

2. GENERAL ISSUES

2.1 Form and components of financial statements

CURRENTLY EFFECTIVE REQUIREMENTS

This publication reflects IFRS in issue at 1 August 2017, and the currently effective requirements cover annual periods beginning on 1 January 2017.

The requirements related to this topic are derived from the following.

STANDARD	TITLE
IFRS 10	Consolidated Financial Statements
IFRS 11	Joint Arrangements
IAS 1	Presentation of Financial Statements
IAS 27	Separate Financial Statements
IAS 28	Investments in Associates and Joint Ventures

FORTHCOMING REQUIREMENTS

For this topic, there are no forthcoming requirements.

FUTURE DEVELOPMENTS

This topic is subject to future developments that may affect several aspects of the presentation and disclosure of information in financial statements. See 2.1.140.

2.1.10 COMPONENTS OF FINANCIAL STATEMENTS

2.1.10.10 The following comprise a complete set of financial statements:

- a statement of financial position (see chapter 3.1);
- a statement of profit or loss and OCI, presented either:
 - in a single statement that includes all components of profit or loss and OCI in two separate sections; or
 - in the form of two separate statements, one displaying components of profit or loss immediately preceding another statement beginning with profit or loss and displaying components of OCI (see chapter 4.1);
- a statement of changes in equity (see chapter 2.2);
- a statement of cash flows (see chapter 2.3);
- notes, comprising significant accounting policies and other explanatory information;
- a statement of financial position as at the beginning of the preceding period when an entity restates comparative information following:
 - a change in accounting policy;
 - a correction of an error; or
 - a reclassification of items in the financial statements (see 2.1.20); and
- comparative information in respect of the preceding period (see 2.1.50). [IAS 1.10–10A]

2.1.10.20 The statements presented outside the notes to the financial statements are generally referred to as 'financial statements' in IAS 1. In this chapter, those financial statements are described when necessary as 'primary financial statements' to distinguish them from the financial statements as a whole. Although IAS 1 provides the titles for the primary financial statements as outlined in 2.1.10.10, which we use throughout this publication, those titles are not mandatory. [IAS 1.BC21]

2.1.10.25 All financial statements within a complete set of financial statements are presented with equal prominence. [IAS 1.11]

2.1.10.30 IFRS specifies disclosures to be made in the financial statements (see 2.1.10.80). However, it does not prescribe specific formats to be followed. In our experience, entities consider the presentation adopted by other entities in the same industry or country.

2.1.10.40 Although a number of disclosures are made in the primary financial statements, IFRS generally allows flexibility in presenting additional line items and subtotals when they are necessary to ensure a fair presentation (see 3.1.10 and 4.1.10). In addition to the information required to be disclosed in the financial statements, many entities provide additional information outside the financial statements, either voluntarily or because of local regulations or securities exchange requirements (see chapter 5.8). [IAS 1.13, 54–55A, 82–85B]

2.1.10.50 Notes to the financial statements are presented, to the extent practicable, in a systematic manner but not necessarily in a prescribed order and are cross-referenced from items in the primary financial statements. [IAS 1.113]

2.1.10.60 In determining a systematic manner of presentation, an entity considers the effect on the understandability and comparability of the financial statements. For example, notes to the financial statements may be presented or grouped in the following ways:

- giving prominence to the areas of the entity's activities that it considers to be most relevant to an understanding of its financial performance and financial position, such as grouping together information about particular operating activities;
- grouping together information about items measured similarly, such as assets measured at fair value; or
- following the order of the line items in the primary financial statements (see 2.1.10.70). [IAS 1.113–114]

2.1.10.70 If an entity follows the order of the line items in the primary financial statements, then the notes are generally presented in the following order:

- a statement of compliance with IFRS;
- the basis of preparation;
- other significant accounting policies applied;
- supporting information for items presented in the primary statements, in the order in which each statement and each line item is presented; and
- other disclosures, including contingencies, commitments and non-financial disclosures. [IAS 1.112–117]

2.1.10.80 Disclosures that are not material need not be provided in a set of financial statements, even if IFRS contains a list of specific requirements or describes them as minimum requirements (see 1.2.18). [IAS 1.31, BC30H–BC30I]

2.1.20 Third statement of financial position and related notes

2.1.20.10 A third statement of financial position is presented as at the beginning of the preceding period following a retrospective change in accounting policy, the correction of an error or a reclassification that has a material effect on the information in that statement of financial position. [IAS 1.10(f), 40A]

2.1.30 Materiality considerations

2.1.30.10 When interpreting the requirement to present a third statement of financial position, in our view an entity should consider materiality based on its particular facts and circumstances. An assessment of materiality requires consideration of the effect of retrospective application of the relevant accounting policy, retrospective restatement or reclassification on the information in the statement of financial position as at the beginning of the preceding period. For example, an entity may have previously presented its obligation for post-employment benefits entirely as non-current as allowed by IAS 19 (see 4.4.1090). If the entity subsequently decides to split the amount into current and non-current components in the statement of financial position, then it restates the comparatives. In this case, to the extent that the effect of the reclassification is material to the statement of financial position as at the beginning of the preceding period, a third statement of financial position would be required (see 2.8.130.20). [IAS 1.40A, 19.133]

2.1.40 Presentation

2.1.40.10 The third statement of financial position relates to the beginning of the preceding period. Therefore, as a minimum, a statement of financial position will be presented for the following dates:

- the end of the current reporting period;

- the end of the preceding reporting period; and
- the beginning of the preceding reporting period. [IAS 1.40B]

2.1.40.20 The third statement of financial position is not required in condensed interim financial statements (see 5.9.30.22). [IAS 1.BC33]

2.1.40.30 When an entity presents additional comparative information (see 2.1.70), the date of the third statement of financial position is required to be the beginning of the preceding period regardless of the earlier periods covered by the additional comparative information. [IAS 1.40D]

2.1.40.40 If an entity presents an additional comparative statement of financial position identical to the third statement of financial position that would otherwise be required, then it does not need to present the same statement of financial position twice. However, this fact is disclosed.

EXAMPLE 1 – THIRD STATEMENT OF FINANCIAL POSITION – ADDITIONAL COMPARATIVE INFORMATION



2.1.40.50 Company C usually includes an additional comparative statement of financial position and statement of profit or loss and OCI in its annual financial statements. During the reporting period ended 31 December 2017, C discovers a material error in respect of the depreciation of property, plant and equipment. The correction of the error will have a material effect on the statement of financial position at 1 January 2016. C's financial statements for 2017 will therefore include:

- a statement of financial position at 31 December 2017; and
- comparative statements of financial position at 31 December 2016 and 31 December 2015.

2.1.40.60 Because the statement of financial position at 31 December 2015 would be identical to the statement of financial position at 1 January 2016, C need not present the same statement of financial position twice. This fact could be indicated in various ways; for example, C could provide a note or specifically label the additional comparative statement of financial position – i.e. 31 December 2015/1 January 2016.

2.1.40.70 When an entity presents a third statement of financial position, it is not required to present the related notes. However, it includes the explanatory disclosures required by paragraphs 41–44 of IAS 1 and IAS 8. [IAS 1.40C, 41–44, BC32C]

2.1.40.80 For a discussion of the requirement to present a third statement of financial position and related notes for first-time adopters of IFRS, see 6.1.1540.

2.1.50 Comparative information

2.1.60 Minimum comparative information

2.1.60.10 Comparative information is required for the immediately preceding period. Unless there is a specific exemption provided in an IFRS, an entity presents comparative information in

respect of the preceding period for all amounts reported in the current period's financial statements. The preceding period's related narrative and descriptive information is generally required only if it is relevant to understanding the current period's financial statements. For example, comparative segment information would be disclosed. [IAS 1.38]

2.1.60.20 No particular format is required for the presentation of comparatives. In our experience, most entities reporting under IFRS provide comparative information about the immediately preceding period alongside that for the current period.

2.1.60.30 When an entity is adopting IFRS for the first time, the required comparatives are prepared in accordance with IFRS (see 6.1.20.30–40). [IFRS 1.7, 21]

2.1.70 Additional comparative information

2.1.70.10 More extensive comparatives may be presented voluntarily or to meet regulatory – e.g. securities exchange – requirements. Such additional comparative information and related notes need to comply with IFRS. However, it need not comprise a complete set of financial statements. [IAS 1.38C–38D]

2.1.70.20 When an entity is adopting IFRS for the first time, any additional comparatives included in the financial statements need not comply with IFRS provided that those comparatives are labelled clearly and explanatory disclosures are included (see 6.1.1540.10). [IFRS 1.22]

2.1.80 REPORTING PERIOD

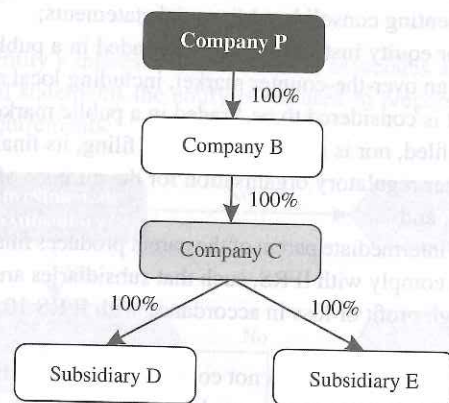
2.1.80.05 A number of terms are used, either in the literature or in practice, to describe the end of an entity's financial year, including 'reporting date', 'end of the reporting period', 'statement of financial position date', 'year end' and 'financial year end'. Generally, these terms are used interchangeably and have the same meaning. This publication consistently uses the term 'reporting date' throughout, which refers to the end of the reporting period and does not refer to the date on which the financial statements are prepared, authorised for issue, made public or filed.

2.1.80.10 The annual reporting date may change in certain circumstances – e.g. following a change of major shareholder or because of regulatory or taxation requirements. If the annual reporting date does change, then the financial statements for that period will cover either more or less than 12 months. In this case, the entity discloses the reasons for using a longer or shorter period and the fact that information in the financial statements is not fully comparable. In addition, pro forma information for the comparable preceding reporting period might be presented (see 2.1.130). [IAS 1.36]

2.1.80.20 IFRS is silent on the approach to take when a subsidiary changes its annual reporting date to align it with that of the parent. In our view, the consolidated financial statements should include the results of the subsidiary from its last reporting date to its new reporting date. Therefore, the subsidiary's results included in the consolidated financial statements might cover a period of either more or less than 12 months (see 2.5.440).

EXAMPLE 2 – EXEMPTION FROM PREPARING CONSOLIDATED FINANCIAL STATEMENTS

2.1.100.80 Company B is an intermediate parent of Company C, and B is owned by Company P, the ultimate parent. C has subsidiaries.



2.1.100.90 C is not required to prepare consolidated financial statements if the following conditions are met:

- either P or B prepares consolidated financial statements in accordance with IFRS and those consolidated financial statements are available to the users of the financial statements of C;
- C's debt or equity instruments are not traded in a public market, including stock exchanges and over-the-counter markets; and
- C has not filed, and is not in the process of filing, its financial statements with a regulatory organisation for the purpose of issuing any class of instruments in a public market. [IFRS 10.4(a)]

2.1.100.100 In our view, if an entity disposes of its last subsidiary during the current reporting period, then consolidated financial statements are not required to be prepared because the entity is no longer a parent at the reporting date. In such cases, we believe that the financial statements, including comparatives, should be presented as unconsolidated financial statements – i.e. individual or separate financial statements as appropriate (see 2.1.110 and 120, respectively) – unless the consolidated financial statements are required by a regulator. However, the entity may wish to present supplementary information on a consolidated basis (see chapter 5.8).

2.1.110 Individual financial statements

2.1.110.10 Although the term is not formally defined in IFRS, individual financial statements are those of an entity that has no subsidiaries and either:

- has investments in associates and/or joint ventures that are equity accounted – i.e. the entity does not use any exemption from equity accounting (see 2.1.110.20); or
- has neither an investment in an associate nor a joint venturer's interest in a joint venture. [IFRS 11.24, IAS 27.7, 28.3, 16]

2.1.110.20 An interest in an associate or joint venture is accounted for using the equity method unless one of the following criteria is met.

- The interest (or a portion thereof) is classified as held-for-sale in accordance with IFRS 5 (see 3.5.160).
- All of the following criteria are satisfied:
 - the entity is a wholly owned subsidiary, or is a partially owned subsidiary and its other owners (including those not otherwise entitled to vote) have been informed about, and do not object to, the entity not applying the equity method;
 - the entity's debt or equity instruments are not traded in a public market (see 5.2.10.12), including stock exchanges and over-the-counter markets;
 - the entity did not file, and is not in the process of filing, its financial statements with a regulatory organisation for the purpose of issuing any class of instruments in a public market; and
 - the ultimate or any intermediate parent of the entity produces financial statements that are available for public use and comply with IFRS, such that subsidiaries are either consolidated or measured at fair value through profit or loss in accordance with IFRS 10.
- The entity is a venture capital or similar organisation and elects to measure the interest at fair value through profit or loss in accordance with IAS 39 (see 3.5.100). [IAS 28.17–20]

2.1.110.30 An entity that has a subsidiary cannot prepare individual financial statements.

2.1.110.40 In our view, an entity may label its individual financial statements as such, or use alternative titles that may be more understandable to readers – e.g. 'financial statements of the entity and investees'. Whatever label is used to identify individual financial statements, we believe that the notes to the financial statements should explain clearly the basis used in preparing those financial statements.

2.1.110.50 An entity that prepares individual financial statements may elect to prepare separate financial statements in addition to the individual financial statements.

2.1.110.60 In our view, if an entity meets and uses the exemption from preparing individual financial statements, then IFRS does not require it to prepare financial statements. However, such an entity may elect to prepare separate financial statements as its only set of IFRS financial statements (see 2.1.120).

2.1.120 Separate financial statements

2.1.120.10 A parent or an investor in an associate or joint venture that is not required to prepare consolidated financial statements (see 2.1.100.30) or individual financial statements (see 2.1.110) may prepare separate financial statements (see 3.5.660). Alternatively, separate financial statements may be prepared in addition to consolidated or individual financial statements. [IAS 27.6, 8–8A]

2.1.120.15 In separate financial statements, investments in subsidiaries, associates and joint ventures, unless they are classified as held-for-sale (see 3.5.660.20), are accounted for either:

- at cost;
- in accordance with IAS 39 (see 7.4.10.10); or

- using the equity method as described in IAS 28 (see 3.5.660.10–30). [IAS 27.10, 28.44, 39.2(a), IFRS 11.26]

2.1.120.20 The entity applies the same accounting for each category of investments. For a further discussion, see 3.5.660.40. [IAS 27.10]

2.1.120.25 IAS 27 states that the financial statements of an entity that does not have an investment in a subsidiary, associate or joint venture are not separate financial statements. However, in all material respects, the requirements that will apply to those financial statements will be identical to individual financial statements. [IAS 27.7]

2.1.120.30 Entities may elect, or be required by local regulations, to prepare separate financial statements. However, an investment entity that in accordance with IFRS 10 does not consolidate its subsidiaries (see 2.1.100.35) is required to prepare separate financial statements. [IAS 27.8A]

2.1.120.40 IFRS does not preclude an entity from including both consolidated and separate financial statements within the same report. If an entity chooses to do so, then there is no required format or order in which the financial statements are presented. However, the information presented needs to be identified clearly as related to either the separate or the consolidated financial statements.

2.1.120.50 If an entity prepares separate financial statements in accordance with IFRS, then all relevant IFRSs apply equally to those separate financial statements (see 1.1.170).

2.1.120.60 All separate financial statements disclose:

- the fact that the financial statements are separate financial statements;
- a list of significant investments in subsidiaries, joint ventures and associates, including the name, principal place of business and, if it is different, country of incorporation, proportion of ownership interest and, if it is different, the proportion of voting rights; and
- a description of the method used to account for these investments. [IAS 27.16–17]

2.1.120.70 In addition, separate financial statements of a parent that meets the criteria and uses the criteria for exemption from preparing consolidated financial statements disclose:

- the fact that the exemption from consolidation has been used;
- the name and principal place of business and, if it is different, the country of incorporation of the entity whose consolidated financial statements that comply with IFRS have been produced for public use; and
- the address at which those consolidated financial statements are obtainable. [IAS 27.16]

2.1.120.80 The separate financial statements of an entity that is not exempt from preparing consolidated or individual financial statements disclose the reason for preparing them if it is not required by law and identify the related consolidated or individual financial statements. [IAS 27.17]

2.1.130 PRESENTATION OF PRO FORMA INFORMATION

2.1.130.10 IFRS is generally silent on the presentation of pro forma information within the financial statements, with the exception of the requirement in IFRS 3 to present, following a business

combination, revenue and profit or loss of the combined entity determined as if the acquisition had been effected at the beginning of the period. [IFRS 3.B64(q)(ii)]

2.1.130.20 In some cases, an entity may wish to present pro forma information that is not required by IFRS – e.g. pro forma comparative financial statements following a change in the reporting date (see 2.1.80.10) or a pro forma statement of profit or loss and OCI following significant changes in the composition of the entity. In our view, such additional information is generally acceptable to the extent that it is allowed by local regulations and relevant stock exchange rules and provided that:

- the information is labelled clearly to distinguish it from the financial statements prepared in accordance with IFRS and is marked clearly as unaudited if that is the case;
- the entity discloses the transaction or event that is reflected in the pro forma financial information, the source of the financial information on which it is based, the significant assumptions used in developing the pro forma adjustments and any significant uncertainties about those adjustments; and
- the presentation indicates that the pro forma financial information should be read in conjunction with the financial statements and that the pro forma financial information is not necessarily indicative of the results that would have been attained if, for example, the transaction or event had taken place on a different date.

2.1.140 FUTURE DEVELOPMENTS

2.1.150 Disclosure initiative

2.1.150.10 The IASB is working on a broad initiative aimed at improving disclosures in the financial statements. The disclosure initiative covers various areas and includes the following projects.

- *Definition of material – Amendments to IAS 1 and IAS 8*: This standard-setting project is aimed at refining the definition of materiality and clarifying its characteristics. An exposure draft is expected in September 2017.
- *Principles of disclosure (including standard-level review of disclosures)*: This research project is aimed at developing a set of principles for disclosure in IFRS to assist the IASB in setting better disclosure requirements and help preparers communicate information more effectively to the users of financial statements. A discussion paper was published in March 2017. The proposals are open for comments until October 2017.
- *Materiality Practice Statement*: This non-authoritative guidance on how to use judgement when applying the concept of materiality is expected in September 2017.

2.1.160 Primary financial statements

2.1.160.10 The IASB is working on a research project on primary financial statements. This project considers potential targeted improvements to the structure and content of the primary financial statements focusing primarily on the statements of financial performance and cash flows. A consultation document is expected in the first half of 2018.

2.2 Changes in equity

2.2.10	Statement of changes in equity	40
2.2.20	Entities with no equity	40
2.2.30	Changes in accounting policies and errors	40

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2.2 Changes in equity

CURRENTLY EFFECTIVE REQUIREMENTS

This publication reflects IFRS in issue at 1 August 2017, and the currently effective requirements cover annual periods beginning on 1 January 2017.

The requirements related to this topic are derived from the following.

STANDARD	TITLE
IAS 1	Presentation of Financial Statements

FORTHCOMING REQUIREMENTS AND FUTURE DEVELOPMENTS

For this topic, there are no forthcoming requirements or future developments.

