

## Introduction *continued*

### Changes since the 2013 Briefing

The changes made since the 2013 Briefing are as follows:

- The basis of preparation has been changed. The 2013 Briefing contained high level summaries of Standards that would apply at 1 January 2013 for a preparer that chose to apply early all Standards that had been issued at that date even if they had a later effective date. This 2015 Briefing contains high level summaries of Standards that are required for annual reporting periods beginning on 1 January 2015 for a preparer that chooses not to apply early any Standards that had an effective date for annual reporting periods beginning later than 1 January 2015.
- An appendix has been added. This is as a consequence of the above change in the basis of preparation. The appendix contains high level summaries of Standards that apply for annual reporting periods beginning later than 1 January 2015 that had been issued by 30 June 2015; such Standards are available for early application.

- It has been updated for recent changes in IFRS:
  - Changes that were not required for annual reporting periods beginning on 1 January 2013 but are required for annual reporting periods beginning on 1 January 2015. Because the basis of preparation of the Briefing was different in 2013, most of these changes were considered when preparing the 2013 Briefing. Because the Briefing is a high-level summary, not all the changes are explicitly discussed in this Briefing. The changes are to be found in the following publications:
    - *Offsetting Financial assets and Financial Liabilities* (Amendments to IAS 32);
    - *Investment Entities* (Amendments to IFRS 10, IFRS 12 and IAS 27);
    - *Recoverable Amount Disclosures for Non-Financial Assets* (Amendments to IAS 36);
    - *Novation of Derivatives and Continuation of Hedge Accounting* (Amendments to IAS 39);
    - *Defined Benefit Plans: Employee Contributions* (Amendments to IAS 19);
    - Amendments to IFRS 2, 3, 8 and 13 and IAS 16, 24 and 38 in *Annual Improvements to IFRSs 2010-2012 Cycle*;

- Amendments to IFRS 1, 3 and 13 and IAS 40 in *Annual Improvements to IFRSs 2011-2013 Cycle*; and
- IFRIC 21 *Levies*.
- Changes that are not mandatory for annual reporting periods beginning on 1 January 2015, but that can be applied early. The changes are listed in the Appendix, and include:
  - IFRS 9 *Financial Instruments*;
  - IFRS 14 *Regulatory Deferral Accounts*; and
  - IFRS 15 *Revenue from Contracts with Customers*.

## The Conceptual Framework for Financial Reporting

### The Conceptual Framework

*The Conceptual Framework sets out concepts underlying the preparation and presentation of financial statements for external users.*

The purpose of the *Conceptual Framework* is to assist: the International Accounting Standards Board (IASB) when it develops Standards; preparers of financial statements in accounting for transactions and events; auditors in forming an opinion on whether financial statements comply with International Financial Reporting Standards (IFRS); as well as a number of others. Consequently, the *Conceptual Framework* is the starting point for understanding IFRS information.

Sets out the concepts that underlie IFRS financial statements.

The *Conceptual Framework* is not, however, a Standard. Nor does it override any Standards. Nevertheless, the *Conceptual Framework* provides the background to understand IFRS and also serves as a basis for judgement in applying IFRS, including determining an accounting policy when there is no Standard that applies to a specific transaction or event.

The *Conceptual Framework* specifies the objective of IFRS financial statements and the IASB has this in mind when formulating Standards. That objective is to provide financial information about the reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions about providing resources to the entity. Those decisions involve buying, selling or holding equity and debt instruments, and providing or settling loans and other forms of credit.

Such decisions depend on the returns, for example, dividends, principal and interest payments or market price increases, that investors, lenders and other creditors expect from an investment. Their expectations about returns depend on their assessment of future net cash inflows to the entity. Consequently, the *Conceptual Framework* explains that they need information about the entity's resources, claims against the entity and how efficiently and effectively the entity's management have discharged their responsibilities to use the entity's resources, ie what is sometimes called stewardship.

IFRS financial statements are designed to meet the needs of external users. They are not designed to meet the needs of a controlling shareholder, management or regulators, because those groups can prescribe the form and content of reports to meet their specific needs. However, the *Conceptual Framework* explicitly states that IFRS financial statements cannot provide all the information needed by external users. Users need to consider pertinent information from other sources, for example, political events and industry outlooks. IFRS financial statements are not designed to show the value of the entity, but provide information to external users for them to make their own estimate of the value of the entity.

The *Conceptual Framework* sets out the qualitative characteristics of useful financial information. To be useful, financial information must be relevant (ie capable of making a difference in the decisions made by users) and it should faithfully represent what it purports to represent (ie financial information should be complete, neutral and free from error). The usefulness of financial information is enhanced if it is comparable, verifiable, timely and understandable to users who have a reasonable knowledge of business and economic activities and who review and analyse the information diligently.

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# The Conceptual Framework for Financial Reporting *continued*

The *Conceptual Framework* also defines the elements of financial statements. The following elements are relevant to an entity's financial position:

- An asset is a resource controlled by the entity as a result of past events. Future economic benefits are expected to flow to the entity from this resource.
- A liability is a present obligation of the entity arising from past events. Settlement of the obligation is expected to result in an outflow of economic benefits from the entity.
- Equity is the residual interest in the entity's assets after deducting all its liabilities.

An asset or a liability is recognised, that is, included, in the statement of financial position (balance sheet) if it is probable that future economic benefits will flow to or from the entity, and if its cost or value, or the amount of the outflow, can be reliably measured.

The following elements are relevant to financial performance:

- Income is increases in economic benefits during the accounting period. It takes the form of inflows of or increases in assets or decreases in liabilities. It does not include equity contributions from the entity's owners.
- Expenses are decreases in economic benefits during the accounting period. They take the form of outflows or reductions of assets or increases in liabilities. They do not include equity distributions to the entity's owners.

To be useful, financial information must be relevant (ie capable of making a difference in the decisions made by users) and it should faithfully represent what it purports to represent (ie financial information should be complete, neutral and free from error).

## Recent developments

The IASB is updating and improving the *Conceptual Framework* and an Exposure Draft was published in May 2015. The exposure draft proposes a number of enhancements including:

- a new chapter on measurement that describes appropriate measurement bases (historical cost and current value, including fair value), and the factors to consider when selecting a measurement basis;
- confirming that the statement of profit or loss is the primary source of information about a company's performance, and adding guidance on when income and expenses could be reported outside the statement of profit or loss, in 'Other Comprehensive Income'; and
- refining the definitions of the basic building blocks of financial statements—assets, liabilities, equity, income and expenses.

## IFRS 1

### First-time Adoption of International Financial Reporting Standards

#### The Standard

*This Standard applies when an entity first adopts IFRS in its annual financial statements. It also applies to interim financial reports for any part of the period covered by the entity's first IFRS financial statements.*

Financial statements include comparative information for one or more prior periods. To improve the usefulness of financial information, whenever an entity changes one or more of its accounting policies these comparatives are generally restated and presented as though the new accounting policy had always been applied. Adopting IFRS for the first time, say, in financial statements for the financial year ended 31 December 2015, is no different; the comparatives presented, say, for 2014 or 2014 and 2013, are not left as the figures reported under the entity's immediately previous accounting; in general, they are presented as though IFRS had always been applied. For example, if employee share options are not recognised as an expense under the previous accounting but are recognised as an expense under IFRS, it might look as though 2015 was less profitable than 2014 if comparatives are not restated, when in fact it might have been more profitable.

For pragmatic reasons, new accounting Standards sometimes include transition provisions permitting the new Standard, or specific parts of it, to be applied prospectively (rather than as though the new accounting policy had always been applied)—see IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.

An entity's first IFRS financial statements are the first annual financial statements in which the entity adopts IFRS, by an explicit and unreserved statement in those financial statements of compliance with IFRS.

Such transition provisions do not apply to entities adopting IFRS for the first time. However, adopting IFRS for the first time gives rise to many practical issues, including:

- how many years should an entity go back when restating its comparatives; for example, if it has made business acquisitions in most years during the past 20 years does it have to revisit the accounting for each of those business combinations to see whether the figures would be different under IFRS?
- where Standards allow entities a choice of accounting, but only if certain criteria are met, does the entity have to determine whether the criteria had been met at the relevant date in the past, which might be several years earlier, or could it make the determination at a later date such as upon adoption of IFRS for the first time?

