



**ASIC**

Australian Securities & Investments Commission

**REPORT 497**

# **Response to submissions on CP 267 Remaking ASIC class orders on audit and financial reporting**

September 2016

## **About this report**

This report highlights the key issues that arose out of the submissions received on [Consultation Paper 267](#) *Remaking ASIC class orders and guidance on audit and financial reporting requirements* (CP 267) and details our responses to those issues.

### About ASIC regulatory documents

In administering legislation ASIC issues the following types of regulatory documents.

**Consultation papers:** seek feedback from stakeholders on matters ASIC is considering, such as proposed relief or proposed regulatory guidance.

**Regulatory guides:** give guidance to regulated entities by:

- explaining when and how ASIC will exercise specific powers under legislation (primarily the Corporations Act)
- explaining how ASIC interprets the law
- describing the principles underlying ASIC's approach
- giving practical guidance (e.g. describing the steps of a process such as applying for a licence or giving practical examples of how regulated entities may decide to meet their obligations).

**Information sheets:** provide concise guidance on a specific process or compliance issue or an overview of detailed guidance.

**Reports:** describe ASIC compliance or relief activity or the results of a research project.

### Disclaimer

This report does not constitute legal advice. We encourage you to seek your own professional advice to find out how the Corporations Act and other applicable laws apply to you, as it is your responsibility to determine your obligations.

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## A Overview/Consultation process

- 1 In [Consultation Paper 267](#) *Remaking ASIC class orders and guidance on audit and financial reporting requirements* (CP 267) we consulted on our proposals to remake certain class orders that are due to sunset on various dates in 2016–17. The class orders generally relate to audit and financial reporting under Pt 2M.3 of the *Corporations Act 2001* (Corporations Act). In addition, we sought feedback on revisions to related guidance and pro formas.
- 2 Class Order [CO 98/1417] *Audit relief for proprietary companies* relieves a large proprietary company from the requirement to have its financial report audited. The relief is conditional on the company lodging its financial report with ASIC on time and demonstrating that it is well managed and in a sound financial condition. All directors and members must resolve annually to dispense with an audit.
- 3 Class Order [CO 98/1418] *Wholly-owned entities* relieves a wholly owned entity from preparing a financial report and having it audited. Relief is conditional upon the company entering into a deed of cross-guarantee with a holding entity and other wholly owned entities. The deed of cross-guarantee is required as protection for creditors of the company that will not have access to the company's financial report. It is a further condition that the directors of the holding entity state that there are reasonable grounds to believe that the parties to the deed will be able to meet any obligations or liabilities to which they are, or may become, subject.
- 4 Class Order [CO 01/1256] *Qualified accountant* specifies the members of a professional body that are approved to provide particular certifications under the Corporations Act.
- 5 Our view is that it is necessary to remake these class orders because they are operating effectively and efficiently, and continue to form a necessary and useful part of the legislative framework.
- 6 This report highlights the key issues that arose out of the submissions received on CP 267 and our responses to those issues. This report is not meant to be a comprehensive summary of all responses received. We have limited this report to the key issues.
- 7 We received five non-confidential submissions and one confidential submission on CP 267. We are grateful to respondents for taking the time to send us their comments. For a list of the non-confidential respondents to CP 267, see the appendix. Copies of those submissions are currently on the ASIC website at [www.asic.gov.au/cp](http://www.asic.gov.au/cp) under CP 267.

## B Remaking ASIC class orders

### Key points

This section outlines the key issues raised by respondents—and our responses to those issues.

### Class Order [CO 98/1417] *Audit relief for proprietary companies*

8 No key issues were brought to our attention.

### Class Order [CO 98/1418] *Wholly-owned entities*

9 For [CO 98/1418] we received feedback on:

- (a) inconsistencies in definitions;
- (b) timing requirements to meet conditions;
- (c) opt-out notices;
- (d) notices of disposal;
- (e) the impact on existing deeds of cross-guarantee;
- (f) companies that cease to be wholly owned; and
- (g) the obligations of holding entities.

#### Inconsistencies in definitions

10 One respondent pointed out that:

- (a) the definition of ‘Wholly-owned Entities’ in draft updated Pro Forma 24 *Deed of cross guarantee* (PF 24) differed from the definition in draft ASIC Corporations (Wholly-owned Companies) Instrument/XX; and
- (b) the definition of ‘ASIC Instrument’ in draft updated PF 24 differed from the definition in draft updated Pro Forma 27 *Assumption deed* (PF 27).

11 The different definitions of wholly owned entities have no impact on the operation of the instrument or PF 24. The definition in the draft instrument was modified to clarify which entities are included in the closed group and extended closed group for the purpose of presenting ‘consolidated financial statements’ and ‘additional consolidation information’ under paragraphs 6(1)(s)–(v) of the instrument.

*ASIC's response*

We have amended the definition of 'ASIC Instrument' to ensure consistency between PF 24 and PF 27.

### Timing requirements to meet conditions

- 12 One respondent identified that the timing of when certain conditions of relief had to be satisfied varied between periods that are before the end of the financial year, at or about the end of the financial year or from the end of the financial year until the reporting date.
- 13 In the respondent's view, the reporting date is a more appropriate deadline because it accords with the financial reporting process and directors are in a better position to determine whether the company needs to seek relief. For similar reasons, companies seeking relief for their 'first reliance year' should not be required to become party to a deed of cross-guarantee before the end of the relevant financial year, but would be required to do so before the reporting date.
- 14 Another respondent interpreted the conditions of relief to mean that an opt-in notice ([Form 389](#) *Opt-in/change of holding entity notice by wholly owned entity relieved from financial reporting obligations*) or opt-out notice ([Form 399](#) *Opt-out notice by wholly owned entity relieved from financial reporting obligations*) can only be lodged in the period of four months following the end of the relevant financial year or first non-reliance year respectively. The respondent suggested that a company should be able to lodge either notice at any time during the financial year.