2.2.10 STATEMENT OF CHANGES IN EQUITY

2.2.10.10 A statement of changes in equity includes:

- total comprehensive income for the period, separately showing the total amounts attributable to owners of the parent and to NCI;
- for each component of equity, the effects of retrospective application or retrospective restatement recognised in accordance with IAS 8; and
- for each component of equity, a reconciliation between the carrying amount at the beginning and at the end of the period, separately disclosing changes resulting from:
 - profit or loss;
 - OCI; and
 - transactions with owners in their capacity as owners, showing separately contributions by and distributions to owners and changes in ownership interests in subsidiaries that do not result in a loss of control. [IAS 1.106]

2.2.10.20 An analysis of OCI by item – for each component of equity – is presented either in the statement of changes in equity or in the notes. [IAS 1.106A]

2.2.10.30 All owner-related changes in equity are presented in the statement of changes in equity, separately from non-owner changes in equity. As such, dividends and the related per-share amounts are disclosed either in the statement of changes in equity or in the notes to the financial statements. Such disclosures are not included in the statement of profit or loss and OCI. [IAS 1.107]

2.2.20 Entities with no equity

2.2.20.10 Entities that have share capital that is not equity (e.g. some co-operative entities) and entities that do not have equity as defined in IAS 32 (e.g. some mutual funds) may need to adapt the financial statement presentation of members' or unit holders' interests. Because a statement of changes in equity is not relevant for such entities, a statement of changes in net assets attributable to members or unit holders may be presented. Although IFRS does not require presentation of this statement, it may provide useful information with respect to the components underlying the movements in the net assets of the entity attributable to the members or unit holders during the year. [IAS 1.6]

2.2.30 Changes in accounting policies and errors

2.2.30.10 A change in accounting policy or the correction of a material prior-period error is generally presented by adjusting the opening balance of each affected component of equity of the earliest period presented and the other comparative amounts disclosed for each prior period presented (see chapter 2.8). The adjustments for each prior period and the beginning of the period are disclosed in the statement of changes in equity. [IAS 1.106(b), 110, 8.22]

2.2.30.20 The total adjustment to each component of equity resulting from changes in accounting policies is presented separately from the total adjustment resulting from the correction of errors. [IAS 1.110]

2.2.30.30 In addition, a third statement of financial position as at the beginning of the preceding period is presented following a change in accounting policy, the correction of an error or a reclassifica-

tion if those changes have a material effect on the information in the statement of financial position at the beginning of that period (see 2.1.20 and 2.8.140). [IAS 1.10(f), 40A–40D]

2.3 Statement of cash flows

2.3.10	Cash and cash equivalents	46
2.3.20	Operating, investing and financing activities	47
2.3.30	Direct vs indirect method	49
2.3.40	Classification issues	49
2.3.50	Interest, dividends and taxes	49
2.3.55	Assets held for rental and subsequently held for sale	50
2.3.60	Hedging	50
2.3.70	Factoring arrangements	51
2.3.72	Factoring of trade receivables without recourse	51
2.3.73	Factoring of trade receivables with recourse	52
2.3.74	Disclosures	52
2.3.75	Reverse factoring arrangements	53
2.3.80	Foreign exchange differences	54
2.3.90	Cash held in foreign currency	55
2.3.100	Other foreign exchange differences	56
2.3.110	Offsetting	57
2.3.120	Taxes collected on behalf of third parties	58
2.3.123	Changes in liabilities arising from financing activities	59
2.3.125	Cash flow disclosure requirements of other standards	60
2.3.150	Future developments	60

2.3 Statement of cash flows

CURRENTLY EFFECTIVE REQUIREMENTS

This publication reflects IFRS in issue at 1 August 2017, and the currently effective requirements cover annual periods beginning on 1 January 2017.

The requirements related to this topic are derived from the following.

STANDARD	TITLE
IAS 7	Statement of Cash Flows

The currently effective requirements include newly effective requirements arising from *Disclosure Initiative – Amendments to IAS 7*, which are effective for annual periods beginning on or after 1 January 2017. On initial application of the amendments, an entity is not required to provide comparative information for preceding periods. See 2.3.123.

FORTHCOMING REQUIREMENTS

For this topic, there are no forthcoming requirements.

FUTURE DEVELOPMENTS

This topic is subject to future developments that may affect several aspects of the statement of cash flows. See 2.3.130.

2.3.10 CASH AND CASH EQUIVALENTS

2.3.10.10 Cash comprises cash on hand and demand deposits. Cash equivalents are short-term highly liquid investments that are readily convertible to known amounts of cash and that are subject to an insignificant risk of changes in value. [IAS 7.6]

2.3.10.20 Demand deposits are not defined in IFRS, but in our view they should have the same level of liquidity as cash and therefore should be able to be withdrawn at any time without penalty. In addition, in our view demand deposits need not be held with a financial institution – e.g. monies held by solicitors for clients in separate and designated accounts could be considered demand deposits if they are not restricted. Even if a deposit fails to be classified as cash it may still meet the definition of cash equivalents.

2.3.10.30 Because the investments comprising cash equivalents are required to be readily convertible to known amounts of cash, only debt securities and deposits can generally qualify for inclusion, subject to the other criteria being met. Equity investments may also qualify if they are, in substance, cash equivalents – e.g. preference shares acquired within a short period of their maturity and with a specified redemption date.

2.3.10.35 An overriding test is that cash equivalents are held for the purpose of meeting short-term cash commitments rather than for investment or other purposes. For example, an entity gives a three-month loan to a customer to help the customer in managing its short-term liquidity position. In our view, the investment in this loan is not a cash equivalent because it was given for a purpose other than for the entity to manage its own short-term cash commitments. [IAS 7.7]

2.3.10.40 'Short-term' is not defined in IAS 7, but the standard encourages a cut-off of three months' maturity from the date of acquisition. In our view, three months is a presumption that may be rebutted only in rare cases when facts and circumstances indicate that the investment is held for the purpose of meeting short-term cash commitments (see 2.3.10.35) and when the instrument otherwise meets the definition of a cash equivalent (see 2.3.10.10). Cash flows related to an investment that is not a cash equivalent – e.g. those with a longer maturity for which the presumption is not rebutted – may be investing activities. [IAS 7.7, IU 05-13]

2.3.10.45 An investment that is redeemable at any time is a cash equivalent only if the amount of cash that would be received is known at the time of the initial investment, is subject to an insignificant risk of changes in value, and the other IAS 7 criteria for cash equivalents are met (see 2.3.10.10). The IFRS Interpretations Committee discussed this issue and noted that the fact that an investment can be converted at the market price at any time does not mean that the 'readily convertible to known amounts of cash' criterion has been met. [IAS 7.6-7, IU 07-09]

2.3.10.50 An investment that does not meet the definition of a cash equivalent on acquisition does not become a cash equivalent as it nears maturity. [IAS 7.7, IU 05-13]

2.3.10.55 An entity discloses the policy that it adopts in determining the composition of cash and cash equivalents. The effect of any change in the policy for determining components of cash and cash equivalents is then reported in accordance with IAS 8. [IAS 7.46-47]

2.3.10.60 Bank overdrafts repayable on demand are included as cash and cash equivalents to the extent that they form an integral part of the entity's cash management. However, even though a bank

overdraft might be netted against cash and cash equivalents in the statement of cash flows, this is not permitted in the statement of financial position unless the offsetting criteria are met (see 3.1.50 and 7.8.90). [IAS 7.8, 32.42]

2.3.10.70 A reconciliation of cash and cash equivalents in the statement of cash flows to the equivalent amount presented in the statement of financial position is disclosed and may be included in the notes to the financial statements. For example, if an entity has cash balances in a disposal group that is classified as held-for-sale in the statement of financial position, then this would be a reconciling item between cash and cash equivalents in the statement of cash flows and the equivalent amount presented in the statement of financial position. [IAS 7.45]

2.3.20 OPERATING, INVESTING AND FINANCING ACTIVITIES

2.3.20.10 The statement of cash flows presents cash flows during the period classified by operating, investing and financing activities.

- 'Operating activities' are the principal revenue-producing activities of the entity and other activities that are not investing or financing activities.
- 'Investing activities' relate to the acquisition and disposal of long-term assets and other investments not included in cash equivalents.
- 'Financing activities' relate to shareholders' equity and borrowings of the entity. [IAS 7.6, 10]

2.3.20.11 The wording of the definitions means that operating activities is the default classification when a cash flow does not meet the definition of either investing or financing cash flows. There is perceived inconsistency between the primary classification principle in IAS 7 and certain specific guidance in the standard. The primary principle is that cash flows are classified based on the nature of the activity to which they relate. Such classification is done in a manner that is most appropriate to the business of the entity. However, certain guidance in IAS 7 may not lead to a consistent application of this principle. [IAS 7.10-11]

2.3.20.13 For example, IFRS 6 allows entities in the extractive industries to choose an accounting policy, to be applied consistently, in respect of qualifying exploration and evaluation (E&E) expenditure. Such expenditure may be either capitalised as an asset or expensed as it is incurred (see 5.11.30). The nature of the activity to which the cash flows relate is the same regardless of the accounting policy chosen. However, IAS 7 requires the related cash flows to be classified as investing activities only if the expenditure is capitalised, because only expenditure that results in the recognition of an asset can be classified as investing activities. If such expenditure is expensed, then the related cash flows are classified as operating activities in the statement of cash flows. As a result, cash flows related to the identical activities of two entities with different accounting policies are classified differently because of the accounting policy chosen by each entity. [IFRS 6.24, IAS 7.11, 16, 8.10]

2.3.20.14 Although aggregate cash flows arising from obtaining or losing control of subsidiaries or other businesses are presented separately and classified as investing activities, only expenditure that results in the recognition of an asset can be classified as investing activities. In some cases, significant judgement may be needed to classify certain cash flows that relate to business combinations. In particular, consideration may be needed of whether the cash flow relates to obtaining control and whether the expenditure results in a recognised asset in the statement of financial position. [IAS 7.16, 39]

2.3.20.15 In our view, in the consolidated financial statements transaction costs associated with a business combination, although they are ancillary to the assets acquired, should be classified as operating activities because the transaction costs are not capitalised.

2.3.20.16 If deferred consideration arising from a business combination is settled in cash, then the payment will reflect both the initial fair value and amounts recognised in profit or loss as a finance expense. The cash flow classification of the cash paid may require judgement, taking into account the nature of the activity to which the cash outflow relates (see 2.3.20.11). To the extent that the amount paid reflects the finance expense, classification consistent with interest paid may be appropriate. Depending on the accounting policy adopted, this may be classified as either financing or operating activities (see 2.3.50.20).

2.3.20.17 To the extent that the amount paid reflects the settlement of the fair value of the consideration recognised on initial recognition (see 2.6.270), classification of the cash flow as a financing activity would be consistent with the settlement of other financial liabilities – e.g. a loan or a finance lease obligation. However, classification as an investing activity may also be appropriate. IAS 7 is not clear whether the settlement of a financial liability is always classified as a financing activity. For example, the settlement of trade payables is often classified in line with the nature of the underlying expenditure, including as an investing activity if the payment is for an item of property, plant and equipment. Accordingly, judgement will be needed to determine whether the cash settlement arises from obtaining control or the settlement of financing provided by the seller. Factors that may be relevant to this judgement include the length of the period between initial recognition of the liability and settlement, whether the period reflects a normal credit period and whether the liability is discounted to reflect its deferred settlement; the latter would suggest that there is a financing element to the arrangement.

2.3.20.18 Similar judgements to those described in 2.3.20.16–17 apply in respect of the classification of cash outflows for contingent consideration in a business combination (see 2.6.280). Further judgement is needed if the cash payment is greater than the amount recognised on initial recognition as a result of the resolution of uncertainties – e.g. the better-than-expected operating performance of the acquired business. In this case, classification as an operating activity, or classification consistent with interest paid (see 2.3.50.20), may be appropriate.

2.3.20.20 The separate components of a single transaction are each classified as operating, investing or financing; IFRS does not allow a transaction to be classified based on its predominant characteristic. For example, a loan repayment comprises interest (which may be classified as operating or financing (see 2.3.50.20)) and principal repayment (which is classified as financing). [IAS 7.12]

2.3.20.30 However, the aggregate net cash flows from obtaining or losing control of subsidiaries and other businesses are presented separately as a single line item as part of investing activities. For example, when a subsidiary is acquired, a single line item equal to the consideration paid by cash and cash equivalents, less any cash and cash equivalents held by the subsidiary at the time of acquisition, is shown as an investing cash outflow, rather than as separate cash outflows and inflows for the various net assets and liabilities acquired. [IAS 7.39–42]

2.3.20.35 A subsequent purchase of an additional interest or a sale by a parent of a subsidiary's equity instruments that does not result in a loss of control is classified as cash flows from financing

activities because such changes in ownership interests are accounted for as transactions with equity holders (see 2.3.20.10 and 2.5.570.20). [IAS 7.42A]

2.3.20.40 Non-cash investing or financing transactions – e.g. shares issued as consideration in a business combination, or acquisition of assets via a finance lease – are not included in the statement of cash flows, but are disclosed to provide relevant information about investing and financing activities. [IAS 7.43–44]

DIRECT VS INDIRECT METHOD

2.3.30

2.3.30.10 Cash flows from operating activities may be presented either under the direct method (receipts from customers, payments to suppliers etc) or under the indirect method (profit or loss for the period reconciled to the total net cash flow from operating activities). Although the standard encourages use of the direct method, in our experience the indirect method is usually used. [IAS 7.18–20]

2.3.30.20 For an entity that elects to present operating cash flows under the indirect method, there is often confusion about the correct starting point: should it be profit or loss or can a different figure, such as profit before income tax, be used? The standard itself refers to profit or loss, but the example provided in the appendix to the standard starts with a different figure (profit before taxation). Because the appendix is illustrative only and therefore does not have the same status as the standard, it would be more appropriate to follow the standard (see 1.1.100.50). [IAS 7.18, 20, IEA]

2.3.30.30 Alternatively, an entity using the indirect method may choose to present its operating cash flows by showing revenues and expenses before working capital changes as the starting point, followed by changes during the period in inventories, and operating receivables and payables. However, in our experience this approach is less common. [IAS 7.20, IEA]

2.3.40

CLASSIFICATION ISSUES

2.3.50

Interest, dividends and taxes

2.3.50.10 IFRS requires cash flows from interest and dividends received and paid, and income taxes paid, to be disclosed separately. In our view, this means that disclosure is required in the statement of cash flows rather than in the notes. [IAS 7.31–36]

2.3.50.20 The standard does not, however, specify the classification of such cash flows, and an entity is required to choose its own policy for classifying each of interest and dividends paid as operating or financing activities and each of interest and dividends received as operating or investing activities. An entity chooses a presentation method that will present these cash flows in the most appropriate manner for the business or industry (e.g. banking), if applicable, and the method selected is applied consistently. Taxes paid are classified as operating activities unless it is practicable to identify them with, and therefore classify them as, financing or investing activities. [IAS 7.31–36]

2.3.50.30 Even if it is practicable for an entity to classify certain taxes as investing or financing activities, the standard is not clear on whether:

- to allocate *all* taxes paid among the three categories of cash flows; or

- to allocate only certain taxes paid because they relate to transactions classified as investing or financing, leaving the balance in operating activities.


2.3.50.35 In our view, it is acceptable to allocate only certain material tax cash flows, while leaving the balance in operating activities, as long as the approach taken is applied consistently and disclosed appropriately. We believe that allocating, for example, 60 percent of the tax cash flows as it represents the material tax cash flows known to be from investing or financing activities, with appropriate disclosure, provides better information than not allocating any.

2.3.50.37 When borrowing costs are capitalised in accordance with IAS 23 (see 4.6.10), interest expenditure forms part of the cost of a recognised asset. Although paragraph 33 of IAS 7 specifies that interest paid may be classified as a cash flow from operating or financing activities, paragraph 16 of IAS 7 permits expenditure that results in a recognised asset to be classified as investing activities. [IAS 7.16(a), 33]

2.3.50.38 Given these inconsistencies, in our view an entity should choose an accounting policy, to be applied consistently, to classify cash flows related to capitalised interest as follows:

- as cash flows from investing activities if the other cash payments to acquire the qualifying asset are reflected as investing activities; or
- consistently with interest cash flows that are not capitalised (see 2.3.50.20).

EXAMPLE 1 – CAPITALISED INTEREST – PRESENTATION



2.3.50.40 Company C builds a plant and pays cash of 1,000, which includes 50 of capitalised interest. C should choose an accounting policy, to be applied consistently, to present the interest paid of 50 as cash flows from operating, financing or investing activities (see 2.3.50.38). The remaining 950 is included in investing activities. This is consistent with the requirement to classify separately the different components of a single transaction (see 2.3.20.20).

2.3.50.50 The total amount of interest paid is disclosed in the statement of cash flows, regardless of whether the related expense has been recognised in profit or loss or capitalised as borrowing costs. [IAS 7.32]

2.3.55 Assets held for rental and subsequently held for sale

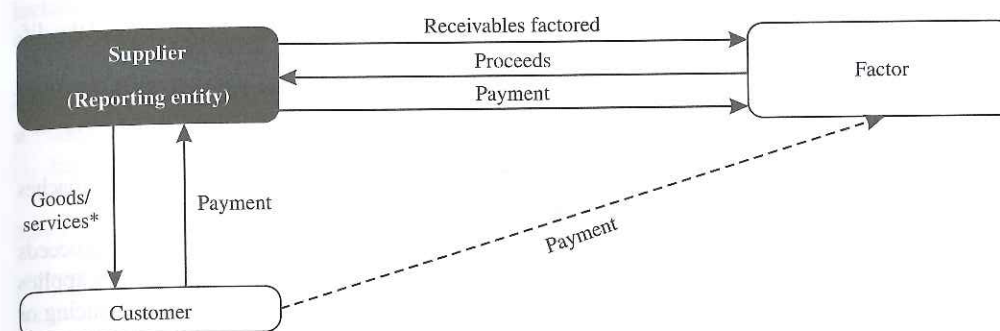
2.3.55.10 Cash flows related to the acquisition of an asset recognised in accordance with IAS 16 are generally cash flows from investing activities (see 2.3.20.10). However, cash payments to manufacture or acquire assets held for rental that subsequently become held-for-sale (i.e. are transferred to inventory) are cash flows from operating activities (see 3.2.380.40). Cash flows from rental payments and subsequent sales of these assets are also classified as operating. [IAS 7.14, 16.68A]

2.3.60 Hedging

2.3.60.10 If a hedging instrument is accounted for as a hedge of an identifiable position (see chapter 7.7), then the cash flows of the hedging instrument are classified in the same manner as the cash flows of the position being hedged. For a discussion of the presentation of hedging instruments, see 7.8.225. [IAS 7.16]

2.3.70

Factoring arrangements



* Goods/services – Guidance in this section focuses on factoring arrangements related to goods or services that are operating in nature (e.g. inventory) rather than, for example, the sale of property, plant and equipment.

2.3.70.10 In a traditional factoring arrangement, an entity that is a supplier of goods or services (the entity) obtains cash from a bank or other financial institution (i.e. the factor) against receivables due from the entity's customers. The arrangement might take different legal forms – e.g. the receivables might be sold to the factor or pledged as security for a loan from the factor and the factor may or may not have recourse to the entity in the event that the customer does not settle. A traditional factoring arrangement is initiated by the entity and the factor, rather than the customer. In many cases, the customer might be unaware of the arrangement.

2.3.70.20 There is no specific guidance in IFRS on the classification of cash flows from traditional factoring arrangements – e.g. whether the entity should classify the cash inflows from the factor as operating or financing in the statement of cash flows. Presenting a single *financing* cash inflow may significantly affect the statement of cash flows – e.g. in an extreme case, if the entity factored all of its receivables, then there may be no operating cash inflows presented for the sale of goods or services. The primary consideration for the classification of cash flows is the nature of the activity to which they relate (see 2.3.20.11) and judgement may be needed to apply this to factoring arrangements. For a discussion of cash flow classification of factoring of receivables without recourse, see 2.3.72, and with recourse, see 2.3.73. For a discussion of derecognition of financial assets and securitisations, see 7.5.60–320.