Consequently, in order to provide a suitable starting point for IFRS accounting that can be generated at a cost that does not exceed the benefits, IFRS 1 specifies some mandatory exceptions, and some optional exemptions, from its general principle that a first-time adopter recognises and measures all assets and liabilities in its first IFRS financial statements as if it had always applied IFRS. For example, an entity may choose not to revisit the accounting for any business combinations that occurred before the start of the earliest comparative period presented. Alternatively it can choose a date, before the start of the earliest comparative period presented, and restate all business combinations occurring after this date. Another example is that an entity may elect to measure an item of property, plant or equipment at a previous revaluation (if it meets specified criteria for doing so) or at its fair value and use this as deemed cost. At the end of each summary, mandatory exceptions and/or optional exemptions pertinent to that Standard are summarised.

## IFRS 2

### Share-based Payment

#### The Standard

*IFRS 2 specifies the accounting treatment for purchases of goods or services paid for with the purchasing entity's shares, share options or other equity instruments, or those of another group entity, or with cash or other assets when the amount is based on the price of such shares.*

Common forms of share-based payment are share options awarded to employees and long-term incentive plans (LTIPs) in which shares or share appreciation rights (SARs) are given to employees. With SARs, employees receive cash equal to the increase in the share price over a specified period.

Before IFRS 2 some companies issuing share options to employees did not recognise an expense in profit or loss; instead, they simply recognised the share issue, when it occurred, in return for the share option exercise price. IFRS 2 clarifies that all goods or services acquired in share-based payment transactions, not merely employee remuneration (see below), are recognised as expenses or assets as appropriate. In addition, the transaction is recognised in equity if equity-settled, or as a liability if cash-settled or settled using other assets.

Goods or services received in equity-settled share-based payment transactions are measured at the fair value of the goods or services received. For example, if inventory is paid for by issuing shares, both the inventory acquired and the shares issued in exchange for the inventory are measured at the fair value of the inventory.

**Share options granted to employees are recognised as expenses in profit or loss.**

There is a rebuttable presumption that the fair value of the goods or services received can be estimated reliably. If the fair value of the goods or services received cannot be estimated reliably, the fair value of the equity instruments issued (shares, in the inventory example) is used as a proxy for the fair value of the goods or services received.

For employee services, and similar services, IFRS 2 acknowledges that it is difficult to estimate reliably the fair value of the employee services received by the entity in exchange for the share options, SARs, etc. Consequently, IFRS 2 requires the fair value of the equity instruments, for example, share options, to be used to estimate the fair value of employee services. As the employees provide services, the fair value is recognised as an expense in profit or loss, unless it qualifies to be capitalised as an asset; for example, as part of the cost of inventory. For employee and similar services, the fair value is measured at grant date. For all other transactions, whether measured by valuing the goods and services received or by valuing the equity instruments issued, the fair value is measured at the date the entity obtains the goods or as the other party renders the service.

Share options granted to employees as part of their remuneration package can often be exercised only if specified vesting conditions are met. For example, share options granted on Day 1 might be exercisable between Years 4 and 10 if the employee holding them remains employed with the company up to the date of exercise and if the company's profit for Years 1 to 3 exceeds a specified amount. In this example, the vesting conditions are not related to the price or value of the company's shares or those of another group company and so are not market conditions. If they had been market conditions, they would have been reflected in the fair value of the share options. In developing IFRS 2, the IASB took account of a number of practical concerns, one of which was the difficulty of reflecting non-market vesting conditions in measuring the fair value of equity instruments issued. Consequently, non-market vesting conditions are not reflected in the fair value of the instruments granted (options, in this example); the fair value is measured as though those vesting conditions did not exist. The resulting fair value will be higher than if those conditions were reflected in it. Consequently, to compensate, if the non-market vesting conditions are not met the Standard does not require an expense to be recognised.

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## IFRS 2

### Share-based Payment *continued*

For example, using the earlier example, if 50 share options were given to each of three employees and it was expected that the profit target would be met but that one of the employees would leave before the end of Year 3 (ie, before the options become exercisable), the expense would be recognised in Years 1 to 3. In Year 1 the expense would be one-third of the fair value of 100 share options, which is, the number of options expected to vest. If the expectations were unchanged, the same treatment would apply in Year 2. Alternatively, if in Year 2 it was expected that two of the employees would have left by the end of Year 3, the expense for Year 2 would be equal to two-thirds of the fair value of 50 options, less the amount that was recognised as an expense in Year 1. The expense is trued up each year for the number of options expected to vest. In Year 3 the expense is based on the number of options that actually vested as a result of the non-market vesting conditions. If the profit target had not been met, none of the share options would vest and would thus not be exercisable. Because this is a non-market vesting condition, there would be no expense for the share options, regardless of how many employees remained employed by the company. Any expense that had been charged to profit or loss in Years 1 and 2, on the expectation that the profit target would be met, would be reversed in Year 3.

If in the example, it was the company's share price, not its profit, that had to exceed a specified amount, the share price condition would be a market condition. This means that it has to be reflected when measuring the fair value of the share option and the resulting fair value will be lower than without the condition. There is therefore no further adjustment for *this* condition. Thus, if the share price condition was not met because the company's share price did not reach the specified amount, none of the share options would vest and be exercisable but, in contrast to the first employee example, an expense would be charged to profit or loss. Because there was also a service condition (the employee had to remain employed by the company), the expense relates to the options granted to the employees that remain employed by the company at the end of Year 3. For example, if only one of the three employees remained employed by the company at the end of Year 3, there is an expense for the 50 share options that would have vested if the share price had exceeded the specified target price.

Cash-settled share-based payments, for example, SARs, are measured at the fair value of the liability. The liability is remeasured at the end of each reporting period and at the date of settlement. Changes in the fair value of the liability are recognised in profit or loss. In contrast, equity-settled share-based payments are not remeasured.

In some cases, the entity or the other party may choose whether the transaction is settled in cash or by issuing equity instruments. The accounting treatment depends on whether the entity or the counterparty has the choice regarding settlement.

If the identifiable consideration received appears to be less than the fair value of the equity instruments granted or the liability incurred, then unidentifiable goods or services might have been received. These are measured by reference to the difference between the fair value of the equity instruments granted, or liability incurred, and the fair value of the goods or services received.

IFRS 3 *Business Combinations*, instead of IFRS 2, applies to equity instruments, eg shares, that are issued as consideration in a business combination. In addition, some contracts within the scope of IAS 32 and IAS 39 (or IFRS 9) are excluded from the scope of IFRS 2.

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## IFRS 3

### Business Combinations *continued*

Before an acquisition the employees in the acquired business might:

- (a) have been granted share options over shares in the acquired business;
- (b) be participating in a long-term incentive plan, which gives them rights to shares in the acquired business; or
- (c) hold some other share-based payment award, which gives them rights to shares in the acquired business. If the acquirer replaces those awards with new awards, for example, options over its own shares, careful consideration is required to determine whether all or part of the replacement award is part of the consideration paid for the business (and consequently affects the amount of goodwill, if any, recognised) or is post-acquisition employee remuneration (and consequently is recognised in profit or loss after acquisition).

### First-time adoption

For business combinations, there are no mandatory exceptions from the general principle in IFRS 1 *First-time Adoption of International Financial Reporting Standards*. However, a first-time adopter may, subject to specified conditions, elect not to apply IFRS 3 retrospectively to business combinations that occurred before the date of its transition to IFRS or, if it chooses, before an earlier date selected by the first-time adopter. Consequently, with limited exceptions, a first-time adopter may leave unchanged its accounting for business combinations that it recognised in accordance with its previous GAAP. Irrespective of any elections, the entity must test any goodwill in the opening IFRS statement of financial position for impairment.

## IFRS 4

### Insurance Contracts

### The Standard

*IFRS 4 specifies accounting for insurance contracts issued by any entity. It also specifies accounting for reinsurance contracts issued or held by an entity. The Standard applies to these contracts irrespective of whether the entity is regulated as an insurer and irrespective of whether the contract is regarded as an insurance contract for legal purposes.*

An insurance contract is a contract under which one party (the insurer) accepts significant insurance risk from another party (the policyholder) by agreeing to compensate the policyholder if a specified uncertain future event (the insured event) adversely affects the policyholder. Insurance risk excludes financial risk, eg the risk of changes in market prices or interest rates.

There are some scope exclusions in IFRS 4. For example, IFRS 4 does not apply to:

- product warranties issued directly by a manufacturer, dealer or retailer; and
- contingent consideration payable or receivable in a business combination.

