### 7.2.16.2 Recognition of previously unrecognised deferred tax assets

At the date of transition, a first-time adopter that has elected not to restate past business combinations in accordance with IFRS 3 will need to determine whether any tax loss carryforwards or other deferred tax assets not recognised at the date of acquisition of subsidiaries meet the recognition criteria under IAS 12. If so, they should be recognised at the date of transition.

When a deferred tax asset is recognised on transition that was not previously recognised in a past business combination, the resulting adjustment will be made in retained earnings or another reserve used by the entity for its IFRS 1 adjustments. The carrying amount of goodwill should not be adjusted because the recognition of previously unrecognised deferred tax assets is not one of the permitted adjustments to goodwill specifically identified in IFRS 1:C4 (see **7.2.12.1**). (But this does not preclude the adjustment of goodwill if the date of transition falls during the 'measurement period', as discussed in **example 7.2.12.6**).

The realisation of previously unrecognised deferred tax assets after the date of transition is accounted for in accordance with the general requirements of IFRS 3 and IAS 12:68 (IFRS 1 does not allow any ongoing exemptions from these requirements). Therefore, when an entity that has not restated a past business combination subsequently realises an unrecognised deferred tax asset that did not satisfy the recognition criteria at the date of transition, the impact will typically be recognised in profit or loss, and not as an adjustment to goodwill. The only exception to this will be when acquired deferred tax benefits are recognised within the 'measurement period' (generally 12 months after the date of the acquisition) that result from new information about facts and circumstances that existed at the acquisition date. These will be adjusted against goodwill.

Although the adjustment of goodwill for acquired deferred tax benefits recognised within the measurement period is not one of the adjustments to goodwill permitted under IFRS 1:C4(g) (see **7.2.12.1**), it is consistent with the treatment adopted for other adjustments to 'provisional' values (see **7.2.12.6**).

**Example 7.2.16.2**

**Recognition of previously unrecognised deferred tax asset**

Entity B presents its first IFRS financial statements for the year ended 31 December 20X5 with a date of transition of 1 January 20X4. In preparing those financial statements, Entity B chooses not to restate business combinations prior to the date of transition in accordance with IFRS 3.

Entity B had previously acquired Entity C during 20X2 in a business combination in which CU300 of goodwill was recognised under previous GAAP, but CU500 of deferred tax assets arising from loss carryforwards were not recognised. The loss carryforwards expire on 31 December 20X6. Under Entity B's previous GAAP, goodwill amortisation was prohibited and the carrying amount of goodwill at the date of transition is CU300.

At the date of transition, Entity B assesses future profitability and determines that CU100 of the deferred tax benefit can be recovered by the end of 20X6. The following journal entry is recorded.

| | | CU | CU |
|---|---|---|---|
| Dr | Deferred tax asset | 100 | |
| Cr | Retained earnings | | 100 |

*Recognition of the deferred tax asset.*

During the year ended 31 December 20X6, Entity B's profitability is even higher than expected and, consequently, all of the tax loss carryforwards are utilised before they expire.

Entity B will account for the realisation of the deferred tax assets after the date of transition in accordance with IAS 12:68. Because the realisation occurs after the measurement period (i.e. more than 12 months after the date of the original acquisition of Entity C), it cannot be adjusted against goodwill.





### 7.2.16.3 Deferred tax asset relating to goodwill previously written off directly to equity

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A deferred tax asset may arise when goodwill has been written off directly to equity but attracts tax relief on an amortisation basis. Subject to the usual recoverability criteria, a deferred tax asset should be recognised, at the date of transition, based on the difference between the carrying amount (i.e. nil) and the tax base (i.e. the amount of future tax deductions). The adjustment is made against retained earnings (or another appropriate category of equity); the carrying amount of any other goodwill may not be adjusted because the recognition of previously unrecognised deferred tax assets is not one of the permitted adjustments to goodwill specifically identified in IFRS 1:C4.

**Example 7.2.16.3**

**Deferred tax asset relating to goodwill previously written off directly to equity**

Company D operates in a jurisdiction in which, under previous GAAP, goodwill was written off directly to equity immediately following a business combination. The local tax law allows a deduction of 1/20 of the purchased goodwill in each of the 20 years following an acquisition. Company D acquired a business two years before the date of transition to IFRSs, and all related goodwill was written off directly to equity at that time. At the date of transition, Company D is still entitled to claim 18/20 of the amount of purchased goodwill as a deduction over the next 18 years. Company D has elected not to restate past business combinations prior to the date of transition in accordance with IFRS 3.

In accordance with IAS 32, all or part of the amounts recognised for shares in the statement of financial position may be classified as liabilities. The above disclosure requirements apply irrespective of whether the shares are classified as equity or debt or a combination of the two (see also **4.5.2.1**).

It is unclear whether the requirement to disclose 'shares in the entity held by the entity or by its subsidiaries or associates' refers to the number of shares held or the amount of the deduction from equity in respect of such holdings. In the context of the other disclosures required by this paragraph of IAS 1, the text appears to refer to the number of shares. This would be appropriate for all of the types of holding referred to in IAS 1:79(a), including shares held by associates of the entity which are not deducted from equity as is required for shares held by the entity and its subsidiaries under paragraph 33 of IAS 32 *Financial Instruments: Presentation*.

However, IAS 32:34 states that "[t]he amount of treasury shares held is disclosed separately either in the statement of financial position or in the notes, in accordance with IAS 1". This text refers to the 'amount' of treasury shares rather than their number, but it appears to be a reminder of the disclosure requirement in IAS 1 rather than an additional requirement.

Because of the uncertainty regarding this disclosure requirement, it is recommended that both of the following be disclosed: (1) the number of shares held by the entity and by its subsidiaries and associates, and (2) when relevant, the amount of any deduction from equity in respect of treasury shares.

Some entities such as partnerships or trusts do not have share capital. In such cases, information equivalent to that described above for share capital should be disclosed, showing changes during the period in each category of equity interest and the rights, preferences and restrictions attaching to each category of equity interest. [IAS 1:80]

If an entity has reclassified:

- a puttable instrument classified as an equity instrument, or
- an instrument that imposes on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation and is classified as an equity instrument,

between financial liabilities and equity, the amount reclassified into and out of each category (financial liabilities or equity), and the timing and reason for that reclassification, should be disclosed. [IAS 1:80A]





The terms used in the two bullet points above have the meaning specified in IAS 32 (see **2.1.2** and **2.1.3** in **chapter B3** or, for entities that have not yet adopted IFRS 9, **2.1.2** and **2.1.3** in **chapter C3**).

#### *4.5.2.5 Disclosures about reserves*

Entities are required to provide a description of the nature and purpose of each reserve within equity, either in the statement of financial position or in the notes. [IAS 1:79(b)]

While IAS 1 requires financial statements to include additional information as to the nature and purpose of each reserve, it does not provide any further clarification regarding what information is needed.

By allowing this information to be disclosed in the statement of financial position, the IASB has indicated that the required information might be sufficiently disclosed by a precise wording of the name of the reserve. Thus, for reserves that are commonly encountered (revaluation reserves on property, plant and equipment, share premium account, translation reserves in respect of foreign operations etc.), no further explanation is necessary for investors to understand the nature and purpose of the reserves.

