

CLARITY

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SPRING

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CYBER SECURITY – IS YOUR BUSINESS IN THE DARK?

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WELCOME TO THE SPRING EDITION OF CLARITY



Welcome to our Spring 2018 edition of Clarity. Our aim is to deliver greater clarity and understanding to our clients on the current and emerging accounting and audit issues. We also look to provide thought leadership, and share our knowledge and expertise, in areas that will solve problems and create solutions for clients. We hope you find this edition of value and please feel free to contact your local Audit Partners for any further assistance.



Josh Gambrell
IT Manager
PKF Sydney & Newcastle
jgambrell@pkf.com.au



“ The unfortunate reality is that in a world where businesses and people are constantly connected and online through computers and mobile devices, there are greater risks arising and opportunities for the hackers.

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CYBER SECURITY – ARE YOU IN THE DARK?

How much would it cost your business if one of your direct competitors could see exactly how much you were charging customers, or if they had full access to your research and development projects? What about if they could browse through your latest financial information, grab a list of every customer you have had interactions with and their contact details? What if those details were then made public on the internet for everyone to view? How much business would your company lose through reputation damage, being undercut by competitors and losing suppliers?

We have seen many examples of actual and suspected breaches recently which have hit the media.

The Government has recently made significant steps to mitigate the risk by introducing the mandatory data breach legislation, which requires companies to disclose when any data is lost to the affected customers and the privacy commissioner. It has been demonstrated that companies who are on the front foot and address data breach issues when they occur in a timely manner, significantly better than companies who ignore or cover them up, so the legislation is a step in the right direction.

The unfortunate reality is that in a world where businesses and people are constantly connected and online through computers and mobile devices, there are greater risks arising and opportunities for the hackers. So, what can your business do to mitigate the risks and opportunities?

The first line of defence is the ‘people’ – this may seem like a backwards approach to what seems like a technical problem, however, in the real-world social engineering in its various forms is significantly easier than most of the real ‘hacking’ techniques. Why go to all the trouble of digging through great tomes of IP addresses, ports and vulnerabilities, trying to find some way in, when you can just call and pretend to be from the IT team, or one of your suppliers, and obtain the password? Making your people security conscious and aware of what to watch out for and letting them know who to talk to if they have a concern can massively reduce the risk to the organisation. Other things like educating users about password reuse and how to identify scam or spam emails will also help.

The second line of defence relates to the ‘technical’ aspects - this still includes people components, including ensuring you have the right team in place (including outsourcing arrangements), sufficient budget and appropriate processes to escalate issues and concerns directly to the business owners if required. These need to be challenged constantly and PKF has provided independent IT technology and security audits which have been proved to be very beneficial in this regard.

Have you also considered the networks of your suppliers, and in turn their suppliers? Asking questions of your suppliers about the state of their IT systems might not seem like a very interesting conversation but remember anything you share with them has the potential to become public information. Asking a few questions, or encouraging them to undergo an IT audit, could turn out to be a cheap insurance.

Other technical aspects to consider could include:

- Ensuring there are appropriate firewalls
- Encryption of hardware
- Ongoing security updates being undertaken
- Secure Wi-Fi and network access
- Appropriate Business Continuity Plan and Disaster Recovery Plan
- Physical security of IT assets e.g. server

Cyber security is something which has traditionally been left to IT specialists. However, the risk has become so heightened that it needs to be owned and mitigated throughout your organisation, from business owners, executive management and employees at all levels.

Please contact your local PKF office for advice around your IT security needs. ■

WHY WHISTLEBLOWING SHOULD BE ENCOURAGED IN THE WORKPLACE

Whistleblowers have been found to be one of the most likely means of detecting fraud and corruption, according to the findings of the Association of Certified Fraud Examiners (ACFE) in its *Report to the Nations, 2018*.

It is also apparent from the ACFE Report that a significant number of those who reported misconduct did not want their identities known. Whistleblowers often have a fear of being identified or retaliated against for making a disclosure. There have been many examples of whistleblowers in both Australia and overseas, who have paid a heavy price both personally and professionally, in acting ethically and reporting inappropriate behaviours. This issue is further compounded when employees don't have confidence in the whistleblower framework inside the organisation that they work within.