IFRS 4 has been issued as a temporary measure to fill a gap in IFRS. It makes only limited improvements to accounting practices for insurance contracts, but introduces disclosure requirements about the contracts. In the absence of IFRS 4, entities would be required to account for insurance contracts following precedents in other Standards, and the definitions, recognition criteria and measurement concepts for assets, liabilities, income and expenses in the *Conceptual Framework*. For many entities, applying the other Standards and the *Conceptual Framework* would result in changes from the way in which they accounted for insurance contracts under their previous accounting before adopting IFRS.

In most respects, IFRS 4 allows an entity to continue to account for insurance contracts in terms of its previous accounting policies. The following are some of the limited improvements that the Standard makes to accounting for insurance contracts:

- Provisions for possible claims under contracts that are not in existence at the end of the reporting period (such as catastrophe provisions and equalisation provisions) are not permitted. They are not liabilities.
- The adequacy of insurance liabilities must be tested at the end of each reporting period. The liability adequacy test is based on current estimates of future cash flows. Any deficiency is recognised in profit or loss. Furthermore, reinsurance assets are tested for impairment.
- Insurance liabilities are presented without offsetting them against related reinsurance assets.
- Discretionary participation features (as found in with-profits and participating contracts) must be reported as liabilities or as equity (or split into liability and equity components). They may not be reported separately from liabilities and equity.

Some insurance contracts contain both an insurance component and a deposit component. In some cases the entity must 'unbundle' the components and account for them separately. This requirement is particularly relevant for long-term insurance products, for example, life insurance, and for reinsurance.

The IFRS restricts accounting policy changes. Any changes in accounting policies for insurance contracts must result in the financial statements being more relevant and no less reliable, or more reliable and no less relevant, than the previous accounting.

A significant review of accounting for insurance contracts is being considered by the IASB in Phase II of its project on insurance contracts. Meanwhile, an entity must not introduce, but may continue, the following practices:

- measuring insurance liabilities on an undiscounted basis;
- measuring contractual rights to future investment management fees at an amount that exceeds their fair value (as implied by current fees charged in the market);

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## IFRS 5

### Non-current Assets Held for Sale and Discontinued Operations *continued*

In the statement of profit or loss (or the statement of profit or loss section of the statement of profit or loss and other comprehensive income), all the line items, for example, revenue and cost of sales, are presented for continuing operations only and the result for discontinued operations is presented as a single item. The single item reported for discontinued operations is the sum of:

- the post-tax profit or loss from the discontinued operations; and
- the post-tax gain or loss on disposal of the discontinued operations or, if it has not been disposed of by the year-end, the impairment loss, if any.

An analysis of the single amount, showing revenue, expenses, pre-tax profit or loss, tax and the gain or loss on disposal or impairment loss, must be shown either in the notes or in the statement of profit or loss and other comprehensive income. The net cash flows attributable to the operating, investing and financing activities of the discontinued operations must be disclosed in the notes or presented in the statement of cash flows. Finally, the amount of income from continuing operations and from discontinued operations attributable to the owners of the parent must be disclosed separately.

#### Non-current assets and disposal groups held for sale

The discontinued operations requirements of the Standard focus on analysing the statement of profit or loss and other comprehensive income and the statement of cash flows, so that the results and cash flows from discontinued operations and from continuing operations can be identified. To complement this, the requirements about non-current assets and disposal groups classified as held for sale focus on analysing the assets and liabilities presented in the statement of financial position so that those held for sale can be readily identified and distinguished from all the other assets and liabilities.

A disposal group is defined more widely than discontinued operations. A disposal group is a group of assets, including goodwill if relevant, to be disposed of, by sale or otherwise, together as a group in a single transaction, and a group of liabilities directly associated with those assets that will be transferred in the transaction.

A disposal group is classified as held for sale if its carrying amount will be recovered principally through a sale transaction instead of through continuing use. This will be the case if it is available for immediate sale in its present condition, subject only to terms that are usual and customary for sales of such disposal groups, and if its sale is highly probable. Both the luxury sports car division and the headlight manufacturing subsidiary would be classified as disposal groups held for sale if not sold at 31 December 2015. Although a group that is being closed down, instead of being sold, can meet the definition of a discontinued operation in the period that it is closed down, it cannot be classified as a disposal group held for sale at the year-end prior to it being closed down (because it is not held for sale).

From the time it is classified as held for sale, a disposal group is measured at the lower of its carrying amount and its fair value less costs to sell. In addition, because the assets within the disposal group are expected to be recovered principally through sale (instead of being consumed through use) they are no longer depreciated. Any impairment loss is recognised immediately. In the statement of financial position the assets in the disposal group are presented in current assets separately from other assets. In addition, the liabilities are presented separately in current liabilities from other liabilities.

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## IFRS 5

### Non-current Assets Held for Sale and Discontinued Operations *continued*

Just as a disposal group to be sold is separately identified in the statement of financial position, so too is a single non-current asset that is classified as held for sale at the year-end. In the car manufacturing example, if the group had moved its head office function to a new building and was in the process of selling its former head office building at 31 December 2015, the former head office building would be moved to current assets in the statement of financial position, assuming various conditions were met. These conditions include that it is available for immediate sale in its present condition, subject only to terms that are usual and customary for sales of such assets and that a sale was expected within one year of classification as held for sale. The building would be depreciated until its classification changed to held for sale and it would thereafter be carried at the lower of its carrying amount and its fair value less costs to sell. As an asset held for sale, the building would be shown separately from other current assets in the statement of financial position, although it could be combined with the assets from a disposal group held for sale. Various conditions must be met in order to be classified as held for sale. For example, if the car manufacturing group decided to renovate its former head office in order to increase the sales proceeds, the building could not be classified as held for sale while the renovation works were ongoing, because the building would not be 'available for immediate sale in its present condition'.

The Standard contains similar guidance if an asset or disposal group is held for distribution rather than for sale.

#### Judgements and estimates

The classification of a disposal group or an asset as 'held for sale' is based on actions taken by management at or before the end of the reporting period and management's expectation and judgement that the disposal group or asset is available for immediate sale in its present condition and is being marketed at a reasonable price, and that a sale will be completed within a year of classification. The assessment of availability for immediate sale requires judgement of what represents usual and customary timing and other terms for the disposal. An entity may continue to use an asset that is held for sale, but must be able to cease using the asset immediately (subject only to usual and customary timing and closing conditions). Other judgements include:

- an assessment of the likelihood of obtaining shareholder approval when required;
- judging what constitutes sufficient evidence of management's commitment to sell; and
- determining whether the price is reasonable in relation to fair value.

Measuring assets held for sale requires measuring their fair value and estimating costs to sell. See IFRS 13 *Fair Value Measurement* for the judgements and estimates relating to the measurement of fair value.

Determining whether a component of an entity is a discontinued operation or part of continuing operations will be straightforward in many cases, but significant judgement will occasionally be needed. For example, if a major business segment is being broken up and the parts sold separately, significant judgement may be needed in determining whether there is a single co-ordinated plan to dispose of a separate major line of business or geographical area of operations.

#### First-time adoption

There are no specific mandatory exceptions or optional exemptions from the general principle in IFRS 1 *First-time Adoption of International Financial Reporting Standards* relevant to IFRS 5.

The results and cash flows from discontinued operations and from continuing operations must be presented separately. Assets and liabilities in a disposal group held for sale, and non-current assets held for sale, must be presented separately in the statement of financial position.

# IFRS 10

## Consolidated Financial Statements *continued*

An exception to the principle that all subsidiaries must be consolidated is provided for parents that are investment entities. An investment entity is an entity that: (a) obtains funds from one or more investors for the purpose of providing investment management services; (b) its business purpose is to invest funds solely for returns from capital appreciation, investment income, or both; and (c) measures and evaluates the performance of substantially all its investments on a fair value basis. A parent that is an investment entity measures its investments in its subsidiaries at fair value, with changes in fair value recognised in profit or loss for each period, unless that subsidiary is providing investment-related services that support its parent's investment activities, in which case the subsidiary is consolidated.

The disclosure requirements for subsidiaries are specified in IFRS 12 *Disclosure of Interests in Other Entities*.

Consolidated financial statements present financial information of a group (a parent and its subsidiaries) as a single economic entity.

### Judgements and estimates

Determining whether control exists requires an assessment of all relevant facts and circumstances, including an evaluation of the purpose and design of the investee, the activities of the investee, how decisions about those activities are made, and the rights held by the investor in the investee. This will often be a relatively straightforward assessment, eg when one investor owns more than 50 per cent of the voting rights of an investee and this ownership gives rise to control. In other cases, however, that assessment can require significant judgement.

