December.

ASIC reviewed MMA Offshore's 30 June report as part of its surveillance program, raising concerns about the value of property, plant and equipment in the company's vessels business.

ASIC also noted Spotless Group Holdings Limited's decision to write down goodwill in its resources business by \$99.2 million in its financial report for the half-year to 31 December.

ASIC had questioned the recoverable amount of goodwill in the company's report for the year ended 30 June.

ASX-listed Pacific Star Network Limited announced an impairment charge of \$4.5 million on publishing mastheads and goodwill arising from the acquisition of Morrison Media following ASIC enquiries.

The commission had queried the company on the carrying value of non-current assets in its 30 June financial report. It was concerned that assumptions used in impairment models for the publishing business were too optimistic.

An ASIC media release has asked preparers to focus on useful and meaningful reports, adding that impairment testing and asset values remained under surveillance and that assumptions used in impairment models should be supportable and realistically reflect business conditions.

Improvements proposed to operating segments

The International Accounting Standards Board has published proposed improvements to IFRS 8, which covers operating segments. They are open for public comment.

IFRS 8 *Operating Segments* was issued in 2006. It sets out disclosure requirements for information about a company's operating segments, products and services, as well as about the geographical areas in which it operates and its major customers.

The proposed amendments follow on from a post-implementation review of IFRS 8. It confirmed that the standard generally works well but areas were identified that might be improved.

Proposed improvements in the exposure draft include amendments to:

- Clarify and emphasise the criteria that must be met before two operating segments may be aggregated
- Require companies to disclose the title and role of the person or group that performs the function of the chief operating decision-maker, and
- Require companies to provide information in the notes to financial statements if segments in them differ from those reported elsewhere in annual reports and accompanying materials.

The board has also proposed to amend IAS 34 *Interim Financial Reporting* to require companies that change their segments to restate earlier information for prior interim periods.

The exposure draft *Improvements to IFRS 8 Operating Segments* (Proposed amendments to IFRS 8 and IAS 34) is open for comments until 31 July.

Locally, the Australian Accounting Standards Board has issued an equivalent exposure draft *Improvements to AASB 8 Operating Segments*, proposing amendments to AASB 8 and AASB 134.

Comments to the AASB on the exposure draft are required by 23 June.

Discussion paper on disclosure released

The International Accounting Standards Board has published a discussion paper on principles that should make financial-statement disclosures more effective.

Disclosure Initiative – Principles of Disclosure could lead to amendments to IAS 1 *Presentation of Financial Statements*, the standard covering general disclosure requirements, or the development of a new general-disclosure standard.

Stakeholders have said that financial statements sometimes include too little relevant information, too much irrelevant information and information disclosed ineffectively.

The board believes that the development of clear principles governing what, how and where information should be disclosed will improve information provided to users, help companies communicate disclosures more effectively and assist the board in improving disclosure requirements in IFRS standards.

Some specific suggestions in the discussion paper include:

- Seven principles of effective communication, which could be included in a general disclosure standard or described in non-mandatory guidance
- Possible approaches to improve disclosure objectives and requirements in IFRS standards, and
- Principles of fair presentation and disclosure of performance measures and non-IFRS information in financial statements to ensure that such information fails to mislead.

Board chairman Hans Hoogervorst said: 'Investors and companies have told us that there is room for improvement in the disclosures in the financial statements. Agreeing which principles underpin effective disclosures is a vital step towards encouraging the behavioural changes required to make financial statements better communication tools in the future'.

The paper is the latest instalment of the board's disclosure initiative, which was established in 2013 with a 10-point plan to deliver tangible improvements in financial reporting.

The principles-of-disclosure project complements several others the board has undertaken, including amendments to IAS 1 *Presentation of Financial Information* and IAS 7 *Statement of Cash Flows*, and the development of guidance to help companies make materiality judgements when preparing their financial statements.

The disclosure initiative is an important part of the board's central theme, *Better Communication in Financial Reporting*.

The paper is open for comments until 2 October.

Locally, the AASB is seeking views on it.

The Australian board noted that proposals to define and restrict the use of unusual or infrequently occurring items in financial statements will also affect the way entities determine alternative-profit measures such as underlying earnings. It also noted that the IASB paper explores the challenges around providing relevant entity-specific information and proposes principles for disclosures to help preparers.