Here in Australia, a current piece of research being led by Griffith University, called, *Whistling While You Work Part 2* is currently analysing how management responds to whistleblowing across both the public and private sectors. The early survey results from that research indicate that most people inside Australian organisations understand how valuable whistleblowers are to uncovering wrongdoing. However, the survey results thus far also indicate that there is a distinct lack of confidence that an organisation will handle a whistleblower complaint appropriately. In PKF's experience, this lack of trust, unfortunately, leads to a culture of underreporting inside the Australian workplace.

In our Summer 2018 edition of Clarity, Martin Matthews in his [article](#) explained the *New Legislation: Treasury Laws Amendment (Whistleblowers) Bill 2017* which is likely to be introduced later this year, in recognition of the shortcomings.

Notwithstanding these new reforms, organisations and agencies should carefully consider how they implement a practical and effective reporting framework. The key wording in the legislation in relation to the required whistleblower policy ensures 'fair treatment' of a company's employees. There are a number of components necessary to make this a reality, but a critical mechanism is one which will allow whistleblowers to make disclosures confidently

and without fear of reprisal.

One of the mechanisms to do this effectively is through an independent whistleblower hotline, which provides employees with the confidence to escalate suspected incidents of fraud, corruption and misconduct without the fear of recognition, retribution or reprisal.

The employees within an organisation or agency assigned with the responsibility of receiving and/or assessing disclosures received from whistleblowers should also be adequately trained to ensure effective management of such matters. Many organisations and agencies, however, elect to use an outsourced Whistleblower Hotline service as they are independent, often are a fully resourced 24/7 service and staffed by experienced investigation professionals who not only provide the right level of support to whistleblowers but are also able to ensure the right questions are being asked and the appropriate evidence is secured. Organisations need to then also ensure that their internal reporting lines have rigour, different avenues and a degree of independence. When your whistleblower is about to shed light on corrupt behaviour of a senior executive/manager, there are only a limited number of people who can probably help. A Whistleblower Hotline provides a discreet method for the whistleblower to seek assistance which can ensure your business maintains its integrity and reputation.

PKF Integrity is conducting a roadshow across Australia, where it will present on the many different facets of developing an effective reporting framework, how a whistleblower can be an asset to an organisation and how to ensure that wrongdoing is uncovered. PKF also provides an independent Whistleblower Hotline run by a team of expert investigators. For more information, visit our website where you can find the contact details of our representatives. ■

David Morgan
PKF Hacketts (Brisbane)
Managing Director of
PKF Integrity
david.morgan@pkf.com.au



“ A Whistleblower Hotline provides a discreet method for the whistleblower to seek assistance which can ensure your business maintains its integrity and reputation.

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Ken Weldin
Partner
PKF Melbourne
kweldin@pkf.com.au



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ASX INTERVIEW WITH JAMES GERRATY

With a renewed focus on good governance and the behaviours of our public companies and their leaders, we have heard a lot in recent months about the Australian Prudential Regulation Authority (APRA), Australian Securities and Investments Commission (ASIC), Royal Commissions and the views of shareholder advocacy groups. But what about the ASX? What role does it play?

The Australian Stock Exchange (ASX) is our country’s primary securities exchange and one of the world’s leading market exchanges. Through the ASX Corporate Governance Council’s Corporate Governance Principles and Recommendations, the benchmark in good governance practice for our listed companies is set.

We took the opportunity to catch up with James Gerraty, ASX Listings Manager to discuss the role of the ASX, how it operates and some of the trends and issues it is dealing with.

Q: To kick off James, please tell us what you do at ASX?

A: I joined ASX all the way back in 1995 having studied a Bachelor of Economics. The role has changed over the years but throughout most of that time I have been working with the listed companies in Melbourne and managing the team who provide all the services that listed entities would need from us.

These services include helping them with any of their disclosure issues, interpretation of the listing rules, capital raisings and IPOs.

Q: How different is the role today compared to what it was back in 1995?