The assessment of control can be particularly challenging for some structured entities, because the relevant activities in those entities are not usually directed by voting or similar rights. Furthermore, the benefits or returns expected from such investments can be more difficult to assess.

### First-time adoption

When a subsidiary becomes a first-time adopter earlier than its parent, or a parent adopts IFRS in its separate financial statements earlier than in its consolidated financial statements, the subsidiary's or parent's assets and liabilities are recognised in the consolidated financial statements at the same amounts they are recognised in the subsidiary's financial statements or parent's separate financial statements, except for any consolidation adjustments.

A first-time adopter applies specific requirements of IFRS 10 dealing with non-controlling interests and dealing with loss of control of a subsidiary only from its date of transition to IFRS, unless the first-time adopter elects to apply IFRS 3 to past business combinations, in which case it must also apply IFRS 10 retrospectively from the same date. The assessment of whether a first-time adopter that is a parent is an investment entity is on the basis of facts and circumstances at the date of transition. For accounting periods ending on or before 31 December 2014, investment entities may apply the particular temporary transition provisions relevant to such entities in their first IFRS financial statements.

### Recent developments

*Investment Entities: Applying the Consolidation Exception* (Amendments to IFRS 10, IFRS 12 and IAS 28) was issued by the IASB in December 2014 and is effective for annual reporting periods beginning on or after 1 January 2016, although it can be applied early. It clarifies the instances when an investment entity consolidates a subsidiary rather than accounts for it at fair value through profit or loss. If a subsidiary's main purpose and activities are to provide investment-related services that support its parent's investment activities, that subsidiary is consolidated only if it is not itself an investment entity.

# IFRS 11

## Joint Arrangements

### The Standard

IFRS 11 specifies the accounting for an interest in an arrangement that is jointly controlled.

Many entities collaborate with one or more other entities. For example, they may collaborate to undertake a construction project, such as building a road, to carry out research into a possible new product, or to manufacture items to be sold to third parties.

Although IFRS 11 may be the Standard that will apply to such collaborations, it will not always be the relevant Standard. For example, IFRS 10 *Consolidated Financial Statements* or IAS 28 *Investments in Associates and Joint Ventures* might instead apply.

To be within the scope of IFRS 11 an entity must be a party to an arrangement in which two or more parties have joint control, that is, the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control. The arrangement may be short- or long-term in nature.

To be a joint arrangement, more than one party must be able to veto decisions about relevant activities.

To be a joint arrangement, more than one party, but not necessarily all parties (see next page), must be able to veto decisions about relevant activities. However, having more than one party that can veto decisions does not automatically make the arrangement a joint arrangement. To be a joint arrangement, the right of veto has to be over decisions about relevant activities, that is, activities that significantly affect the returns of the arrangement. Some rights might be protective, such as the rights of a bank that has lent money to an entity, and might not be over decisions about relevant activities.

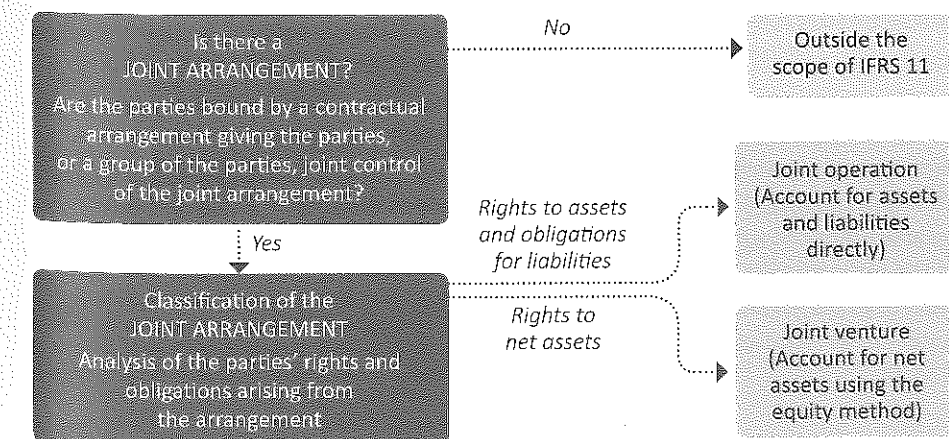
Joint arrangements are classified as either joint operations or joint ventures:

- *Joint operations* are joint arrangements in which the parties that have joint control (joint operators) have rights to the assets, and obligations for the liabilities, relating to the arrangement.
- *Joint ventures* are joint arrangements in which the parties that have joint control (joint venturers) have rights to the net assets of the arrangement.

The principle of the Standard is that a party to a joint arrangement recognises its rights and obligations arising from the arrangement.

A joint operator has rights to assets and obligations for liabilities, and is required to recognise those assets and liabilities and to account for the revenues and expenses relating to its interest in the joint operation (sometimes called 'gross accounting').

A joint venturer has rights only to net assets and accounts for those net assets, using the equity method (see IAS 28), as a single line item in its statement of financial position (sometimes called 'net accounting').



# IAS 1

## Presentation of Financial Statements

### The Standard

*IAS 1 sets out the overall requirements for the preparation and presentation of financial statements.*

IAS 1 is the cornerstone of financial statement preparation and presentation. It lays down the fundamental basics: what is in a complete set of financial statements; the underlying principles governing their preparation; minimum line items and requirements regarding overarching note disclosures; and the frequency of reporting. Other Standards specify the recognition, measurement and disclosure of specific transactions and events.

A complete set of financial statements, which should be presented, including comparatives, at least annually, comprises:

- a statement of financial position (sometimes called the balance sheet);
- either: a single statement of profit or loss and other comprehensive income; or two statements—a statement of profit or loss (sometimes called an income statement), and a statement of comprehensive income (starting with profit or loss and presenting income and expenses that are not recognised in profit or loss);
- a statement of changes in equity;
- a statement of cash flows; and
- notes, comprising a summary of significant accounting policies, significant management judgements, sources of estimation uncertainty and other explanatory information.

Financial statements must present fairly the entity's financial position, financial performance and cash flows. Fair presentation requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the *Conceptual Framework*. The application of the Standards, with additional disclosure when necessary, is presumed to result in financial statements that achieve a fair presentation.

In general, financial statements are prepared on a going concern basis, that is, assessing that the entity will continue in operation for the foreseeable future. IAS 1 requires financial statements to be prepared on a going concern basis unless management intends to, or has no realistic alternative but to, liquidate the entity or to cease trading. Financial statements are prepared using the accruals basis of accounting, for example, if goods are sold in one year but payment is not received until the subsequent year, the revenue, and profit, is recognised in the earlier year, because this is when the revenue and profit was earned.

In preparing financial statements, transactions are aggregated. However, IAS 1 specifies minimum line items to be presented, if they are material, in the statement of financial position, statement of profit or loss and other comprehensive income and statement of changes in equity. IAS 7 *Statement of Cash Flows* provides guidance on line items in the statement of cash flows. Additional items must be presented if they are relevant to understanding the entity's financial position and financial performance. Dissimilar items are presented separately, unless they are immaterial.

Items in other comprehensive income must be classified by nature and be grouped into those that will, and those that will not, be subsequently reclassified to profit or loss.

Assets and liabilities are classified as current or non-current, except when a presentation based on liquidity would provide information that is reliable and more relevant. In addition to cash and cash equivalents, items classified as current are: assets expected to be realised, used or sold and liabilities expected to be settled within the entity's normal operating cycle; held for trading; or expected to be realised or settled within twelve months after the reporting period. The classification is based on conditions at the end of the reporting period, and is not affected by events, such as refinancing, after that date.

*continued*

# IAS 1

## Presentation of Financial Statements *continued*

Financial statements are required to present fairly the financial position, financial performance and cash flows of the entity.

### Judgements and estimates

Management must assess whether the financial statements as a whole present fairly the financial position, financial performance and cash flows of the entity.

Management must assess the entity's ability to continue as a going concern. In some cases that assessment requires much judgement. If management determines that the going concern basis is appropriate, but there is nevertheless significant doubt about the entity's ability to continue as a going concern, IAS 1 requires disclosures to be given in the financial statements.

Management exercises judgement when assessing whether or not an item is material. An item is material if it could, individually or collectively, influence the economic decisions that users make on the basis of the financial statements. Materiality depends on the size and nature of the omission or misstatement, as judged after taking into consideration the surrounding circumstances. The size or nature of the item, or a combination of both, could be the determining factor.