2.3.72 Factoring of trade receivables without recourse

2.3.72.10 If the receivables are factored without recourse, then in our view the proceeds from the factor should be classified as part of operating activities even if the entity does not enter into such transactions regularly. This is because the proceeds do not generally fit clearly into the definitions of either investing or financing activities (see 2.3.20). In addition, factoring of receivables without recourse can be likened to the early collection of amounts due from customers and as such the related cash inflow is considered operating in nature.

2.3.72.20 In some cases, an entity may continue to collect cash from customers on behalf of the factor even if the receivables are factored without recourse. In these circumstances, the entity may collect the cash and transfer it onwards to the factor, and it may be appropriate to either exclude these cash flows from the cash flow statement or to present the relevant cash inflow and outflows net (similar to 2.3.73.30 below).

2.3.73 **Factoring of trade receivables with recourse**

2.3.73.10 If receivables are factored with recourse, then the factoring arrangement may take different legal forms and structures – e.g. the customer may be required to remit cash directly to the factor (see 2.3.73.20) or to the entity, which then transfers the cash to the factor (see 2.3.73.30). For a discussion of derecognition of receivables in factoring with recourse arrangements, see 7.5.310.

2.3.73.20 If the customer remits cash directly to the factor, then in our view the following approaches to presenting cash flows are acceptable and should be applied consistently.

- **Approach 1:** Present a single financing cash inflow or a single operating cash inflow for the proceeds received from the factor against receivables due from the entity's customers. An entity applies judgement in determining whether to classify proceeds received from the factor as financing or operating cash inflows, giving consideration to the nature of the activity to which the cash inflow relates (see 2.3.70.20). Although the nature of the arrangement may be viewed as collateralised borrowing (see 7.5.310) and as such be classified as a financing cash inflow based on the guidance in paragraph 17(c) of IAS 7, we believe that it may also be acceptable to classify the proceeds from the factor as part of operating activities on the basis that the principal nature of cash flows related to the provision of goods and services will often be operating (see 2.3.20.10). Approach 1 considers the settlement of the liability to the factor by the customer as a non-cash transaction for the entity – i.e. the entity presents only a single cash flow receipt from the factor – therefore it needs to provide disclosure of non-cash transactions (see 2.3.74.20).
- **Approach 2:** Present gross cash flows. Under this approach, the entity would present a financing cash inflow for the proceeds received from the factor, followed by an operating cash inflow when the factor collects the amounts from the customer in respect of goods or services sold by the entity and a financing cash outflow for settlement of amounts due to the factor. Approach 2 reflects that, in substance, the factor is collecting receivables on behalf of the entity and retains the proceeds in settlement of the entity's liability to the factor.

2.3.73.30 If the customer remits cash directly to the entity, then this arrangement involves multiple actual cash flows for the entity – i.e. proceeds from the factor on factoring of the receivables, receipts from the customer and payment to the factor. In this case, the entity presents a financing cash inflow for the proceeds received from the factor, followed by an operating cash inflow for the proceeds received from the customer and a financing cash outflow to settle the liability due to the factor. We do not believe that the entity could report a single operating cash flow in this case. However, the entity may be able to report the proceeds received from, and the settlement of the liability due to, the factor on a net basis if the relevant criteria are met (see 2.3.110). [IAS 7.22, 23A(c)]

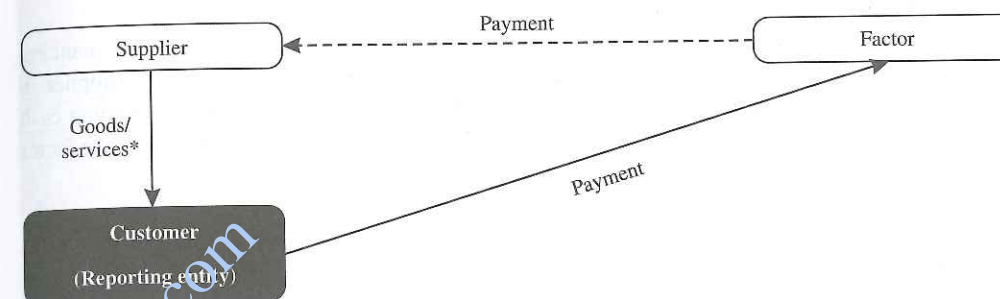
2.3.74 **Disclosures**

2.3.74.10 In addition to the appropriate classification in the statement of cash flows, an entity that is a supplier of goods and services in a factoring arrangement is required to disclose information about those arrangements that is relevant to an understanding of its cash flows. This disclosure may include an explanation of the nature of the arrangement and how it is reflected in the financial statements. Relevant IFRS disclosure requirements include:

- disclosure of significant accounting policies; and
- disclosure of significant judgements that management has made in the process of applying the accounting policies and that have the most significant effect on the amounts recognised in the financial statements. [IAS 1.117–122]

2.3.74.20 The additional disclosure requirements that may be relevant to these arrangements include:

- reporting separately major classes of gross cash receipts and gross cash payments arising from investing and financing activities;
- disclosure of non-cash transactions; and
- additional information that may be relevant to users in understanding the financial position and liquidity of the entity. [IAS 7.21, 43, 50]

2.3.75 **Reverse factoring arrangements**

* Goods/services – Guidance in this section focuses on arrangements related to goods or services received from the supplier that are operating in nature (e.g. inventory) rather than, for example, the acquisition of property, plant and equipment.

2.3.75.10 Under a reverse factoring arrangement (see 7.8.45 and 7.5.425), a factor agrees to pay amounts to a supplier in respect of invoices owed by the supplier's customer and receives settlement from that customer (the entity) at a later date. A reverse factoring arrangement is often initiated by the customer and the factor.

2.3.75.20 There is no specific guidance in IFRS on the classification of cash flows for an entity that is the customer in a reverse factoring arrangement – i.e. whether it should classify the cash outflows to settle amounts owed to the factor as operating or financing in the statement of cash flows. Presenting a single *financing* cash outflow may significantly affect the statement of cash flows – e.g. in an extreme case, if all of the entity's payables were reverse factored, then there may be no operating cash outflows presented for its purchases.

2.3.75.30 The appropriate presentation in the statement of financial position and disclosure about liabilities related to reverse factoring arrangements are discussed in 7.8.45.70–90, 205 and 375. However, in our view it is the nature of the activity, rather than the classification of the related item in the statement of financial position, that determines the appropriate classification of the cash outflow. [IAS 7.10–11, IU 03-12, 07-12, 03-13]

2.3.75.40 Reverse factoring arrangements may take different legal forms and structures. In our view, the following approaches to presenting cash flows are acceptable and should be applied consistently.

- **Approach 1:** Present a single operating cash outflow or a single financing cash outflow for the payments made to the factor. Under this approach, an entity applies judgement in determining whether to classify payments made to the factor as an operating or financing cash outflow, giving

consideration to the primary principle that cash flows are classified according to the nature of the activity to which they relate (see 2.3.20.11), taking into account the specific facts and circumstances. For example, an entity needs to consider if the principal business purpose of the reverse factoring arrangement is to provide funding to the supplier or to facilitate efficient payment processing, and whether the reverse factoring arrangement significantly extends payment terms beyond the normal terms agreed with other suppliers (see 7.8.45.80). In our experience, the principal nature of cash payments related to the purchase of goods and services will often be operating. This approach considers the payment to a supplier by the factor not to be a cash transaction of the customer—i.e. the entity presents a single cash flow for cash payments made to the factor. If an entity follows this approach, then it provides disclosure of non-cash transactions (see 2.3.75.60).

- **Approach 2:** Present gross cash flows. Under this approach, the entity would present financing cash inflows and operating cash outflows when the factor makes a payment to the supplier in respect of the purchase of goods or services made by the entity, together with a financing cash outflow for settlement of amounts due to the factor. This approach presents payments by the factor to suppliers as payments made on behalf of the entity.

2.3.75.50 In addition to the appropriate classification in the statement of cash flows, an entity that is the customer in a reverse factoring arrangement (see 7.8.45) is required to disclose information about those arrangements that is relevant to an understanding of its cash flows. This disclosure may include an explanation of the nature of the arrangement and how it is reflected in the financial statements. Relevant IFRS disclosure requirements include:

- disclosure of significant accounting policies; and
- disclosure of significant judgements that management has made in the process of applying the accounting policies and that have the most significant effect on the amounts recognised in the financial statements. [IAS 1.117–122]

2.3.75.60 The additional disclosure requirements that may be relevant to these arrangements include:

- reporting separately major classes of gross cash receipts and gross cash payments arising from investing and financing activities;
- disclosure of non-cash transactions; and
- additional information that may be relevant to users in understanding the financial position and liquidity of the entity. [IAS 7.21, 43, 50]

2.3.80 FOREIGN EXCHANGE DIFFERENCES

2.3.80.10 Cash flows arising from an entity's foreign currency transactions are translated into the entity's functional currency (see 2.7.30) at the exchange rates at the dates of the cash flows; when exchange rates have been relatively stable, an appropriate average can be used. When the presentation currency is different from the functional currency, the functional currency cash flows are translated into the presentation currency at the rates at the dates of the cash flows (or appropriate averages). For example, the functional currency cash flows of a foreign operation will need to be translated into the group presentation currency when preparing consolidated financial statements. The effect of exchange rate changes on the balances of cash and cash equivalents is presented as part of the reconciliation of movements therein. [IAS 7.25–28]

2.3.90

Cash held in foreign currency

EXAMPLE 2 – EFFECT OF EXCHANGE RATE CHANGES – CALCULATION AND PRESENTATION

2.3.90.10 This example illustrates the calculation of the effect of exchange rate changes on the balances of an individual entity's cash and cash equivalents and its presentation in the statement of cash flows.

	FOREIGN CURRENCY	RATE	FUNCTIONAL CURRENCY
Balance of cash held in foreign currency on 1 January 2017	100	1:1	100
Receipts from customers	100	1.5:1	150
Payments to suppliers	(50)	1.6:1	(80)
Balance of cash held in foreign currency on 31 December 2017	150		170
Translated cash at the reporting date	150	2:1	300
Gain on cash held in foreign currency			130

Statement of financial position

	FUNCTIONAL CURRENCY 2017	FUNCTIONAL CURRENCY 2016
Share capital	100	100
Retained earnings	200 ⁽¹⁾	-
Cash	300	100

Note

1. Calculated as (150 - 80 + 130).

Statement of cash flows extract – Direct method

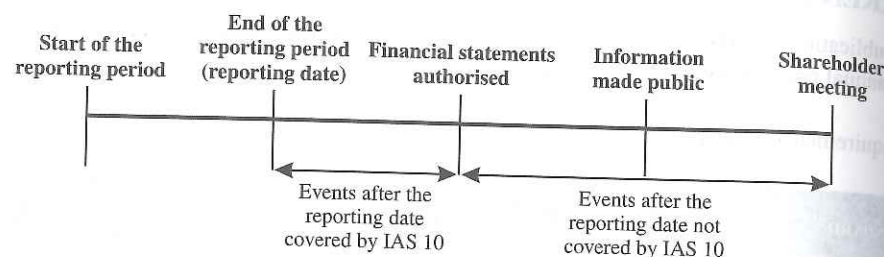
	2017
Receipts from customers ⁽¹⁾	150
Payments to suppliers ⁽²⁾	(80)
Net increase in cash	70
Cash and cash equivalents at 1 January 2017	100
Effect of exchange rate fluctuations on cash held	130
Cash and cash equivalents at 31 December 2017	300

Notes

1. All receivables collected by the reporting date.
2. All invoices paid by the reporting date.

2.9.10 OVERALL APPROACH

2.9.10.10 The following diagram illustrates the scope of IAS 10, which deals with events that occur after the reporting date but before the financial statements are authorised for issue. [IAS 10.3]



2.9.10.20 A number of terms are used, either in the literature or in practice, to describe the end of an entity's financial year, including 'reporting date', 'end of the reporting period', 'statement of financial position date', 'year end' and 'financial year end'. Generally, these terms are used interchangeably and have the same meaning. This publication consistently uses the term 'reporting date' throughout, which refers to the end of the reporting period and does not refer to the date on which the financial statements are prepared, authorised for issue, made public or filed.

2.9.15 Date on which the financial statements were authorised for issue

2.9.15.10 Disclosure is required in the financial statements of the date on which the financial statements were authorised for issue and who gave such authorisation, to inform users of the date to which events have been considered. If the shareholders have the power to amend the financial statements after issue, then the entity discloses that fact. [IAS 10.17]

2.9.15.20 The date on which the financial statements are authorised for issue is generally the date on which the financial statements are authorised for issue by management, either to the supervisory board or to the shareholders. Even if the shareholders are required to approve the financial statements, the date on which the financial statements are authorised for issue is the date of issue, not the date on which shareholders approve the financial statements. [IAS 10.5-6]

2.9.15.22 Identification of the date on which the financial statements are authorised for issue is a key area in the application of IAS 10. This is because any event that occurs after this date is not disclosed or reflected in the financial statements of the current period. However, the date on which the financial statements are authorised for issue is not always easily identifiable. In our view, the determination of this date should be based on all facts and circumstances, including the rights and responsibilities of the governing body and local governance rules on authorisation protocols. [IAS 10.4-7]

2.9.15.25 In our view, two different dates of authorisation for issue of the financial statements (dual dating of financial statements) should not be disclosed, because we believe that only a single date of authorisation for issue of the financial statements complies with IAS 10. [IU 05-13]

2.9.15.30 The financial statements of each entity have their own date of authorisation. For example, if financial statements of a subsidiary are authorised for issue after the publication of the consolidated

financial statements of the group that includes this subsidiary, then the financial statements of the subsidiary have a later date of authorisation.

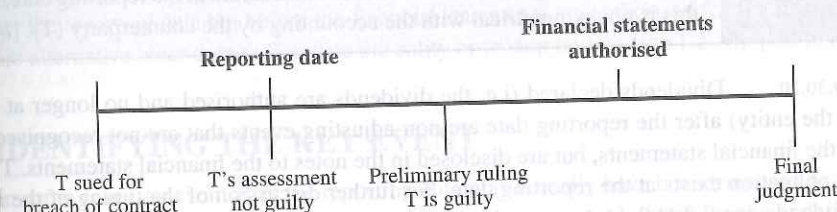
2.9.15.40 In our view, the authorisation for issue of the financial statements of the current period does not itself require the reconsideration of adjusting and non-adjusting events in respect of comparative information that is derived from financial statements (annual or interim) of a previous period that were themselves previously authorised for issue. [IAS 1.38, 10.3, 8-11]

2.9.20 ADJUSTING EVENTS

2.9.20.10 The financial statements are adjusted to reflect events that occur after the reporting date, but before the financial statements are authorised for issue, if either they provide evidence of conditions that existed at the reporting date (adjusting events) or they indicate that the going concern basis of preparation is inappropriate (see 2.9.55). [IAS 10.3, 8, 14]

EXAMPLE 1A – LEGAL CLAIM – DEFENDANT

2.9.20.20 Company T is being sued for breach of contract. At the reporting date, T asserted that it had not breached the contract and had legal opinions supporting this as the most likely outcome. Therefore, T had not recognised any provision in its draft financial statements (see chapter 3.12). Before the financial statements are authorised by the directors, the judge in the case delivers a preliminary ruling that T is guilty and liable for damages of 1,000. A final judgment is made after the financial statements have been authorised for issue.



2.9.20.25 In our view, the financial statements should be adjusted and a provision of 1,000 recognised because the preliminary ruling provides enough evidence that an obligation existed at the reporting date, in the absence of any evidence to the contrary, notwithstanding the fact that a final judgment had not yet been reached.

2.9.20.30 For other examples of adjusting events, see paragraph 9 of IAS 10.

2.9.30 NON-ADJUSTING EVENTS

2.9.30.10 Financial statement amounts are not adjusted for non-adjusting events. Non-adjusting events are events that are a result of conditions that arose after the reporting date. An exception is

when events after the reporting date indicate that the financial statements should not be prepared on a going concern basis (see 2.9.55). [IAS 10.3, 10, 14]

EXAMPLE 1B – LEGAL CLAIM – CLAIMANT



2.9.30.15 Continuing Example 1A from the point of view of Company V, which is suing Company T for breach of the contract, V is uncertain about the outcome of the legal proceeding at the reporting date. V's financial statements are authorised for issue after the final court judgment. V considers whether the favourable court ruling is an adjusting or non-adjusting event in respect of its claim, which has been treated as a contingent asset (see 3.12.107) because its realisation was probable but not virtually certain.

2.9.30.17 In our view, the change in probability of the realisation of income and the recovery of the related asset as a result of the court ruling is an event that should be reflected in the financial statements of the period in which the change occurs and should not be treated as an adjusting event in the prior-period financial statements. This is because the recognition of an asset for an item that is a contingent asset is specified as 'recognised in the period in which the change occurs'. [IAS 37.33, 35]

2.9.30.18 We believe that the phrase 'in which the change occurs' refers to the change in probability of the related inflows of economic benefits, which provides enough evidence that from that point in time the item meets the definition of and the recognition requirements for an asset. We believe that this specific guidance should be applied rather than considering the change in probability to be an event that provides additional information about circumstances at the reporting date, even though this is not symmetrical with the accounting by the counterparty (T). [IAS 37.33, 35]

2.9.30.20 Dividends declared (i.e. the dividends are authorised and no longer at the discretion of the entity) after the reporting date are non-adjusting events that are not recognised as a liability in the financial statements, but are disclosed in the notes to the financial statements. This is because no obligation exists at the reporting date. For further discussion of the timing of the recognition of dividends, see 7.3.600. [IAS 10.12–13]

2.9.30.25 A change in income tax rate or income tax law enacted or substantively enacted after the reporting date is a non-adjusting event that would generally result in disclosure (see 3.13.480.50). [IAS 10.22(h), 12.46–47]

2.9.30.28 An entity considers changes in market conditions after the reporting date to determine whether they indicate an adjusting or non-adjusting event. For example, if the assumptions made in determining recoverable amounts at the reporting date are consistent with market data at that date, then no further adjustment is necessary (see 3.10.180.70–110). However, the entity considers whether disclosure would be appropriate (see 2.9.30.30). [IAS 10.11, 21]

2.9.30.30 For material non-adjusting events, an entity discloses the nature of the event and an estimate of its financial effect or a statement that an estimate cannot be made. A non-adjusting event is consid-

ered to be material if it is of such importance that non-disclosure would affect the ability of users of the financial statements to make proper evaluations and decisions. In all cases, if a business combination happens after the annual reporting date but before the financial statements are authorised for issue, then an entity discloses information as prescribed by IFRS 3 (see 2.6.1160). [IFRS 3.59–60, B66, IAS 10.21]

2.9.30.40 For other examples of non-adjusting events, see paragraph 22 of IAS 10.

CURRENT VS NON-CURRENT CLASSIFICATION

2.9.40 Generally, the classification of long-term debt as current or non-current reflects circumstances at the reporting date. Refinancings, amendments, waivers etc that are agreed after the reporting date are not considered in determining the classification of debt, but are disclosed as non-adjusting events (see 2.9.30.30). However, if an entity expects, and has the discretion, at the reporting date to refinance or to reschedule payments on a long-term basis, then the debt is classified as non-current (see 3.1.40). [IAS 1.72–76]

EARNINGS PER SHARE

2.9.50 EPS is restated to include the effect on the number of shares of certain share transactions that happen after the reporting date even though the transactions themselves are non-adjusting events (see 5.3.530). [IAS 33.64]

GOING CONCERN

2.9.55 An entity does not prepare its financial statements on a going concern basis if management determines, after the reporting date but before the financial statements are authorised for issue, that it intends or has no alternative other than to liquidate the entity or to stop trading (see 1.2.70). [IAS 10.14]

IDENTIFYING THE KEY EVENT

2.9.60 In some cases, an event after the reporting date may actually have been triggered by an event that occurred before the reporting date. In such cases, it is necessary to determine the underlying causes of the event and its timing to determine the appropriate accounting. [IAS 10.3]

EXAMPLE 2A – THE KEY EVENT – CUSTOMER BANKRUPTCY




2.9.60.20 Company B receives notice after the reporting date that one of its major customers has gone into liquidation. In this case, the standard states that the bankruptcy of a customer after the reporting date usually confirms that a loss existed at the reporting date. [IAS 10.9]

2.9.60.25 Therefore, B concludes that the bankruptcy is an adjusting event unless evidence to the contrary exists – e.g. the customer became bankrupt because its main operating plant was destroyed in a fire that happened after the reporting date.