A: I guess there are a number of signposts that reflect change through that time – the internet most obviously, and how that has seen information spread so much more quickly and leading to changes in how investors actually trade. What has been interesting is the continued strong role of technology in the things we have been doing at the exchange and the listings we’ve seen. This includes the so called ‘tech boom’ then ‘bust’ in the early 2000s when at times the fundamentals of the business models were not always clearly defined or understood. We’ve come a long way since those times, but it remains an issue today in some emerging technologies. A key part of our role today is scrutinising business models if they’re at that early stage – not to determine if the business will succeed, as that’s not our role – but to see that investors and we can make sufficient sense of it, that the risks are reasonably clear, and the capital raised is going to be sufficient.



In 2000 it was more the case that if you met the rules you were able to list. Today importantly, we have a discretion which we have been using, to decide who we won’t list and we are not shy in exercising that discretion if we think the business model does not make sense, it won’t be adequately capitalised to meet its objectives or there are other concerns, such as with the quality and track record of its directors and management.

Q: So that’s IPOs, but what other changes have occurred since then in relation to trading and ASX’s oversight role of all the listed stocks?

A: Well, again on the technology point, when I first started, everything a company might announce was delivered by way of fax or by hand (via bicycle courier – what do they all do now?!). Nowadays, of course, there is a significant increase in the speed with which information gets to the market and also the speed and volume of trading that happens. It’s increased the importance of the technology we use in our monitoring role.

We have very good systems to detect price movement in stocks allowing us to respond quickly. And any market information we do receive no longer has to wait until tomorrow morning’s newspaper to reach mum and dad investors.

Q: If something doesn’t look right with trading in a stock what are your responses?

A: One of our most important responsibilities is to take action if we think the market is not informed. We have an obligation under our licence to make sure the market is fair and transparent. From that, we have to take action if the market shows key changes which cannot be immediately explained.

Ultimately it is overlaid with human judgement. We need to determine whether it needs to be monitored for further movement, if there is further movement, we can let the relevant people know about it. That goes through the process of talking to the company and more than likely a price query.

In simple terms, this means going to the company to ask what information they have that could explain the price change.

Q: Is that as simple as picking up the phone?

A: Initially yes, but if we cannot get in contact with the company and the share price has moved quite significantly, we have to assess whether we feel people are trading on an uninformed basis and if so we have to make a decision whether to suspend trading. That is not a regular occurrence but it has happened.

Q: You have used the “please explain” but how do you define ‘significant’?

A: Deciding what is ‘significant’ is really case-by-case and factors in a number of things such as past trading history, volatility in the sector and whether trading volume is also increased, but if we think it is significant we may consider that a formal query is required. The market then gets to see ASX’s written questions and the company’s written responses.

Q: How do you find your phone calls are received? Does it ever get antagonistic? Or, is the company usually expecting you to call?

A: It varies, if someone thinks their price move is not remarkable, they might find it a distraction to deal with the query. Generally, however, they will understand there is a market that has to know about what has happened to the share price.

It gets difficult when a piece of information the company has is material, but is incomplete or confidential and therefore not ready for disclosure.

Q: How much of your working day is spent monitoring or watching for changes as opposed to dealing with something you know has happened?

A: We have a team in Sydney that watches those prices for us and give us information periodically through the day. With this task centralised it allows us to do our day to day work, receiving queries from our listed clients and their advisers, having conversations about interpretations or waivers of listing rules or reviewing draft documents and proposals.

Q: Do you think that is a well understood service offering that ASX is there to help with queries and provide clarification?

A: I think so. It should be anyway. We had this in mind when we rewrote ASX Guidance Note 8 on continuous disclosure. We put a lot more detail into it which shows people what information they need to consider when deciding if they should make disclosure. They can always ask their lawyer which often is necessary and appropriate, but you don’t necessarily need to. For things that are less about interpreting the law, they can ask us.

Q: What other trends are you noticing, perhaps around the new accounting standards on revenue or leases?

A: Not much to do with accounting standards per se, but when it comes to IPO planning, we are talking more to accountants and advisers these days than we ever have. One of the key reasons for that is that at the end of 2016 we changed the rules so there is a requirement that if you come in under the asset tests admission, you still need two years of audited accounts. This raises questions around audit work of prior periods, which can be expensive, and what they must do to meet these rules.

Q: And forecasts in a prospectus?

A: Forecasts in prospectuses are not something we are particularly concerned about. We are more concerned about continuous disclosure obligations after the date of listing in terms of tracking with those forecasts.

Q: What are your views on the current state of the accounting profession?