However, if, for example, the entity wishes to designate special reserves within equity that are not familiar to users of financial statements, supplementary information should be provided regarding the purpose of the reserve, and how it will be utilised.

## 5 Statement of profit or loss and other comprehensive income

### 5.1 General requirements regarding the presentation of profit or loss and other comprehensive income

#### *5.1.1 Option to present a single statement or two statements*

As discussed in **2.4.2**, an entity may either:

[IAS 1:10A]

- present a single statement of profit or loss and other comprehensive income, with profit or loss and other comprehensive income presented in two sections (a 'one-statement' approach); or
- present the profit or loss section in a separate statement of profit or loss (a 'two-statement' approach).

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the particular asset will be sold or the liability transferred and, consequently, in determining what price will be achieved if the sale or transfer occurs in that market at the measurement date.

For the purposes of measuring fair value, the transaction to sell the asset or transfer the liability is assumed to take place either:

[IFRS 13:16]

- in the 'principal market' for the asset or liability; or
- in the absence of a principal market, in the 'most advantageous market' for the asset or liability.

The principal market is defined as "[t]he market with the greatest volume and level of activity for the asset or liability". [IFRS 13:Appendix A]

The most advantageous market is defined as "[t]he market that maximises the amount that would be received to sell the asset or minimises the amount that would be paid to transfer the liability, after taking into account transaction costs and transport costs". [IFRS 13:Appendix A]

Note that, although transaction costs are not deducted (for an asset) or added (for a liability) when measuring fair value, they are considered when identifying the most advantageous market for an asset or a liability (see **3.5.3**).

The principal market should be identified on the basis of the volume or level of activity for the asset or liability rather than the volume or level of activity of the reporting entity's transactions in a particular market. [IFRS 13:BC52] Therefore, the assessment as to which of two or more accessible markets is the principal market is made from the perspective of market participants rather than the entity.

Equally, in the absence of a principal market, the most advantageous market is identified using the assumptions that market participants would use.

A principal market may not exist, for example, when the volume or level of activity for the asset or liability is the same in two different markets to which the entity has access, or when there is no observable market for the asset or liability. In such circumstances, an entity needs to identify the most advantageous market or develop assumptions from the perspective of a market participant in a hypothetical most advantageous market.

IFRS 13 does not require an entity to conduct an exhaustive search of all possible markets to identify the principal market (or, in the absence of a principal market, the most advantageous market), but an entity is required





to take into account all information that is reasonably available. In the absence of evidence to the contrary, the market in which an entity would normally enter into a transaction to sell the asset or to transfer the liability is presumed to be the principal (or most advantageous) market. [IFRS 13:17]

Therefore, an entity is permitted to use the price in the market in which it normally enters into transactions unless there is evidence that the principal market and that market are not the same. [IFRS 13:BC53]

If there is evidence that the market in which an entity would normally transact is not the principal (or most advantageous) market, the principal (or most advantageous) market should be identified by:

- firstly, identifying other markets to which the entity has access; and
- secondly, when relevant, assessing which of two or more accessible markets is the principal (or most advantageous) market.

If there is a principal market for the asset or liability, the fair value measurement should reflect the price in that market, even if the price in a different market is potentially more advantageous at the measurement date. [IFRS 13:18]

### 3.3.2 *Access to the market*

To use the price in the principal (or most advantageous) market as the basis for measuring fair value, an entity must have access to that market at the measurement date. Because different entities (and businesses within those entities) with different activities may have access to different markets, the principal (or most advantageous) market for the same asset or liability might be different for different entities (and businesses within those entities). Therefore, the principal (or most advantageous) market should be considered from the perspective of the entity, thereby allowing for differences between and among entities with different activities. [IFRS 13:19]

Example 7 of the illustrative examples accompanying IFRS 13 (summarised at **7.2**) illustrates a scenario in which two entities measure the same instrument differently because each identifies its principal market on the basis of the market to which it has access.

Although an entity must be able to access the market, the entity does not need to be able to sell the particular asset or transfer the particular liability on the measurement date to be able to measure fair value on the basis of the price in that market. [IFRS 13:20]

For example, as discussed in **example 3.2.2.2A**, an entity may be restricted from selling a particular asset at the measurement date. Nevertheless, if the entity has access to the principal market at that

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- **Step 2** Entity X adjusts the unobservable forward price points at Years 4 to 10 on the forward price curve such that the model produces a fair value of zero.

  Because Entity X attributed the inception difference solely to the unobservable electricity prices in the relevant market, any calibration adjustment represents a calibration of these unobservable electricity prices to the most recent available information (the forward contract's transaction price). As a result, if Entity X owns a portfolio of contracts whose fair values are estimated using long-dated electricity prices in the same market, the calibration adjustment to the electricity forward prices would most likely also affect the fair value of those other long-dated contracts.

  Similar considerations are also relevant when a calibration results in valuation adjustments to the pricing model's output. In general, calibration adjustments provide updated information about assumptions used by market participants in assessing unobservable inputs or valuation adjustments. Therefore, calibration adjustments may have an effect beyond the recently executed transaction.
- **Step 3** Assuming no other calibration adjustments are made and that observable forward prices remain available for the next three years, the calibration adjustments would be removed as the inputs for Years 4 to 10 become observable. (For example, at the end of Year 1 of the contract, observable forward prices would be available for Years 2 to 4, and unobservable inputs for Years 5 to 10 would be used. As a result, the calibration adjustments for Year 4 should be removed from the valuation as this input has become observable.) All calibration adjustments should be removed once all the unobservable inputs become observable (e.g. in the last 3 years of the contract). In addition, no calibration adjustments should remain in the model in a period in which settlement has occurred.

### 8.9 Changes in valuation techniques

Once a valuation technique has been selected, it should be applied consistently. A change in a valuation technique or its application (e.g. a change in its weighting when multiple valuation techniques are used or a change in an adjustment applied to a valuation technique) is only appropriate if the change results in a measurement that is equally or more representative of fair value in the circumstances. [IFRS 13:65]

The Standard provides the following examples of events that might appropriately lead to a change in valuation technique:

[IFRS 13:65]

- new markets develop;
- new information becomes available;
- information previously used is no longer available;
- valuation techniques improve; or
- market conditions change.





If a valuation technique does not use unadjusted quoted prices, and in a subsequent period a quoted price in an active market becomes available, the quoted price should be used because IFRS 13:77 states that "a quoted price in an active market provides the most reliable evidence of fair value and shall be used without adjustment to measure fair value whenever available", with limited exceptions.