2.9.60.30 An entity considers whether adjusting events impact not only recognised items but also previously unrecognised items. [IAS 10.9]

EXAMPLE 2B – THE KEY EVENT – PREVIOUSLY RECOGNISED AND UNRECOGNISED ITEMS



2.9.60.35 A bank extends a loan to Company C before its reporting date. Company D provides a financial guarantee to the bank so that D has the credit risk of non-repayment of the loan by C to the bank. After its reporting date, D receives notice that C has gone into administration (bankruptcy).

2.9.60.37 D concludes that the bankruptcy is an adjusting event (subject to evidence to the contrary (see Example 2A)) and recognises a provision for its estimate of the amount that it will pay under the guarantee (see 3.12.750), despite not having recognised the loan as an asset in its own accounting records. [IAS 10.9, 37.16]

2.9.60.40 In other cases, multiple events may happen, some before and some after the reporting date, and it is necessary to determine which of the events triggers the recognition of the event in the financial statements.

2.9.70 DISCOVERY OF FRAUD AFTER REPORTING DATE

2.9.70.10 A fraud may be discovered after the financial statements have been authorised for issue. In our view, if information about the fraud could reasonably be expected to have been obtained and taken into account by an entity preparing financial statements when those financial statements were authorised for issue – e.g. in the case of a fraud within the entity itself – then subsequent discovery of such information is evidence of a prior-period error in those financial statements. In contrast, a fraud that occurred outside the entity and that had no direct effect on the entity's transactions might not reasonably be expected to have been known to the entity's management. Such a fraud could still have had an effect on the reported amounts of the entity if it had an effect on market prices; however, we believe that this is not a prior-period error because the definition of a prior-period error focuses on whether information was available or reasonably could have been obtained and taken into account (see 2.8.80). [IAS 8.5, 10.9]

2.9.70.20 In other circumstances, such an external fraud may be discovered after the reporting date but before the financial statements are authorised for issue. In our view, in concluding whether the discovery of the fraud should be treated as an adjusting or non-adjusting event related to reporting the fair value of financial assets under IAS 39 in financial statements that have not yet been authorised for issue, management first identifies whether there is a question of existence, valuation or both.

2.9.70.30 In our view, if the discovery of a fraud raises issues related to the existence of the financial assets involved, then it should be treated as an adjusting event for financial statements that have not yet been authorised for issue. This is because the discovery of the fraud provides additional information about the existence of financial assets at the reporting date.

2.9.70.35 If, however, the fraud raises issues related only to the valuation of financial assets at the reporting date that do exist, then in our view it should be treated as a non-adjusting event for reporting

the fair values of financial assets in the scope of IAS 39. This is because of the following fair value measurement requirements.

- **Level 1 fair value measurement** – i.e. based on unadjusted quoted prices in active markets for identical assets or liabilities that the entity can access at the reporting date (see 2.4.280). In our view, although the market may have been mispricing the underlying value of the securities because of inaccurate or incomplete information, a quoted price for a financial instrument in an active market should not be overridden.
- **Level 2 or Level 3 fair value measurement** – i.e. based on inputs other than quoted prices included within Level 1 that are observable for the financial asset (Level 2) or unobservable inputs (Level 3) (see 2.4.290). The measurement objective for such fair value measurements is the same as that for a Level 1 fair value measurement: what the price was or would have been at the reporting date. Therefore, in our view any valuation that has as its objective fair value at the reporting date should not reflect information that neither was nor would have been reasonably available to market participants at that date. [IFRS 13.9, 76, 81, 86]

2.9.70.40 In some cases, it may be difficult to separate the existence and the valuation issues. In our view, if it is impracticable to separate the existence and the valuation issues, then the entire effect should be treated as an issue related to the existence of assets. For example, Fund Q reports an investment in government bonds and had its investment adviser, K, act as a custodian; Q discovers in March 2016 that K has been charged with fraud. In this case, K is alleged to have reported these government bonds as assets of multiple investors and their owner of record is an affiliate of K. Although these government bonds were in existence, the existence of Q's claim to those assets is uncertain.

2.9.70.50 If an entity concludes that the subsequent discovery of a fraud is a valuation issue, and therefore it is treated as a non-adjusting event, then the non-adjusting event is disclosed if it is material. [IAS 10.21]

2.10 Hyperinflation

2.10.10	Scope	394
2.10.20	Indicators of hyperinflation	394
2.10.30	Measuring inflation rate	395
2.10.40	Appropriate price index	395
2.10.50	Cumulative inflation rate	395
2.10.60	No index available	396
2.10.70	Restating financial statements for hyperinflation	396
2.10.80	Step 1: Restate opening statement of financial position	396
2.10.90	Step 2: Restate closing statement of financial position	397
2.10.100	Step 3: Restate statement of profit or loss and OCI	398
2.10.110	Worked example of IAS 29 restatements	398
2.10.115	Presentation of gain or loss on net monetary position	404
2.10.120	Impairment of non-monetary assets	404
2.10.130	Comparative information	405
2.10.140	First application of hyperinflationary accounting	405
2.10.150	Cessation of hyperinflationary accounting	407
2.10.160	Translation to presentation currency different from functional currency	407
2.10.170	Supplementary historical cost information	407
2.10.180	Changing prices	408

2.10 Hyperinflation

CURRENTLY EFFECTIVE REQUIREMENTS

This publication reflects IFRS in issue at 1 August 2017, and the currently effective requirements cover annual periods beginning on 1 January 2017.

The requirements related to this topic are derived from the following.

STANDARD	TITLE
IAS 21	The Effects of Changes in Foreign Exchange Rates
IAS 29	Financial Reporting in Hyperinflationary Economies
IFRIC 7	Applying the Restatement Approach under IAS 29 Financial Reporting in Hyperinflationary Economies

FORTHCOMING REQUIREMENTS AND FUTURE DEVELOPMENTS

For this topic, there are no forthcoming requirements or future developments.

2.10.10 SCOPE

2.10.10.10 When an entity's functional currency (see 2.7.30) is hyperinflationary (i.e. it is the currency of a hyperinflationary economy), its financial statements are 'restated' so that all items are presented in the measuring unit current at the reporting date – i.e. it adopts the current purchasing power concept. Moreover, when an entity has foreign operations (e.g. a subsidiary, associate or joint arrangement) whose functional currency is the currency of a hyperinflationary economy, the investee's financial statements are restated before being translated and included in the investor's financial statements. Comparative amounts are excluded from the restatement requirement when the presentation currency of the ultimate financial statements into which they will be included is non-hyperinflationary (see 2.7.270). [IAS 21.42–43, 29.8]

2.10.10.20 Restatement for hyperinflation (see 2.10.20) is not elective. The IFRS Interpretations Committee discussed whether an entity, whose functional currency is not hyperinflationary, is permitted to use the concept of financial capital maintenance defined in terms of constant purchasing power units and, if so, whether it should follow the requirements in IAS 29 to present its financial statements. Under the concept of financial capital maintenance, a profit is earned only if the amount of net assets at the end of the period exceeds the amount of net assets at the beginning of the period, after excluding any distributions to and contributions from owners during the period. [CF4.59(a), 4.63, IU 01-14]

2.10.10.30 The Committee noted that an entity is not permitted to apply a concept of financial capital maintenance that is in conflict with the requirements of a particular IFRS or to override the requirements of a particular standard. For example, IAS 29 cannot be applied simply because an entity whose functional currency is not hyperinflationary believes that the cumulative effects of inflation are significant and therefore that restatement would be helpful. In such cases, the entity may instead consider presenting supplementary current cost information (see chapter 5.8). [IU 01-14]

2.10.20 Indicators of hyperinflation

2.10.20.10 Under IFRS, it is a matter of judgement to determine when restatement for hyperinflation becomes necessary. Hyperinflation is indicated by the characteristics of an economy, which include but are not limited to the following.

- The general population prefers to keep its wealth in non-monetary assets or in a relatively stable foreign currency – amounts of local currency held are invested immediately to maintain purchasing power.
- The general population regards monetary amounts not in terms of the local currency but in terms of a relatively stable foreign currency – prices may be quoted in the stable currency.
- Sales and purchases on credit take place at prices that compensate for the expected loss of purchasing power during the credit period, even if the period is short.
- Interest rates, wages and prices are linked to a price index.
- The cumulative inflation rate over three years is approaching, or exceeds, 100 percent. [IAS 29.3]

2.10.20.20 Although the 100 percent numerical indicator is a key factor in identifying hyperinflation, it is not the only factor and should not be considered in isolation. Applying all of these factors

could result in a country being considered hyperinflationary when its three-year cumulative inflation rate is, for example, only 80 percent.

2.10.20.30 Although judgement is involved in determining the onset of hyperinflation in a particular case, a preference is stated in the standard for all affected entities to apply the standard from the same date. [IAS 29.4]

MEASURING INFLATION RATE

Appropriate price index

2.10.30

2.10.40

2.10.40.10 For most countries there are two main indices that are generally used in measuring the general inflation rate: a consumer price index (CPI) and a producer or wholesale price index (PPI or WPI). The CPI measures the change in the cost of a fixed basket of products and services consumed by a 'typical household', generally including housing, electricity, food and transportation. The PPI or WPI measures wholesale price levels.

2.10.40.20 IFRS requires the use of a general price index that reflects changes in *general* purchasing power. In addition, two of the indicators of hyperinflation refer to the *general* population rather than a specific sector. For these reasons, in our view the CPI is the most appropriate index to use in measuring the inflation rate, because it is a broad-based measurement across all consumers in an economy. Some jurisdictions have multiple price indices published and further analysis and judgement may be required to determine an appropriate index that reliably reflects changes in general purchasing power. As noted in IAS 29, it is preferable that all entities that report in the currency of the same economy to use the same index. [IAS 29.37]

2.10.50 Cumulative inflation rate

2.10.50.10 IAS 29 refers to a cumulative inflation rate, but is silent on whether the calculation should be done on a simple or compounded basis. In our view, a compounded inflation rate should be calculated because the simple rate aggregates three discrete results without viewing the three-year period itself on a cumulative basis. [IAS 29.3]

EXAMPLE 1 – DETERMINING CUMULATIVE INFLATION RATE



2.10.50.20 The inflation rate in three consecutive years is 20%, 30% and 40%, respectively. The cumulative rate calculated on a simple basis is 90% (20 + 30 + 40). However, on a compounded basis the rate is 118%, which is calculated as follows.

- At the start of year 1, assume the index to be 100.
- At the end of year 1, the index is 120 (100 x 1.2).
- At the end of year 2, the index is 156 (120 x 1.3).
- At the end of year 3, the index is 218 (156 x 1.4), which gives a cumulative inflation rate of 118%, calculated as (218 - 100) / 100 or (((1 + 20%) x (1 + 30%) x (1 + 40%)) - 1).

2.10.60 No index available

2.10.60.10 When there is no index available, the standard requires an index to be estimated. The example it provides is using an estimate based on exchange rate movements between the functional currency and a relatively stable foreign currency. However, this approach might not be appropriate if the exchange rate is not freely floating. An estimate based on exchange rate movements might be adjusted for the effect of inflation, if there is any, in the foreign currency used as a benchmark. Although the standard uses this example in the context of the restatement of property, plant and equipment, in our view this method could be used for the restatement of the entire financial statements when no index is available. The same issue will arise when the official indices are considered unreliable, but this problem should be rare. [IAS 29.17]

2.10.60.20 If an entity estimates the index, then it discloses the following information:

- how the index was estimated;
- the level of the index at the reporting date; and
- movement in the index during the current and the previous reporting period. [IAS 29.39(c)]

2.10.70 RESTATING FINANCIAL STATEMENTS FOR HYPERINFLATION

2.10.70.10 To prepare a statement of financial position and a statement of profit or loss and OCI in a hyperinflationary economy, an entity needs to determine the impact of changes in purchasing power and restate its comparatives. To prepare these statements, there are four separate steps to be considered.

- **Step 1:** Restate the statement of financial position at the beginning of the reporting period.
- **Step 2:** Restate the statement of financial position at the end of the reporting period.
- **Step 3:** Restate the statement of profit or loss and OCI for the reporting period.
- **Step 4:** Calculate and separately disclose the gain or loss on the net monetary position. [IAS 29.8–10]

2.10.70.20 There will also be impacts on the statement of changes in equity and statement of cash flows from this process. [IAS 29.33]

2.10.80 Step 1: Restate opening statement of financial position

2.10.80.10 In the statement of financial position *at the beginning of the reporting period* both monetary and non-monetary items are 'indexed up' such that they are stated in the measuring unit current at the reporting date, and therefore reflect the purchasing power on that later date.

2.10.80.20 Non-monetary items, such as property, plant and equipment and inventory, may have been acquired many periods ago when the purchasing power of the currency was greater. Non-monetary items at the beginning of the reporting period are indexed up from the date of acquisition or contribution to reflect the purchasing power at the reporting date. However, if an asset or liability has been revalued, then it is indexed up only from the date of the most recent valuation. [IAS 29.15, 18]

2.10.80.30 Monetary items – i.e. money held and items to be received or paid in money – are, on any given date, always stated at their current purchasing power at that date. Therefore, the monetary

items at the beginning of the reporting period also need to be indexed up to reflect their purchasing power at the reporting date – i.e. their opening balance is increased by the change in the price index during the reporting period to reflect the fact that the asset had higher purchasing power. The change in the price index is calculated by dividing the index at the reporting date by the index at the beginning of the reporting period. [IAS 29.8, 12]

2.10.80.40 Deferred income tax balances are calculated after the restatement of non-monetary items and require particular consideration. An entity calculates deferred tax balances in the opening statement of financial position applying the following methodology:

- remeasure the carrying amounts of non-monetary items by applying the measuring unit current at the date of the opening statement of financial position – i.e. by indexing up for the change in the price index from the date of acquisition or subsequent revaluation to the date of the opening statement of financial position;
- measure deferred tax at the date of the opening statement of financial position in accordance with IAS 12 based on those revised carrying amounts; and
- remeasure those deferred tax balances for the change in the measuring unit from the date of the opening statement of financial position to the reporting date – i.e. by indexing up for the change in the price index during the reporting period (see 2.10.140.20). [IFRIC 7.4]

2.10.80.50 If an entity applied IAS 29 in its previous period's financial statements, then the most efficient method of obtaining a restated opening statement of financial position is to restate all line items – i.e. monetary and non-monetary items – in the closing statement of financial position reported in the previous period's financial statements by applying the change in the price index during the current reporting period. This alternative approach achieves the same result because all items reported in the previous period's financial statements would have been previously restated to reflect changes in the price index to the previous reporting date. This is also consistent with how the previous period's financial statements are restated when included as comparative information in the current period's financial statements (see 2.10.130).

2.10.90 Step 2: Restate closing statement of financial position

2.10.90.10 The statement of financial position *at the reporting date* is also indexed up to current purchasing power terms.

2.10.90.20 Because monetary items are, on any given date, always stated at their current purchasing power at that date, this means that monetary amounts held at the reporting date do not require restatement.

2.10.90.30 Non-monetary items at the beginning of the reporting period are already restated to reflect the purchasing power at the reporting date in accordance with Step 1 (see 2.10.80.20). Therefore, assuming no changes to the non-monetary items in the reporting period – i.e. no additions or disposals and ignoring depreciation, amortisation and impairment – non-monetary items are carried at the same amount as in the adjusted statement of financial position at the beginning of the reporting period (i.e. the same for both years presented in the statement of financial position). If a non-monetary item is subject to depreciation or amortisation, then its carrying amount is adjusted to reflect depreciation or amortisation measured in terms of purchasing power at the reporting date.

2.10.90.40 For example, an item of land measured at cost at the beginning and at the end of the reporting period will be stated at the same amount in both statements of financial position, absent any impairment. Otherwise, a non-monetary asset purchased during the reporting period is indexed up to reflect the change in the price index from that at the date of acquisition to that at the reporting date. However, if an asset or liability has been revalued, then it is adjusted only from the date of the valuation. If the item is stated at the fair value at the reporting date (e.g. investment property), then it is not restated. [IAS 29.12–16]

2.10.90.50 Deferred taxes are calculated in accordance with IAS 12 after the restatement of non-monetary items (see chapter 3.13).

2.10.100 Step 3: Restate statement of profit or loss and OCI

2.10.100.10 A hyperinflationary statement of profit or loss and OCI includes the gain or loss from holding monetary assets or liabilities and income and expenses during the period. The gain or loss from holding monetary assets or liabilities is included in profit or loss. Any income earned or expense incurred during the period will need to be indexed up from the date initially recorded to reflect the purchasing power at the reporting date. For practical reasons, average indexation rates may be acceptable if the overall result is not materially different from the result that would be obtained by indexing individual items of income and expense based on the date at which the transaction took place. In our experience, a single annual average often may not be appropriate because of the speed and exponential way in which the index rises in a hyperinflationary economy. [IAS 29.26]

2.10.100.20 The gain or loss from holding monetary assets or liabilities is an economic concept. Suppose that an entity held 1,000 of cash (and 1,000 of share capital), and had no other assets, liabilities or transactions throughout a year when the CPI index has moved from 100 to 150. The entity has made an economic loss in purchasing power terms, and current purchasing power accounting forces this to appear in the financial statements. The economic loss exists as follows: the entity would need 1,500 of cash at the reporting date to be in the same purchasing power position as having 1,000 of cash at the beginning of the reporting period, and a loss of 500 has actually occurred.

2.10.110 Worked example of IAS 29 restatements

EXAMPLE 2 – RESTATEMENTS TO REFLECT PURCHASING POWER AT REPORTING DATE



2.10.110.10 Company H was incorporated in December 2015 with a cash capital contribution of 100, and started its operations in 2016.

2.10.110.20 The following facts are also relevant for this example.

- In December 2016, H bought a piece of land for 600, and entered into a five-year loan. The land is measured at cost.
- In October 2017, H bought inventories, which remained unsold on 31 December 2017.
- H's functional currency has been considered hyperinflationary since 2015.

2.10.110.30 The following table shows a general price index of the economy in which H operates, on specified dates.

Price index at:

31 December 2015	100
31 December 2016	150
31 October 2017	180
31 December 2017	200
Average price index during 2017	175

Statements of financial position before IAS 29 restatement

	HISTORICAL PURCHASING POWER	
	31 DEC 2017	31 DEC 2016
Share capital (contributed on 31 December 2015)	100	100
Retained earnings	1,050	800
Total equity	1,150	900
Land (acquired on 31 December 2016)	600	600
Investment securities held for trading	250	150
Inventories (acquired on 31 October 2017)	100	-
Trade receivables	500	200
Cash	100	350
Loan payable	(400)	(400)
Net assets	1,150	900

Statement of profit or loss and OCI before IAS 29 restatement

	2017
Revenue	1,150
Gain on change in fair value of investment securities	100
Interest on loan payable	(100)
Other expenses	(900)
	250

Step 1: Restate opening statement of financial position

2.10.110.40 The statement of financial position as at 31 December 2016 (1 January 2017) is restated so that it is expressed in the measuring unit current as at 31 December 2017. H can apply one of the following approaches.

