

International experience regulatory risk-based financial statement IFRS Accounting Standards compliance review practices: South Africa

Prepared by: Darrel Scott

Date: October 2022

Vietnam



THE WORLD BANK
IBRD • IDA | WORLD BANK GROUP

The views expressed in this presentation are my own and not necessarily those of any organization with which I am associated.

Disclaimer

This course contains copyright material of the IFRS® Foundation in respect of which all rights are reserved. Reproduced by Darrel Scott with the permission of the IFRS Foundation. No permission granted to third parties to reproduce or distribute. For full access to IFRS Standards and the work of the IFRS Foundation please visit <http://eifrs.ifrs.org>

The International Accounting Standards Board® (IASB), the IFRS Foundation, the authors and the publishers do not accept responsibility for any loss caused by acting or refraining from acting in reliance on the material in this publication, whether such loss is caused by negligence or otherwise.

Unless specified otherwise, the accounting requirements that are the subject matter of this presentation are the IFRS Standards as issued by the IASB that are applicable on or after 1 January 2022

Purpose of session

This session aims to provide an understanding of bases for resolving IFRS technical issues including observations from mechanisms employed at the international level and for encouraging and enforcing consistent application in South Africa and the UK.

South Africa: Security regulator's IFRS compliance review mechanism

JSE's IFRS compliance review mechanism

Overview

- ▶ The JSE is the **frontline regulator**, for listed companies, although it would refer criminal cases to the government regulator (FSCA)
- ▶ South Africa applies a **'twin peaks' model** with the Prudential Authority responsible for prudential supervision of banks, insurance companies and market infrastructures (e.g. exchanges and clearing houses).
- ▶ The JSE as frontline regulator **reports to the FSCA** as the lead regulator.
- ▶ JSE is rated as one of the World's best rated Stock Exchanges¹.

¹ World Economic Forum's Global Competitiveness Survey

JSE's IFRS compliance review mechanism

Objective of Proactive monitoring¹

- ▶ Objective is to consider the integrity of financial information and contribute toward production of quality financial reporting.
- ▶ Process causes healthy debate between the JSE and issuers.
- ▶ Publishes an annual report with an overview of activities and important findings
 - ▶ Issuers and audit committees required to consider the content
- ▶ Annexure includes advice from the Financial Reporting Investigation Panel (“FRIP”).
 - ▶ The FRIP is an advisory body, providing advice on cases of possible non-compliance.
 - ▶ Some FRIP matters arise from investigations.

¹ Note: I am an advisor to the JSE proactive monitoring staff, and a member of the FRIP

JSE's IFRS compliance review process

Selection

1. Selection approach **considers risk** to investors in terms of market concentration.
2. **Process is random** but with a **focus on issuers** (equity and debt:
 1. with a larger market capitalization and/or
 2. Level of activity in both the equity and interest rate markets
3. Review cycles are 'once within a set window' (either a 3, 5, 8 or 10-year), depending upon the size of the issuer.
4. Eg issuer within the top 40 index will now be selected at least once in the period 2021 to 2023 and then again once somewhere in the period 2024 to 2026.