Depending on the particular circumstances, a change from a valuation technique that uses unadjusted quoted prices to a different valuation technique (such as a discounted cash flow technique) may be appropriate when:

- quoted prices for an identical asset or liability are no longer available; or
- quoted prices are available, but the market is no longer active. Note, however, that prices from relevant observable transactions must be considered in determining fair value even if the market is not active (see 9.5); or
- the entity no longer has access to the market in which the prices are quoted. The entity must be able to access the market in order to use a quote from that market without adjustment to reflect the lack of access, but the entity does not need to be able to sell the particular asset or transfer the particular liability on the measurement date (see **section 3.3** for further details); or
- quoted prices are no longer based on relevant observable market data and do not reflect assumptions that market participants would make in pricing the asset at the measurement date. As discussed at **9.7**, an entity cannot necessarily assume that a price provided by an external source is representative of fair value at the measurement date.

A decrease in the volume or level of activity in a market does not necessarily mean that the market is no longer active (see **10.2.1.1** for a discussion of active vs. inactive markets) and, consequently, that a change in the valuation technique is warranted.

In selecting another valuation technique, when appropriate, an entity should maximise the use of relevant observable inputs (e.g. quoted prices for a similar asset or liability with adjustments as appropriate) and minimise the use of unobservable inputs.

If there is a change in the valuation technique used or its application, any resulting difference should be accounted for as a change in accounting estimate in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*; however, the disclosures generally required under IAS 8 regarding a change in accounting estimate are not required for revisions resulting from a change in a valuation technique or its application. [IFRS 13:66]

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estimate differs significantly from previous estimates of residual value, the effect is accounted for prospectively as a change in estimate, in accordance with the requirements of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. [IAS 16:51] Effectively, the depreciation recognised over the remaining useful life of the asset is adjusted to take account of the revised estimate of residual value.

If the revised estimate of residual value is equal to or greater than the asset's carrying amount, whether due to inflation or otherwise, then the asset's depreciation charge is zero unless and until its residual value subsequently decreases to an amount below the asset's carrying amount. [IAS 16:54]

The definition of residual value refers to the potential disposal value of the asset if it were already of the age and in the condition expected at the end of its useful life. The amount is therefore quite separate from the current fair value of the asset. If the fair value of the asset exceeds its carrying amount (generally because the entity has adopted the cost model for accounting for its property, plant and equipment), this does not remove the obligation to recognise depreciation. [IAS 16:52]

> Further, the definition focuses on the amount that could currently be obtained on disposal of the asset, rather than the amount that is expected to be obtained at the end of the asset's useful life. Therefore, expectations as to future increases or decreases in that disposal value are not taken into account. Thus, an increase in the expected residual value of an asset because of past events will affect the depreciable amount; expectations of future changes in residual value other than the effects of wear and tear will not. [IAS 16:BC29]

## 7.4 Estimates of useful lives

### 7.4.1 *Definition of useful life*

The useful life of an asset is defined as:

[IAS 16:6]

- the period over which an asset is expected to be available for use by an entity; or
- the number of production or similar units expected to be obtained from the asset by an entity.

### 7.4.2 *Commencement of depreciation*

Depreciation of an asset commences when it is available for use, i.e. when it is in the location and condition necessary for it to be capable of operating in the manner intended by management. [IAS 16:55] This is the same point in time at which the entity is required to cease capitalising costs within the carrying amount of the asset. (See **4.2.9** for guidance as to when this point in time occurs.)





### 7.4.3 *Cessation of depreciation*

Depreciation of an asset ceases at the earlier of:

[IAS 16:55]

- the date that the asset is classified as held for sale (or included in a disposal group that is classified as held for sale) in accordance with IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations* (see **9.1**); and
- the date that the asset is derecognised.

IFRS 5 requires that a non-current asset (or disposal group) be classified as held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use. [IFRS 5:6] For this to be the case, the asset (or disposal group) must be available for immediate sale in its present condition, and its sale must be 'highly probable' (see **chapter A20** for further guidance).

IAS 16 sets out requirements in respect of the derecognition of items of property, plant and equipment – see **section 9**.

Therefore, depreciation of an asset does not cease when an asset becomes idle or is retired from active use unless the asset is fully depreciated. If the depreciation is calculated by reference to the usage of the asset, however, the depreciation recognised may be zero while there is no production. [IAS 16:55] In any case, when an asset becomes idle, or is retired from active use, this may trigger the recognition of an impairment loss which will result in the reduction of the carrying amount of the asset to its estimated recoverable amount.

> **Example 7.4.3**
>
> **Depreciation of an asset retired from active use**
>
> Company Q uses specialised machinery to manufacture its products and is the only entity in its market that operates this type of machinery.
>
> Company Q plans to increase its production capacity by introducing new specialised machinery with improved technology. As a result, Company Q will discontinue using the specialised machinery currently in use. However, in order to protect its competitive advantage and deny other market participants access to the technology, Company Q will not sell the machinery currently in use, even though it is still in good working condition; instead, the machinery will be retired from active use and 'mothballed' by Company Q for potential further use or sale at a later date.
>
> At the date of retirement, the fair value less costs to sell of the specialised machinery exceeds its carrying amount.
>
> *Should Company Q continue to depreciate the machinery when it is retired from active use and, if so, over what period?*
>
> Company Q should continue to depreciate the depreciable amount of the machinery on a systematic basis over its estimated useful life. The useful life

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IAS 17 *Leases* applies to a disposal effected by entering into a finance lease and to a sale and leaseback (see **chapter A17**). [IAS 40:67]

The gain or loss on the retirement or disposal of an investment property is calculated as the difference between the net disposal proceeds and the carrying amount of the property and is recognised in profit or loss in the period of the retirement or disposal. This is subject to the requirements of IAS 17 in the case of a sale and leaseback transaction. [IAS 40:69]

The consideration receivable on the disposal of an investment property is recognised initially at fair value. In particular, if payment is deferred, the consideration is recognised initially at its cash price equivalent. The difference between this amount and the nominal amount is recognised as interest revenue under the effective interest method in accordance with IAS 18. [IAS 40:70]

There is no definition of 'cash price equivalent' in IAS 40. It is presumably intended to equate to the present value of the deferred payment but might also encompass a cash price offered by the vendor as an alternative to the deferred payment terms.

When any liabilities are retained relating to the property after its disposal, IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* or other relevant Standards are applied to those liabilities. [IAS 40:71]

## 8 Compensation for impairment of investment property

Impairments or losses of investment property, related claims for or payment of compensation from third parties and any subsequent purchase or construction of replacement assets are separate economic events and are accounted for separately. Therefore:

[IAS 40:73]

- impairments of investment property are recognised in accordance with IAS 36 *Impairment of Assets*;
- retirements or disposals of investment property are recognised as set out in **section 7** in accordance with IAS 40:66 to 71;
- compensation from third parties for investment property that was impaired, lost or given up is recognised in profit or loss when it becomes receivable; and
- the cost of assets restored, purchased or constructed as replacements is determined as set out in **section 4** in accordance with IAS 40:20 to 29.





**Example 8**

**Insurance claim**

A building carried as an investment property burns down during the reporting period. A valuation of the building in its damaged state is performed at the end of the reporting period.

*Should the value of the property at the end of the reporting period include any amount receivable from insurance?*

The amount receivable from insurance should be recognised separately in the statement of financial position if it meets the relevant recognition criteria. Any valuation of the property recognised as an investment property should not include the insurance receivable.