- **Approach 1:** Restate the historical statement of financial position at the beginning of the reporting period:
 - non-monetary items in the statement of financial position as at 31 December 2016 are multiplied by the change in the index from the date the non-monetary items were acquired or contributed to 31 December 2017; and
 - monetary items as at 31 December 2016 are multiplied by the change in the index from 31 December 2016 to 31 December 2017 ($1.33 = 200 / 150$).
- **Approach 2:** Multiply all assets and liabilities reported in the hyperinflationary statement of financial position as at 31 December 2016 (i.e. as restated for changes in the price index to 31 December 2016) by the change in the index from 31 December 2016 to 31 December 2017 ($1.33 = 200 / 150$). [IAS 29.34]

2.10.110.50 This example does not include any income taxes. If H applied Approach 1, then to determine the opening balance of the deferred tax it would need to follow the methodology described in 2.10.80.40. Therefore, it will be more practical to apply Approach 2 because H can simply restate all the assets and liabilities including deferred tax items in its opening statement of financial position by applying the change in the price index during the current reporting period (see 2.10.80.50).

This example illustrates Approach 2.

Statement of financial position as at 1 January 2017

	31 DEC 2016 HISTORICAL PURCHASING POWER	31 DEC 2016 REPORTED IN PRIOR PERIOD ⁽¹⁾	1 JAN 2017 EXPRESSED IN 31 DEC 2017 PURCHASING POWER ⁽²⁾
Share capital (contributed on 31 December 2015)	100	150 ⁽³⁾	200
Retained earnings	800	750 ⁽⁴⁾	1,000
Total equity	900	900	1,200
Land (acquired on 31 December 2016)	600	600	800
Investment securities held for trading	150	150	200
Inventories (acquired on 31 October 2017)	-	-	-
Trade receivables	200	200	267
Cash	350	350	467
Loan payable	(400)	(400)	(534)
Net assets	900	900	1,200

Notes

1. As included in the 2016 hyperinflationary financial statements.
2. As restated for inclusion as comparatives/opening position in the 2017 financial statements. All assets and liabilities are adjusted to be expressed in 31 December 2017 purchasing power. All amounts are calculated by multiplying the corresponding figures in the statement of financial position at 31 December 2016 as reported in the prior period by the change in the price index during 2017 – i.e. $(200 / 150)$.
3. Calculated as historical purchasing power amount multiplied by change in price index from date of contribution to 31 December 2016 – i.e. $(150 / 100)$.
4. Restated retained earnings are a balancing figure derived from the other amounts in the restated statement of financial position.

Step 2: Restate closing statement of financial position

2.10.110.60 The statement of financial position as at 31 December 2017 is restated so that it is expressed in the measuring unit current at that time. Non-monetary items – i.e. share capital, land and inventories – are restated from their acquisition or contribution date. The investment securities held for trading are not restated, because they are stated at fair value at the reporting date. Monetary items – i.e. trade receivables, cash and the loan payable – as at 31 December 2017 are not restated, because they are already expressed in purchasing power at that date. [IAS 29.12, 14–15, 18]

Statement of financial position as at 31 December 2017

	31 DEC 2017 HISTORICAL PURCHASING POWER	31 DEC 2017 EXPRESSED IN 31 DEC 2017 PURCHASING POWER
Share capital	100	200 ⁽¹⁾
Retained earnings	1,050	1,161 ⁽²⁾
Total equity	1,150	1,361
Land	600	800 ⁽³⁾
Investment securities held for trading	250	250
Inventories	100	111 ⁽⁴⁾
Trade receivables	500	500
Cash	100	100
Loan payable	(400)	(400)
Net assets	1,150	1,361

Notes

1. Share capital contributed in 2015, calculated using the change in the index from 31 December 2015 to 31 December 2017 as $((200 / 100) \times 100)$.
2. Restated retained earnings are a balancing figure derived from the other amounts in the restated statement of financial position. The increase reflects the net result for the period, which includes the monetary loss of 125 (see 2.10.110.70).

3. Land bought at end of 2016, calculated using the change in the index from 31 December 2016 to 31 December 2017 as $((200 / 150) \times 600)$.
4. Inventory bought in October 2017, calculated using the change in the index from 31 October 2017 to 31 December 2017 as $((200 / 180) \times 100)$.

Step 3: Restate statement of profit or loss and OCI

2.10.110.70 Income and expenses recorded in the statement of profit or loss and OCI are restated to reflect changes in the price index from the date on which they are recorded initially in the financial statements. In this example, an average index is applied. [IAS 29.26]

Statement of profit or loss and OCI

	31 DEC 2017 HISTORICAL PURCHASING POWER	RESTATEMENT	31 DEC 2017 EXPRESSED IN 31 DEC 2017 PURCHASING POWER
Revenue	1,150	165	1,315 ⁽¹⁾
Gain on change in fair value of investments	100	14	114 ⁽²⁾
Interest on loan payable	(100)	(14)	(114) ⁽³⁾
Other expenses	(900)	(129)	(1,029) ⁽⁴⁾
Profit before gain or loss on net monetary position	250	36 ⁽⁶⁾	286
Loss on net monetary position	-	-	(125) ⁽⁵⁾
Net assets	250	-	161

Notes

1. Revenue calculated using average index for 2017 – i.e. $((200 / 175) \times 1,150)$.
2. Gain on change in fair value of investments calculated using average index for 2017 – i.e. $((200 / 175) \times 100)$.
3. Interest on loan payable calculated using average index for 2017 – i.e. $((200 / 175) \times 100)$.
4. Other expenses calculated using average index for 2017 – i.e. $((200 / 175) \times 900)$.
5. See calculation in 2.10.110.80.
6. Restatement of items in the statement of profit or loss and OCI.

Step 4: Calculate gain or loss on net monetary position

2.10.110.80 The gain or loss on the net monetary position can be:

- derived as the difference resulting from the restatement of non-monetary assets, owners' equity and items in the statement of profit or loss and OCI and the adjustment of index linked assets and liabilities (Approach 1); or
- estimated by applying the change in the general price index to the weighted average for the period of the net amounts of monetary assets and liabilities (Approach 2). [IAS 29.27]

Approach 1: Difference from restatement of non-monetary items

NON-MONETARY ITEMS				
	EXPRESSED IN PURCHASING POWER AT	AMOUNT	EXPRESSED IN PURCHASING POWER AT 31 DEC 2017	DIFFERENCE RESULTING FROM THE RESTATEMENT
Restatement of non-monetary assets				
Land	Dec 2016	600	800	200
Inventories	Oct 2017	100	111	11
Restatement of owner's equity				
Share capital	Dec 2016	(150)	(200)	(50)
Retained earnings	Dec 2016	(750)	(1,000)	(250)
Restatement of items in the statement of profit or loss and OCI (see 2.10.110.70)				(36)
Loss on net monetary position				125

Approach 2: Effect on the net monetary amounts

- Calculate the gain/loss on holding monetary items in the statement of financial position at the beginning of the reporting period based on the purchasing power as at 31 December 2017.
- Adjust the above amount for the effect of net monetary transactions that occurred during 2017 by comparing the restated carrying amounts to the historical transaction amounts.

Loss on net monetary position

	1 JAN 2017	NET CHANGE IN MONETARY ITEMS		31 DEC 2017
		RELATED TO TRANSACTIONS DURING 2017	RELATED TO TRANSACTIONS IN OCTOBER 2017	
Investment securities held for trading	150	100	-	250
Trade receivables	200	300	-	500
Cash	350	(150)	(100)	100
Loan payable	(400)	-	-	(400)

4.3.10 DEFINITIONS

4.3.10.10 Government grants are transfers of resources to an entity by a government entity in return for compliance with certain past or future conditions related to the entity's operating activities – e.g. a government subsidy. The definition of 'government' refers to governments, government agencies and similar bodies, whether local, national or international. [IAS 20.3]

4.3.10.15 Government assistance that is provided for an entity in the form of benefits that are available in determining taxable profit or tax loss, or are determined or limited on the basis of income tax liability, are not in the scope of IAS 20. [IAS 20.2(b)]

4.3.10.20 Government assistance meets the definition of a government grant even if the conditions are only a requirement to operate in certain regions or industry sectors. [SIC-10]

4.3.10.30 IAS 20 establishes accounting requirements only for government assistance in the form of grants. Therefore, the distinction between government grants and other forms of government assistance is important. Government assistance is not considered a government grant if the assistance cannot reasonably have a value placed on it or is a transaction with a government body that cannot be distinguished from the normal operating transactions of the entity. [IAS 20.3, 34–38]

4.3.10.35 If a government provides free technical or marketing advice or other services or guarantees, then the assistance is not normally recognised in the financial statements. Similarly, a government procurement contract, or similar arrangement, whereby a government body agrees to buy certain output produced by an entity is not normally distinguished from the normal operations of the entity and is not treated as a government grant. The extent of government assistance that does not take the form of a grant is, however, disclosed if it is significant and benefits the entity directly. [IAS 20.3, 34–38]

4.3.10.40 In addition, if the government provides support to an entity and is also a shareholder in that entity, then the entity needs to assess whether the government is acting in its capacity as shareholder or as government (see 7.5.390.20). If there are no terms attached to a government contribution requiring the entity to comply with certain conditions, then that contribution is most likely not a government grant. For example, a local bus company receives buses from the government; the government is also the sole shareholder of the bus company and a similar contribution is not available to other bus companies. There are no further conditions attached to the contribution of the buses, but there is a general expectation that the company will provide bus services to the local community. To determine the proper accounting for the contributed assets, the economic substance of the transaction needs to be analysed. In our view, providing public transportation in the local area is an objective of the company itself, and not a condition of the contributed assets. In addition, the contribution is not available to other companies. Therefore, we believe that in this example the contributed assets do not meet the definition of a government grant; the government is acting in its capacity as a shareholder and the asset contribution should be recognised as a capital contribution. For a discussion of the evaluation of shareholder transactions, see 1.2.80. [IAS 20.3]

4.3.20 Forgivable loans

4.3.20.10 A government may extend a loan that will be forgiven if certain conditions are met (a forgivable loan). A forgivable loan is treated as a government grant only when there is reasonable

assurance that the entity will meet the terms for forgiveness of the loan. Otherwise, the loan is recognised as a liability (see 4.3.100). [IAS 20.3, 10, IU 11–15]

EXAMPLE 1 – LOAN FORGIVABLE IF CERTAIN CONDITIONS MET



4.3.20.20 Company C is launching an airline. Government Z provides C with financing to fund the launch. The financing is in the form of a loan that will be repayable by C if the business is successful, but the amount advanced will not be repaid if the airline is launched but the business is unsuccessful. In our view, C should recognise the amount received as a liability. We believe that the liability would become a government grant (forgivable loan) if, and only if, the venture does not succeed – i.e. when it is reasonably assured that the business is not successful.

4.3.30 Waiver of expenses

4.3.30.10 In some cases, instead of providing a cash grant, a government may waive amounts payable by the entity – e.g. a liability for taxes. In our view, these qualify as government grants because in substance there is a transfer of resources, although it is in the form of a waiver of expenses (see 4.3.80).

4.3.40 RECOGNITION AND MEASUREMENT

4.3.40.10 Government grants are recognised when there is reasonable assurance that the entity will comply with the relevant conditions and the grant will be received. [IAS 20.7]

4.3.40.20 Grants are recognised in profit or loss on a systematic basis as the entity recognises as expenses the costs that the grants are intended to compensate. [IAS 20.12]

4.3.40.30 Grants that relate to the acquisition of an asset are recognised in profit or loss as the asset is depreciated or amortised. For a discussion of the presentation of such grants in the statement of financial position and in the statement of profit or loss and OCI, see 4.3.130. [IAS 20.17]

4.3.40.40 If a grant relates to a non-depreciable asset, then an entity considers the conditions related to the grant. For example, an entity is granted land on the condition that it operates a building on that land. The entity recognises the land at its fair value. In this case, the grant is recognised in profit or loss as the building is depreciated because the operation of the building is the condition attached to the grant. [IAS 20.18]

4.3.40.50 In some cases, a grant may relate to an asset that will be used both to fulfil the conditions of the grant and for other activities of the entity. In our view, the grant should be recognised in profit or loss systematically based on the cost incurred in meeting the conditions of the grant – i.e. excluding consideration of the timing of recognition of the costs of activities that are not related to the conditions of the grant.

EXAMPLE 2 – GRANT OF LAND – CONDITIONAL ON CONSTRUCTION AND OPERATION



4.3.40.60 Company D receives a grant of land. D recognises the land at its fair value. The conditions of the grant require D to construct on the land and to operate, for a given period, a sports stadium. D assesses whether the arrangement is in the scope of IFRIC 12 (see 5.12.01) and concludes that it is not. The piece of land is larger than is required to construct the stadium and D disposes of the excess land to a third party. In our view, the whole of the grant (i.e. the value of all of the land granted) should be recognised systematically based on the costs incurred in fulfilling the conditions of the grant – i.e. the costs of operating the stadium.

4.3.40.70 A grant that is compensation for expenses or losses already incurred, or for which there are no future related costs, is recognised in profit or loss in the period in which it becomes receivable. Therefore, if a government provides an entity with annual grants that do not relate to future costs, then the grant in respect of each period is recognised as it becomes receivable. [IAS 20.20]

4.3.50 Non-monetary grants

4.3.50.10 If a government grant is in the form of a non-monetary asset, then an entity chooses an accounting policy, to be applied consistently, to recognise the asset and grant at either the fair value of the non-monetary asset or the nominal amount paid (nominal value). For example, Government X gives Company Y an item of property, plant and equipment with a fair value of 50 for no consideration. Y measures both the item of property, plant and equipment and the grant either at 50 or at nominal value, which in this case is zero. IAS 20 notes that fair value is the usual approach. [IAS 20.23]

4.3.50.20 Fair value is measured in accordance with IFRS 13, which is the subject of chapter 2.4.

4.3.60 Grants related to biological assets

4.3.60.10 As an exception to the general recognition principle, an unconditional government grant related to biological assets that are measured at fair value less costs to sell (see 3.3.70.20) is recognised in profit or loss when it becomes receivable. If the government grant is conditional, then it is recognised in profit or loss when the condition is met. IAS 20 applies to government grants related to biological assets to which the cost model applies (see 3.9.70.10). [IAS 41.34–35, 37]

4.3.70 Grants related to other assets measured at fair value through profit or loss

4.3.70.10 Although there is specific guidance on accounting for government grants related to biological assets that are measured at fair value less costs to sell (see 4.3.60), there is no similar guidance for government grants related to other assets that are measured at fair value with changes therein recognised in profit or loss – e.g. investment property for which the entity applies the fair value model (see 3.4.150). In our view, in such cases, the treatment required for government grants related to biological assets should be applied by analogy. Therefore, we believe that a grant related to an asset measured at fair value with changes therein recognised in profit or loss should be recognised in profit or loss when it becomes receivable, provided that any attached conditions are fulfilled.

EXAMPLE 3A – GRANT OF INVESTMENT PROPERTY – UNCONDITIONAL



4.3.70.20 On 25 January 2017, Local Government F grants Company G a property with a fair value of 450; ownership of the property is transferred to G at the same time. G classifies the property as investment property, which it measures at fair value. The fair value of the property on 31 December 2017 is 480. There are no conditions attached to the grant.

4.3.70.23 We believe that the government grant of 450 should be recognised in profit or loss on 25 January 2017. A gain on revaluation of the property of 30 is recognised on 31 December 2017 when the investment property is revalued in accordance with the requirements of IAS 40 (see chapter 3.4).

EXAMPLE 3B – GRANT OF INVESTMENT PROPERTY – CONDITIONAL



4.3.70.25 On 30 September 2017, Company H buys a residential building, which is partially funded by a grant from local government. H classifies the building as investment property and measures it at fair value. The nominal value of the grant is repayable if specified works intended to improve the energy efficiency of the building are not finished by 30 June 2018. The specified works are finalised in May 2018.

4.3.70.30 At the end of 2017, H revalues its investment property and recognises any changes in fair value in profit or loss. Notwithstanding the fact that H received the grant attached to the building before the end of 2017, H defers recognition of the grant in profit or loss until the date on which the conditions are met. Accordingly, H recognises income from the grant on completion of the specified works in May 2018; for a discussion of repayable grants, see 4.3.90.

4.3.80

Grants in form of waiver of expenses

4.3.80.10 In our view, the general recognition principles apply to grants in the form of a waiver of expenses. Therefore, we believe that such grants should be recognised in profit or loss on a systematic basis as the entity recognises as expenses the costs the grant is intended to compensate.

EXAMPLE 4 – WAIVER OF CURRENT TAX PAYABLE



4.3.80.20 Company N receives an investment tax credit (ITC) in the form of a waiver of current taxes payable and it concludes that accounting for the ITC by analogy to a government grant is appropriate (see 3.13.710).

4.3.80.25 If the expenditure to which the grant relates is incurred in the period in which the tax is waived, then the benefit of the tax relief is reflected in that period. If the expenditure will be incurred in a future period, then the benefit of the tax relief is deferred in the statement of financial position until the expenditure is incurred.

4.3.80.27 Similarly, if the grant relates to the acquisition of an asset, then the benefit of the tax relief is deferred in the statement of financial position and recognised in profit or loss as the related asset is depreciated.

4.3.80.30 For guidance on the presentation of grants in the form of a waiver of expenses, see 4.3.150.

4.3.90 Repayment

4.3.90.10 A government grant may be required to be repaid under certain conditions – e.g. if the actual costs to which the grant relates are lower than expected.

4.3.90.20 If the amount is recognised as a government grant and subsequently some or the entire amount becomes repayable unexpectedly, then the repayment is accounted for as a change in estimate (see 2.8.110). In our view, the effect of the change in estimate should be recognised in the period in which management concludes that it is no longer reasonably assured that the terms for forgiveness will be met. In our view, a financial liability should be recognised at the same time for the amount of the repayment, based on the general requirements of IAS 39 – i.e. at fair value (see 7.6.20). The amount would differ from the face value of the grant if the interest rate is not a market rate of interest (see 4.3.100). In our view, the repayable portion of the credit previously recognised should be reversed as follows:

- the credit may have been shown as deferred income or a credit to an asset, in which case the reversal should be against the appropriate line item in the statement of financial position; and/or
- the credit may have been recognised as a reduction in depreciation or amortisation of an asset or as income, in which case the reversal should be against the appropriate line item in profit or loss. [IAS 20.32]

4.3.90.30 The entity also considers whether the change in circumstances that gave rise to the repayment of the loan is an indication of impairment (see 3.10.110). [IAS 20.33]

4.3.90.40 In some circumstances, a financial liability in respect of a grant that becomes repayable may be forgiven; for a discussion of forgivable loans, see 4.3.20. In our view, if there is reasonable assurance that the entity will meet the terms for forgiveness of such a loan, then it should be accounted for as a government grant and the amount received recognised over the compliance period. Otherwise, we believe that the loan should be treated as a financial liability.