Other areas of interest to Australian constituents include preliminary views on permitting entity-specific performance measures, such as EBIT and EBITDA in financial statements, clarifying 'other' information that can be included, and cross-referencing information outside financial statements.

AASB chair Kris Peach said: 'The IASB proposals to define unusual or infrequently occurring items is likely to significantly restrict the types and amounts of adjustments some entities currently make to determine

underlying earnings and will address user and regulator concerns that entities "cherry pick" the adjustments made. As a result, comparability over time for each entity and between entities should improve.

'For those entities taking up the challenge to improve the value of their financial statements as a communication tool, not just treating them as a compliance exercise, these proposals will be beneficial. We are particularly interested in entities that have started this process with decluttering exercises to understand what benefits they have found'.

The AASB wants to hear Australian views on the discussion paper, particularly:

- What challenges and opportunities does it pose for Australian entities?
- What non-IFRS information in financial statements would be useful? and
- Are non-listed entities likely to amend current practice? If not, what are the barriers to doing so?

Governance

ATO updates tax-risk guide

The Australian Taxation Office has included in the latest update of its tax-risk management guide a summary of directors' roles in overseeing an organisation's protocols.

'There are no additional responsibilities on directors. The guide really restates what [directors'] responsibilities are,' ATO assistant commissioner Jeff Stevenson said.

The update of the *Tax risk management and governance review guide* and the accompanying summary for directors are aimed at helping large organisations develop and improve their governance and internal controls.

'We suggest an initial gap analysis by business. They can compare and contrast their framework with the guide,' Mr Stevenson advised.

While the guide outlines best practice, it is not mandatory and organisations are not required to comply with every element of it. The ATO recommends an 'if not, why not' approach when using the guide.

'If an entity does not have a particular control in place that we've articulated in the guide, it doesn't necessarily mean a fail. It's more of a prompt for a conversation on why the control might not be there and how the risk might be managed otherwise,' Mr Stevenson said.

The guide explains that tax risk comes in two forms. The first involves paying or accounting for an incorrect amount of tax. The second derives from tax positions adopted by companies that are out of step with what directors have authorised or believe is prudent.

The new 'Director's summary' section outlines directors' responsibilities for tax-risk management and the ATO's initial areas of focus for governance reviews. Also included in the guide for the first time is a set of self-assessment procedures for tax-governance

reviews, which set out methods for examining tax-risk practices. These procedures can be used by companies, advisers and the ATO.

The guide's aim is to help organisations understand the ATO's better practices on tax governance so that they may develop and improve their own governance and internal control frameworks, test the robustness of their approaches, and demonstrate the effectiveness of internal controls.

The ATO has included the summary because directors asked for a more concise version of the guide. It provides guidance on how a board should consider tax risks.

The director's summary covers:

- Corporate governance and risk management – explaining how the existence of a strong tax governance process could stave off a more costly ATO review
- Justified trust and key controls – the process the ATO uses to assess tax risks of taxpayers, which includes gathering evidence on their governance process
- Three lines of defence as one approach to risk management
- Board-level controls – clarifying the responsibilities of the board and management
- Internal-controls testing – setting the expectation that directors will understand internal controls at the company in their oversight role
- Management-level controls – the board should oversee that managerial responsibilities are assessed and met, and
- Directorship responsibilities and liabilities – reminding directors of their legal responsibilities and personal liability concerning unpaid PAYG withholding amounts and unpaid superannuation-guarantee-charge obligations.

Record \$45 million civil penalty against Tabcorp

The Federal Court has fined Tabcorp \$45 million for failing to comply with anti-money-laundering and counter-terrorism laws.

It is the highest civil penalty in corporate Australian history.

Paul Jevtovic, CEO of the Australian Transaction Reports and Analysis Centre (AUSTRAC), said that the record \$45 million penalty is a stark reminder to all reporting entities that serious consequences follow non-compliance with the Anti-Money Laundering and Counter-Terrorism Financing Act 2006.

'Today the court found that Tabcorp had contravened the Act on 108 occasions over a period of more than five years,' said Mr Jevtovic.