Judgement is required in determining the best way to present information in financial statements. For example:

- Judging when to present additional line items, headings and subtotals in the primary financial statements depends on assessing when such presentation is relevant to an understanding of the entity's financial position, financial performance or cash flows.

- Judging whether to present an analysis of expenses recognised in profit or loss using a classification based on their nature, or instead basing the analysis on their function within the entity, depends on management's assessment of which presentation format provides information that is reliable and more relevant. An analysis of expenses by function can sometimes provide more relevant information to users than the classification of expenses by nature, but allocating costs to functions (eg cost of sales, distribution costs, administrative expenses) may require arbitrary allocations and involve considerable judgement.
- Judging whether to present current assets and current liabilities separately from non-current items, or whether to present assets and liabilities in order of their liquidity, depends on management's assessment of which presentation format provides information that is reliable and more relevant.
- Judgement is required to select the best way in which to present the financial statements; for example, determining the most appropriate order for the notes to the financial statements.

*continued*

# IAS 8

## Accounting Policies, Changes in Accounting Estimates and Errors *continued*

While undertaking repairs at the end of 2015, it detects a defect in a model released in 2014, which means that at the end of 2015 it expects to incur more costs in 2016 than originally expected. In preparing its 2015 financial statements, the entity increases the provision for warranty costs that it expects to incur in 2016 in respect of goods sold in 2014. This extra cost is recognised as an expense in calculating its 2015 profit or loss; the entity does not adjust the provision included in its 2014 comparatives.

Errors can arise from mistakes and oversights or misinterpretations of available information. Errors are corrected in the first set of financial statements issued after their discovery. Because an error relates to information that was available when preparing the financial statements for an earlier period, material errors are corrected by restating the comparative amounts, for the prior period(s) presented, as if the error had never occurred. The error and the effect of its correction on the financial statements are disclosed. For example, if during the preparation of the 2015 financial statements an entity discovers that in 2014 it had provided for the expected cost of warranty repairs for goods sold in 2014 twice in error, the amounts for 2014 included as a comparative in the 2015 financial statements would be adjusted if the error was material. That is, if the error was material, the correcting adjustment does not affect the 2015 profit or loss.

### Judgements and estimates

To a large extent, financial reports are based on estimates, judgements and models rather than being exact depictions. Consequently, the use of reasonable estimates is an essential part of the preparation of financial statements and does not undermine their reliability. Estimation involves judgements based on the latest available reliable information. Estimates will inevitably require adjusting. The effect of revising estimates made in the previous period's financial statements will therefore be reflected in current, and possibly future, periods.

In the absence of a Standard that specifically applies to a transaction, other event or condition, management exercises its judgement in developing and applying an accounting policy that results in information that is relevant and reliable.

**Aims to enhance the relevance and reliability of an entity's financial statements, and the comparability of those financial statements over time and with the financial statements of other entities.**

An entity may voluntarily change an accounting policy only if the change results in the financial statements providing reliable and more relevant information. Making that determination will in some cases require judgement. However, for some assets for which a choice of measurement models is available, for example, investment property, it is highly unlikely that a change from the fair value model to the cost model will result in more relevant information.

Judgements are also made in relation to the accounting for the correction of prior period errors. For example, an entity must determine if an error is material, because, if so, the entity must restate comparatives to correct that error. Materiality is not determined purely by size and can be highly reliant on judgement.

### First-time adoption

In essence, IFRS 1 *First-time Adoption of International Financial Reporting Standards* is a special version of IAS 8 dealing with changing accounting policies when adopting IFRS for the first time. However, the criteria in IAS 8 on selecting appropriate accounting policies apply to a first-time adopter in the same way as they apply to entities that adopted IFRS in an earlier reporting period.

# IAS 10

## Events after the Reporting Period

### The Standard

*Specifies which of the events that occur after the end of the reporting period affect the amounts included in the financial statements and which require only disclosure.*

**Dividends declared after the end of the reporting period are not recognised as a liability at the end of the reporting period.**

IAS 1 *Presentation of Financial Statements* requires a complete set of financial statements to be presented at least annually; for example, Entity A prepares financial statements for each 31 December financial year. Financial statements are authorised for issue some time after the end of the reporting period; in this example, mid-March. IAS 8 requires, among other things, that estimates are based on the latest available reliable information. Continuing with the example and using financial statements for the year ending 31 December 2015, IAS 10 sets out which of the events that occur after the end of a reporting period, for example, events occurring in February 2016, are reflected in amounts reported in the 2015 financial statements and which events are only disclosed in the 2015 financial statements (and affect the amounts recognised in the 2016 financial statements).

Events after the reporting period are events that occur between the end of the reporting period and the date the financial statements are authorised for issue.

Amounts reported in financial statements are adjusted for events after the reporting period that provide evidence of conditions that existed at the end of the reporting period; these are called adjusting events. An example of an adjusting event is the judgement, after the end of the reporting period, in a court case that relates to a customer claim made during the reporting period. Depending on the outcome, it will either confirm that the entity had a liability (present obligation) at the end of the reporting period, and if so, the amount of that liability, or confirm that the entity did not have a liability at the end of the previous reporting period. Another example of an adjusting event is the receipt of information that indicates that an asset was impaired at the end of the reporting period. For example, the bankruptcy of a customer that occurs after the end of the reporting period usually confirms that the trade receivable due from that customer at the end of the reporting period was not recoverable, or not recoverable in full. Similarly, the sale of inventories below cost after the reporting period may give evidence about their net realisable value at the end of the reporting period.

IAS 10 contains specific guidance on dealing with one particular adjusting event. It mandates that an entity must not prepare its financial statements on a going concern basis if management determines after the reporting period that it intends either to liquidate the entity or to cease trading, or that it has no realistic alternative but to do so. In this instance, events after the reporting period indicate that the going concern assumption is not appropriate.

In contrast, non-adjusting events reflect conditions that arise after the reporting period. Examples of non-adjusting events are changes in the market value of investments, and changes in currency exchange rates, after the reporting period. Reverting back to the post-year-end sale of inventory, if the inventory was silver ingots and the reason that the sale was below cost was that the market price of silver fell after the end of the reporting period, then the sale at below cost would not be an indication that the inventory was impaired and needed to be written down to its net realisable value at the end of the reporting period. The fall in market price, and the sale at below cost, would be a non-adjusting event.

*continued*

# IAS 12

## Income Taxes *continued*

**Example:** Interest receivable of CU100 recognised in Year 1, but cash not received until Year 2. Consequently, interest receivable of CU100 is carried as an asset in the statement of financial position at the end of Year 1. The applicable tax rate is 25 per cent. Is there a deferred tax liability at the end of Year 1?

	Scenario 1: interest is taxed when recognised in profit or loss	Scenario 2: interest is taxed when received
Interest income is included in taxable profits of Year 1?	✓	✗
Tax effect of interest is included in current tax for Year 1?	✓	✗
Does tax arise in Year 2?	✗	✓
Tax base at end of Year 1	CU100	nil
Temporary difference (= receivable of CU100 less tax base)	nil	CU100
Deferred tax (= temporary difference x 25%)	nil	CU25

A deferred tax asset can result from unused tax losses and tax credits as well as from temporary differences. Deferred tax assets, ie tax recoverable, can only be recognised if it is probable that there will be taxable profit available against which the tax losses, or other tax deductible items, can be utilised. The taxable profit can be available either in the future or, if carry-back of losses is allowed, in an earlier period. There are some specified exceptions to recognising deferred tax assets and deferred tax liabilities, for example, deferred tax is not recognised when goodwill is first recognised.

In jurisdictions where asset revaluations do not affect their tax base, that is, where the tax deductible amount is not similarly increased, deferred tax arises on the revaluation gain.

The tax rate that is used to compute deferred tax is the rate that is expected to apply when the tax is recovered or paid, based on tax rates and laws that have been wholly or substantively enacted by the end of the reporting period.

### Judgements and estimates

There are several aspects of accounting for income taxes that require management judgements and estimates. For example, deferred tax assets can be recognised only if it is probable that future taxable profit will be available to absorb tax losses or credits or other deductible differences. Consequently:

- Management must judge whether it is probable that taxable profit will be available against which a deductible temporary difference can be utilised. This can only happen if there are sufficient taxable temporary differences relating to the same taxation authority and the same taxable entity, which are expected to reverse: (a) in the same period as the expected reversal of the deductible temporary difference; or (b) in periods into which a tax loss arising from the deferred tax asset can be carried back or forward.
- When management judges that it is not probable that there will be sufficient taxable profit, as set out above, to utilise all the deferred tax asset, management must estimate the extent of the taxable profit as set out above or through tax planning opportunities available to the entity that will create taxable profit in appropriate periods.