4.3.100 Low-interest loans

4.3.100.10 Low-interest or interest-free loans from a government are recognised and measured in accordance with IAS 39. IAS 39 requires loans at below-market rates to be initially measured at their fair value – e.g. the present value of the future cash flows discounted at a market interest rate – and interest expense to be recognised on the loan subsequently under the effective interest rate method (see 7.6.60 and 240). The benefit that is the government grant is measured as the difference between the fair value of the loan on initial recognition and the amount received, which is accounted for according to the nature of the grant. [IAS 20.10A, 39.43, AG64]

4.3.100.20 In some situations, a government may provide a loan at market rate that will be modified to a lower rate when the entity spends the funds provided on qualifying research and development

activities. In our view, the difference between the fair value of the loan at a market interest rate and the fair value of the low interest rate loan should be accounted for as a government grant. Payments on research activities are expensed as they are incurred, whereas payments on development activities are capitalised when the criteria set out in IAS 38 are met (see 3.3.120). Therefore, in this situation, we believe that the part of the government grant related to research activities and development costs that are not capitalised should be recognised in profit or loss when the related costs are incurred; we also believe that an entity should choose an accounting policy, to be applied consistently, either to deduct the grant related to capitalised development costs from the related intangible asset or to recognise such grants as deferred income and release them to profit or loss as the capitalised development costs are amortised; for a discussion of the presentation of grants related to assets, see 4.3.130. In this way, the benefit of the grant is recognised on a systematic basis because the entity recognises, as expenses, the costs the grant is intended to compensate.

4.3.110 Emissions allowances

4.3.110.10 IFRS does not have any specific guidance on accounting for emissions allowances received in a 'cap and trade' scheme. In our view, if an allowance is received from a government for less than its fair value, then the entity should choose an accounting policy, to be applied consistently, either to recognise the resulting government grant at fair value (as the difference between the fair value of the allowance and the consideration (if any) paid) or to recognise it at the nominal amount paid for the certificate. IAS 20 notes that fair value is the usual approach for non-monetary grants (see 3.3.160 and 4.3.50.10). The grant is recognised as deferred income and recognised in profit or loss on a systematic basis over the compliance period, regardless of whether the allowance received continues to be held by the entity. Disposals of certificates or changes in their carrying amount – e.g. because of impairment, which is the subject of chapter 3.10 – do not affect the manner in which grant income is recognised. As an alternative to the deferred income approach, we believe that an entity may present an allowance net of the deferred government grant. For further discussion of the accounting for emissions allowance schemes, see 3.12.510. [IAS 20.23]

4.3.110.20 Fair value is measured in accordance with IFRS 13, which is the subject of chapter 2.4.

4.3.120 PRESENTATION AND DISCLOSURES

4.3.130 Presentation of grants related to assets

4.3.130.10 Government grants related to assets other than biological assets measured at fair value less costs to sell and other assets measured at fair value with changes therein recognised in profit or loss (see 4.3.70), may be either deducted from the cost of the asset (net presentation) or presented separately as deferred income that is amortised over the useful life of the asset (gross presentation). In our view, this approach also applies to grants related to assets held by a lessee under a finance lease. An entity chooses a presentation format in the statement of financial position, to be applied consistently to all government grants related to assets. [IAS 8.13, 20.24]

4.3.130.15 If net presentation in the statement of financial position is used, then the grant reduces the cost and therefore reduces the depreciation expense recognised. However, if an entity presents government grants related to assets (other than biological assets measured at fair value less costs to

sell and other assets measured at fair value with changes therein recognised in profit or loss) gross in the statement of financial position, then IAS 20 does not require a specific presentation in the statement of profit or loss and OCI. In our view, an entity should choose an accounting policy, to be applied consistently, to present such grants either as income or as a reduction in the related expense. [IAS 20.27]

EXAMPLE 5A – GRANT RELATED TO ASSET – PRESENTATION IN STATEMENT OF FINANCIAL POSITION AND DEPRECIATION



4.3.130.20 Company F received a government grant of 200 to acquire machinery. The machinery costs 700 and has an estimated useful life of five years. If F presents the grant as a deduction from the cost of the machinery, then the asset is shown in the statement of financial position at its net cost of 500 (700 - 200). The grant is recognised in profit or loss over the useful life of the depreciable asset and presented as a reduction to the annual depreciation expense of 100 (500 / 5).

4.3.130.30 If the grant is presented as deferred income, then the machinery is shown at its gross cost of 700 and annual depreciation on the machinery is 140 (700 / 5). In addition, F presents deferred income of 200. Each year, 40 (200 / 5) is recognised in profit or loss.

4.3.130.35 In our view, the choice of net or gross presentation (see 4.3.130.10) has no impact on the timing of recognition in profit or loss.

EXAMPLE 5B – GRANT RELATED TO ASSET – PRESENTATION OF DEPRECIATION AND AMORTISATION OF DEFERRED INCOME



4.3.130.40 Continuing Example 5A, assume that the machinery is used in F's production plant for producing inventories for sale in the ordinary course of business. The depreciation of the machinery is reflected in the cost of inventories. In accordance with F's accounting policies, the machinery is shown at its gross cost – i.e. the grant is presented as deferred income.

4.3.130.45 In our view, the amortisation of the deferred income should be included in the cost of inventory. This means that the amortisation of the deferred income will be recognised in profit or loss at the same time as the depreciation on the machinery – i.e. as inventory is sold. This approach is consistent with the principle in IAS 20 that the benefit of a government grant is recognised at the same time as the expenses to which it relates.

4.3.130.50 In our view, if an entity presents government grants as a deduction from the related asset, but the grant is received before the asset is recognised, then the grant should be shown as deferred income until the asset is built or acquired.

4.3.130.60 The deferred income is generally classified as a non-current liability when an entity presents a classified statement of financial position (see 3.1.10.10).

Presentation of grants related to income

4.3.140

4.3.140.10 An entity chooses a presentation format, to be applied consistently, either to offset a grant related to income against the related expenditure or to include it in other income. For example, Company P receives a government grant of 100 to fund research costs of 500. P has a choice of presenting net research costs of 400, or gross research costs of 500 and other income of 100. Regardless of P's choice, it is applied consistently. [IAS 8.13, 20.29]

Presentation of grants in form of waiver of expenses

4.3.150

4.3.150.10 In our view, either a net or a gross approach may be used to present a grant in the form of a waiver of expenses.

4.3.150.20 For a discussion of the accounting and presentation consequences of a waiver of taxes that is determined to be an ITC, see 3.13.670.

Related party disclosures

4.3.160

4.3.160.10 If the government is also a shareholder, then additional related party disclosures are required (see chapter 5.5).

4.4

Employee benefits

4.4.10	Scope	1042
4.4.20	Share-based payment or IAS 19 employee benefit	1042
4.4.30	Components with different features	1042
4.4.40	Equity instruments of entities outside group	1043
4.4.50	Tax payments related to share-based payments	1043
4.4.60	Cash payments based on estimates of fair value	1043
4.4.70	Cash payments depending on share price vs based on share price	1043
4.4.80	Types of employee benefit	1044
4.4.90	Post-employment benefits	1044
4.4.100	Definition and scope of post-employment benefits	1044
4.4.110	Severance payments	1045
4.4.120	Constructive obligations	1045
4.4.130	Distinction between defined contribution and defined benefit plans	1045
4.4.140	Minimum benefit guarantees	1046
4.4.150	Impact of vesting conditions	1046
4.4.160	Change in classification	1046
4.4.170	Multi-employer plans	1047
4.4.180	Availability of sufficient information	1048
4.4.190	Change in accounting treatment	1048
4.4.200	Group plans	1049
4.4.210	Contractual agreement or stated policy exists	1049
4.4.220	No contractual agreement or stated policy in place	1050
4.4.230	Introduction or removal of stated policy or contractual agreement	1051
4.4.240	State plans	1052
4.4.250	Defined contribution plans	1052
4.4.260	Vesting conditions and advance contributions	1052
4.4.270	Refund of contributions or contribution holiday	1052
4.4.280	Refund or contribution holiday for multi-employer plan	1053
4.4.290	Presentation and disclosures	1053
4.4.300	Defined benefit plans	1053
4.4.310	Basic principles	1053
4.4.320	Interest in a fund	1054
4.4.330	Inter-related post-employment benefit plans	1054
4.4.340	Recognition and measurement	1055
4.4.350	Timing and frequency of actuarial valuations	1055
4.4.370	Net defined benefit liability (asset)	1056
4.4.380	Defined benefit obligation	1056
4.4.390	Actuarial valuation method	1056
4.4.395	Contribution-based promises	1056
4.4.400	Attributing benefits to periods of service	1057
4.4.410	Actuarial assumptions	1058
4.4.420	Demographic assumptions	1059
4.4.430	Benefits	1059
4.4.460	Risk-sharing arrangements	1060
4.4.500	Taxes payable by plan	1062
4.4.510	Discount rate	1062
4.4.520	High-quality corporate bonds	1062
4.4.530	Deep market	1063
4.4.540	Discount rate methodologies	1063

4.4.550	Plan assets	1065
4.4.560	Criteria for qualifying as plan assets	1065
4.4.570	Restriction on availability	1066
4.4.580	Reimbursement for benefits paid	1066
4.4.590	Ability to use plan assets	1066
4.4.600	Financial instruments issued by entity	1066
4.4.610	Replacement assets	1067
4.4.620	Measurement	1067
4.4.630	Assets that do not qualify as plan assets	1068
4.4.640	Reimbursement rights	1068
4.4.650	Insurance policies	1070
4.4.660	Insurance policies that qualify as plan assets	1070
4.4.680	Insurance policies that do not qualify as plan assets	1072
4.4.690	Asset ceiling	1072
4.4.700	Sharing benefits	1072
4.4.710	Economic benefits available	1073
4.4.720	Intended use of surplus	1073
4.4.730	Economic benefit available as refund	1073
4.4.740	The right to a refund	1073
4.4.750	Measurement of economic benefit	1074
4.4.770	Economic benefit available as reduction in contributions	1075
4.4.780	Minimum funding requirements	1075
4.4.790	Minimum funding requirement for future service	1076
4.4.800	Minimum funding requirement to cover existing shortfall	1077
4.4.810	Multi-employer plans	1077
4.4.820	Defined benefit cost	1077
4.4.830	Components of defined benefit cost	1077
4.4.840	Refunds of contributions	1077
4.4.850	Service cost	1078
4.4.860	Current service cost	1078
4.4.870	Past service cost	1078
4.4.880	Plan amendment	1078
4.4.890	Curtailment	1079
4.4.900	Timing of recognition of past service cost	1080
4.4.910	Settlements	1081
4.4.920	Definition and scope	1081
4.4.930	Timing of recognition	1083
4.4.940	Net interest	1084
4.4.950	Remeasurements	1084
4.4.960	Actuarial gains and losses	1084
4.4.970	Return on plan assets	1085
4.4.980	Administration costs	1085
4.4.990	Taxes payable by plan	1086
4.4.1000	Taxes payable by entity	1086
4.4.1010	Net defined benefit liability (asset) denominated in foreign currency	1087
4.4.1020	Determining remeasurements	1087
4.4.1030	Change in estimate	1089
4.4.1040	Recognition of remeasurements	1089
4.4.1050	Errors	1089
4.4.1060	Presentation and disclosures of defined benefit plans	1090
4.4.1070	Presentation	1090
4.4.1080	Offsetting	1090

4.4.1090	Current and non-current presentation	1090
4.4.1100	Service cost and net interest	1090
4.4.1110	Curtailments or settlements	1090
4.4.1120	Group plans	1091
4.4.1130	Disclosures	1091
4.4.1140	Expected contributions and benefit payments	1091
4.4.1150	Related party disclosures	1091
4.4.1160	Multi-employer plans and group plans	1092
4.4.1170	Insured benefits	1092
4.4.1180	General principles	1092
4.4.1190	Insurance policies qualifying as plan assets	1092
4.4.1200	Current salary policies and other limited cover	1092
4.4.1210	Death-in-service benefits	1093
4.4.1220	Short-term employee benefits	1094
4.4.1230	Definition and scope	1094
4.4.1240	Change in classification	1095
4.4.1250	Paid absences	1096
4.4.1260	Measurement	1097
4.4.1270	Profit-sharing and bonus plans	1097
4.4.1280	Measurement	1098
4.4.1290	Low-interest loans	1099
4.4.1300	Non-monetary benefits	1100
4.4.1310	Other long-term employee benefits	1100
4.4.1320	Definition and scope	1100
4.4.1330	Defined contribution long-term benefit plans	1102
4.4.1340	Accounting for defined benefit long-term benefit plans	1102
4.4.1350	Long-term profit-sharing and bonus plans	1103
4.4.1360	Stay period	1105
4.4.1390	Separate awards with different service periods	1106
4.4.1400	One single award	1107
4.4.1410	Disability benefit	1109
4.4.1420	Long-term benefits not service-related	1109
4.4.1430	Presentation and disclosures	1109
4.4.1440	Termination benefits	1109
4.4.1450	Definition and scope	1109
4.4.1460	Recognition	1112
4.4.1470	Measurement	1113
4.4.1480	Presentation and disclosures	1114
4.4.1490	Consolidation of employee benefit plans and employee benefit trusts	1114
4.4.1500	Loans granted to and by post-employment or other long-term benefit plans	1114
4.4.1510	Pension plan loans to sponsor	1115
4.4.1520	Future developments	1116

4.4 Employee benefits

CURRENTLY EFFECTIVE REQUIREMENTS

This publication reflects IFRS in issue at 1 August 2017, and the currently effective requirements cover annual periods beginning on 1 January 2017.

The requirements related to this topic are derived from the following.

STANDARD	TITLE
IAS 19	Employee Benefits
IFRIC 14	IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction

FORTHCOMING REQUIREMENTS

For this topic, there are no forthcoming requirements.

FUTURE DEVELOPMENTS

The currently effective requirements that may be affected by future developments are highlighted with a * and are briefly discussed in 4.4.1520.

falls, then the employee is not entitled to the payment. In our view, although the cash payment depends on the share price, it is not based on the share price. Therefore, we believe that the cash payment is not a share-based payment but an employee benefit in the scope of IAS 19 (see 4.5.1950.10).

4.4.70.20 A cash payment may be based on but not equal to the share price. If an employee is entitled to a payment equal to the share price at vesting date, then the employee participates one-to-one in share price increases. In our view, a payment determined as a linear function of the share price (or its movements) is based on the share price and therefore is a share-based payment. For example, if the employee is entitled to 60 percent of the share price or to 200 percent of the share price, then we believe that the payment is based on the value of the equity instruments and therefore is a share-based payment (see 4.5.1950.20).

4.4.80 Types of employee benefit

4.4.80.10 Employee benefits are all forms of consideration given by an entity in exchange for service rendered by employees or for the termination of employment. [IAS 19.8]

4.4.80.20 IAS 19 sets out the requirements for four types of employee benefit:

- provided in exchange for services rendered by employees:
 - post-employment benefits (see 4.4.90);
 - short-term employee benefits (see 4.4.1220); and
 - other long-term employee benefits (see 4.4.1310); and
- provided in exchange for termination of employment:
 - termination benefits (see 4.4.1440). [IAS 19.5]

4.4.90 POST-EMPLOYMENT BENEFITS

4.4.100 Definition and scope of post-employment benefits

4.4.100.10 Post-employment benefits are employee benefits (other than termination benefits and short-term employee benefits) that are payable after the completion of employment (before or during retirement) – e.g. pensions, lump sum payments on retirement or medical benefits after employment. [IAS 19.5(b), 8, 26]

4.4.100.20 Some plans are specifically established to provide benefits both during and after the completion of employment. For example, Company K has a fund for paid annual leave. Any surplus in the fund is used to make pension payments. In our view, a plan that is established specifically to pay benefits both during and after the completion of employment should be treated as a long-term employee benefit plan (see 4.4.1310), rather than as a post-employment benefit plan.

4.4.100.30 If a plan offers different benefits (i.e. under different benefit formulas) to different groups of beneficiaries (e.g. active employees vs retirees) and is funded by separate pools of assets or a single pool of assets but with appropriate controls in place, then the benefits offered during employment and post-employment are accounted for separately because separate promises are made to employees and retirees, and under different benefit formulas. As such, benefits offered to retirees are accounted for as a post-employment benefit (see 4.4.200.20–30 and 330.20).

4.4.100.40 Long-term disability benefits are an example of other long-term employee benefits (see 4.4.1410). However, if a long-term disability benefit is payable only after termination of employment, then in our view the benefit is a post-employment benefit. In addition, in our view a long-term disability benefit that is payable only if an employee remains employed but is no longer providing services should also be accounted for as a post-employment benefit. We believe that this is, in substance, the same as if employment ends for the employee. [IAS 19.155, 157]

4.4.110 Severance payments

4.4.110.10 Severance payments and other amounts that are always payable on cessation of employment, regardless of the reason for the employee leaving, are post-employment benefits, rather than termination benefits. For example, Company B makes payments to its employees on cessation of employment regardless of the reason that the employee leaves B's employment. The employee is entitled to one week's salary for each year of service provided, based on the employee's final salary. Because the amount is payable on cessation of employment regardless of the reason for leaving, the plan is a post-employment benefit plan. [IAS 19.164]

4.4.110.20 The normal principles apply in determining whether such post-employment plans give rise to defined benefit or defined contribution plans. The amount of the payments is often based on factors such as the number of years of service or final salary. Therefore, these plans often give rise to a defined benefit plan. The principles set out in 4.4.300–1200, including the requirements to discount the obligation and to use the projected unit credit method, apply to any defined benefit arrangements and therefore also to these plans. Example 31, illustrating the year one calculations for an other long-term employee benefit, also applies to severance payments.

4.4.120 Constructive obligations

4.4.120.10 Post-employment benefit plans include not only formal arrangements but also informal practices that give rise to 'constructive obligations'. Therefore, the accounting treatment is the same, regardless of whether an obligation is legal or constructive. [IAS 19.61]

4.4.120.20 Constructive obligations arise when an entity has no realistic alternative but to pay the employee benefits. They may arise from informal past practices or communication with employees. For further discussion of:

- classification, see 4.4.130.60;
- actuarial assumptions, see 4.4.430; and
- general guidance on constructive obligations, see 3.12.60.

4.4.130 Distinction between defined contribution and defined benefit plans

4.4.130.10 Post-employment plans are classified as either defined contribution or defined benefit plans. The classification determines the accounting treatment. [IAS 19.27]

4.4.130.20 A post-employment plan is classified as a defined contribution plan if the entity pays fixed contributions into a separate entity (a fund) and will have no further obligation (legal or constructive) to pay further amounts if the fund has insufficient assets to pay all employee benefits relating to current and prior service. All other post-employment plans are defined benefit plans. [IAS 19.8, 28]

4.4.170.50 Whether an entity applies defined benefit or defined contribution accounting, it applies IAS 37 in determining when to recognise and how to measure a liability that arises from the wind-up of a multi-employer defined benefit plan or the entity's withdrawal from a multi-employer defined benefit plan (see chapter 3.12). [IAS 19.39]

4.4.180 **Availability of sufficient information**

4.4.180.10 It is clear from their definition that multi-employer plans expose participating entities to the actuarial risk of other entities' employees, yet the standard envisages that it may be possible for an entity to apply defined benefit accounting to its proportionate share of the plan. Therefore, exposure to the actuarial risk of other entities' employees alone is not enough to justify the application of defined contribution accounting to a defined benefit multi-employer plan. In our view, sufficient information is available for defined benefit accounting to be applied for participation in a multi-employer defined benefit plan if:

- the participant in the multi-employer plan has access to information about all components of the plan (e.g. plan assets, defined benefit obligation, remeasurements, service cost, net interest) and not only knowledge of the net deficit or surplus (i.e. an actuarial valuation on an IAS 19-compliant basis for the plan as a whole is available to participating entities); and
- the stated basis for allocating the deficit or surplus is reasonably stable. For this to be the case, the methodology for allocating the deficit or surplus should remain consistent and the allocation should not result in significant variability of the entity's proportion of the deficit or surplus. [IAS 19.36]

4.4.180.20 In our view, the assessment of whether the stated basis for allocating the deficit or surplus is reasonably stable should be made in relation to the entity participating in the plan. As such, the size of the entity's share of the plan may affect this assessment.