A: Like everything, it varies. The best auditors and the best accountants are those who can explain complicated accounting matters in plain English, that a non-accountant can make sense of.

Q: Moving to the current debate around the 4th Edition of the ASX’s Corporate Governance Council’s Principles and Recommendations?

A: In simple terms, our role is to ensure there is annual disclosure in corporate governance

statements. And it is clear. There is a little confusion, or an attitude may be a better way of putting it, amongst some investor groups that the larger companies ought not have any “if not, why not” disclosures and should comply in full with everything. That is not how it is meant to work.

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Q: What does your team consider when looking at governance statements and Appendix 4Gs?

A: The general quality and completeness for all reporters, with our particular focus that the larger companies are complying with the listing rules as set out in the Principles dealing with Audit and Remuneration Committees including appropriate composition.

Q: To what extent would you agree or sympathise that the disclosures have become more boilerplate?

A: It may be the case for some smaller entities where a formulaic approach to disclosure is taken, but overall, I would say there is less boiler plate nowadays.

Q: What is ASX’s message to the audit community as a governance intermediary?

A: I think the financial system relies on all the players doing their roles to a very high standard. Auditors have a hugely important role. It is interesting as new business and new technologies grapple with questions around the interpretation of accounting standards.

One wish is plainer English from accountants and less of those double negatives auditors seem to like.

Q: What is your favourite governance principle?

A: *Laughs* It’s got to be the risk one. Principle 7.

Q: Any final comments?

A: Do approach us with any questions you might have. We are here to help. ■



Steven Russo
Partner
PKF Adelaide
steven.russo@pkfsa.com.au



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AASB 15 REVENUE – TIME TO ACT IS (ALMOST!) OVER

Reporting entities that are producing general purpose financial statements should now be adopting the requirements of AASB 15 Revenue from Contracts with Customers as it applies for financial years commencing 1 January 2017 (i.e. 31 December 2018 and 30 June 2019 financial statements).

Grant Chatham, a Partner in the PKF Gold Coast practice covered this effectively in the [Spring 2017](#) edition of Clarity.

Recently, there was a timely reminder of the significance that AASB 15 can have over the former AASB 118 Revenue accounting standard with media comment on Big Un which was suspended from its ASX listing some six months ago following significant adverse media comment on its business structure and operations.

[Big Un has now released financial statements](#) for the six months ended 31 December 2017 and has adopted AASB 15 early. It blames the adoption of AASB 15 as the reason why its cash flows have deteriorated with the particular statistic that its positive operating cash flow of \$4.2 million under AASB 118 is actually a negative operating cash flow of \$8.6 million.

Interestingly, unlike some other companies that (after some Australian Securities & Investments Commission (ASIC) questioning) have early adopted AASB 15, Big Un’s explanation for the difference between the two accounting standards is all about the definition of a customer as its major sponsor can no longer be claimed as a customer. Big Un also confessed to five other accounting errors, including its definition of cash.

Grant Chatham’s Clarity article mentioned the requirement in AASB 15 of determining whether a contract exists with your customers, although the focus from the International Accounting Standards Board (IASB) that issued IFRS 15 which has been re-badged by the Australian Accounting Standards Board (AASB) as AASB 15, was the need for a performance obligation to be met. Specific examples where the old AASB 118 differed from AASB 15 included Upfront fees, Performance Fees, Awards and penalties, and Variations of contracts.



ASIC has also been critical of companies’ loose accounting under the former AASB 118 and this has led to a number of companies early adopting the more precise requirements of AASB 15 following ASIC review. Particular examples are: [Academies Australia reducing revenue relating to the provision of tuition income over the period that the tuition is provided rather than upon enrolment](#); and [Genworth Mortgage Insurance Australia changing its recognition of premium revenue, having regard to the pattern of historical claims](#).

ASIC has also been critical of companies’ loose accounting under the former AASB 118 and this has led to a number of companies early adopting the more precise requirements of AASB 15 following ASIC review.

Whilst ASIC has generally only taken action via media releases to date on accounting standards, the mood following the on-going Royal Commission into misconduct in the Banking, Superannuation and Financial Services Industry, suggests that ASIC may be prepared to take punitive legal action where there is non-compliance with the law and that includes accounting standards.