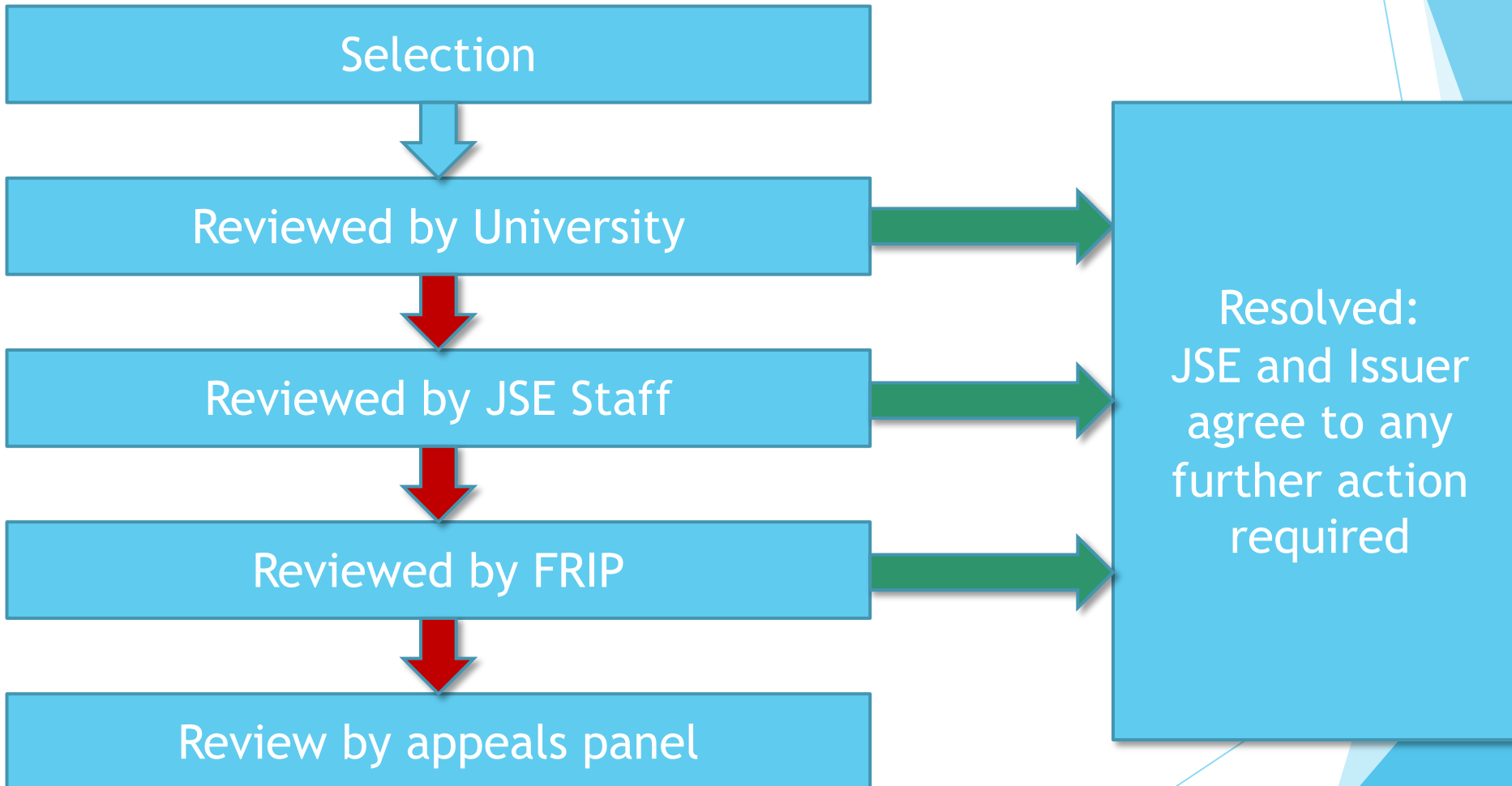
JSE's IFRS compliance review process

University review

- ▶ The JSE has an agreement with a leading South African University
- ▶ In terms of the agreement:
 - ▶ Once selected, a set of financial statements are reviewed by a pair of post graduate university students
 - ▶ The students are supervised by a senior lecturer
 - ▶ The students follow a prescribed format for the review and the subsequent report
 - ▶ The review forms part of the class work
- ▶ The agreement allows the JSE to leverage its own resources and
- ▶ The university to provide students with real life exposure

JSE's IFRS compliance review process

Selection



JSE's IFRS compliance review mechanism

Format of the annual reports

- ▶ Two reports are prepared
 - ▶ Proactive monitoring in the current year, and
 - ▶ Combined findings for life to date
- ▶ For the latter, findings
 - ▶ are grouped under a specific topic or IFRS.
 - ▶ from previous reports are included, ordered from most recent matter to oldest. If an older matter is identical, the newest latter is omitted
 - ▶ are distinguished between 'focus areas' and 'common disclosure omissions'
- ▶ FRIP cases are separately identified in the body of the report