Justice Perram found that Tabcorp had failed to:

- Have a compliant AML/CTF program for more than three years to manage the risks of money laundering and terrorism financing
- Give AUSTRAC reports about suspicious matters on time – or at all – on 105 occasions. Tabcorp has admitted that the suspicions related to unlawful activity, including money laundering and credit-card fraud
- Identify a customer who collected \$100,000 in winnings, and
- Enrol with AUSTRAC on time.

'Failing to uphold a robust AML/CTF program creates opportunities for serious and organised crime and terrorist groups to conceal the movement and use of illicit funds for attacks and crimes against Australian citizens,' said Mr Jevtovic.

'In our view, Tabcorp had a corporate culture indifferent to meaningful AML/CTF compliance and risk mitigation until we intervened.'

Tabcorp admitted that it had had insufficient processes for consistent management, assurance and operational execution of its AML/CTF program. Its program was under-resourced, and Tabcorp's senior management failed to receive regular compliance reports.

Mr Jevtovic said: 'Boards and senior management across all industries should take note to ensure that they are fully informed of their AML/CTF compliance.'

'Such contraventions are not to be taken lightly, and this unprecedented civil penalty highlights AUSTRAC's resolve to take enforcement action against reporting entities that engage in significant, extensive and [systematic] non-compliance.'

AUSTRAC's agreed court costs and Tabcorp's disclosed defence costs are expected to double the company's bill.

Governance Institute launches 'must-have' guide for aged-care directors

The Governance Institute of Australia has launched a must-have guide for directors and senior management in the aged-care sector.

Profitability, return on assets and equity are under pressure in what is soon to be the largest employer in the country and governance challenges are immense.

Adding value to governance in aged care is a practical guide for the sector's board members on workplace arrangements, staff roles, IT, business processes and capital expenditure.

Increasing Choice in Home Care reforms have changed the regulatory framework from 27 February, and the guide addresses a broad range of issues, including the unique challenges facing the sector, factors to consider before taking a board position, issues that boards should consider when appointing a new member, the relationship between boards and management, interaction with stakeholders, volunteer management and risk-management responsibilities.

Aged care is a significant part of the Australian economy. About 2000 providers employ about 350,000 staff.

'Boards of aged-care providers will be subject to increasing scrutiny and pressures as the forces of demographics press up against the issues of affordability and sustainability. [They] will need to ensure that they are capable of making informed and effective decisions and have in place governance frameworks to enable this,' said Governance Institute chief executive Steven Burrell.

'A lot of boards, particularly not-for-profits, may not be prepared for the regulatory change sweeping the sector and the demands this brings. Boards need to have a designated skillset to overcome the multiple challenges their organisations are facing,' he said.

'Importantly, the guide does not tell boards how to run their organisation, but it does step directors through the issues that they should consider in terms of their governance responsibilities.'

Fundraising code of conduct proposed

The Fundraising Institute of Australia has released an exposure draft of a revised fundraising code of conduct for the charity sector.

The code aims to reflect best practice and addresses public concerns about fundraising practices. Among them are how fundraisers approach vulnerable people and the due diligence charities carry out when working with fundraising contractors.

FIA CEO Rob Edwards says proposed changes could result in 'spot checks' and compulsory code training for professional fundraisers. Charities will have to ensure that fundraising staff appointed from 1 July have completed FIA-code training within six months of their appointments.

The code is self-regulatory and does not replace or override any law, but adherence to it will be a requirement for FIA membership. Compliance will be monitored and enforced by the FIA's ethics committee.

Among new protections for people in vulnerable circumstances, the code requires FAI members not to accept a donation where they have a reasonable belief that the donor is in vulnerable circumstances or lacks the capacity to make a decision to donate.

In addition, FIA members must:

- Not subject donors to undue influence, harassment, intimidation or coercion
- Maintain an appropriate professional relationship with donors over bequests
- Not prevent or discourage a donor from seeking independent legal advice about a donation
- Not prevent or discourage a donor from having a family member or other trusted adviser present when considering a donation, and
- Not, after obtaining a donation, change the conditions of the donation without first telling the donor about changes and gaining consent for them.

The FIA's proposed code will also require members to provide information about how prospective donors can opt-out of receiving further solicitations.

In addition to new requirements for their promotional materials, members must ensure that relevant parties in their supply chain are aware of their obligations under the code and do not act in ways that could result in the member's breaching the code.