It is definitely worth having a chat with your local PKF audit team on how your AASB 15 implementation is working. ■

AASB 16 LEASES – ASSESS THE FINANCIAL IMPACT NOW



George Diamond
Partner
PKF Canberra
george@pkfcanberra.com.au

Is the new Leasing Accounting Standard AASB 16 just changing accounting numbers or will disclosure of the financial impact which is imminent, change the way business operates?

While AASB 16 Leases which requires Operating Leases to be put on the balance sheet, does not apply to financial statements for reporting entities until 31 December 2019 and 30 June 2020 balances dates, the market has for some time been estimating what the impact of AASB 16 will have on various companies and industries.

<https://www.smh.com.au/business/retailers-face-multibilliondollar-hit-from-proposed-lease-accounting-changes-20150422-1mqjx9.html>

Additionally, whilst there has to date been little disclosure by companies of the likely impact of AASB 16, December balancers are on notice that if they have not made disclosures to date, they will need to disclose the impact in their 31 December 2018 financial statements and June balancers in their June 2019 financial statements according to the Australian Securities & Investments Commission (ASIC). The only exception is for those companies that prepare reduced disclosure requirements financial statements.

<https://asic.gov.au/about-asic/media-centre/find-a-media-release/2018-releases/18-159mr-major-changes-affecting-reported-net-assets-and-profit-and-other-focuses-for-30-june-2018-reporting/>

The initial market analysis suggests that the way Leases are currently structured, may drastically change, given the impact on key metrics such as increasing Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA), but reducing pre-tax profit, and a significant blow out in net debt and gearing ratios that it is argued will lead to additional complexity when discussing borrowings and debt covenants with bankers and other funding providers, including shareholders.

[The Australian Financial Review 5 September 2018](#) quotes Macquarie Equities as estimating that Myer's net debt would



rise from \$66 million to \$2 billion with net debt /EBITDA leverage rising from 0.4 to 5.3. Similar changes are estimated for Woolworths with net debt rising from \$3.8 billion to \$5.8 billion with net debt /EBITDA leverage rising from 0.4 to 2.8.

Back in [April 2015, Morgan Stanley](#) stated that adoption of the new leasing accounting standard would “will boost earnings before interest, tax, depreciation and amortisation but will reduce pre-tax and net profits, as the amortisation and financing costs will exceed rental payments, especially for faster growing retailers with relatively new leases.” In particular, Morgan Stanley argued that “the impact on retailers will be considerable”, blowing out gearing levels and reducing return on capital employed, but will vary from retailer to retailer.”

[Clarity's Autumn 2017 edition](#), in particular, an article authored by Shaun Lindemann, Partner of PKF Hacketts (Brisbane), drew attention to the need to carefully consider the impact of AASB 16, including EBITDA, Net Debt/Gearing and remuneration and dividend policies.

As we get closer to the operative date of AASB 16, and only three months before disclosures of the impact of AASB 16 for December balancers, action becomes more imminent. It may be time to talk to your trusted PKF audit team. ■



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About PKF

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In Australia, PKF offers clients the expertise of more than 94 Partners and 750 staff, across audit, taxation and specialist advisory services.

PKF Australia's Audit & Assurance Contacts

PKF Sydney

Scott Tobutt
Partner
02 8346 6000
stobutt@pkf.com.au

PKF Canberra

Ross Dibartolo
Partner
02 6257 7500
ross@pkfcanberra.com.au

PKF Hacketts Brisbane

Liam Murphy
Partner
07 3839 9733
liam.murphy@pkf.com.au

PKF Newcastle

Martin Matthews
Partner
02 4962 2688
mmatthews@pkf.com.au

PKF Melbourne

Steven Bradby
Partner
03 9679 2222
sbradby@pkf.com.au

PKF Gold Coast

Grant Chatham
Partner
07 5553 1000
grant.chatham@pkf.com.au

PKF Perth

Simon Fermanis
Partner
08 9426 8999
sfermanis@pkfperth.com.au

PKF New England North West

Marg van Aanholt
Partner
02 6768 4500
mvanaanholt@pkf.com.au

PKF Adelaide

Steven Russo
Partner
08 8373 5588
steven.russo@pkfsa.com.au



Our values

- Passion
- Teamwork
- Clarity
- Quality
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