JSE's IFRS compliance review mechanism

Findings of the report (2022)

- ▶ 50 financial statements (2021: 62) were reviewed during the year
- ▶ No cases (2021: 2) resulted in restatement of AFS and public announcements being made.
- ▶ 1 case (2021: 6) where non-compliance was material but not price sensitive. As such, matters corrected in the issuers' next results announcement.
- ▶ 14 cases (2021: 20), no material misstatement but amendments needed to be made within the next published results to avoid potential investor prejudice.
- ▶ 21 cases (2021: 24) involved smaller disclosure issues that the issuer agreed to clarify or correct in the future.

JSE's IFRS compliance review mechanism

Findings of the report (2022 focus areas)

- ▶ Geography of the income statement - problems with:
 - ▶ Use of sub-totals
 - ▶ Consistency in the treatment of associates
 - ▶ Presentation by nature versus by function
- ▶ Effect of covid and social unrest - problems with
 - ▶ Discussions in management reports, and
 - ▶ Poor disclosures, especially of changes in risks

JSE's IFRS compliance review mechanism

Findings of the report (common disclosures)

- ▶ IAS 12 Income Tax (detailed tax rate reconciliations, disclosures to support the recognition of deferred tax assets)
- ▶ IAS 24 Related Party Disclosures (full disclosure for all related party transactions and balances)
- ▶ IAS 36 Impairment of Assets (information regarding impairment calculations)
- ▶ IAS 7 Statement of Cash Flows (misapplication of this statement-most commonly in the classification of cash/cash equivalents and restricted cash)
- ▶ Covid 19 disclosures more generally, and going concern more specifically

JSE's IFRS compliance review mechanism

Findings of the report (by issuer type)

Coverage	2022 Equity	2022 Debt	2019 Equity	2019 Debt
AFS needed restatement	-	-	6	-
Correction in next AFS	1	-	6	-
Prospective change required	11	3	21	1
Smaller disclosure issues	15	6	13	8
No issues identified	10	4	30	2
Total cases closed	37	13	60	11

JSE's IFRS compliance review mechanism

Actions available

- ▶ Reports do not name transgressors
- ▶ JSE can:
 - ▶ require **restatement and/or issuance** of financial statements, together with a public announcement
 - ▶ require **prospective changes** in future financial statements
 - ▶ make **referrals for criminal prosecution**
 - ▶ make **referrals to lead regulators**
- ▶ JSE can update **listing requirements**
- ▶ JSE can also **suspend or disqualify** company from the exchange.

JSE's IFRS compliance review mechanism

Future reviews

- ▶ The JSE announces the targets of future review cycles
 - ▶ Review of previous findings (noting that audit committees confirm they are aware of these findings in annual certification)
- ▶ 2021 focus areas:
 - ▶ New standards (including IFRS 16, leases)
 - ▶ Application of standards to Covid 19 effects and implications (particularly roll forward from 2020)

South Africa: Security regulator's IFRS compliance review mechanism

Mechanisms and tools for resolving IFRS technical issues

IASBs support for consistent application

Overview

1

Support for consistent application
Overview

2

Support for new Standards

3

Work of the IFRS Interpretations Committee

How the IASB supports consistent application

Objective in supporting the Standards

IASB...

helps stakeholders obtain a **common understanding** of the requirements - ie what they are aiming for

In order to...