*continued*

# IAS 12

## Income Taxes *continued*

- Furthermore, when an entity has a history of recent losses, additional judgement is required. Where there will not be sufficient taxable temporary differences to utilise the tax losses or other tax-deductible items, the Standard requires management to consider whether there is 'convincing other evidence' that there will be sufficient taxable profit available against which the unused tax losses or unused tax credits can be utilised by the entity. Disclosure of the amount recognised and the nature of the evidence supporting its recognition have to be disclosed.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply when the tax is recovered or paid. These rates are based on tax rates and laws that have been wholly or substantively enacted by the end of the reporting period, and that reflect the manner in which the entity expects, at the end of the reporting period, to recover (settle) the carrying amount of its assets (liabilities). This gives rise to a number of judgements and estimates, for example, when different tax rates apply in different periods and/or to different levels of taxable income, management must:

- forecast the period in which temporary differences are expected to reverse; and

- estimate the average rates that are expected to apply to the taxable profit (tax loss) of the periods in which the temporary differences are expected to reverse.

For some share-based payment transactions, the amount that the taxation authorities will permit as a deduction in future periods might not be known at the end of the period. Consequently, the tax base must be estimated, based on information available at the end of the reporting period.

### First-time adoption

Despite there being no specific mandatory exceptions or optional exemptions from the general principle in IFRS 1 *First-time Adoption of International Financial Reporting Standards* that apply to the requirements of IAS 12 for first-time adopters, a number of mandatory exceptions and optional exemptions might affect the carrying amount of recognised assets and liabilities and consequently affect the deferred tax balance recognised by an entity.

**Example:** Interest receivable of CU100 recognised in Year 1, but cash not received until Year 2. Applicable tax rate is 25 per cent.

The illustration shows that, regardless of when the interest is taxed, the tax effect is reflected in the financial statements in the same reporting period that the interest is recognised.

	Scenario 1: interest is taxed when recognised in profit or loss		Scenario 2: interest is taxed when received	
	Year 1	Year 2	Year 1	Year 2
Profit before tax (interest income)	100	-	100	-
Current tax	(25)	-	-	(25)
Deferred tax	-	-	(25)	25
<b>Profit after tax</b>	<b>75</b>	<b>-</b>	<b>75</b>	<b>-</b>

# IAS 18

## Revenue

### The Standard

*IAS 18 prescribes the accounting for revenue from the sale of goods, the rendering of services, and the use by others of entity assets yielding interest, royalties and dividends.*

Revenue is a subset of income (as defined in the *Conceptual Framework*). Revenue is an entity's gross earnings from its ordinary activities; for example, what it earns for selling goods to its customers or for providing services to them. If a company that sells new and used bicycles as well as renting out bicycles, sells one of its buildings because it moved to larger premises during the year, its revenue for that year would be from the sale of new and used bicycles and rental income from renting out the bicycles, but it would not include an amount for the sale of the land and building. This is because occasionally selling properties is incidental to the main revenue-generating activities. Amounts collected on behalf of third parties, such as sales taxes, are excluded from revenue. In general, revenue is recognised when it is probable that economic benefits from the transaction will flow to the entity and those benefits can be measured reliably.

Revenue is measured at the fair value of the consideration received or receivable by the entity. It is stated after reflecting any trade discounts and volume rebates allowed by the entity.

The Standard requires an entity to look at the substance of a transaction or series of transactions in order to identify when revenue should be recognised.

For example, an entity sells a piece of equipment and agrees to service that equipment for the two years immediately following the sale. The Standard requires the total revenue to be divided, with part recognised for the sale of the equipment and part recognised for the servicing contract. The revenue for selling the goods is likely to be recognised immediately, while the revenue for the servicing will be recognised over two years. In other scenarios, two or more separate transactions may need to be combined in order to identify the substance. For example, an agreement to sell goods, and a separate agreement to repurchase those goods, might in effect be a contract for the short-term hire of the goods, be a sale or return type agreement, be a loan with the goods acting as security, or be something else.

If loyalty points are awarded to a customer purchasing goods and the loyalty points can be redeemed for other goods in the future, the consideration received from the customer is allocated partly to the goods sold and partly to the loyalty points.

Revenue from the sale of goods is recognised when specified conditions are satisfied, including:

- significant risks and rewards of ownership of the goods have been transferred to the buyer; and

- the entity has neither continuing managerial involvement to the degree usually associated with ownership, nor effective control, over the goods.

For example, if goods are shipped subject to installation and inspection, when the installation and inspection are substantial, assuming all other conditions are met, revenue is not normally recognised until the installation and inspection are complete. This is because until then the significant risks and rewards of ownership are not generally regarded as having transferred to the buyer until this time. This would apply even in situations in which the entity has a long history of successful delivery and installation.

Revenue from the rendering of services is recognised as the work is performed if the outcome of the contract can be estimated reliably. This is commonly referred to as the 'stage of completion method'. For example, if a contract is 45 per cent complete, 45 per cent of the revenue is recognised. However, when the outcome of a service contract cannot be estimated reliably, revenue is recognised only to the extent of expenses recognised that are recoverable. Nevertheless, if it is not probable that the costs incurred will be recovered, no revenue is recognised even though the costs are recognised as expenses.

Interest is recognised over time, computed on the effective yield on the asset.

*continued*

# IAS 18

## Revenue *continued*

Royalties are usually recognised as they accrue in accordance with the terms of the relevant agreement unless, having regard to the substance of the agreement, it is more appropriate to recognise revenue on some other systematic and rational basis.

Dividends are recognised when the shareholder has the right to receive payment.

An exchange of similar goods or services does not give rise to revenue, because the transaction lacks commercial substance. For example, exchanging a quantity of a certain grade of oil in one location for the same quantity of the same grade of oil in a second location might simply be a practical expedient to be able to fulfil a contract to supply oil to a particular customer located in the second location. In this case the exchange transaction would not give rise to revenue. Only the transaction with the end customer would give rise to the recognition of revenue. An exchange of dissimilar items is regarded as having commercial substance; the resulting revenue is measured at the fair value of the goods or services received.

IAS 18 prescribes the accounting for revenue only from the sale of goods, the rendering of services, and the use by others of entity assets yielding interest, royalties and dividends. Other Standards prescribe how to account for other revenue. For example, IAS 11 *Construction Contracts* specifies accounting for revenue associated with construction contracts.

Determining whether an agreement for the construction of real estate is within the scope of IAS 11 or IAS 18 depends on the terms of the agreement and all the surrounding facts and circumstances. If the buyer can specify the major structural elements of the design of the real estate before construction begins, and/or can specify major structural changes once construction is in progress, the contract will be within the scope of IAS 11.

### Judgements and estimates

Management exercises judgement when identifying separate components of a multiple element sale and in allocating the consideration received, or to be received, to the components. Management also exercises judgement in determining the timing of the recognition of the resulting revenues.

Judgement and estimation may also be necessary when determining the appropriate fair value of the consideration received or receivable.

Determining when the criteria for the recognition of sale or service revenue are first satisfied can be challenging in some cases. Examples of circumstances in which the timing of recognition of revenue requires careful consideration include: sales with delayed delivery; sales subject to conditions including installation and inspection and right of return; sale and repurchase agreements; consignment sales; sales to others for resale; multiple element contracts; subscriptions for products or fees for

services delivered in parts over time; sales of products with an agreement to provide future services; barter transactions, including capacity swaps; commitment fees received to make a loan; and franchise fees.

Determining the percentage of completion of a service contract may require judgement, as does assessing whether the outcome of the contract can be estimated reliably.

Revenue is measured at the fair value of the consideration received or receivable.

### First-time adoption

There are no specific mandatory exceptions or optional exemptions from the general principle in IFRS 1 *First-time Adoption of International Financial Reporting Standards* that apply to the requirements of IAS 18 for first-time adopters.

### Recent developments

IFRS 15 *Revenue from Contracts with Customers* was issued by the IASB in May 2014 and is effective for annual reporting periods beginning on or after 1 January 2017, although it can be applied early. IFRS 15 replaces IAS 11 and IAS 18. A summary of IFRS 15 and recent developments is included in the Appendix.

