

15 July 2016

Australian Securities and Investments Commission
GPO Box 9827
Sydney NSW 2001
Attention: Terence Kouts

Email: policy.submissions@asic.gov.au

Dear Mr Kouts

Submission on Consultation Paper 257: *Improving disclosure of historical financial information in prospectuses: Update to RG 228*

Ernst & Young welcomes the opportunity to offer its views on ASIC's Consultation Paper 257: *Improving disclosure of historical financial information in prospectuses: Update to RG 228* released in May 2016 ("CP257").

On the whole, we support the proposed amendments that ASIC plans to make to Section F of Regulatory Guide 228 *Prospectuses: Effective disclosure for retail investors* ("RG228") which aims to improve the disclosure of historical financial information in prospectuses and assist companies and advisers to better understand their disclosure obligations. However, there are a number of key conceptual issues which we would like ASIC to consider prior to finalising the proposed amendments to RG228 which are outlined below. We have also responded to each of the proposals raised in CP257 in more detail in Appendix 1.

Historical Reporting Requirements

Requiring two-and-a-half or three years of financial information

ASIC has proposed that an issuer should disclose audited historical financial information for two-and-a-half or three years.

We are supportive of ASIC's proposal that two-and-a-half years is sufficient disclosure of historical financial information of the issuer where the most recent half year historical information is included as part of the disclosure of historical financial information in the offer document.

We note however that CP 257 is not clear with respect to the inclusion of the half year financial statements as to whether this period requires an audit or review by the assurance practitioner. It appears that ASIC may expect this to be audited in certain circumstances. We believe that the half year financial information should be reviewed as this is consistent to current ASX listing rules and market practice. We recommend that ASIC clarify this proposal in the guidance.

Interaction with ASX Consultation Paper: Updating ASX's admission requirements for listed entities

We would like to highlight that the ASX proposals requiring three full financial years audited historical financial information appear to be inconsistent with ASIC's CP257 which proposes to require issuers to include at least two-and-a-half or three years of audited historical financial information, regardless of whether the profits or assets test is applied. ASIC has not previously differentiated whether this requirement extends to both tests, whereas the ASX listing rules have.

We believe that the ASX proposals may act to inhibit certain issuers from listing on the ASX, such as early stage entities like start-ups, mining and oil and gas exploration entities, who may have limited historical financial information available but may have a viable prospective outlook.

The ASX consultation paper does not outline the circumstances in which two-and-a-half years of historical financial information would be appropriate and acceptable to ASX given it does not satisfy the ASX proposed admission requirement of three years. We recommend that ASIC link CP257 to the ASX admission requirements to provide greater clarity to the market on when less than three years historical financial information would be acceptable to ASIC prior to the proposed amendments to RG 228 becoming effective.

Requiring audited accounts for business acquisitions

ASIC has proposed that an issuer should disclose audited historical financial information for two-and-a-half or three years for both the issuer and business it acquires. This is regardless of whether the financial statements were required by law to be produced (apart from being in the prospectus) or whether the business is in a corporate form.

Whilst we agree with ASIC that these proposals are appropriate in a backdoor listing scenario, recent transactions in the market would indicate that there may be substantial practical difficulties for prospective issuers in obtaining historical financial information and having these subject to audit with respect to all of the acquisitions it may have undertaken within the historical track record period. We are aware that in practice both the ASIC and ASX have exercised discretion for alternative approaches to be adopted.

Consequently, we are not supportive of this proposal in its current form. In our view, it does not take into account the following:

- The increased cost and timeliness of obtaining two-and-a-half or three full financial years of historical financial information and the associated costs of the audit of such financial information;
- The profile of the acquired businesses may significantly change after the acquisition and subsequent listing of the issuer which will result in limited relevance of the historical financial performance of business acquisitions to potential investors, especially in earlier years;
- The quantity and quality of historical financial information required is not mindful of the significance of the business acquisition to the potential issuer, including the fact that the volume of historical financial information which will be required to be attached to offering document is highly dependent on the number of business acquisitions the potential issuer has undertaken or will undertake during the track record period; and
- The proposed requirement appears to be in excess of what is expected of an existing listed entity with respect to its financial statement disclosure requirements of such transactions.