*ASIC's response*

If proper accounting records are maintained, the directors should be able to determine whether a proprietary company will be large or small on a timely basis. In the event of doubt, directors can take steps to obtain relief. They need to weigh the benefits of relief against the costs incurred to satisfy the conditions of relief.

We consider the intent of the conditions in [CO 98/1418] was to require the opt-in or opt-out notice to be lodged no later than four months after the end of the relevant financial year or first non-reliance year. [ASIC Corporations \(Wholly-owned Companies\) Instrument 2016/785](#) has been drafted to clarify this intent.

### Opt-out notices

- 15 One respondent expressed concern at the consequence of failing to lodge an opt-out notice with us on a timely basis. The company will be unable to reapply the relief in future years.

- 16 An example cited was a company becoming a small proprietary company after previously being large and unintentionally failing to lodge an opt-out notice. The disqualification from reapplying the relief at a later time was seen to be significantly disproportionate to the failure to lodge. The respondent proposed that we allow a company to reapply the relief at a later time if it continued to be party to a deed of cross-guarantee until it lodged an opt-out notice.

*ASIC's response*

It is the responsibility of the company to comply with all of the conditions of relief. Potential users of a company's financial report need to be aware of the company's current and future reporting status.

We note that becoming a small proprietary company after being large does not, of itself, trigger the need to lodge an opt-out notice—the company is small and does not need to rely on the relief rather than intentionally not relying on the relief as contemplated by s7(1) of ASIC Corporations (Wholly-owned Companies) Instrument 2016/785.

### Notices of disposal

- 17 When a group entity is sold, there are obligations placed on both the group entity and its holding entity to lodge documents with us so that the group entity is released from its obligations under the deed of cross-guarantee.
- 18 One respondent proposed that the documents should only need to be lodged by either the group entity or the holding entity because, due to the change of control, either entity may overlook its obligations.

*ASIC's response*

The responsibilities of the group entity are not the responsibilities of the holding entity, and vice versa, after the parent/subsidiary relationship ends. The group entity needs to meet the requirements of ASIC Corporations (Wholly-owned Companies) Instrument 2016/785 to be relieved of its obligations under the deed of cross-guarantee.

### Impact on existing deeds of cross-guarantee

- 19 To minimise changes that companies may need to make as a result of us remaking [CO 98/1418], we have tried to preserve and grandfather pre-existing deeds of cross-guarantee.
- 20 However, companies cannot be joined to a pre-existing deed of cross-guarantee in its current form after ASIC Corporations (Wholly-owned Companies) Instrument 2016/785 becomes operative for financial years ending on or after 1 January 2017. Clause 5.1 of PF 24 only allows further

controlled entities to be joined to the pre-existing deed of cross-guarantee by execution of an assumption deed when those entities are eligible for the benefit of [CO 98/1418].

- 21 One respondent pointed out that entities will need to vary their pre-existing deeds to reflect the new PF 24 or enter into new deeds.

*ASIC's response*

A consequence of remaking [CO 98/1418] is that pre-existing deeds of cross-guarantee will need to be varied, or companies will need to execute new deeds, to facilitate joining further companies to a deed.

### **Companies that cease to be wholly owned**

- 22 If a company ceases to be a wholly owned entity after relying on the relief for a relevant financial year it must, unless certain exceptions apply, prepare a financial report and directors' report for that financial year and lodge them with us. The documents must be prepared and lodged within two months of ceasing to be wholly owned.

- 23 One respondent questioned the relevance of preparing a financial report for a financial year where the company was wholly owned and party to a deed of cross-guarantee. The utility of that financial report to potential users may be reduced by the passage of time and events that precipitated the departure of the company from the closed group.

- 24 It was also pointed out that we can give the company written notice that it does not need to prepare and lodge those documents. However, there is no guidance on the circumstances in which such notice will be given.

*ASIC's response*

The intent of s7(3) of ASIC Corporations (Wholly-owned Companies) Instrument 2016/785 is to ensure that financial information is available on a timely basis to creditors and other users of the financial report who no longer have the protection afforded by a deed of cross-guarantee.

We will consider the circumstances in which we might issue a notice to a company when developing any guidance on the practical application of ASIC Corporations (Wholly-owned Companies) Instrument 2016/785.

### **Obligations of holding entities**

- 25 A condition of relief is that the holding entity prepares consolidated accounts together with notes for the relevant financial year. Certain financial information about the closed group and extended closed group must be disclosed in the notes.



- 26 The consolidated accounts must be lodged within four months after the end of the financial year if the holding entity is:
- (a) not a registered foreign company and not a reporting entity;
  - (b) not a registered foreign company and a grandfathered exempt proprietary company; or
  - (c) a registered foreign company.
- 27 One respondent had concerns that there is no lodgement requirement or deadline for a holding entity that is not of the type specified in paragraph 26.

*ASIC's response*

The holding entities specifically referred to in paragraph 26 would not otherwise lodge consolidated accounts with us or lodge them within four months after the end of the financial year. Other holding entities have an obligation to lodge consolidated financial statements with us within four months after the end of the financial year.

**Class Order [CO 01/1256] *Qualified accountant***

- 28 No key issues were brought to our attention.

## Appendix: List of non-confidential respondents

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- Ashurst
  - Governance Institute of Australia
  - Hardidge, Mr David
  - Herbert Smith Freehills
  - KPMG
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