At least one board member, on behalf of the board of directors, or the CEO of the charity will have to sign off annually on the member's adherence to the code.

AAT upholds director's appeal over ban

The Administrative Appeals Tribunal has upheld an appeal by Derry Bernard Hill against an ASIC decision disqualifying him from managing corporations for a year.

Mr Hill was a director of Reed Constructions Australia Pty Ltd and several other businesses. He was disqualified from managing corporations for a year from 1 May 2015 after ASIC found that he had failed to exercise his powers and discharge his duties as a director with the degree of care and diligence required.

The tribunal set aside ASIC's decision and ordered that no disqualification order be made. The AAT found that the breaches of duty alleged by ASIC were not established by the evidence.

Director disqualified from managing companies

ASIC has banned Michael Ian Davey of Slacks Creek, Queensland, from managing corporations for two-and-a-half years.

Mr Davey's banning follows the appointment of liquidators to two companies he managed, Refractory Construction Pty Ltd and A4dable Geeks Pty Ltd.

As a result of information contained in reports provided by the failed companies' liquidators, ASIC was concerned that Mr Davey had:

- Failed to prevent the companies from trading while insolvent
- Failed to ensure the companies paid their taxes
- Failed to discharge his duties as a director, and
- Had engaged in illegal 'phoenix activity'.

Mr Davey has appealed to the AAT for a stay of the disqualification.

ASIC commissioner Peter Kell said: 'Directors need to be vigilant when it comes to managing companies and need to discharge their duties both lawfully and ethically. Where they fail to do so, ASIC will take steps to protect consumers and creditors from such directors by disqualifying them from managing companies.'

Director fined for failing to notify market of share trading

Angus Matthew Holt, of Sunshine Beach, Queensland, has been convicted and fined for failing to lodge notices regarding his share trading between 13 January and 3 July 2015.

Mr Holt was a director and executive chairman of Optiscan Imaging Limited between February 2009 and July 2015.

He pleaded guilty to nine charges of failing to notify the Australian Securities Exchange within 14 days of any change in the director's interest in a listed public company, and three charges of failing to notify the ASX within two business days of the changes in his substantial holdings in a listed public company.

He was convicted on all 12 counts and fined \$4500.

'Investors and the market in general, have a legitimate interest in the trading by directors in the company. It is important that directors uphold their responsibilities to ensure market transparency and efficiency. Where ASIC becomes aware of repeated and lengthy failures to make the required disclosures, ASIC will bring the matter before the courts,' said ASIC commissioner Cathie Armour.

Mr Holt voluntarily co-operated with ASIC in the investigation of the offences.

Class actions – Spotless and Bellamy's

ACA Lawyers has been investigating allegations that Spotless Holdings Limited had no basis for growth forecasts of increased EBITDA and NPAT that it made or reiterated on 24 February 2015, 25 August 2015 and 22 October 2015.

On 2 December 2015, Spotless announced that EBITDA would be flat year on year and

NPAT approximately 10 per cent below the financial year 2015. Spotless's share price dropped by about 40 per cent after its 2 December 2015 announcement.

On 2 December last year, Bellamy's Australia Limited announced a significant revenue downgrade. Its share price dropped by almost half in response to the 2 December downgrade, resulting in shareholder losses of more than half a billion dollars.

The Australian Securities Exchange asked Bellamy's to explain the timing of its announcements. On 9 December Bellamy's agreed to a voluntary trading suspension, which was lifted on 11 January when Bellamy's released a market update in which it substantially changed its explanation for the downgrades and announced its CEO's departure.

ACA Lawyers is investigating whether Bellamy's has breached its continuous-disclosure obligations and/or engaged in misleading or deceptive conduct in statements made from 14 April last year to 11 January.

Regulators

ACNC update

The Australian Charities and Not-for-profits Commission (ACNC) has:

- Stated that 1300 double-defaulters were at risk of losing their ACNC registration
- Reminded 4000 charities of the consequences for overdue annual reporting
- Revoked the charity status of Nest Egg Guardians
- Launched the *Charity Compliance 2015 and 2016* report, and
- Published a guide to help charities consider the issues of information and data management.

AFS licensees

ASIC releases guidance on risk management

ASIC has released regulatory guide 259 *Risk Management systems of responsible entities* to provide more guidance on financial-services licence-holders' obligations to maintain adequate risk-management systems under s912A(1)(h) of the Corporations Act.