## 9 Presentation and disclosure

### 9.1 Presentation

IAS 1 *Presentation of Financial Statements* requires that, when material, the aggregate carrying amount of the entity's investment property should be presented in the statement of financial position. [IAS 1:54(b)]

### 9.2 Disclosure

#### *9.2.1 General disclosures*

The disclosures required by IAS 40 are made in addition to the disclosures required by IAS 17 *Leases* for leases entered into by lessees and lessors.

An entity is required to disclose:

[IAS 40:75]

- whether it applies the fair value or the cost model;
- whether, and in what circumstances, properties held under operating leases are classified as investment property when the fair value model is used;
- the criteria used to distinguish investment property from owner-occupied property or property held for sale in the normal course of business, when that classification is difficult;
- the extent to which the fair value of investment property (as measured or disclosed in the financial statements) is based on a valuation by an independent valuer who holds a recognised and relevant professional qualification and has recent experience in the location and category of



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[IAS 36:BC209M & N] Consequently, it appears that the previous segregation continues to apply between losses or reversals that are individually material (covered by IAS 36:130), and other losses or reversals that are material in aggregate (covered by IAS 36:131).

## 11.6 Unallocated goodwill

If any portion of the goodwill acquired in a business combination during the period has not been allocated to a CGU (group of CGUs) at the end of the reporting period (see **8.2.8.3**), the amount of the unallocated goodwill should be disclosed, together with the reasons why that amount remains unallocated. [IAS 36:133]

## 11.7 Cash-generating units containing goodwill or intangible assets with indefinite useful lives

### *11.7.1 Information to be disclosed for cash-generating units to which significant goodwill or indefinite-life intangible assets have been allocated*

The wording below reflects the amendments to IAS 36:134(c) in May 2013 (see also the discussion at **11.1**). Previously, the Standard required disclosure, in every reporting period, of the recoverable amount of each CGU or group of CGU's to which a significant portion of the overall carrying amount of goodwill (or other intangible assets with indefinite useful lives) had been allocated. The IASB had intended to limit such disclosures to reporting periods in which an impairment loss was recognised or reversed. To achieve this effect, the requirement to disclose the recoverable amount of each CGU or group of CGUs has been moved from IAS 36:134(c) to IAS 36:130(f) (see **11.4.1**).

The following information should be disclosed for each CGU (or group of CGUs) for which the carrying amount of goodwill or intangible assets with indefinite useful lives allocated to that unit (or group of units) is significant in comparison with the entity's total carrying amount of goodwill or intangible assets with indefinite useful lives:

[IAS 36:134]

(a) the carrying amount of goodwill allocated to the unit (or group of units);

(b) the carrying amount of intangible assets with indefinite useful lives allocated to the unit (or group of units);

(c) the basis on which the unit's (or group of units') recoverable amount has been determined (i.e. value in use or fair value less costs of disposal);





(d) if the unit's (or group of units') recoverable amount is based on value in use:

 (i) each key assumption on which management has based its cash flow projections for the period covered by the most recent budgets/forecasts. Key assumptions are those to which the unit's (or group of units') recoverable amount is most sensitive;

 (ii) a description of management's approach to determining the value(s) assigned to each key assumption, whether those value(s) reflect past experience or, if appropriate, are consistent with external sources of information, and, if not, how and why they differ from past experience or external sources of information;

 (iii) the period over which management has projected cash flows based on financial budgets/forecasts approved by management and, when a period greater than five years is used for a CGU (or group of CGUs), an explanation as to why that longer period is justified;

 (iv) the growth rate used to extrapolate cash flow projections beyond the period covered by the most recent budgets/forecasts, and the justification for using any growth rate that exceeds the long-term average growth rate for the products, industries, or country or countries in which the entity operates, or for the market to which the unit (or group of units) is dedicated; and

 (v) the discount rate(s) applied to the cash flow projections;

(e) if the unit's (or group of units') recoverable amount is based on fair value less costs of disposal, the valuation technique(s) used to measure fair value less costs of disposal. An entity is not required to provide the disclosures required by IFRS 13. If fair value less costs of disposal is not measured using a quoted price for an identical unit (or group of units), the following information should also be disclosed:

 (i) each key assumption on which management has based its determination of fair value less costs of disposal. Key assumptions are those to which the unit's (or group of units') recoverable amount is most sensitive;

 (ii) a description of management's approach to determining the value (or values) assigned to each key assumption, whether those values reflect past experience or, if appropriate, are consistent with external sources of information, and, if not, how and why they differ from past experience or external sources of information;

 (iii) the level of the IFRS 13 fair value hierarchy (see **section 10** of **chapter A6**) within which the fair value measurement is categorised in its entirety (without giving regard to the observability of 'costs of disposal'); and

 (iv) if there has been a change in valuation technique, the change and the reason(s) for making it.

 In addition, if fair value less costs of disposal is measured using discounted cash flow projections, the following information should also



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- the legal description or characteristics of the tax imply that the tax is calculated based on taxable profits; and
- there is any withholding related to the tax.

The IFRIC (now the IFRS Interpretations Committee) referred to this topic in a rejection notice published in the March 2006 *IFRIC Update*. The IFRIC noted that the definition of taxable profit implies that not all taxes are in the scope of IAS 12, and that the requirement to disclose an explanation of the relationship between the tax expense and the accounting profit implies that taxable profit need not be the same as accounting profit.

Taxes that are unlikely to meet the definition of an income tax include:

- sales taxes (because they are transactional taxes based on sales value rather than on taxable profits);
- production-based taxes (see **example 2.5A**); and
- 'tonnage' taxes (see **2.3**).

Care should be exercised in respect of taxes imposed in different jurisdictions that are referred to by common titles but for which the detailed application varies significantly between jurisdictions (such as 'petroleum revenue taxes' – see **example 2.5B**). The determination as to whether such taxes are income taxes should be made on a case-by-case basis.

### 2.2 Levies

IFRIC 21 *Levies*, which was issued in May 2013, provides guidance on when to recognise a liability for a 'levy' imposed by a government; a levy is defined as "an outflow of resources embodying economic benefits that is imposed by governments on entities in accordance with legislation (ie laws and/or regulations), other than:

(a) those outflows of resources that are within the scope of other Standards (such as income taxes that are within the scope of IAS 12); and

(b) fines or other penalties that are imposed for breaches of the legislation".

Therefore, any levy imposed by a government should be assessed to determine if it meets the definition of an income tax (see **2.1**). If it does, it should be accounted for in accordance with IAS 12 rather than in accordance with IFRIC 21.

**Section 9.4** of **chapter A12** provides a detailed description of the requirements of IFRIC 21.





### 2.3 Tonnage tax

In some jurisdictions, shipping entities can choose to be taxed by means of a 'tonnage tax' instead of under general corporate income tax regulations. Tonnage tax may be paid on the basis of tonnage transported, tonnage capacity or a notional profit.