We believe it would be more appropriate for this requirement for historical audited accounts to be based on materiality of the entity or business acquired/ to be acquired by the potential issuer. We recommend that ASIC give due consideration as to whether this proposal may be more effective on the basis of a materiality framework so that an acquisition of the business or entity can be assessed against how material it is to the entity being listed and consequently, the relevance of its historical financial information to potential investors.

Furthermore, whilst we understand that the ASIC may exercise discretion of the proposed guidance in light of the specific circumstances of an issuer, we believe it should provide appropriate application guidance for the framework under which it expects to exercise such discretion to provide greater transparency and clarity to the market.

Updating Financial Disclosure

Historical Financial Information

ASIC has proposed to clarify the guidance on when financial information is considered current in a prospectus on the basis of it including the most recent:

- (a) Half-year audited or reviewed financial statements (where the prospectus is lodged with ASIC less than three months after year end); or
- (b) Full-year audited financial statements (where the prospectus is lodged with ASIC less than 75 days after half-year end).

We note that under ASX Listing Rules Chapter 1.2.3(b)/1.3.5(a), separate half year financial statements are required if the last full financial year of the issuer ended more than eight months before the entity applied for admission. However under ASIC's proposal, as outlined in (a) above and in Case Study 10 in CP 257, this may lead to ASIC accepting an issuer having financial information which may, in fact, be up to nine months old. We believe that the current eight month rule provides more appropriate and up to date information for stakeholders to consider.

We recommend that ASIC determine whether the intended consequences of the above proposals is appropriate and clarify the timing of updating financial disclosure to align with current ASX requirements.

Post-Balance-Date Events

ASIC has proposed that where the business that is the subject of the fundraising has changed substantially that audited financial information be based on a more current balance date reflecting any unaudited post-balance-date material event disclosure.

We are not supportive of ASIC's proposals that an audit should be performed to a later balance sheet date if there are material post-balance-date events. In our view, ASIC's proposals are onerous and will not be widely understood in the market. We believe that where such material post-balance-date events occur, such events either require restated audited accounts to be prepared for a previous period or are taken into consideration as pro forma adjustments, negating the need for these to be separately reflected in audited historical financial information prepared to a later accounting period end date. The proposals also appear to be in excess of what is expected of an existing listed entity with respect to its financial statement disclosure requirements.

Areas Requiring Further Guidance

Whilst we are supportive of ASIC developing guidance with respect to the disclosure of historical financial information in offer documents, there are a number of areas, outlined below, where we also believe further principles-based guidance would be useful to companies and their advisers to better understand their disclosure obligations.

Pro Forma Adjustments

RG 230 *Disclosing non-IFRS financial information* ("RG 230") is currently the only guidance available in the market which is relevant to understanding the nature of pro forma adjustments. In our view, RG 230 is not sufficiently principles-based to provide an appropriate framework to determine what would constitute an acceptable or reasonable pro forma assumption or adjustment in an offer document.

As an illustration, one of the more common considerations in terms of a pro forma adjustment relates to purchase price allocation ("PPA") for business acquisitions. We find that entities widely differ in their approach and the level of detail described in the offer document with respect to the PPA adjustment depending on when an entity undertakes its detailed PPA review. A common practice for many entities is to not perform a detailed PPA allocation exercise prior to an acquisition and disclose this as an assumption to the pro forma financial information along with a preliminary indication of the potential impact on amortisation.

Another area of divergence is whether pro forma adjustments are appropriate to make with respect to business acquisitions which are a normal part of an issuer's business model such as when an issuer may have grown fast through business acquisitions throughout the historical track period, for example through a franchise-business model.