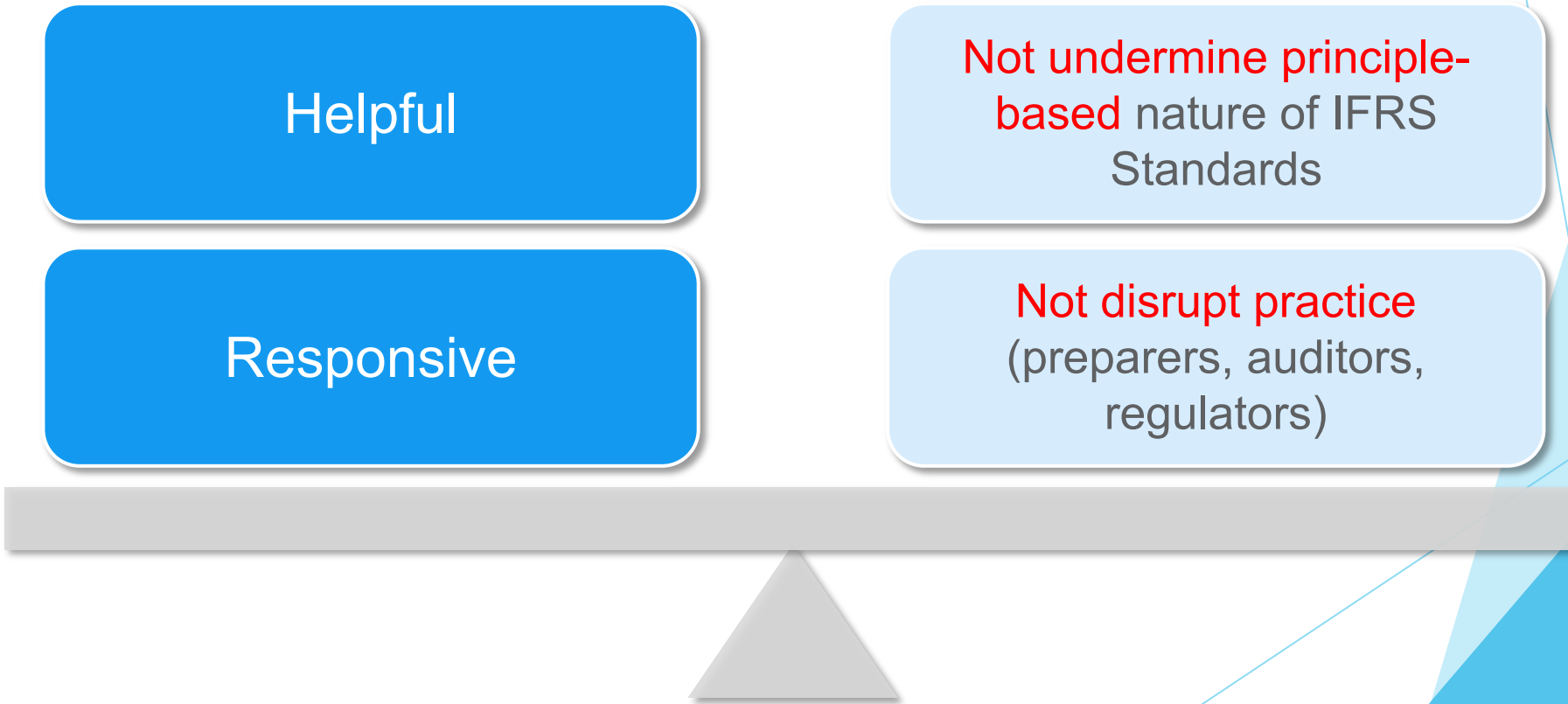
support **consistent application** of IFRS Standards

Because it...