The IFRIC (now the IFRS Interpretations Committee) considered tonnage taxes in a rejection notice published in the May 2009 *IFRIC Update*. The IFRIC noted that taxes based on tonnage transported or tonnage capacity are based on a gross rather than a net amount, and taxes on notional income are not based on the entity's actual income and expenses. Such taxes should not be considered income taxes in accordance with IAS 12 and should not be presented as part of tax expense in the statement of comprehensive income. However, the IFRIC also noted that an entity subject to tonnage tax might present additional subtotals in the statement of comprehensive income if that presentation is relevant to an understanding of its financial performance.

### 2.4 Interest and penalties

In many jurisdictions, interest and penalties are assessed on underpayments or late payments of income tax. In some circumstances, interest and penalties arise because the tax amount payable could not be agreed with the tax authority until significantly after the due date and, therefore, the interest and penalties could not have been avoided by the entity. Alternatively, interest and penalties may arise because the entity has made a deliberate choice not to make the appropriate tax payments before the due date.

Interest and penalties assessed on underpayments or late payments of income tax do not meet the definition of current or deferred tax under IAS 12:5 (see **3.1** and **4.1**, respectively), regardless of the circumstances in which they arise, and they should be presented in the financial statements based on their nature, i.e. either as a finance cost (interest) or an operating cost (penalties).

### 2.5 Hybrid taxes

Entities are sometimes subject to a tax that has different components. It is necessary to exercise careful judgement when determining whether each of the components meets the definition of an income tax under IAS 12.

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share of Company A's current year profits (i.e. CU15,000) were distributed. A deferred tax liability of CU3,750 (CU15,000 × 25%) should therefore be recognised in the consolidated financial statements to 31 December 20X3, in addition to the recognition of the tax consequences arising from the remittance of CU5,000.

For deductible temporary differences arising in relation to investments, it is not necessary to consider the investor's ability to control distributions from the investee. Recognition of the deferred tax asset is only required if it is probable that the temporary difference will reverse in the foreseeable future and that taxable profit will be available against which the temporary difference can be utilised.

The determination of the expected manner of recovery of an investment in an associate will often require careful judgement. Factors to consider in making this judgement include, but are not limited to:

- whether the investor intends to sell its interest;
- the dividend yield on the investment; and
- the reason for acquiring and holding the investment.

When, for example, there has been a regular flow of dividends from the investment in the past, and there is no evidence of an intention to dispose of the associate (even though a disposal may be a possibility at some future point), this may lead to a determination that the investment will be recovered via remittance of earnings by dividend.

### 4.4.7.6 *Recognition of temporary differences associated with interests in joint arrangements*

Under IFRS 11 *Joint Arrangements*, the accounting for a joint arrangement is determined by whether the arrangement is classified as a joint venture or a joint operation (as defined in that Standard).

Irrespective of the method of accounting for joint arrangements, the same general considerations apply in respect of deferred tax.

The arrangement between the parties to a joint arrangement usually deals with the distribution of the profits and identifies whether decisions on such matters require the consent of all of the parties or a group of the parties. When the joint venturer or joint operator can control the timing of the distribution of its share of profits of the joint arrangement, and it is probable that its share of the profits will not be distributed in the foreseeable future, a deferred tax liability is not recognised. [IAS 12:43]





*Interests in joint ventures*

The determination as to who controls the timing of the reversal of the temporary difference in the case of joint ventures is not as clear-cut as it is for associates (see **4.4.7.5**). Investments in joint ventures involve joint control, i.e. there is a contractual agreement to share control and no joint venturer exercises unilateral control.

The arrangements for distributions or disposals of shareholdings are generally dealt with in the joint venture agreement. In most cases, although each joint venturer cannot unilaterally declare a dividend, neither can such dividend be declared without each joint venturer's agreement. Therefore, each joint venturer has the ability to prevent distributions and, accordingly, prevent the reversal of the temporary difference. If this is the case, no deferred tax liability should be recognised if the joint venturer does not anticipate that it will authorise such distributions in the foreseeable future.

*Interests in joint operations*

Under IFRS 11, the determination of the tax implications for joint operations will depend on whether the joint operation is structured through a legal entity.

For joint arrangements that are structured through a legal entity but are determined to be joint operations because of other facts and circumstances (see **chapter A27**), the same considerations apply as above for joint ventures.

For joint operations that are not structured through a legal entity, the absence of a legal entity would mean that the joint operator does not generally have the ability to control the reversal of the temporary difference. Accordingly, deferred tax should normally be recognised.

### 4.4.7.7 *Change in investment from subsidiary to associate*

A parent may cease to have control over a subsidiary (e.g. because the parent sells a portion of the investment or because the subsidiary issues additional shares to a third party) but may retain some of its ownership interest such that the investment is subsequently classified as an associate and is, therefore, accounted for using the equity method. This change from subsidiary to associate may have deferred tax consequences.

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Initially, the revaluation uplift and the related deferred tax are recognised in other comprehensive income and accumulated in the revaluation reserve. Each year a transfer is made from the revaluation reserve to retained earnings equal to the depreciation of the revaluation surplus net of tax.

At the time of the downward revaluation, the balance in the revaluation reserve is CU140. This is calculated as follows.

| | CU |
|---|---|
| Original revaluation uplift | 350 |
| Deferred tax thereon (CU350 × 30%) | (105) |
| | 245 |
| Three years' depreciation on net uplift (CU245 × 3/7) | (105) |
| | 140 |

Therefore, the first CU200 of the downward revaluation is recognised as a loss in other comprehensive income, net of CU60 related tax. The remaining downward revaluation of CU200 is recognised in profit or loss (along with CU60 related tax).

The downward revaluation reduces the carrying amount below the tax base, resulting in a deferred tax asset which is recognised because the entity has forecast taxable profits.

| | Carrying amount | | | | Deferred tax liability (asset) | Movement for the year | Recognised in | |
|---|---|---|---|---|---|---|---|---|
| | Historical cost | Revaluation uplift | Tax base | Temporary difference | | | Other comp. income | Profit or loss |
| | CU | CU | CU | CU | CU | CU | CU | CU |
| 20X0 | 1,000 | – | 1,000 | – | – | – | – | – |
| 20X1 | 900 | – | 900 | – | – | – | – | – |
| 20X2 | 800 | – | 800 | – | – | – | – | – |
| 20X3 | 700 | 350 | 700 | 350 | 105 | 105 | 105 | – |
| 20X4 | 600 | 300 | 600 | 300 | 90 | (15) | – | (15) |
| 20X5 | 500 | 250 | 500 | 250 | 75 | (15) | – | (15) |
| 20X6 | 200 | – | 400 | (200) | (60) | (135) | (60) | (75) |
| 20X7 | 150 | – | 300 | (150) | (45) | 15 | – | 15 |
| 20X8 | 100 | – | 200 | (100) | (30) | 15 | – | 15 |
| 20X9 | 50 | – | 100 | (50) | (15) | 15 | – | 15 |
| 20Y0 | – | – | – | – | – | 15 | – | 15 |

If a decision is subsequently taken to dispose of the property, then the deferred tax implications will need to be re-examined. Because the temporary difference is calculated on the basis of management expectations as to the manner of recovery of the property, when those expectations change the deferred tax position may also change.