EXAMPLE 1 – MULTI-EMPLOYER PLAN – ASSESSING STABILITY OF ALLOCATION BASIS



4.4.180.30 Companies B and D, together with other companies, participate in a multi-employer benefit plan. The plan allocates the deficit or surplus based on a plan-wide contribution rate that is calculated based on each company's relative percentage of pensionable earnings. B and D estimate that their relative percentage of pensionable earnings may increase or decrease by five percentage points from year to year. B's share of the plan is significant, and therefore it determines that a five percentage point change in its relative percentage of pensionable earnings would not result in significant variability in the proportion of the deficit or surplus that would be allocated. Conversely, D does not have a significant share of the plan and it determines that a five percentage point change in its relative percentage of pensionable earnings would result in significant variability, and therefore this may not be considered a reasonably stable basis for allocating the deficit or surplus.

4.4.190 **Change in accounting treatment**

4.4.190.10 If an entity has been accounting for a multi-employer defined benefit plan as a defined benefit plan and the information that was previously available becomes unavailable, then the plan is accounted for going forward as if it were a defined contribution plan. In our view, this should be treated as a change in estimate following the specific requirements for changes in estimates related to

defined contribution plans – i.e. as a change in estimate recognised as part of the defined contribution cost in profit or loss in the period. [IAS 19.36]

4.4.190.20 If an entity has been accounting for a multi-employer defined benefit plan as a defined contribution plan but sufficient information then becomes available that enables it to account for that plan as a defined benefit plan (see 4.4.300), then in our view this should be treated as a change in estimate following the specific requirements for changes in estimates related to defined benefit plans – i.e. as remeasurements in the period (see 4.4.950). We believe that any deficit or surplus at the date of reclassification of the plan should be included in the calculation of remeasurements of the net defined benefit liability (asset) as if the gain or loss arose in the first year in which defined benefit accounting is applied as a result of new information becoming available. It is not a plan amendment (see 4.4.880) because the entity neither introduces a defined benefit plan nor changes the benefits payable under an existing defined benefit plan. [IAS 19.104]

4.4.200 **Group plans**

4.4.200.10 Defined benefit plans in which entities under common control share risks are group plans rather than multi-employer plans. Group plans are classified as either a defined contribution plan or a defined benefit plan in accordance with the terms of the plan (see 4.4.130). Under IAS 19, the accounting for defined benefit group plans in separate or individual financial statements (see 2.1.110–120) depends on whether there is a contractual agreement or stated policy for charging the net defined benefit cost to individual group entities (see 4.4.210–220). [IAS 19.40–41]

4.4.200.20 IAS 19 does not specifically address group plans that have both defined contribution and defined benefit components – e.g. defined benefit for all employees of some group entities and defined contribution for all employees of other group entities.

EXAMPLE 2 – GROUP PLAN WITH DEFINED CONTRIBUTION AND DEFINED BENEFIT COMPONENTS



4.4.200.30 Companies C and B are under the common control of Parent P. C and B participate in a single plan with P for the benefit of their employees, with a stated policy for charging the IAS 19 cost for the plan as a whole (see 4.4.210.10). C's employees are entitled to a defined contribution award on retirement and B's employees are entitled to a defined benefit award on retirement. The contributions made by C and B and their employees are held in a single asset pool in a trust. C and B might wish to account for the defined contribution and defined benefit components of the plan separately – i.e. C accounts for the plan as a defined contribution plan whereas B accounts for it as a defined benefit plan. In our view, for this to be appropriate, as a minimum there should be controls in place within the trust that prevent any use of assets related to defined contribution members to settle obligations related to defined benefit members and vice versa. If such restrictions on availability are not in place, then we believe that the plan as a whole should be accounted for as a single plan and defined benefit accounting should be applied at a group level (see 4.4.210.10).

4.4.210 **Contractual agreement or stated policy exists**

4.4.210.10 If a contractual agreement or stated policy exists for charging individual group entities the IAS 19 cost for the plan as a whole, then an entity recognises the net defined benefit cost allocated

- a policy or agreement is removed by a legal sponsor, then other participants should derecognise their portion of the deficit and recognise the gain resulting from that change in estimate in profit or loss (see 4.4.190.10), whereas the sponsor should account for a remeasurement loss on the net defined benefit liability (see 4.4.190.20); or
- a policy or agreement is introduced, then this would result in a remeasurement gain on the net defined benefit liability for the legal sponsor and a remeasurement loss equal to the newly recognised share of net defined benefit liability for other participants.

4.4.240 State plans

4.4.240.10 State plans are established by legislation to cover all, or specific groups of, entities and are not operated by the employer. [IAS 19.44]

4.4.240.20 State plans are accounted for in the same way as multi-employer plans. If the employer has an obligation only to pay contributions and has no legal or constructive obligation to pay future benefits, then state plans are defined contribution plans. Otherwise, they are defined benefit plans. [IAS 19.43, 45]

4.4.240.30 In our experience, there is generally insufficient information available about defined benefit state plans to apply defined benefit accounting. Therefore, defined contribution accounting is normally applied to such state plans.

4.4.250 DEFINED CONTRIBUTION PLANS

4.4.250.10 An entity accounts for its contributions to defined contribution plans on an accrual basis. An asset or liability may result from advance payments or payments due, respectively, to a defined contribution fund. [IAS 19.51]

4.4.260 Vesting conditions and advance contributions

4.4.260.10 If contributions are made to a defined contribution plan in advance of services being rendered, or if a defined contribution plan has vesting conditions, then some believe that under paragraph 51(a) of IAS 19 the contributions should be recognised as a prepayment and that the prepayment should be expensed as the employee provides services that entitle them to the benefits. However, under IAS 19 the entity's obligation for each period is determined by the amounts to be contributed for that period. The IFRS Interpretations Committee discussed the issue of vesting conditions and noted that each contribution to a defined contribution plan is recognised as an expense over the period of service that obliges the employer to pay this contribution to the defined contribution plan, rather than over the period of service that entitles the employee to receive the benefit. [IAS 19.51, IU 07-11]

4.4.270 Refund of contributions or contribution holiday

4.4.270.10 In unusual cases, an entity may be entitled to a refund of contributions, to a contribution holiday or to a reduction in future contributions in respect of past services under a defined contribution plan – e.g. if the plan has vesting conditions and an employee forfeits benefits as a result of failing to meet the required service conditions. The IFRS Interpretations Committee discussed a scenario in which an entity is entitled to a refund of contributions and noted that a refund is recognised as an asset and as income when the entity becomes entitled to it – e.g. by the employee failing to meet the vesting condition. In our view, a contribution holiday or a reduction in contributions for past services, the cost of which has already been recognised as personnel expenses, should be treated in the same

way as a refund. Accordingly, we believe that a contribution holiday or a reduction in future contributions that will accrue in future periods for services to be provided after the reporting date should not be anticipated. Instead, the benefit should be recognised by way of a lower (or no) contribution expense in those future periods. [IU 07-11]

EXAMPLE 5 – DEFINED CONTRIBUTION PLAN WITH POTENTIAL REFUND OF CONTRIBUTIONS



4.4.270.20 Company Y makes contributions to a defined contribution plan on behalf of its employees. Each employee's vested interest is 100% if employment ends after age 60; 75% if employment ends after age 55; and 50% if employment ends before age 55. To the extent that the interest does not vest, Y is entitled to a contribution refund. Y expenses 100% of the defined contributions that fall due in respect of each period. If an employee does not complete the required service to become entitled to 100% of the contributions, then Y recognises an asset and income when it becomes entitled to the resultant refund – i.e. on a termination of employment.

4.4.280 Refund or contribution holiday for multi-employer plan

4.4.280.10 An employer that participates in a defined benefit multi-employer plan may become entitled to a refund of contributions (see 4.4.840) or to a contribution holiday if the plan is in surplus. In our view, an asset should not be recognised for an anticipated refund of contributions or a contribution holiday for a defined benefit multi-employer plan that is accounted for as a defined contribution plan because insufficient information is available to apply defined benefit accounting. This is because the factors that give rise to the exemption from defined benefit accounting – i.e. the inability to obtain sufficient information to calculate the entity's proportionate share – and therefore the exemption from recognising an asset or liability, apply until the refund is received or receivable. However, the surplus and the implications – i.e. the expected reduction in contributions – should be disclosed. [IAS 19.148(d)(iv)]

4.4.290 Presentation and disclosures

4.4.290.10 Assets and liabilities related to defined contribution plans are classified as current or non-current in accordance with the general classification requirements (see 3.1.20).

4.4.290.20 The amount recognised as an expense for defined contribution plans is disclosed. Information about contributions to defined contribution plans for key management personnel is also disclosed, if applicable. [IAS 19.53–54, 24.17]

4.4.300 DEFINED BENEFIT PLANS

4.4.310 Basic principles

4.4.310.10 IAS 19 establishes requirements for the basis of the valuation as well as principles for the actuarial assumptions to be used in valuing defined benefit plans.

4.4.310.20 Estimates, averages and computational shortcuts may be used only if they provide a reliable approximation of the detailed computations that are required. Computational shortcuts may be appropriate in practice when performing a roll-forward of a previous valuation – e.g. from valuation date to a subsequent reporting date (see 4.4.350). [IAS 19.58, 60]

4.4.320 **Interest in a fund**

4.4.320.10 An entity offsets qualifying plan assets against the related obligation to employees; it does not consolidate the fund that holds the plan assets. For further discussion, see 4.4.1490. [IAS 19.57(a)(iii), 113]

4.4.330 **Inter-related post-employment benefit plans**

4.4.330.10 An entity may have more than one post-employment benefit plan. In our view, if the post-employment benefits are financed through a single scheme, funded by one asset pool, and therefore share the same investment risk, then they should generally be considered and reported as a single plan, and the terms of each component of the plan should be disclosed separately.

4.4.330.20 Conversely, if different benefits are funded through different funds or are administered by one fund but have different arrangements, subject to different investment risk, then we believe that they should be considered as separate plans. They may be combined in preparing disclosures for the financial statements if they are all in a net surplus or a net liability position. Otherwise, offsetting is appropriate only if there is a legal right to set off between underfunding of one plan and overfunding of another plan (see 4.4.1080). [IAS 19.131]

4.4.330.30 In our view, the fact that there are the same beneficiaries in two different plans does not automatically result in a single plan even if one plan may have certain rights to the surplus in the other plan. For example, access of an unfunded post-employment medical benefit plan under specific circumstances to part of the surplus of another post-employment plan does not generally result in a plan asset in the medical benefit plan if the amount of the surplus is not transferred but only 'reserved' – i.e. the surplus 'reserved' for the medical benefit plan would decline if the investments decreased or the defined benefit obligation increased in the original post-employment benefit plan. Treating such an arrangement as one plan could result in disguising the true position of the arrangement, because the 'unreserved' surplus of the post-employment plan could be offsetting the deficit of the medical plan. However, if there is a right to set off, then the 'reserved' surplus may be a plan asset of the medical plan. In this case, an entity needs to consider its legally enforceable right to use a surplus in one plan to settle obligations under another plan and its intention to settle the plans on a net basis (see 4.4.1080).

EXAMPLE 6 – DEFINED BENEFIT PLANS – INTER-RELATED POST-EMPLOYMENT BENEFIT PLANS

4.4.330.40 Company H is required by law to make severance payments to employees when they retire or leave. Severance payments reduce pension entitlement. If H anticipates that the severance payments will be such that no pension payments will be required, then we believe that the net defined benefit liability (asset) should reflect only the severance payments. If pension payments will be required in addition to the severance payments, then the pension liability should reflect the amounts that will be payable as a top-up to the severance payment. In any case, we believe that the calculation of the severance liability and the pension liability should reflect consistent actuarial assumptions, such as estimated future salary increases, but may have different inputs – e.g. benefits may be based on the final salary for the pension scheme, but on the average salary for the severance liability.

Recognition and measurement

4.4.340

4.4.340.10 Accounting for defined benefit plans involves the following steps.

- Determining the deficit or surplus in the plan, by:
 - determining the present value of the defined benefit obligation (see 4.4.380); and
 - deducting the fair value of any plan assets (see 4.4.550).
- Adjusting the amount of the deficit or surplus for any effect of limiting a net defined benefit asset to the asset ceiling (see 4.4.690).
- Determining the amounts to be recognised in profit or loss (see 4.4.830).
- Determining the remeasurements of the net defined benefit liability (asset) to be recognised in OCI (see 4.4.950). [IAS 19.57]

4.4.350 **Timing and frequency of actuarial valuations**

4.4.350.10 To determine the present value of the defined benefit obligation, an entity needs to obtain an actuarial valuation. The timing or frequency of actuarial valuations is not mandated by IFRS. Actuarial valuations are required to be regular enough for the amounts recognised in the financial statements not to differ materially from the amounts that would be determined at the reporting date. Therefore, a valuation a few months before the reporting date is acceptable if it is adjusted for material subsequent events – e.g. discount rate changes – up to the reporting date. [IAS 19.58]

4.4.350.20 IFRS is silent on the treatment of a change in the timing of actuarial valuations. In our view, because the change in the timing does not change the measurement objective, it is not a change in accounting policy (see chapter 2.8). In our view, such a change can be made if the measurement of the obligation would still not be materially different from a measurement based on an actuarial valuation obtained at the reporting date.

EXAMPLE 7 – DEFINED BENEFIT PLANS – TIMING OF ACTUARIAL VALUATION

4.4.350.30 Company D previously measured its defined benefit obligation based on an actuarial valuation obtained at the reporting date; the most recent actuarial valuation was obtained at 31 December 2016. We believe that D may measure the obligation at 31 December 2017 based on an actuarial valuation obtained at 30 September 2017 if it adjusts the obligation for material subsequent events up to 31 December 2017.

4.4.350.40 In our view, asset values should generally be determined at the annual reporting date, even if the valuation of the obligation is done in advance and is adjusted forward, because these values are generally observable in the market. [IAS 19.58]

4.4.360 **Interim reporting**

4.4.360.10 The preparation of interim financial information does not necessarily involve obtaining an updated actuarial valuation. Although the basic requirement of IAS 19 is that remeasurements are recognised in the period in which they arise, for interim financial statements a greater degree of estimation may be appropriate. Determining whether an updated valuation of the net defined benefit liability (asset) is necessary at the interim reporting date requires judgement (see 5.9.150). [IAS 34.B9, 19.BC59]

4.4.360.20 Entities may nevertheless choose to update their actuarial valuation at the each interim reporting date.

4.4.360.30 An updated valuation of the net defined benefit liability (asset) at the interim reporting date does not affect the measurement of service cost and net interest for the remainder of the current annual reporting period. Their measurement continues to be based on the assumptions at the prior annual reporting date. [IAS 19.BC63–BC64]

4.4.370 Net defined benefit liability (asset)

4.4.370.10 The net defined benefit liability (asset) is recognised in the statement of financial position and is determined as follows.

- *Step 1:* Present value of the defined benefit obligation (see 4.4.380) minus the fair value of any plan assets (see 4.4.550) equals the deficit or surplus in the defined benefit plan.
- *Step 2:* Adjustment for any effect of limiting a net defined benefit asset to the asset ceiling (see 4.4.690). [IAS 19.8, 63–64]

4.4.380 DEFINED BENEFIT OBLIGATION

4.4.390 Actuarial valuation method

4.4.390.10 The projected unit credit method is used to determine the present value of the defined benefit obligation. This involves projecting future salaries and benefits to which an employee will be entitled at the expected date of leaving. [IAS 19.67–68]

EXAMPLE 8 – MEASURING DEFINED BENEFIT OBLIGATION AND CURRENT SERVICE COST



4.4.390.20 Company F operates a defined benefit plan that provides an annual pension of $\frac{1}{60}$ of final salary for each year of service. The total expected annual salary on retirement of employees covered by the plan is 600,000. All the employees are expected to retire in 10 years and have worked for five years to date. After retirement, the employees are expected to live for 15 years.

4.4.390.30 The defined benefit obligation is the present value of the expected payment of 750,000 ($\frac{5}{60} \times 600,000 \times 15$). The employee cost for the period (current service cost) is equal to ($\frac{1}{60} \times 600,000 \times 15$) discounted to its present value, adjusted for the actuarially determined probability of the outcome.

4.4.395 Contribution-based promises

4.4.395.10 Contribution-based promises are defined benefit plans with a promised return on actual or notional contributions that is based on either or both of the following features:

- a guaranteed return of a fixed amount or rate; and/or
- a benefit that depends on future asset returns.

4.4.395.20 IAS 19 is silent on the accounting for contribution-based promises. Because these plans are defined benefit plans, the projected unit credit method generally applies to the measurement of the related defined benefit obligation. However, in our experience, in some jurisdictions entities predominantly apply the methodology of IFRIC Draft Interpretation D9 *Employee Benefit Plans with*

a *Promised Return on Contributions or Notional Contributions* and therefore measure benefits that depend on future asset returns at the fair value of the related assets.

4.4.395.30 The IFRS Interpretations Committee discussed this issue and acknowledged that divergence in practice exists; however, it decided not to proceed with a project on the issue. In our view, an entity applying IFRIC D9 should update its approach as necessary to comply with the currently effective IAS 19 – e.g. to reflect the amended calculation of net interest – because IFRIC D9 was based on an earlier version of the standard. [IU 05-14]

4.4.400 Attributing benefits to periods of service

4.4.400.10 Benefits are attributed to periods of service in accordance with the plan's benefit formula, unless that formula is back-end-loaded – i.e. service in later periods will lead to a materially higher level of benefit than service in earlier periods – in which case a straight-line attribution is used. [IAS 19.70]

4.4.400.20 In determining whether straight-line attribution is required, an entity considers whether an employee's service throughout the period will ultimately lead to benefits at that higher level. [IAS 19.73]

EXAMPLE 9A – DEFINED BENEFIT OBLIGATION – ATTRIBUTING BENEFITS TO PERIODS OF SERVICE



4.4.400.30 Company G sponsors a pension plan in which employees earn defined benefits for service provided between the ages of 25 and 65. As part of the pension plan, G offers an early retirement scheme under which employees earn early retirement benefits for service provided between the ages of 47 and 62. The early retirement benefits are earned regardless of the period of service before the age of 47 – i.e. an employee joining G at age 46 is entitled to the same early retirement benefit as an employee who has been employed since the age of 26. Because services provided from the age of 47 to 62 lead to the early retirement benefit, the obligation for the early retirement scheme is attributed to services provided from the age of 47 through to 62.

4.4.400.40 If a straight-line attribution is used, then benefits are attributed from the date on which service first leads to benefits under the plan until the date on which further service by the employee will lead to no material amount of further benefits under the plan, other than from salary increases. This method of attribution is required because the employee's service throughout the period will ultimately lead to benefits at a higher level. [IAS 19.70, 73]

4.4.400.50 An entity evaluates the terms of a plan to determine the date on which service first leads to benefits under the plan, because it may not necessarily be the date of hire.

EXAMPLE 9B – DEFINED BENEFIT OBLIGATION – DETERMINING START OF ATTRIBUTION PERIOD



4.4.400.60 Company H offers post-employment medical benefits to its retirees under the following conditions:

- they provided 20 years of service; and
- they were employed at the age of 60.

4.4.400.70 The start of the attribution period may differ depending on whether the benefit is earned after 20 years of cumulative service or 20 years of consecutive service. In the cumulative service (first) scenario, the employee may leave at the age of 35 after seven years of service and return at the age of 38 and still earn the benefit. If 20 years of cumulative service is required, then the benefit would be attributed from the date of original hire – i.e. when the employee was 28 – because the services provided from that date contribute to the benefits earned. However, if 20 years of consecutive service is required, then the attribution would start from the age of 40 because the first seven years of employment did not give rise to benefit entitlement. However, all facts and circumstances need to be considered – e.g. an entity does not rehire former employees in practice – to ensure that the appropriate attribution period is used.