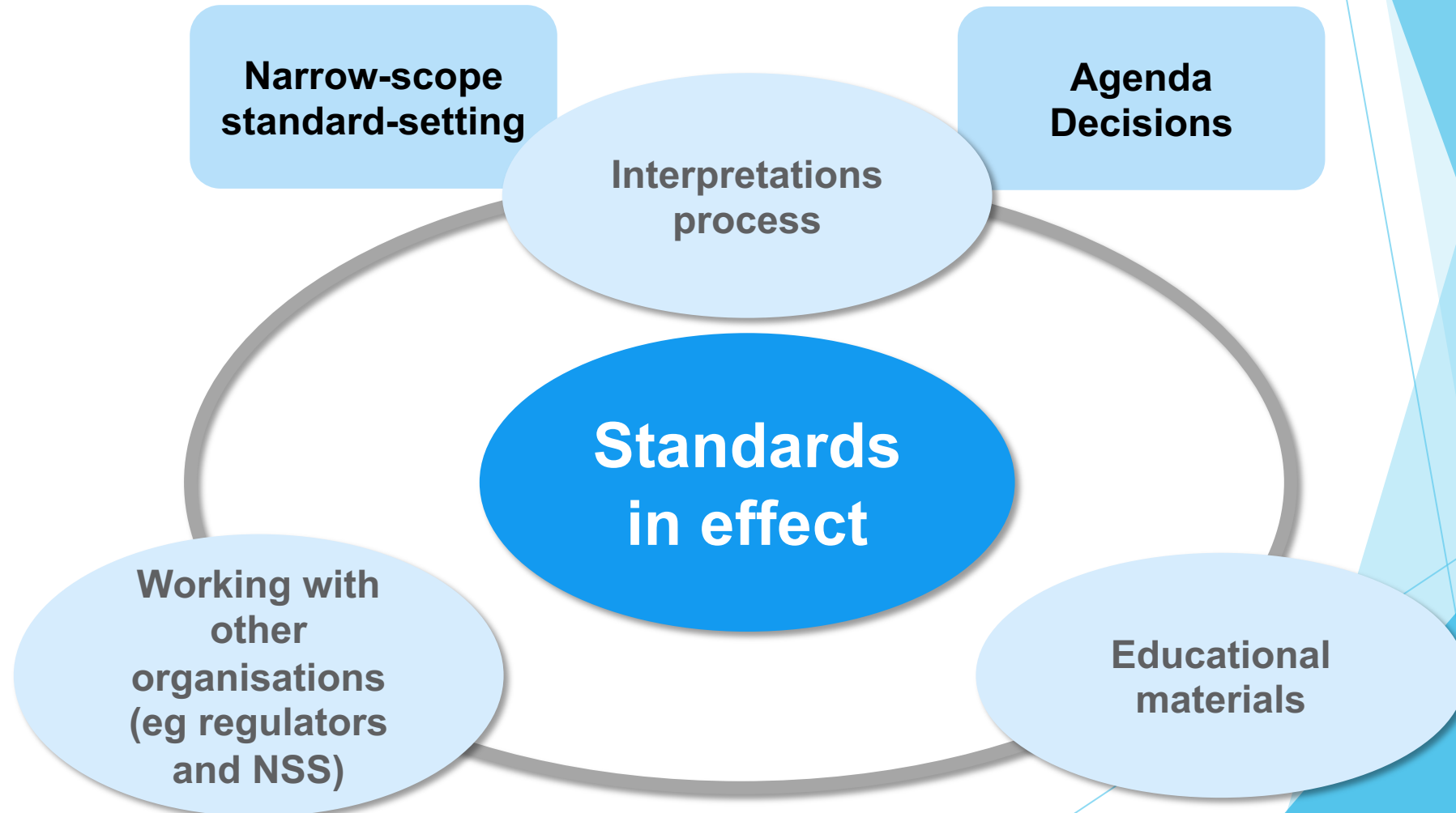
protects IFRS Standards as a single set of **global Standards** for the benefit of users of financial statements