### 5.4.4 *Properties to be recovered through disposal – 'clawback' of tax depreciation*

It may be anticipated that the carrying amount of a revalued property will be recovered through sale (whether based on management intent or on the presumptions established in IAS 12 for non-depreciable properties and investment properties – see **section 4.2.6**). In such cases, the deferred tax implications are determined on the basis of the tax consequences of disposal of the property. It may be that the profit on disposal will be fully taxable, in which case the deferred tax liability arising on any revaluation of the property will be equal to the revaluation uplift multiplied by the tax rate. However, frequently, the taxation of capital gains is on a different basis (e.g. the taxable gain arising may be limited to the amount of tax depreciation previously claimed). This is often referred to as a 'claw-back'.

In such circumstances (i.e. when the disposal is not itself subject to income tax, but any deduction for tax depreciation previously claimed is taxable as a 'claw-back'), the tax base is the carrying amount less future taxable amounts. This may or may not be equal to the cost less tax depreciation to date. This point is illustrated in **example 5.4.4**.

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**Example 5.4.4**

**Property to be recovered through disposal**

A building (classified as property, plant and equipment) is acquired for CU1,000 on 1 January 20X1. No deferred tax arises on initial recognition of the property, which is to be depreciated (both for tax and accounting purposes) over five years. At the end of 20X1, when its carrying amount and tax written down value is CU800, the property is remeasured to its fair value of CU1,200. At that date, it is expected that the carrying amount of the property will be recovered through disposal.

If the property were disposed of, the taxable gain arising would be limited to the amount of the tax depreciation previously claimed. The tax rate is 30 per cent.

At 31 December 20X1 Carrying amount (fair value) = CU1,200

Tax base = CU1,000*

Temporary difference = CU1,200 – CU1,000 = CU200

Deferred tax liability = CU200 × 30% = CU60

* The tax base is the carrying amount of CU1,200 less future taxable amounts (i.e. the allowances that would be clawed back on disposal) of CU200. In these circumstances, the tax base for IAS 12 is not equal to the tax written down value of CU800 (cost less accumulated tax depreciation to date).

Therefore, at the end of 20X1, a deferred tax liability of CU60 is recognised; because it relates to the revaluation of the property, the debit of CU60 is recognised in other comprehensive income.

- timing of adoption;
- reversal of impairment losses; and
- requirements for non-public entities.

## 2 Definitions

Appendix A to IFRS 15 provides the following definitions for terms used in the Standard.

- A **contract** is defined as "[a]n agreement between two or more parties that creates enforceable rights and obligations".
- A **contract asset** is defined as "[a]n entity's right to consideration in exchange for goods or services that the entity has transferred to a customer when that right is conditioned on something other than the passage of time (for example, the entity's future performance)".
- A **contract liability** is defined as "[a]n entity's obligation to transfer goods or services to a customer for which the entity has received consideration (or the amount is due) from the customer".
- A **customer** is defined as "[a] party that has contracted with an entity to obtain goods or services that are an output of the entity's ordinary activities in exchange for consideration".
- **Income** is defined as "[i]ncreases in economic benefits during the accounting period in the form of inflows or enhancements of assets or decreases of liabilities that result in an increase in equity, other than those relating to contributions from equity participants".
- A **performance obligation** is defined as "[a] promise in a contract with a customer to transfer to the customer either:
  (a) a good or service (or a bundle of goods or services) that is distinct; or
  (b) a series of distinct goods or services that are substantially the same and that have the same pattern of transfer to the customer".
- **Revenue** is defined as "[i]ncome arising in the course of an entity's ordinary activities".
- The **stand-alone selling price** of a good or service is defined as "[t]he price at which an entity would sell a promised good or service separately to a customer".
- The **transaction price** for a contract with a customer is defined as "[t]he amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services to a customer, excluding amounts collected on behalf of third parties".





## 3 General principles and scope

### 3.1 Objective of IFRS 15

The objective of IFRS 15 is to establish the principles that should be applied by an entity in order to report useful information to users of financial statements about the nature, amount, timing and uncertainty of revenue and cash flows arising from a contract with a customer. [IFRS 15:1]

### 3.2 Core principle of IFRS 15

The core principle of IFRS 15 is that an entity recognises revenue to depict the transfer of promised goods or services to customers, reflecting the amount of consideration to which the entity expects to be entitled in exchange for those goods or services. [IFRS 15:2]

Note that the core principle is based on the amount to which the entity 'expects to be entitled', rather than the amount it expects to collect. This is different from a fair value measurement model because, for example, it generally does not reflect any adjustments for amounts that the entity might not be able to collect from the customer (i.e. customer credit risk). Although this might appear to be a significant change from the requirements of IFRS 15's predecessor Standards, previous practices were broadly consistent with this approach and many entities have always determined the amount of revenue on the basis of the amounts the customer promised to pay. [IFRS 15:BC478] The IASB decided to measure revenue in this way in response to comments from users of financial statements that they would prefer revenue to be measured at the 'gross' amount, so that revenue growth and receivables management (or bad debts) could be analysed separately. [IFRS 15:BC260 & BC261]

Nevertheless, when a customer pays in arrears and the contract contains a significant financing component, customer credit risk will be reflected in the amount of revenue recognised. This is because customer credit risk will be taken into account in determining the appropriate discount rate (see **7.4.6**).

When applying IFRS 15, it is important to evaluate the terms of the contract and all relevant facts and circumstances. [IFRS 15:3]

### 3.3 Consistent application of IFRS 15

IFRS 15 should be applied consistently to contracts with similar characteristics and in similar circumstances. This requirement for consistent application is specifically extended to the use of any practical expedients. [IFRS 15:3]



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| Product | Allocated transaction price | |
|---|---|---|
| | CU | |
| Product A | 33 | (CU50 / CU150 x CU100) |
| Product B | 17 | (CU25 / CU150 x CU100) |
| Product C | 50 | (CU75 / CU150 x CU100) |
| Total | 100 | |

## 8.3 Allocation of a discount

When the sum of the stand-alone selling prices of the goods or services promised in the contract exceeds the promised consideration in a contract, the customer has received a discount for purchasing a bundle of goods or services. The discount should be allocated proportionately to all performance obligations in the contract unless there is observable evidence that the entire discount does not relate to all performance obligations in the contract. [IFRS 15:81]

A discount is allocated entirely to one or more, but not all, performance obligations in the contract if all of the following criteria are met:

[IFRS 15:82]

(a) the entity regularly sells each distinct good or service (or each bundle of distinct goods or services) in the contract on a stand-alone basis;

(b) the entity also regularly sells on a stand-alone basis a bundle (or bundles) of some of those distinct goods or services on a stand-alone basis at a discount to the stand-alone selling prices; and

(c) the discount attributable to each bundle of goods or services described in (b) is substantially the same as the discount in the contract and an analysis of the goods or services in each bundle provides observable evidence of the performance obligation (or performance obligations) to which the entire discount in the contract belongs.