The guide aims to ensure that responsible entities' risk-management systems, including their minimum procedures and practices, are adaptable to changing market conditions and remain effective.

It promotes early identification of risks to help to avoid adverse consequences that might affect investors. Several responsible entities have collapsed, resulting in significant losses.

The guide expects responsible entities to have:

- Overarching risk-management systems
- Processes for identifying and assessing risks, and
- Processes for managing risks.

The guide also includes good-practice guidance, which is not mandatory. It outlines measures that responsible entities can adopt to enhance their risk-management systems and operate at a level above their statutory obligations.

Registrable Superannuation Entity licensees are also subject to the Australian Prudential Regulation Authority's (APRA) requirements on risk management. ASIC's guidance is intended to act in unison with APRA's requirements.

There is no formal transition period for compliance with the guide.

If a responsible entity can show that it is taking steps to bring its risk management into compliance with the ASIC's guidance the commission intends to take over the next year a constructive and facilitative approach to any breaches.

Financial planner banned for life

ASIC has permanently banned Daniel Peter Logan from providing financial services after finding that he engaged in dishonest conduct and failed to comply with a financial-services law.

Mr Logan, formerly of Brisbane, was a financial planner with Anne Street Partners Financial Services Pty Ltd between October 2012 and October 2015.

ASIC found that between March 2013 and October 2015, Mr Logan:

- Created false documents to entice an acquaintance to invest money through him
- Used investment funds given to him for his personal use
- Created false documents to perpetuate the belief that the funds had been invested on behalf of his acquaintance, and
- Admitted to the misconduct only upon discovery of his wrongdoing.

ASIC determined that Mr Logan's conduct was not a lapse of judgement but deliberate and repeated acts that perpetuated the dishonesty, displaying a lack of integrity and professionalism.

ASIC deputy chairman Peter Kell said: 'Mr Logan's wrongdoing was very serious. His actions were not limited to an isolated incident, but were designed to deceive over a period of time and conceal his initial wrongdoing. ASIC will ensure financial advisers who behave dishonestly are removed from the financial-services industry.'

Licence cancelled for failing to lodge annual statements

ASIC has cancelled the financial-services licences of Rebate Financial Services Pty Ltd and Capstone Capital Pty Ltd for failing to comply with several key obligations.

In particular, ASIC has found that the two licensees failed to:

- Lodge annual financial statements and auditor's reports, and
- Maintain membership with an external dispute resolution scheme that met its approval.

ASIC has also suspended until 1 May the AFS licence of KABM Pty Ltd for failing to lodge financial statements and auditor's reports for three consecutive years. If the company fails

to lodge the required documents on time, the commission will consider cancellation.

ASIC deputy chairman Peter Kell said: 'The annual lodgement of audited accounts is an important part of a licensee's demonstrating it has adequate financial resources to provide the services covered by its licence and to conduct the business lawfully.

'Membership of an external dispute resolution scheme is also an important requirement for licensees and ASIC will not hesitate to act against those who fail to comply with their responsibilities.'

ASIC is empowered to suspend or cancel a licence if the licensee has contravened its obligation to lodge financial statements and maintain membership with an approved EDR scheme.

External dispute resolution gives consumers alternatives to legal proceedings for resolving complaints. Compulsory EDR scheme membership is an important feature of AFS licences.

Guidance updated on conduct and disclosure obligations

ASIC has updated regulatory guide 175 *Licensing: Financial product advisers conduct and disclosure* to reflect regulatory and legislative changes, including revisions to the Future of Financial Advice reforms.

The guide applies to those who provide financial-product advice to retail clients. It details how ASIC will administer the requirement under the *Corporations Act 2001* for financial advisers to prepare and provide a financial-services guide, give a general advice warning, and prepare and provide a statement of advice.