4.4.400.80 IFRS is silent on whether the benefits previously attributed to earlier years of service should be revised if the structure of benefits offered by a plan is amended but benefits earned from the past service are unchanged. In our view, if an amendment offers improved benefits for future services and benefits accrued in respect of past service remain unaffected, then the benefits should not be attributed over the entire service period but rather split into two distinct periods, with the change accounted for prospectively.

EXAMPLE 9C – DEFINED BENEFIT OBLIGATION – ATTRIBUTION OF BENEFITS FOLLOWING PLAN AMENDMENT

4.4.400.90 A defined benefit plan offers different benefit accrual rates for different groups of participants – e.g. one category accrues a benefit of $\frac{1}{60}$ of the final salary per year whereas the other accrues a benefit of $\frac{1}{50}$. From 1 January 2017, the plan is amended to offer all members benefits at the more advantageous accrual rate of $\frac{1}{50}$ and this change applies prospectively – i.e. only to benefits earned after 1 January 2017. We believe that because the benefits earned in respect of service provided until 31 December 2016 are not affected by the amendment, the benefits should not be attributed over the entire working lives of members but instead should be attributed separately over two distinct periods of service – i.e. one before and one after the amendment.

4.4.410 Actuarial assumptions

4.4.410.10 Actuarial assumptions comprise the following.

- Demographic assumptions, such as:
 - mortality (see 4.4.420.10);
 - rates of employee turnover, disability and early retirement (see 4.4.420.20); and
 - the take-up of any benefit payment options available under the plan (see 4.4.440).
- Financial assumptions, such as:
 - future salary (see 4.4.430.30);

- benefit levels (excluding any cost of the benefits to be met by employees or third parties) (see 4.4.430–490);
- certain taxes payable by the plan (see 4.4.500); and
- the discount rate (see 4.4.510). [IAS 19.76]

4.4.410.20 Actuarial assumptions represent the entity's best estimates of the variables that will determine the ultimate cost of settling the defined benefit obligation. They are unbiased (neither imprudent nor excessively conservative) and mutually compatible – e.g. the economic relationship between increases in salaries and future inflation-linked pension increases reflects the same expectations. [IAS 19.76–78]

4.4.410.30 The financial assumptions are based on current market expectations of future events – e.g. medical cost inflation – and are determined in nominal (stated) terms unless real (inflation-adjusted) terms would be more appropriate. [IAS 19.79–80]

4.4.420 Demographic assumptions

4.4.420.10 Mortality assumptions are determined with reference to the entity's current best estimate of the mortality of plan members both during and after employment. Existing mortality tables might therefore need to be adjusted for expected changes in mortality. [IAS 19.81–82, BC142]

4.4.420.20 Although an entity makes estimates of voluntary early retirements, it does not take into account future redundancies or other plan curtailments in determining the defined benefit obligation until the termination or curtailment is recognised (see 4.4.890).

4.4.430 Benefits

4.4.430.10 The calculation takes into account not only the stated plan benefits, but also any constructive obligations. Constructive obligations include those established by informal practices, which the entity has no realistic alternative but to continue, such as 'discretionary' inflationary increases in pensions that would be very difficult for an employer to stop granting. [IAS 19.87, 88(a)]

4.4.430.20 The actuarial assumptions take into account future benefit changes that are set out in the formal terms of a plan. This includes estimated future changes in state benefits that affect benefits payable under the plan and for which there is reliable evidence that the change will happen. [IAS 19.87–88]


4.4.430.30 The measurement of the defined benefit obligation reflects expected future salaries. Therefore, for average salary plans, the *projected* average salary rather than the current average salary is used in measuring the liability. Similarly, even if the plan benefits are expressed in terms of current salaries, expected future salaries are taken into account. [IAS 19.70, 87(b)]

4.4.430.40 Other future changes that the employer currently has a constructive obligation to make – e.g. inflation increases – are also reflected in the measurement of the obligation. However, future changes to the terms of a plan, as long as the employer does not have a constructive obligation to make these changes, are not anticipated in the measurement of the obligation. Therefore, if, for example, the terms of a plan are changed from covering a select group of employees to covering all employees,

4.4.500 **Taxes payable by plan**

4.4.500.10 IAS 19 distinguishes between taxes payable by the plan on contributions relating to service before the reporting date or on benefits resulting from that service, and all other taxes payable by the plan. An actuarial assumption is made about the first type of taxes, which are taken into account in measuring current service cost and the defined benefit obligation, because they are seen as part of the cost of providing the benefits. All other taxes payable by the plan are included in the return on plan assets and therefore form part of remeasurements (see 4.4.970). [IAS 19.8, 76(b)(iv), 130]

EXAMPLE 11 – DEFINED BENEFIT OBLIGATION – TAXES ON CONTRIBUTIONS RELATING TO SERVICE BEFORE REPORTING DATE



4.4.500.20 Company Z has a defined benefit pension plan. The plan is required to pay a 10% tax on all contributions it receives – a ‘contributions tax’. Without considering the impact of investment earnings that might also fund the future benefits, the plan needs to receive contributions of 100 to retain sufficient post-tax plan assets to pay a benefit of 90, effectively increasing Z’s cost of the benefit. This type of tax is included in determining the defined benefit obligation at the end of each reporting date. Changes in the expected timing or amount of contributions tax payable will lead to actuarial gains and losses, which are recognised in OCI.

4.4.500.30 Estimating the amount of contributions tax payable to be included in the calculation of the defined benefit obligation involves making various assumptions, including the following:

- the expected timing of contributions tax payments, which might occur periodically over the employment period; and
- the level of plan assets already held by the plan, because they limit the need for additional contributions and the related taxes.

4.4.510 **Discount rate**

4.4.510.10 The obligation for estimated future payments is measured on a discounted basis. The obligation is discounted using a high-quality corporate bond rate (see 4.4.520) or a government bond rate if there is an insufficiently deep high-quality corporate bond market (see 4.4.530). The currency and maturity of the bonds need to be consistent with the currency and maturity of the defined benefit obligation. [IAS 19.83, IU 06-17]

4.4.520 **High-quality corporate bonds**

4.4.520.10 In our view, ‘high-quality’ should be interpreted as a bond with one of the two highest ratings, i.e. AAA and AA (Standard & Poor’s rating) or Aaa and Aa (Moody’s rating), or equivalent from other ratings agencies.

4.4.520.20 We believe that consideration should be given to adjustments for downgrades subsequent to the reporting date. In some cases, bonds that are included in data underlying a yield curve or bond-matching model (see 4.4.540.10) may be downgraded by a credit rating agency subsequent to the reporting date so that the bonds no longer meet the criteria to be considered high-quality. In other cases, the market index may include corporate bonds that are no longer high-quality. In either

of these cases, the facts and circumstances should be evaluated to determine if there is an adjusting event or a non-adjusting event after the reporting date (see 2.9.20–30).

4.4.520.30 In our view, the incremental borrowing rate of an entity is not an appropriate rate to use, because it reflects the credit quality of the entity. [IAS 19.84, BC134]

4.4.530 **Deep market**

4.4.530.10 The depth of the market for high-quality corporate bonds is assessed at the currency level. [IAS 19.83]

4.4.530.20 An entity that operates in a country with a currency without a sufficiently deep high-quality corporate bond market uses government bonds issued in the same currency to determine the discount rate. In our view, such an entity cannot construct a synthetic equivalent using a bond market in another country’s currency and notional or actual currency swaps. We believe that the hierarchy specified in the standard, which requires a default to the government bond rate, means that the government bond rate should be used. IAS 19, however, is not specific about what level of government should be used to determine the appropriate government bond rate. [IAS 19.83]

4.4.530.30 If bonds with a maturity that matches the maturity of the defined benefit obligation are not available, then an appropriate discount rate is estimated by extrapolating interest rates on shorter-term bonds using the yield curve and considering any available evidence about likely longer-term interest rates. [IAS 19.86]

4.4.540 **Discount rate methodologies**

4.4.540.10 Approaches to determining an IAS 19 discount rate may vary from entity to entity. In our experience, the prevalent methods are a yield curve approach, a bond-matching model or a market index approach under which an entity selects a representative discount rate from a published index representing high-quality corporate bonds (see 4.4.520).

4.4.540.20 In practice, an entity often uses a single weighted-average discount rate to measure the defined benefit obligation, reflecting the estimated timing and amount of benefit payments and the currency in which the benefits are to be paid. In such cases, the entity also uses the same rate to calculate current service cost and interest cost. However, in our view, in measuring the defined benefit obligation, current service cost and interest cost, an entity might instead use different weighted-average discount rates derived from the same yield curve for different categories of plan members in order to match more closely the expected timing of the benefit payments for each category. [IAS 19.85]

4.4.540.30 For example, different weighted-average rates might be used for pensioners and for members still in employment. In this case, rather than using a single weighted-average discount rate, an entity might calculate the defined benefit obligation, current service cost and interest cost separately for pensioners and active members, using the more specific weighted-average discount rate from the same yield curve attributable to each category. This calculation would result in different overall weighted-average discount rates for the defined benefit obligation and current service cost of the entire plan – i.e. when aggregating all categories – because current service is provided only by active members (see 4.4.860). [IAS 19.85]

4.4.560.30 Although there is no explicit requirement in IFRS about the nature of plan assets that can be held, there may be such requirements in local pension regulations, which may have to be considered.

4.4.570 **Restriction on availability**

4.4.570.10 In our view, the restriction on the availability of the assets to creditors of the entity applies both to claims arising from liquidation or similar court proceedings and from normal operations.

4.4.570.20 In our view, the protection from claims of other parties to the assets should not be capable of being overridden by other contracts (e.g. mortgages) or legislation and the assets should be prevented legally from being made available to the entity or its creditors under any circumstances, other than for permitted purposes (see 4.4.560).

4.4.580 **Reimbursement for benefits paid**

4.4.580.10 The definition of plan assets refers to the return of plan assets to the reporting entity for benefits that have already been paid. Therefore, in our view the definition of plan assets is not met if an entity has the ability to receive reimbursement in advance, *before* the reimbursable benefit payments are made. It is possible that a reimbursement right asset might arise in those circumstances (see 4.4.640). [IAS 19.8, 116–119]

4.4.590 **Ability to use plan assets**

4.4.590.10 When determining whether assets qualify as plan assets, in addition to meeting the general criteria for treatment as plan assets (see 4.4.560 and 600.10), in our view it is necessary for the plan to have the ability to use those assets to fund employee benefit payments both legally and in substance; the plan should not be prevented by the entity from accessing the economic benefits attaching to the assets. For example, it is possible for operating assets used by the entity to be plan assets. IAS 19 does not impose any additional conditions for such assets to be classified as plan assets but, if the assets in question are critical to the continued existence of the entity, or highly specialised and/or transferability restrictions are imposed on the plan in connection with those assets, then the plan may not have the ability to use those assets to fund employee benefits both legally and in substance. An analysis of the facts and circumstances may be required in performing this assessment. [IAS 19.8, 114, BC177]

4.4.600 **Financial instruments issued by entity**

4.4.600.10 Plan assets include *transferable* financial instruments issued by the reporting entity if the criteria for treatment as plan assets are met (see 4.4.560). Examples of such transferable financial instruments may include shares issued by the reporting entity (including by its subsidiaries) or loans granted by post-employment benefit plans to the reporting entity (or its subsidiaries) (see 4.4.1500). In our view, transfer would need to be possible both legally and in substance. IAS 19 precludes non-transferable financial instruments issued by the reporting entity from being plan assets in all cases. [IAS 19.8, 114, BC177]

4.4.600.20 For a discussion of insurance policies issued to the plan by the reporting entity or a related party of the reporting entity, see 4.4.660.

4.4.600.30 Plan assets exclude contributions receivable from the reporting entity and other financial instruments issued by the reporting entity and held by the fund that cannot be transferred to third parties – e.g. non-transferable loans by the fund to the reporting entity (see 4.4.1500). [IAS 19.8, 114]

4.4.600.40 In our view, the requirement for financial instruments to be transferable to qualify as plan assets applies to instruments issued by all entities that are part of the group – i.e. parent, intermediate and ultimate parent, and subsidiaries – in both separate and consolidated financial statements. (S)

4.4.600.50 In our view, financial instruments of associates and joint ventures in which group entities have invested qualify for treatment as plan assets if they are transferable and the other criteria for treatment as plan assets are met. If financial instruments issued by associates and joint ventures are not transferable, then we believe that an entity can still treat them as plan assets – in both separate and consolidated financial statements – because they are not part of the group. This is an accounting policy choice that should be applied consistently. (S)

4.4.610 **Replacement assets**

4.4.610.10 In some cases, assets of the fund can be returned to the entity in situations other than when it is for reimbursement of employee benefits paid or when the fund is in surplus. In these cases, the entity is typically required to provide replacement assets to the fund. In our view, an entity's ability to replace existing plan assets does not preclude classification of the assets as plan assets, if the current fair value of the replacement assets is required to be equal to or higher than the fair value of the assets replaced and the substitution can be made only if the trustees of the fund agree. We believe that this is similar to the sale of the assets by the fund. However, it is critical in such cases that the entity delivers equivalent or greater current fair value to be considered similar to a sale. This is because any below-market exchange represents a transfer of value to the entity, which would preclude the assets from qualifying as plan assets (see 4.4.560).

4.4.620 **Measurement**

4.4.620.10 Plan assets are measured at fair value in accordance with IFRS 13, which is the subject of chapter 2.4. For assets measured at fair value that have a bid and ask price, IFRS 13 requires the use of the price within the bid-ask spread that is the most representative of fair value in the circumstances. Under IFRS 13, the use of bid prices for long positions and ask prices for short positions is permitted but not required. For further discussion of the use of inputs based on bid and ask prices in measuring fair value, see 2.4.250. [IAS 19.57(a)(iii), 113, IFRS 13.70]

4.4.620.20 The requirement to measure plan assets at fair value overrides the requirements of other standards. Therefore, in our view if the plan has a controlling interest in another entity, then the investment should be measured at fair value and the underlying entity should not be consolidated (see 4.4.1490). Similarly, shares of the plan sponsor (employer) that qualify as plan assets should be measured at fair value and not presented as a deduction from equity, which is normally the treatment of treasury shares (see 7.3.420).

4.4.620.30 Plan assets may include non-financial assets such as property; in our view, they should also be measured at fair value, even if they were transferred to the fund by the entity in settlement of

contributions due to the fund and were previously measured at cost by the entity. The measurement of fair value under IFRS 13 reflects any special characteristic of the assets – e.g. their location or age (see 2.4.70). Differences between the carrying amount of the asset derecognised by the entity and the fair value of the contribution made may result in a gain or loss on contribution in profit or loss.

EXAMPLE 13 – PLAN ASSETS – TRANSFER OF NON-FINANCIAL ASSETS TO PLAN



4.4.620.40 Company B contributes property to its plan with a carrying amount of 100 and a fair value of 160 in settlement of contributions due to the fund of 160. Because B has transferred the risks and rewards of ownership to the fund and the plan assets are not consolidated by B, we believe that B should recognise a gain of 60 on the contribution in profit or loss in the period in which the asset is contributed.

4.4.620.50 In some cases, the entity may continue to use the asset after the asset has been contributed into the plan – e.g. a leaseback of a contributed office building. In such cases, the entity considers the requirements for the transfer of risks and rewards of ownership under IAS 17, which may affect the assessment of whether a gain should be recognised (see 5.1.470).

4.4.630 Assets that do not qualify as plan assets

4.4.630.10 In our view, investments held by employee benefit plans that do not qualify as plan assets should be accounted for by the entity in the same way as its other financial assets (see chapters 7.5 and 7.6) but also might be classified as a reimbursement right (see 4.4.640). If the investments include shares of the entity itself, then the requirements for treasury shares apply (see 7.3.420).

4.4.640 Reimbursement rights

4.4.640.10 If an entity will be reimbursed for expenditure that is required to settle a defined benefit obligation, but the reimbursement right does not give rise to a plan asset (see 4.4.560), then the reimbursement right is recognised as a separate asset when recovery is virtually certain. For example, an insurance policy that is not a plan asset generally gives rise to a reimbursement right. [IAS 19.116]

S 4.4.640.20 In our view, the reimbursement right needs to be due from a party outside the group (which may include an associate or joint venture (see 4.5.120.60)). Therefore, a right to receive assets from another group entity – e.g. parent, subsidiary – to fund employee benefit obligations is not treated as a reimbursement right in the consolidated financial statements. However, it may be appropriate to recognise a reimbursement right in the separate financial statements of the entity providing that the criteria in paragraph 116 of IAS 19 are met. [IFRS 4.IG2.Ex1.21]

4.4.640.30 Reimbursement rights are accounted for in the same way as plan assets – i.e. they are measured at fair value and the changes in fair value of the reimbursement rights are accounted for in the same way as the changes in the fair value of plan assets. Remeasurements arising on reimbursement rights are recognised in OCI (see 4.4.830.10). However, reimbursement rights are presented differently from plan assets, being shown as a separate asset in the statement of financial position rather than being netted against the related defined benefit obligation. [IAS 19.116]

EXAMPLE 14A – REIMBURSEMENT RIGHT



4.4.640.40 Company O has a defined benefit pension plan for all of its employees. O outsources some of its employees to Company P, a third party. The outsourced employees continue to participate in O's pension plan but O is entitled to recover the costs of the outsourced employees, including costs associated with the defined benefit plan, from P. O accounts for the full net defined benefit liability under the defined benefit plan. If it is virtually certain that P will reimburse O for the pension costs, then O recognises an asset for the reimbursement, which is accounted for in the same way as a plan asset. However, O shows the reimbursement right as a separate asset and does not deduct it from the carrying amount of the defined benefit obligation.

4.4.640.50 In some countries, governments introduce a state subsidy to plan sponsors for costs incurred under plans that meet certain criteria making them equivalent to a specified state plan. Some people believe that such a state subsidy paid to the plan sponsors is a reimbursement right, whereas others believe that it is similar to a state benefit (see 4.4.430.20) that affects the net benefit payable by the entity, the estimated amount of which has now changed. In our view, an entity should choose an accounting policy, to be applied consistently, to treat the state subsidy paid to the sponsor either as a reimbursement right or as a state benefit. In our view, the initial recognition of the state subsidy, regardless of whether it is considered to be a reimbursement right or a state benefit, should be accounted for as a remeasurement gain and not as a plan amendment (see 4.4.950 and 880.30–40). For a discussion of state subsidies that are paid to the plan and treated as third party contributions, see 4.4.490). [IAS 19.87(e), 92–93, 116]

EXAMPLE 14B – REIMBURSEMENT RIGHT OR STATE BENEFIT – STATE SUBSIDY TO PLAN SPONSOR



4.4.640.60 Company M provides post-retirement medical benefits to its employees. The defined benefit obligation at 31 December 2017 is 150, excluding any effects of a state subsidy, and the plan assets are 50. As a result, without the effect of the state subsidy, M would recognise a net defined benefit liability of 100 (net of plan assets of 50) in the 2017 financial statements.

4.4.640.70 M determines that its plan is equivalent to the specified state plan and that, based on its actuarial assumptions about expected costs, M will receive a subsidy of 20. M chooses to treat the state subsidy as a reimbursement right and therefore recognises it as a separate asset. Because the creation of the reimbursement right is a remeasurement gain, M records the following entry. [IAS 19.92, 116]

	DEBIT	CREDIT
Reimbursement right (separate asset)	20	
Remeasurement (OCI)		20
To recognise reimbursement right asset		