# IAS 20

## Accounting for Government Grants and Disclosure of Government Assistance *continued*

### Judgements and estimates

Accounting for government grants requires several judgements and estimates. For example, managers must decide when a grant first satisfies the criteria to be recognised, which requires reasonable assurance that the specified conditions attached to the grant will be met.

It is necessary to determine the costs for which the grant is intended to compensate and the periods in which these costs are expected to be recognised as an expense. This is because IAS 20 requires a grant to be recognised in profit or loss on a systematic basis over the periods in which an entity recognises as expenses the costs that the grant is intended to compensate. For example, the benefit of a below-market rate of interest government loan, that is, the grant, might not be allocated to profit or loss consistent with the interest expense because the conditions might make it clear that the costs that the grant relates to are specific operational costs. A number of conditions might be attached to one grant and it might be necessary to allocate part of a grant on one basis and part of the grant on another basis.

**Unfulfilled conditions and other contingencies relating to grants that have been recognised must be disclosed.**

Judgement may be required to measure the fair value and the 'useful life' of a non-monetary grant, such as a piece of specialised equipment.

In order to determine the fair value of a government loan at a below-market rate of interest, an entity would need to determine the market rate of interest for a similar debt (in order to use this as a discount rate). This may be difficult and may require estimating if there is no published information for similar debts; for example, if the debt has unusual features or is for a long or undefined term.

### First-time adoption

There are no specific mandatory exceptions or optional exemptions from the general principle in IFRS 1 *First-time Adoption of International Financial Reporting Standards* that apply to the requirements of IAS 20 for first-time adopters.

# IAS 21

## The Effects of Changes in Foreign Exchange Rates

### The Standard

*IAS 21 prescribes how to determine an entity's functional (or measurement) currency; how to account for foreign currency transactions and foreign operations; and how to translate financial statements into a presentation currency.*

The Standard requires each entity to determine its functional currency and to measure the items in its financial statements in that currency, although the financial statements may be presented in a different currency—see below. An entity's functional currency is the currency of the primary economic environment in which it operates. IAS 21 lists a number of indicators that must be considered by an entity when determining its functional currency. One of the key indicators listed is the currency that mainly influences the pricing of the entity's goods or services. While this may often be the currency the goods and services are priced in, it is not necessarily so. The currency that mainly influences the entity's costs is another primary indicator of its functional currency.

Transactions in a currency other than the functional currency are translated into the functional currency using the spot exchange rate on the date the transaction qualifies for recognition (the transaction date rate). For example, an entity whose functional currency is CU purchases a specialist machine from an overseas company for FCU1,000<sup>3</sup>, first recognising it on 1 December. The machine and the account payable will be recognised by translating the amount using the spot rate on 1 December.

If the entity's year-end is 31 December and the entity does not pay the machine manufacturer until January, the account payable will be in the entity's statement of financial position at 31 December. Similarly, if the machine has a useful life of 10 years, it too will be in the entity's statement of financial position at 31 December. When items denominated in a foreign currency are still recognised at the end of a reporting period in the statement of financial position, the approach to the translation of the items depends on whether the items are monetary or non-monetary items:

- Foreign currency monetary assets and liabilities (those for which an entity expects to receive or pay a fixed or determinable amount of currency) are retranslated using the spot exchange rate at the end of the reporting period (the closing rate). The resulting exchange differences are recognised as income or expense in the period. In the example above, the liability to pay the machine manufacturer is a monetary item and will be retranslated using the exchange rate at 31 December. The difference from the previous carrying amount will be recognised as income or an expense in profit or loss.

- Non-monetary items are not retranslated at the year-end. They are recognised in the statement of financial position translated using the applicable rate at the date the original cost, or subsequent fair value, was measured. In the example above, if the machine has a nil residual value and a useful life of 10 years, it will be translated into the entity's functional currency using the exchange rate on 1 December and the resulting amount will be recognised as depreciation expense over the 10 years. It will not be retranslated unless it is impaired or revalued using IAS 16's revaluation model and the recoverable amount or valuation is measured in a currency other than the entity's functional currency. In this case, the new carrying amount (recoverable amount or valuation) will be translated at the exchange rate on the date of measurement; subsequent depreciation will be based on this revised amount.

<sup>3</sup> 'FCU' means 'foreign currency units'.

# IAS 24

## Related Party Disclosures

### The Standard

IAS 24 requires disclosures about the existence of specific types of related parties and about transactions and outstanding balances with any related party.

Related party relationships are a normal feature of commerce and business. An entity's profit or loss and financial position may be affected by a related party relationship even if related party transactions do not occur; the mere existence of the relationship may be sufficient to affect transactions between the entity and other parties. On the other hand, related parties may enter into transactions that would not be undertaken by unrelated parties. IAS 24 aims to ensure that financial statements contain the disclosures necessary to draw attention to the possibility that the entity's financial position and profit or loss might have been affected by the existence of related parties and by transactions and outstanding balances with such parties.

A related party is a person or an entity that is related to the reporting entity, that is, a person or an entity that is related to the entity that is preparing its financial statements. The Standard lists some specific relationships that meet the definition of related party—see the two tables on this page.

'Key management personnel' is a defined term meaning those persons having authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly, including any director of that entity.

The Standard requires the substance, and not merely the legal form, of a relationship to be considered.

A person or a close member of that person's family is related to a reporting entity if that person:
<ul style="list-style-type: none"> <li>has control or joint control of, or significant influence over, the reporting entity; or</li> <li>is a member of the key management personnel of the reporting entity or its parent.</li> </ul>

An entity is related to a reporting entity when:
<ul style="list-style-type: none"> <li>they are both members of the same group;</li> </ul>
<ul style="list-style-type: none"> <li>one entity is an associate or joint venture of the other entity or of another entity in the same group as the other entity;</li> </ul>
<ul style="list-style-type: none"> <li>both entities are joint ventures of the same third party;</li> </ul>
<ul style="list-style-type: none"> <li>one entity is a joint venture of a third party and the other is an associate of the third party;</li> </ul>
<ul style="list-style-type: none"> <li>the entity is a post-employment benefit plan for the benefit of employees of the reporting entity or an entity related to the reporting entity;</li> </ul>
<ul style="list-style-type: none"> <li>the entity is controlled or jointly controlled by any person identified as a related party in the other table;</li> </ul>
<ul style="list-style-type: none"> <li>a person with control or joint control over the reporting entity, or a close member of that person's family, has significant influence over the entity or is a member of the key management personnel of the entity or of the entity's parent; or</li> </ul>
<ul style="list-style-type: none"> <li>the entity, or any member of a group of which it is a part, provides key management personnel services to the reporting entity or to the reporting entity's parent.</li> </ul>

Within a group, each parent, subsidiary and fellow subsidiary is related to the others. Simply having a director in common with another company does not, of itself, make the two companies related.

Similarly, merely lending money to a company does not, of itself, make the company and lender related parties, even though the terms of the loan agreement may affect the freedom of action of the company.

*continued*

# IAS 24

## Related Party Disclosures *continued*

Disclosure is required of:

- the name of the reporting entity's parent and, if different, its ultimate controlling party, irrespective of whether there have been transactions between them;
- if neither of the above parties produces consolidated financial statements available for public use (for example, if the first is exempt from producing consolidated financial statements and the second is an individual) the name of the first parent that is above the immediate parent that does so; and
- details of key management personnel compensation in total and by category of benefit, for example, share-based payment would be disclosed separately from short-term employee benefits.

When there are transactions with related parties during the periods covered by the financial statements, that is, the current period and any comparative periods presented, disclosure is required, by category of related party, of:

- the nature of the related party relationship; and
- details of the transactions and outstanding balances, including commitments, to enable users to understand the potential effect of the relationship on the financial statements, including disclosure of the transaction amount and any bad debt expense recognised during the period.

The Standard provides a partial exemption from the disclosure requirements if the related party is:

- a government that has control, joint control or significant influence over the reporting entity; or
- another entity that is a related party because the same government has control, joint control or significant influence over both the reporting entity and the other entity.

Other specified disclosures are required when the partial exemption applies.

When an entity (the 'management entity') provides key management personnel services to the reporting entity, the fee that the reporting entity pays to the management entity is disclosed as a transaction with a related party. The compensation paid by the management entity to the key management personnel is excluded from the details of key management personnel compensation disclosure required by IAS 24.