RG 175 also provides guidance on how ASIC will administer the requirement under the *Corporations Act* for financial advisers providing personal advice to retail clients

to comply with the best-interests duty and related obligations. These were introduced as part of the FOFA reform package to improve the quality of financial advice received by retail clients

RG 175 has been updated to reflect:

- Technical amendments to the FOFA reforms
- Recent amendments to clarify financial advisers' record-keeping obligations in class order [CO 14/923] *Record-keeping obligations for Australian financial services licensees when giving personal advice*
- The application of the tax-agent services regime in the *Tax Agent Services Act 2009* to financial advisers who provide tax (financial) advice from 1 July 2014, and
- The relief available under ASIC Corporations (Facilitating Electronic Delivery of Financial Services Disclosure) Instrument 2015/647 to facilitate the delivery of disclosures by digitising them.

RG 175 has been updated to clarify that while best-interests duty and the appropriate advice requirement introduced as part of FOFA reforms are separate obligations, it is unlikely that advice that fails to meet best-interests duty will be appropriate. Two examples have been included to illustrate the process ASIC will apply in determining whether duty has been satisfied.

RG 175 provides guidance on the use of restricted terms under s923A of the *Corporations Act*, particularly about when commissions can be said to be 'rebated in full'.

ASIC is considering the interpretation of s923A, including whether other terms (such as 'independently owned') are restricted under s923A. The commission will further update RG 175 to provide enhanced guidance on s923A in due course.

Ethics

Revised APES 315 *Compilation of Financial Information*

The Accounting Professional & Ethical Standards Board Limited has issued a revised APES 315 *Compilation of Financial Information* to replace a standard issued in February 2015.

The key change updates a reference in paragraph 1.11 to ASIC Corporations (Audit Relief Instrument) 2016/784, which supersedes ASIC class order CO 98/1417 *Audit relief for proprietary companies*.

The revised APES 315 will be effective on 1 July, early adoption permitted.

Audit

AUASB March meeting highlights

Highlights of the March meeting of the Auditing and Assurance Standards Board included:

- Auditor reporting implementation: The board continued discussions on the communication of key audit matters for parent-entity financial statements, stapled security groups and condensed interim

financial reports. These matters will be finalised at the April meeting. The board agreed to develop a new series of auditor's-responsibilities statements that will include generic terminology to describe the type of entity and those charged with governance

- Concise financial reports: Approved for issue the revised version of GS 001 *Concise Financial Reports Under the Corporations Act*

- Audit Committees: Considered and provided input into the draft *Audit Committees – A Guide to Good Practice*, and
- Compliance Engagements: Considered an initial version of the revised exposure draft of ASAE 3500 *Compliance Engagements* with an updated exposure draft to be approved at the April meeting.

International

US Fraud deterrence

The US Centre for Audit Quality has published a report *Addressing Challenges for Highly Subjective and Complex Accounting Areas* that compiles leading-practice recommendations from dozens of company executives, corporate directors, and auditors who attended two 2016 workshops to discuss ways to help deter fraud and enhance financial reporting.

Taken together, the insights illuminate and underscore how improved accounting policies and internal controls on highly subjective and complex accounting areas are key for stemming financial-reporting fraud and reducing the number of restatements.

UK FRC calls for improved quality control

The UK Financial Reporting Council is calling on audit firms to improve quality control by building on examples of good practice identified in its latest review.

A third of the audits sampled required more than just limited improvements, suggesting that quality control had not been effective.

Some firms' audit-quality procedures go beyond those required by standards. However, the number of audits that required more than just limited improvements shows that much audit quality fails. To achieve faster improvements and greater audit-quality consistency strong leadership and a correct culture is required.

The FRC's *Audit Quality Thematic Review* identified areas of good practice, including:

- Half of the firms have a dedicated board or committee that oversees audit quality, bringing all the elements together and ensuring that it has specific prominence and focus in the firm's leadership agenda
- Two firms have set out their audit-quality procedures in a 'three lines of defence' model, helping to understand how these

procedures interact to achieve quality and minimise the risk of inconsistency

- Initiatives to achieve consistent audit quality, identify areas for improvements and monitor the effectiveness of training in specific areas requiring improvement, and
- Audits with a higher level of partner and director involvement had a greater likelihood of achieving a better outcome before the issue of reports.

The FRC also identified procedures that should be a focus for improvements. These include:

- The appropriate involvement of specialists in the audit with sufficient reporting of their work where this was important to achieve audit quality, and
- That firms should consider whether insights from their root-cause analyses could improve audit quality.