We strongly urge ASIC to formulate more principles-based guidance to ensure that there is an appropriate and consistent approach in the market with respect to pro forma adjustments.

Carve-out Financial Statements

Complexities may also arise when an entity needs to prepare and present carve-out financial statements to meet the historical financial requirements described in CP 257. The preparation of carve out financial statements are typically considered highly judgemental due to the lack of an appropriate, prescribed framework in Australia. Areas subject to judgement include the allocation of corporate and indirect costs which need to be estimated due to the separation of an entity from the group, including the consideration of appropriate adjustments required for transactions previously classified as related parties.

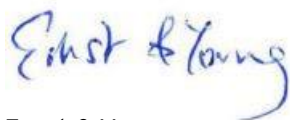
We recommend that ASIC formulate a principles-based framework for carve-out financial statements to further improve the quality and consistency of historical financial information disclosed in offer documents.

Forecast Financial Information

RG170 *Prospective Financial Information* has been extremely useful for practitioners and issuers in providing guidance on both undertaking work and disclosures required with respect to prospective financial information included in offer documents. Following on from this, further detailed principle based guidance would be useful to indicate what ASIC considers a hypothetical adjustment as opposed to a best estimate assumption where, often during an IPO process, a business is growing into new geographies, markets and products and there might be little or no previous audited history to support a growth assumption. We would support additional guidance on what constitutes reasonable grounds in this situation.

We welcome the opportunity to contribute to the clarification of regulatory settings on the quality and quality of historical financial information required by issuers. We would be pleased to discuss our comments with ASIC and its staff. Should you wish to do so, please contact Kathy Parsons (Kathy.Parsons@au.ey.com or on (02) 8295 6882).

Yours sincerely



Ernst & Young



Mike Wright
Oceania Assurance Managing Partner

Appendix 1: Responses to Proposals Raised by ASIC

Ref	ASIC Proposal	Response
B1	We propose to clarify that, subject to the circumstances described in proposals B11-B13, an issuer should disclose audited historical financial statements for two-and-a-half or three years for both the issuer and any business it acquires. This is regardless of whether the financial statements were required by law to be produced (apart from being in the prospectus) or whether the business is in a corporate form: see draft RG 228.88.	<ol style="list-style-type: none"> 1. Specific observations and recommendations with respect to the historical reporting requirements are outlined in our overall response letter. 2. ASIC should consider formulating more, specific guidance for certain types of entities, such as REITs which produce offer documents that can contain unique, market-based disclosures and may have limitations on available historical financial information due to complex business structures or significantly changed asset bases as a result of acquisition of assets or businesses or an entirely new fund being introduced. 3. Although we agree with the disclosure of historical financial information for a material acquisition as outlined in Case Study 4, we disagree with the treatment of the pro forma adjustment as we would consider that this acquisition would have been managed differently had it been part of the group for the entire historical period.
B2	We propose to clarify that where an audit or review opinion (for half-year financial information) included in a prospectus has a qualification or modification that indicates that the audit opinion provides limited independent assurance for investors, we are likely to treat the financial information as effectively unaudited. In the event we treat the information as unaudited, it is likely that we will view the prospectus as not complying with the s710 test: see draft RG 228.92.	We have no issues with this proposal.
B3	We propose to clarify that we will generally accept that audit reports including emphasis of matter paragraphs (e.g. due to uncertainty about whether the company can continue as a going concern in circumstances where a successful fundraising will enable the company to continue its operations) will not result in us regarding the financial information as unaudited: see draft RG 228.93.	This proposal is in line with our expectations and market practice.