**In considering each related party relationship, the substance, and not merely the legal form, of the relationship must be considered.**

### Judgements and estimates

In some cases determining whether a person or an entity is a related party of the reporting entity requires significant judgement. For example, the decision might require assessing the degree of influence exerted by one party over another—is it control, joint control, significant influence or a lower degree of influence? Similarly, in some cases, assessing whether an individual is a close member of the family of a person (for example, of a director of the reporting entity) requires judging whether that individual may be expected to influence, or to be influenced by, that person (in the example, the director) in their dealings with the reporting entity.

When disclosing information about related party transactions, judgement is required to determine the extent to which related party disclosures are disaggregated.

### First-time adoption

There are no specific mandatory exceptions or optional exemptions from the general principle in IFRS 1 *First-time Adoption of International Financial Reporting Standards* that apply to the requirements of IAS 24 for first-time adopters.

## IAS 29

Financial Reporting in Hyperinflationary Economies *continued*

At 31 December 2014 the property was carried at its cost of HCU100,000 and the company had cash at bank of HCU900. The 2014 figures, although presented in the 2014 financial statements as HCU100,000 and HCU900 respectively, will be presented as HCU140,000 and HCU1,260 when they are comparatives to the 2015 figures, that is, both are increased by 40 per cent as they need to be expressed in terms of purchasing power at 31 December 2015.

The gain or loss on restating the 2014 net monetary items for the change in purchasing power over 2015 is recognised in the 2015 profit or loss and separately disclosed. Using the example above, and assuming that the entity had no other monetary assets and had no monetary liabilities, the loss on restating the net monetary items to be recognised in its 2015 profit or loss would be HCU360 (the adjustment in respect of the cash).

Restatement cannot be avoided by electing to use a stable currency for measurement purposes, because an entity determines its functional currency; it cannot select a functional currency.

The gain or loss on restating the prior period's (eg 2014) net monetary items for the change in purchasing power over the reporting period (eg 2015) is recognised in the reporting period's (eg 2015) profit or loss and separately disclosed.

2014:	Per published	Adjustment	For inclusion
	2014 financial	(increase	in 2015
	statements	by 40%)	financial
	HCU	HCU	HCU
Property—cost	100,000	40,000	140,000
Property—accumulated depreciation	—	—	—
Property—net book amount	100,000	40,000	140,000
Cash	900	360	1,260
	100,900	40,360	141,260

The Standard requires a number of disclosures, including: the fact that the figures for the current and comparative periods have been restated for changes in the general purchasing power of the functional currency; the price index used for the restatement; its level at the end of the reporting period; and the change in the index during the current period and during the comparative period.

After restatement in accordance with this Standard, the financial statements may be presented in any other currency by translating the results and financial position in accordance with IAS 21, because an entity does have a free choice for its presentation currency.

### Judgements and estimates

Because IAS 29 does not establish an absolute rate at which hyperinflation is deemed to arise, it is a matter of judgement when the restatement of financial statements in accordance with this Standard becomes necessary. In making that judgement all facts and circumstances must be considered.

*continued*

## IAS 29

Financial Reporting in Hyperinflationary Economies *continued*

Whether or not a country is considered to be experiencing hyperinflation will normally be determined on a countrywide basis, for example, by an agreement of the accounting profession, not by an individual entity.

It is preferable that all entities that report in the currency of the same hyperinflationary economy apply this Standard from the same date.

When multiple price indices are available, the entity must restate its financial statements using a general price index that reflects changes in general purchasing power. Identifying the appropriate general price index may, in some cases, require judgement.

### First-time adoption

There are no specific mandatory exceptions from the general principle in IFRS 1 *First-time Adoption of International Financial Reporting Standards* that apply to the requirements of IAS 29 for first-time adopters.

However, there is a non-mandatory exemption for entities whose functional currency was subject to 'severe hyperinflation' before the date of transition to IFRS. IFRS 1 introduces the term severe hyperinflation and states that a currency is subject to severe hyperinflation if a reliable general price index is not available to all entities with transactions in the currency, and exchangeability between the currency and a relatively stable foreign currency does not exist. When an entity's date of transition to IFRS is on or after the date that severe hyperinflation ceases (the 'normalisation date'), the entity may elect to measure all assets and liabilities held before the normalisation date at fair value on the date of transition and treat this as the deemed cost of those assets and liabilities.

# IAS 34

## Interim Financial Reporting

### The Standard

*An interim financial report is a complete or condensed set of financial statements for a period shorter than a full financial year.*

Neither IAS 34 nor any other Standard requires the publication of an interim financial report. However, securities regulators or other authorities to which particular entities are subject often require the publication of interim financial reports at specified intervals, for example, half-yearly or quarterly.

IAS 34 applies if an entity publishes an interim financial report in accordance with IFRS, whether because it is required to do so or because it chooses to voluntarily do so. The Standard prescribes the minimum content and specifies the accounting recognition and measurement principles applicable to an interim financial report.

Minimum content of an interim financial report (the example dates assume an entity with a 31 December year-end that reports quarterly and is reporting for the three months to 30 September 2015):

	As at end of interim period (eg at 30.09.15)	As at end of preceding full year (eg at 31.12.14)
Condensed statement of financial position	✓	✓
	For interim period* (eg 3 months to 30.09.15)	For current year to date* (eg 9 months to 30.09.15)
Condensed statement(s) of profit or loss and other comprehensive income	✓	✓
Condensed statement of changes in equity		✓
Condensed statement of cash flows		✓
Selected explanatory notes	Generally, year-to-date	

\* Comparatives are required for the equivalent period in the preceding year

The condensed statements should include, as a minimum, each of the headings and subtotals that were included in the entity's latest full-year financial statements. For example, an entity's condensed statement of financial position should include as a minimum the headings and subtotals that were included in its full year statement of financial position. IAS 34 specifies note disclosures that should be included in the interim financial reports. Additional line items or notes are required if their omission would make the interim financial statements misleading.

The same accounting policies are applied in the interim report as in the most recent annual financial statements, subject to any changes in accounting policy that are to be reflected in the financial statements for the full year.

The Standard prescribes that the frequency of an entity's interim reporting, half-yearly, quarterly, etc, should not affect the measurement of its full year results. Consequently, measurements for interim reporting are to be made on a year-to-date basis. This does not mean that results for the first six months of a year should be half of the anticipated full year results. The interim report for the first six months should reflect the transactions that arose in that six months. If a company's business is seasonal, those transactions could be much higher or lower than half those expected for the full year.

*continued*

# IAS 34

## Interim Financial Reporting *continued*

However, IFRIC 10 *Interim Financial Reporting and Impairment* clarifies that entities must not reverse an impairment loss recognised in a previous interim period in respect of goodwill. If income tax is calculated by the tax authorities on the results for the full year, the charge in the interim results is calculated using the best estimate of the weighted average annual income tax rate expected for the full year. If the interim results are consolidated results, a tax rate is estimated for each jurisdiction in which the group operates and the average applied to the interim results for that jurisdiction, instead of making one estimate for the group as a whole.

Disclosures required in interim financial reports include: commentary about the seasonal or cyclical nature of the operations; issues, repurchases and repayments of debt and/or equity; dividends paid; and, if significant, commitments to purchase property, plant and equipment, litigation settlements and related party transactions.

IAS 34 requires one disclosure to be made in the full year financial statements. If an estimate that is used in one interim period, say, in the interim financial report for the six months to 30 June 2015, is changed significantly during the final interim period of a financial year, say, in the six months to 31 December 2015, and an interim financial report is not published for that final period, IAS 34 requires the nature and amount of the change in estimate to be disclosed in the financial statements for the year; in the example, the year to 31 December 2015.

The frequency of an entity's interim reporting should not affect the measurement of its full year results. Consequently, measurements for interim reporting are to be made on a year-to-date basis. However, IFRIC 10 clarifies that entities must not reverse an impairment loss recognised in a previous interim period in respect of goodwill.

### Judgements and estimates

While measurements in both annual financial statements and interim financial reports are often based on reasonable estimates, the preparation of interim financial reports will generally require a greater use of estimates than annual financial statements; for example, estimating the weighted average annual income tax rate expected for the full year, in order to measure the tax charge, is necessary for interim financial reports but not for full year financial statements.

### First-time adoption

An entity is required to apply IFRS 1 *First-time Adoption of International Financial Reporting Standards* in each interim financial report that it prepares in accordance with IAS 34 for part of the period covered by its first IFRS financial statements. In addition to the requirements of IAS 34, IFRS 1 requires additional disclosures in the interim financial report, for example, reconciliations between the entity's previous accounting and IFRS.