When the discount is allocated entirely to one or more performance obligations in the contract in accordance with IFRS 15:82, the allocation is made before using the residual approach to estimate the stand-alone selling price of a good or service in accordance with IFRS 15:79(c) (see **8.2**). [IFRS 15:83]

IFRS 15:82 will typically apply only to contracts for which there are at least three performance obligations. This is because an entity could demonstrate that a discount relates to two or more performance obligations when it has observable information supporting the stand-alone selling price of a group of those promised goods or services when they are sold together. The Basis for Conclusions on IFRS 15 notes that it may be possible for an entity to have sufficient evidence to be able to allocate a discount to only one performance obligation in accordance with the criteria in IFRS 15:82, but the IASB and FASB expected that this could only occur in rare cases. [IFRS 15:BC283]





**Example 8.3**

**Allocating a discount**

[IFRS 15 Illustrative Example 34]

An entity regularly sells Products A, B and C individually, thereby establishing the following stand-alone selling prices:

| Product | Stand-alone selling price |
|---|---|
| | CU |
| Product A | 40 |
| Product B | 55 |
| Product C | 45 |
| Total | 140 |

In addition, the entity regularly sells Products B and C together for CU60.

*Case A—Allocating a discount to one or more performance obligations*

The entity enters into a contract with a customer to sell Products A, B and C in exchange for CU100. The entity will satisfy the performance obligations for each of the products at different points in time.

The contract includes a discount of CU40 on the overall transaction, which would be allocated proportionately to all three performance obligations when allocating the transaction price using the relative stand-alone selling price method (in accordance with [IFRS 15:81]). However, because the entity regularly sells Products B and C together for CU60 and Product A for CU40, it has evidence that the entire discount should be allocated to the promises to transfer Products B and C in accordance with [IFRS 15:82].

If the entity transfers control of Products B and C at the same point in time, then the entity could, as a practical matter, account for the transfer of those products as a single performance obligation. That is, the entity could allocate CU60 of the transaction price to the single performance obligation and recognise revenue of CU60 when Products B and C simultaneously transfer to the customer.

If the contract requires the entity to transfer control of Products B and C at different points in time, then the allocated amount of CU60 is individually allocated to the promises to transfer Product B (stand-alone selling price of CU55) and Product C (stand-alone selling price of CU45) as follows:

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In the circumstances under consideration, Company A has not satisfied the performance obligation at the time when the goods are shipped; the performance obligation is to provide the customer with the goods of which the title and physical possession will only be passed to the customer when the goods reach the agreed destination. Further, the fact that Company A has managed its risk while the goods are in transit, by having a contract with the shipping company, does not mean that it has transferred control of the goods to the customer at the time when the goods are shipped.

With the above analysis, Company A determines that control does not pass to the customer until the goods reach the agreed destination.

It will generally be the case that, when goods are shipped with standard FOB destination shipping terms, control of the goods will be transferred to the customer when the goods arrive at the point of the agreed destination. However, it is important for entities to consider carefully both the terms of the contract and other relevant facts and circumstances to determine when control of the goods is transferred to the customer, especially when a contract contains other than standard shipping terms.

When goods are shipped 'free on board' (FOB) shipping point, title passes to the buyer when the goods are shipped, and the buyer is responsible for any loss in transit. On the other hand, when goods are shipped FOB destination, title does not pass to the buyer until delivery, and the seller is responsible for any loss in transit.

Some entities ship products using FOB shipping point terms but have practices or arrangements with their customers which result in the seller continuing to bear risk of loss or damage while the product is in transit. If there is damage or loss, the seller is obliged to provide (or has a practice of providing) the buyer with replacement products at no additional cost. The seller may insure this risk with a third party or 'self-insure' the risk (however, the seller is not acting solely as the buyer's agent in arranging shipping and insurance in the arrangements). These types of shipping terms are commonly referred to as "synthetic FOB destination" shipping terms because the seller has retained the risk of loss or damage during transit and, consequently, all the risks and rewards of ownership have not been substantively transferred to the buyer.

An entity will need to evaluate when control of a good transfers to a customer under FOB shipping point terms when the entity has a practice (or an arrangement with the customer) that results in the seller continuing to bear risk of loss or damage while the product is in transit.

When control of a good (that represents a separate performance obligation) is deemed to transfer at a point in time, an entity would be required to use judgment in applying the guidance and indicators provided in IFRS 15 to evaluate the impact of shipping terms and practices in determining when control of the good transfers to the customer.





Under typical, unmodified FOB shipping point terms, upon shipment of the goods, the seller usually has a legal right to payment; title and risk of loss/damage to the shipped goods transfer to the buyer, and the seller transfers physical possession of the shipped goods (assuming the buyer, not the seller, has the ability to redirect or otherwise control the shipment through the shipping entity). Shipping terms generally do not affect a customer acceptance term and the latter would have to be evaluated separately as to the impact on when control of a good transfers to the buyer. However, if the seller can objectively determine that the shipped goods meet the specifications agreed-upon in the contract with the buyer, then customer acceptance would be deemed a formality as noted in IFRS 15:B84 (see **9.4.3**). Therefore, under typical unmodified FOB shipping point terms, the buyer would obtain control of the shipped goods and revenue would be recognised (subject to the other requirements of IFRS 15) upon shipment.

The typical FOB shipping point terms as described above may be modified such that a seller is obliged to the buyer (a legal obligation) to replace goods lost or damaged in transit or is not obliged but has a history of replacing any damaged or lost product (a constructive obligation) at no additional cost. Such an obligation is an indicator that would need to be considered in determining when the buyer has obtained control of the shipped goods. In these situations, the seller should evaluate whether the buyer has obtained the 'significant' risks and rewards of ownership of the shipped goods even though the seller maintains the risk of loss or damage to the goods during shipping. Such evaluation would include a determination as to how the obligation maintained by the seller affects the buyer's ability to sell, exchange, pledge, or otherwise use the asset (as noted in IFRS 15:33) and include a consideration of the likelihood and potential materiality of lost or damaged goods during shipping. This determination as to whether the significant risks and rewards have transferred would constitute but one indicator (not in itself determinative) of whether the buyer has obtained control of the shipped goods, to be considered along with the other four indicators in IFRS 15:38 (see **9.4.1**). Subject to the other requirements of IFRS 15, recognition of revenue at the time of shipment would be appropriate if the seller concludes that the buyer has obtained control of the goods upon shipment (based on an overall evaluation of the indicators in IFRS 15:38 and other guidance in IFRS 15).

If control is considered to transfer upon shipment then, as noted in IFRS 15:38(d), the seller needs to consider whether the risk of loss or damage maintained by the seller during shipping gives rise to another performance obligation and, if so, to account for such obligation separately in accordance with IFRS 15. For example, such risks may represent another performance obligation if products are frequently lost or damaged during shipping.



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[IAS 19:11]

- in the statement of financial position, as a liability (accrued expense), after deducting any amounts already paid, or as an asset (prepaid expense), if the amount already paid exceeds the undiscounted amount of the benefits, to the extent that the prepayment is recoverable (e.g. by means of a reduction in future payments or a cash refund); and
- in profit or loss, as an expense, unless another Standard requires or permits inclusion of the benefits in the cost of an asset (e.g. as part of staff costs capitalised in a self-constructed property – see **chapter A7**).

