جهاز أبوظبي للمحاسبة
ABU DHABI ACCOUNTABILITY AUTHORITY

ADAA IFRS digest

IFRS news, updates from ADAA, IASB and the Accounting Profession

April 2019

WHAT'S NEW THIS MONTH

ADAA's hot topics

It's not unusual. IASB considers the Tom Jones classic.

Brexit is inescapable. It's time to face it and report.

UAE banking perspectives 2019. Technology and banks.

IAS 34 Interim financial reporting. How much disclosure is enough?

How aligned is IPSAS and IFRS? IPSASB's March meeting answers.

PCAOB releases latest audit firm inspection report. What does it say about your Audit firm?

And on the back page ***Kingman review of the FRC -*** an insight from ADAA's Hasina Al Adawi.

WHAT'S NEW FROM IFAC AND THE IASB

The IASB is located in Cannon Street, London

It's not unusual. The IASB's latest update evokes the Tom Jones classic. The Board tentatively decided to define unusual items along the following lines: *"Unusual items are income or expenses with limited predictive value because it is reasonable to expect that similar items will not arise for several future reporting periods. Gains and losses arising from the remeasurement of items required to be measured at current value (including fair value) generally should not be classified as unusual items. Entities should provide a narrative description of the transactions or other events that give rise to unusual items."* There is still some disagreement amongst IASB members on these conclusions not least on how many reporting periods is 'several' for unusual purposes, so expect this topic to go on. IASB update here.

How aligned is IPSAS and IFRS? IPSASB's march meeting answers. See Agenda item 1.7. Page 1 pictorially reveals them closer than you think. Table 3 provides the detail for each standard. Table 2 highlights IFRS with no equivalent IPSAS and the IPSASB's views thereon. The ones to watch are Fair Value Measurement, Leases and Revenue. More here.

WHAT'S NEW FROM THE ACCOUNTING PROFESSION

And finally please turn the page for ADAA's monthly accounting insight…

Brexit is inescapable. Its impact should be assessed (directly or indirectly) on financial reporting for going concern, finance arrangements, and post balance sheet events. Uncertainty impacts judgements which affects both balance sheet and income statement for the more-challenging forward looking assessments. One should not factor unknowns that become knowns retrospectively, as they weren't known. So Dec 2018 disclosures could be materially different to Mar 2019 disclosures. Everything impacted involves judgement, and judgement requires sufficiency of disclosures, consistently, under all IFRSs. Listen to KPMG's podcasts here and here.

UAE banking perspectives 2019. LIBOR is being phased out, gradually being replaced with alternatives such as risk-free rate (RFR) benchmarks. Just one of the issues KPMG considers in the 4th edition of their banking report. The top 10 UAE banks enjoyed 11.5% increase in profits even though IFRS 9 replaced IAS 39. That was because the IFRS 9 catch up adjustments passed through retained earnings, not the income statement. Read here.

IAS 34 Interim financial reporting. Grant Thornton has produced example IFRS interim financial statements. Interim financials are prepared either as a condensed set or full set basis. The form and content of interim financial statements depends on the activities and transactions of the individual reporting entity, however this publication will help if you need to prepare interim IFRS financials. Read here.

PCAOB releases latest audit firm inspection report. The countries with perhaps the two largest and most significant stock markets have both published reports critical of the audit profession. On the back page we review Kingman. Here, the PCAOB. They report: *"The inspection team identified matters it considered to be deficiencies in the performance of the work it reviewed. In 13 audits, certain of these were of such significance that it appeared that the Firm, at the time it issued its audit report, had not obtained sufficient appropriate audit evidence to support its opinion…49 of the 55 engagements were integrated audits of internal control and financial statements…In one of the audits, after the primary inspection procedures* (by the PCAOB), *the Firm revised its opinion on the effectiveness of the issuer's internal control over financial reporting ("ICFR") to express an adverse opinion."*

Another finding: Issuer is in the energy industry. Reported declining revenue and gross profit for last few years due to declining prices and demand. The issuer's properties in each segment engaged in different types of sourcing and production activities. Certain properties idle or inactive at the year end. The issuer documented its policy to group long-lived assets at the segment level to assess impairment. The audit firm failed to:

- Identify and test controls over the issuer's determination of asset groupings and identification of impairment indicators.
- Sufficiently evaluate the reasonableness of management's assertion that the cash flows of the properties were largely interdependent, as the Firm's procedures were limited to reading an issuer-prepared memorandum and noting that the issuer also grouped its assets at segment level for testing goodwill.

https://pcaobus.org/Inspections/Reports/Pages/default.aspx

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Kingman review of the FRC - an insight from ADAA's Hasina Al Adawi

Background

In April 2018, the UK Government announced its intention to conduct an independent review of the Financial Reporting Council (FRC). This followed a number of high profile deficient audits and corporate collapses, notably Carillion, which subsequently led to a joint inquiry by the Work and Pensions, and the Business, Energy and Industrial Strategy Government Select Committees. Both of which were highly critical of the current status quo.