Ref	ASIC Proposal	Response
B4	We propose to provide guidance recognising that there may be practical audit issues where up to three years of financial statements are being audited for the first time. In these circumstances, we propose to note that it is generally acceptable for the audit or review opinion to contain opening balance qualifications and, subject to materiality, issues related to inventory inspections: see draft RG 228.94.	This proposal is in line with our expectations and market practice.
B5	We propose to clarify that the audit or review of historical financial information included in the prospectus should be conducted, for businesses and entities in Australia, in compliance with Ch 2M and, for businesses and entities from foreign countries, in substantial equivalence to Ch 2M: see draft RG 228.91.	We have no issues with this proposal assuming that this is referring to the underlying financial statements rather than the financial information disclosed in the prospectus.
B6	We propose to clarify that if assets acquired by an issuer are in substance the acquisition of a business, the issuer should generally disclose historical income statements: see draft RG 228.95.	This proposal does not appear to align to the proposal at B1 which indicates that historical financial statements, not a historical income statement only, are required for two-and-a-half to three financial years in such instances.
B7	We will use the guidance in Appendix B of AASB 3 to assist us in determining whether an issuer has in fact acquired or is operating a business rather than an asset or a collection of assets: see draft RG 228.96.	We have no issues with this proposal.
B8	<p>We propose to clarify our guidance on when financial information is considered current in a prospectus. RG 228.89 already states that issuers should include current financial information in their prospectus.</p> <p>This extends to requiring the inclusion of half-year financial information. Where the existing business that is the subject of the fundraising has not changed substantially and has an acceptable audit history (as described in draft RG 228.91-RG 228.94), the financial information will generally be considered current if the prospectus includes the most recent:</p> <p>(a) half-year audited or reviewed financial statements (where the prospectus is lodged with ASIC less than three months after year end); or</p> <p>(b) full-year audited financial statements (where the prospectus is lodged with ASIC less than 75 days after half-year end).</p>	Specific observations and recommendations with respect to when financial information is considered current are outlined in our overall response letter.

Ref	ASIC Proposal	Response
B9	In some instances the business that is the subject of the fundraising may have changed so substantially that any unaudited post-balance-date material event disclosure would be of similar or greater significance for investors as the disclosure in the most recent audited or reviewed financial statements. We propose that in such cases the audited financial information included in the prospectus should have a more current balance date: see draft RG 228.90.	Specific observations and recommendations with respect to updating financial disclosure are outlined in our overall response letter.
B10	We propose to provide guidance that historical cash flow statements may need to be included in a prospectus where the financial history otherwise requires disclosure: see draft RG 228.87(b)(ii).	We are supportive of the proposal to include historical cash flow statements in the prospectus however, would note that where an issuer or acquired business has not been required to prepare these historically, this does create a practical time and expense onus on the issuer. We have observed in practice that generally where an issuer does not include a forecast cash flow then a historical cash flow statement has also not been included.
B11	We propose to provide guidance describing the circumstances where audited financial information for the past two-and-a-half or three years would include information not relevant to an informed assessment of the issuer's financial position, performance or prospects, or which would not be reasonable for investors and their professional advisers to expect. In such circumstances, the provision of either unaudited information, audited information with a modified audit opinion, or financial information of less than two-and-a-half or three years duration may be consistent with investors receiving sufficient information for the purposes of the s710 test. Issuers may therefore justify departure from the two-and-a-half or three year audited guideline in two broad sets of circumstances, outlined in proposals B12-B13: see draft RG 228.97.	We are supportive of the guidance provided under this proposal.
B12	We propose to provide guidance that historical financial information disclosure may not be necessary where two-and-a-half or three years of audited financial information, or some part of it, is not relevant: see Table 10 in draft RG 228 and Table 1 below for some examples where this may apply.	We have no issues with the examples provided in Table 1.

Ref	ASIC Proposal	Response
B13	We propose to clarify that the historical financial information disclosure may not be necessary if it is not reasonable for investors and their advisers to expect two-and-a-half or three years of audited financial information: see Table 10 at draft RG 228 and Table 2 below for some examples where this may apply.	We have no issues with the examples provided in Table 2.