Melanie McLaren, FRC's executive director for audit and actuarial regulation, said:

'There is evidence of audit quality being of greater focus at firms' leadership level. However, it requires more effort on the basic quality-control procedures if real sustained improvement is to be achieved.'

The FRC reviewed six of the largest audit firms. Twenty-six audits were selected from FTSE 100, FTSE 250 and other listed companies to look at key aspects of the control systems used by firms to support their audit teams.

In 2017-18 the FRC thematic reviews will focus on how firms' governance and culture supports the delivery of further improvements in audit quality.

Global survey of inspection findings shows decline

The International Forum of Independent Audit Regulators fifth annual *Global survey of inspection findings* collates the findings of 36 IFIAR members' inspections of firms affiliated with six big international audit-firm networks.

IFIAR's survey shows a general decline in inspection-finding rates, however, high rates are still a concern. It notes similarities in the nature and extent of findings compared with last year.

Results continue to show a lack of consistency in high-quality audits and point to a need to address quality control, including in the critical area of auditor independence.

Robust root-cause analysis and implementation of remedial actions are fundamental to raising the bar on audit quality. It is critical that firms implement processes that enable a timely, thorough assessment of recurring root-cause issues – positive and negative – and take appropriate actions.

Too many audit firms continue to have high rates of inspection findings, including in the areas of engagement performance (49 per cent), independence and ethical requirements (40 per cent), human resources (31 per cent), and monitoring (28 per cent).

Though the frequency of findings has decreased in every area of quality control, IFIAR believes more improvement is needed. Firms should continue to explore practices to determine why audit deficiencies recur and challenge quality controls to determine whether system changes will drive more consistent audit execution.

The inspection themes with the highest numbers of findings in individual audit engagements were largely consistent with the 2015 survey.

For audits of listed Public Interest Entities (PIEs), these themes were accounting estimates, including fair-value measurement (32 per cent), internal control testing (18 per cent), revenue recognition (13 per cent), and, a new theme added to the 2016 survey, audit sampling (17 per cent).

For audits of systemically important financial institutions internal control-testing was a recurring theme.

INSIDE GAAP CONSULTING

GAAPinar series starts

Our series of 13 GAAPinars has begun. Feedback on the first two sessions, *What's new* and *Going Concern*, has been very encouraging. Missed them? No worries ... recordings are available.

There are 11 GAAPinars remaining, and you may register for any of them.

Our next GAAPinar is on 20 April with Carmen Ridley, AASB member. Its title is *AASB 16 Leases – Let's understand the key principles*.

Remaining sessions are:

1. *Professional scepticism – getting it right* (Thurs 27 Apr)
2. *Lessons from recent frauds and non-compliance with laws and regulations* (Thurs 4 May)
3. *Ethics code – the forgotten standard?* (Thurs 11 May)

4. *New AASB 15 (Part 1) – identifying the contract and performance obligations* (Tues 16 May)
5. *New AASB 15 (Part 2) – determining and allocating the transition price to performance obligations* (Thurs 18 May)
6. *New AASB 15 (Part 3) – recognise revenue* (Thurs 1 June)
7. *Business law for accountants and auditors* (Thurs 8 June)
8. *NFP reporting and ACNC activities – the latest* (Thurs 15 June)
9. *Financial reporting update for 30 June 2017* (Thurs 22 June), and
10. *Provisions and contingencies – a fresh look* (Thurs 6 July).

Each session costs \$297, and discounts are available, including for sole practitioners and multi-offices.

A brochure can be downloaded from www.gaap.com.au. Questions? Contact Colin.

AASB 15 Masterclass in Sydney on 23 May

Calling CFOs and audit partners in NSW. Please lock in 23 May for our one-day *Masterclass AASB 15 Revenue for Customer Contracts* at the Intercontinental Sydney.

Numbers are strictly limited to enhance learning and discussion. Interest is already strong, and we are expecting a sell-out.

A brochure can be downloaded from www.gaap.com.au. Questions to Colin.

We will be taking our masterclass and an *Introduction to Leases* to Brisbane and Melbourne in December, and Adelaide early in 2018.

In the meantime, if you need training on *AASB 15 Revenue from Customer Contracts*, *AASB 9 Financial Instruments* or *AASB 16 Leases*, don't hesitate to contact us.



Colin Parker
GAAP Consulting

Contact Us

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