The FRC is an independent regulator in the UK, responsible for regulating auditors, accountants and actuaries, and setting the UK's Corporate Governance and Stewardship Codes. Sir John Kingman, Chairman of Legal and General, and previous Second Permanent Secretary to HM Treasury led the review.

Kingman's Review Findings

Kingman's review (link) resulted in 83 recommendations, including that the FRC be abolished and replaced by a new Audit, Reporting and Governance Authority, accountable to Parliament, with a new mandate, new clarity of mission, new leadership and new powers.
Below are a few key points from the report.

Structure and purpose

Kingman describes the FRC as *"a rather ramshackle house, cobbled together with all sorts of extensions over time. The house is, just, serviceable, up to a point, but it leaks and creaks, sometimes badly."*

Kingman suggests the FRC was established in a past era, for a different purpose, which does not fit current needs. He notes that the FRC lacks a statutory base (i.e. it has no legal powers) and a new body needs to have not only the responsibility but also the statutory power of oversight of regulation over the actuarial, audit and accounting professions.

Funding source

The review calls for Statutory funding. He argues that the FRC, is tainted by its funding through an industry levy which conveys it merely the status of a trade association, that is dependent on rule by the consent of its constituents. It thus has 'limited or even non-existent' powers.

Staffing

Kingman criticizes the closeness of the FRC with the audit firms, and the closeness with the Big Four in particular, which he considers substantial. He writes *"It's shocking to find that board appointments at the FRC were done in a surprisingly informal way, including using the alumni networks of the Big Four."*

Kingman makes the comment on FRC staffing and culture "*is not as open and attractive to the best talent as it could be."*

Recruitment was described as informal and whilst the staff contained some excellent people, the culture would need changing by a mostly new senior management.

To achieve the vision set out by Kingman a new regulator should consider a strategy for hiring a more diverse and experienced subject specific individuals.

Corporate Failures

Over the past five years, the Big Four's share of FTSE 350 auditing expanded from 95% to 98%, in spite of a series of supposedly rigorous reforms from the EU aimed at tackling perceptions of a lack of competition in the sector since the 2008 financial crisis.
Fears of both monopolization and conflicting interests have grown through 2018, meanwhile. As all of the Big Four were implicated in some way in the collapse of Carillion these fears are precisely why 'breaking up' the Big Four has suddenly become a major talking point among Britain's politicians.

Questioned about the future regulation of the audit profession following the Carillion collapse, Sir John said any new regulator must have the power to *"go in and have a look"* where there were concerns about the financial health of a company. At present the FRC can only punish directors who are qualified accountants, not any of the other directors, something it has repeatedly urged the government to address. Accordingly, Kingman recommends the new regulator should also be given greater powers to ensure that a consistent approach is taken against auditors, accountants and non-accountant directors shortcomings, based on a scheme equivalent to the Audit Enforcement Procedure (AEP).

As to the auditor's duty and oversight, Sir John recommends broadening the auditor's duty to impose a *"duty to alert"* in respect of *"viability or other serious concerns"*. He puts forward a case for improvements to the Auditor's Report to include *"graduated"* audit findings, which would entail presenting the auditor's judgmental views to shareholders on key audit issues in further detail and that the regulator should be permitted to instruct skilled persons, paid for by the company, to investigate where the regulator has concerns as to key audit judgements. (Is Kingman saying ISA 701 isn't working?)

What next?

Kingman recommends, as a priority, the FRC and Government work to identify and agree a set of measures and timetable that can be implemented in the short term, in advance of tabling primary legislation. Until the new regulator is in place the government will work with the FRC to implement 48 of the 83 recommendations. Kingman also strongly welcomes the proposal that a piece of independent work should be done to explore the issues arising from the audit expectation gap.
The call for a more proactive regulator effectively signals the end of the era of self-regulation by the audit and accounting profession in the UK.

Final Thought

On the other hand, Kingman highlights that the accounting regulator needs reform, but what about the other piece of the puzzle – accounting standards themselves? Are they fit for purpose? If the captain of the ship is changed and the problem was with the ship, then the problem is not solved. If so, who will pay the price?
Answer-the same persons who are paying the price now.

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