The cost of all short-term employee benefits is recognised as noted above. No actuarial assumptions are required (therefore, there are no actuarial gains or losses to address) and, due to their short-term nature, obligations are dealt with on an undiscounted basis.

### 3.3.2 *Non-monetary short-term benefits*

When non-monetary short-term benefits are provided, the cost of providing such benefits is measured at the cost to the employer of providing the benefit and is recognised using the same principles as are applied to monetary employee benefits.

### 3.3.3 *Short-term paid absences*

An entity may pay employees for absence for various reasons (e.g. holidays, sickness and short-term disability, maternity or paternity leave, jury service and military service). Short-term paid absences may be classified as accumulating or non-accumulating. [IAS 19:14]

Accumulating paid absences are those that can be carried forward and used in future accounting periods if the current accounting period's entitlement is not used in full. Accumulating paid absences may be further subdivided as vesting (when employees are entitled to a cash payment for unused entitlement on leaving the entity) or non-vesting (when no such entitlement arises). [IAS 19:15]

Non-accumulating paid absences cannot be carried forward, i.e. any unused entitlement is lost at the end of the current period and the employee is not entitled to a cash payment for unused entitlement on leaving the entity. This is commonly the case for sick pay (to the extent that unused past entitlement does not increase future entitlement), maternity or paternity leave, and paid absences for jury service or military service. [IAS 19:18]

In applying the general requirements set out at **3.3.1** to the expected cost of short-term paid absences:





[IAS 19:13 & 16]

- for accumulating paid absences, the expense should be recognised when the employees render service that increases their entitlement to future paid absences, based on the additional amount that the entity expects to pay as a result of the unused entitlement accumulated at the end of the reporting period; and
- for non-accumulating paid absences, the expense should be recognised only when the absences occur. This is because employee service does not increase the amount of the benefit.

For accumulating absences, the difference between vesting and non-vesting does not affect whether an obligation exists and should be recognised, but does affect the measurement of that obligation, because there is a possibility that employees may leave before they use an accumulating non-vesting entitlement. Therefore, the expense is measured as the additional amount that the entity expects to pay, rather than the maximum amount that it could be obliged to pay. [IAS 19:15]

**Example 3.3.3**

**Measurement of obligation for short-term paid absences**

Company A has 200 employees, who are each entitled to 20 working days of paid leave each year. Paid leave is first taken out of the current year's entitlement and then out of the balance brought forward from the previous year (a LIFO basis). Unused leave cannot be carried forward more than one year. Employees are not entitled to a cash payment for unused leave if they leave Company A's employment.

At 31 December 20X1, the average unused entitlement is 3 days per employee (i.e. 600 days in total). Based on past experience, Entity A expects that 175 employees will take no more than their annual entitlement in 20X2 and that the remaining 25 employees will, in total, use 70 days of the entitlement brought forward from 20X1.

The benefit described can be carried forward if the current period's entitlement is not used in full, but only for 12 months; it is therefore an 'accumulating' short-term paid absence. The accumulating paid leave is non-vesting, because employees are not entitled to a cash payment for unused leave when they leave Company A's employment (see IAS 19:15).

IAS 19:16 requires Company A to recognise an obligation at 31 December 20X1 for the amount it expects to pay as a result of the unused entitlement that has accumulated at the end of the period. IAS 19:15 clarifies that, for non-vesting entitlements, the possibility that some employees will not take their entitlement should be reflected in that measurement.

Therefore, at 31 December 20X1, Company A recognises a liability and an expense equal to the undiscounted amount of 70 days of paid leave (i.e. the number of days of the entitlement that are expected to be taken).

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> - the benefit is conditional on future service being provided (including benefits that increase if further service is provided); or
> - the benefit is provided in accordance with the terms of an employee benefit plan; and
>
> - the definitions of the employee benefit categories in IAS 19.
>
> In the circumstances described, Entity A's arrangement has attributes of both required service and termination benefits. However, Entity A's arrangement would not meet the definition of a termination benefit because, consistent with IAS 19:162(a), the fact that the bonus payments are wholly conditional upon completion of employee service over a period indicates that the benefits are in exchange for that service.
>
> This conclusion was confirmed by the IFRS Interpretations Committee (see *IFRIC Update*, January 2012).

Termination benefits do not include employee benefits resulting from termination of employment at the request of the employee without an entity's offer, or as a result of mandatory retirement requirements; those benefits are post-employment benefits. [IAS 19:160]

Some termination benefits are provided in accordance with the terms of an existing employee benefit plan (e.g. by statute, employment contract or union agreement), or they may be implied as a result of the employer's past practice of providing similar benefits. Employee benefits provided in accordance with the terms of an employee benefit plan are termination benefits if they both result from an entity's decision to terminate an employee's employment and are not conditional on future service being provided. [IAS 19:163]

If an entity makes an offer of benefits available for more than a short period, or there is more than a short period between the offer and the expected date of actual termination, the entity should consider whether it has established a new employee benefit plan and, therefore, whether the benefits offered under that plan are termination benefits or post-employment benefits. [IAS 19:163]

## 10.2 Employee benefits payable irrespective of reason for employee departure

Certain employee benefits are payable irrespective of the reason for an employee's departure (subject to any vesting or minimum service requirements) but the timing of their payment is uncertain. Therefore, although such benefits may be described in some jurisdictions as termination indemnities or termination gratuities, they are post-employment benefits rather than termination benefits and should be accounted for as post-employment benefits. [IAS 19:164]





Some entities provide a lower level of benefit for termination of employment at the request of the employee (in substance, a post-employment benefit) than for termination of employment at the request of the entity. In such circumstances, the difference between the benefit provided for termination of employment at the request of the employee and a higher benefit provided at the request of the entity is a termination benefit. [IAS 19:160]

## 10.3 Recognition of termination benefits

A liability and an expense should be recognised for termination benefits at the earlier of the following dates:

[IAS 19:165]

- when the entity can no longer withdraw the offer of those benefits; and
- when the entity recognises costs for a restructuring that is within the scope of IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* and involves the payment of termination benefits.

In considering the issue of the timing of recognition of termination benefits, the Board decided that the factor determining the timing of recognition is the entity's inability to withdraw the offer of termination benefit. The Board also determined that the inability to withdraw an offer is triggered by different events based on whether the termination is subject to acceptance by the employee or is imposed upon the employee.

In the first scenario (termination benefits payable as a result of an employee's decision to accept an offer of benefits in exchange for the termination of employment), the time when an entity can no longer withdraw the offer of termination benefits is the earlier of:

[IAS 19:166]

- when the employee accepts the offer; and
- when a restriction (e.g. a legal, regulatory or contractual requirement or other restriction) on the entity's ability to withdraw the offer takes effect. This would be when the offer is made, if the restriction existed at the time of the offer.

In the second scenario (for termination benefits payable as a result of an entity's decision to terminate an employee's employment), the entity can no longer withdraw the offer when the entity has communicated to the affected employees a plan of termination meeting all of the following criteria:

[IAS 19:167]

- actions required to complete the plan indicate that it is unlikely that significant changes to the plan will be made;

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