The challenge

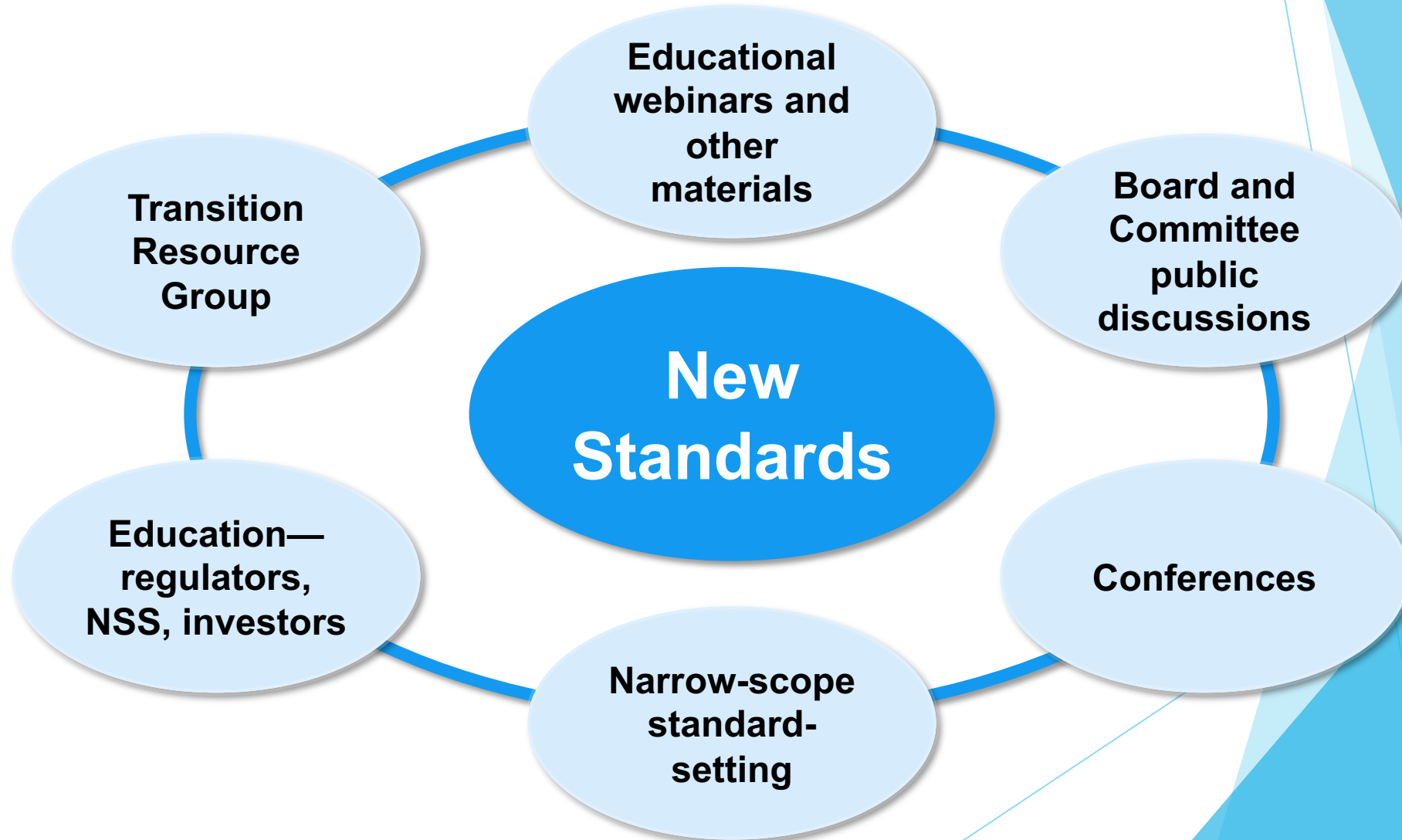
- In supporting consistent application of the Standards, the challenge is to balance:



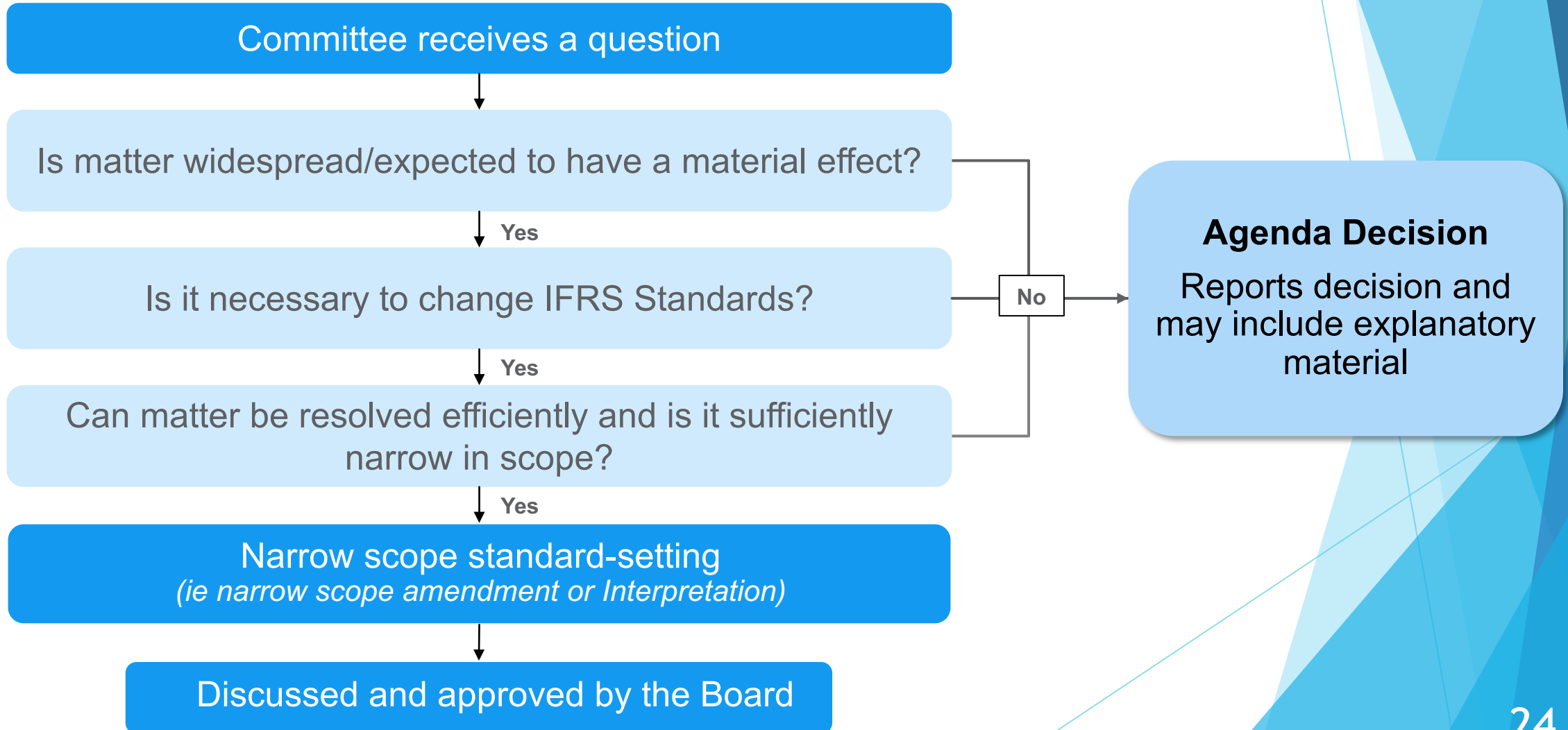
Support for Standards in effect



Support for new Standards



The Interpretations Committee's process



Due Process Handbook & agenda decisions



Revised *Due Process Handbook* published in August 2020

The explanatory material in agenda decisions

- cannot add or change requirements in IFRS Standards
- derives its authority from IFRS Standards
- may provide additional insights that might change a company's understanding of how to apply IFRS Standards

IASB now formally involved in finalisation

A company is entitled to sufficient time to determine and implement any necessary accounting policy change as a result of an agenda decision



If an accounting practice not aligned with agenda decision, it's not IFRS

Discussion