International Financial Reporting Standards

IFRS
The Standards

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International Financial Reporting Standards

IAS 27
Separate Financial Statements

The views expressed in this presentation are those of the presenter,
not necessarily those of the IASB or IFRS Foundation

Introduction

- IAS 27 addresses accounting for investments in subsidiaries, joint ventures and associates, when the investor presents separate financial statements.
- IAS 27 does not mandate which entities present separate financial statements. However, in some jurisdictions the investor must present separate financial statements in addition to the consolidated financial statements.
- Must identify the primary financial statements to which the separate financial statements relate.

Measurement principle

- For separate financial statements, the focus is upon the performance of the assets as investments.
- Consequently, investments in subsidiaries, joint ventures and associates are accounted for either at cost or in accordance with IAS 39 or IFRS 9.

Exceptions to the measurement principle

- If cost used, then apply IFRS 5 when classified ‘held for sale’.
- If in its primary financial statements (eg consolidated) a venture capital organisation or similar entity elects to measure its investments in associates or joint ventures at fair value through profit or loss in accordance with IFRS 9, it also account for those investments at fair value in its separate financial statements.

Business Implications

- Using the fair value method provide a measure of the economic value of the investments.
- Using the cost method can result in relevant information, depending on the purpose of preparing the separate financial statements (eg, they may be needed only by particular parties to determine the dividend income from subsidiaries).

International Financial Reporting Standards

IAS 28
Investments in Associates and Joint Ventures

The views expressed in this presentation are those of the presenter, not necessarily those of the IASB or IFRS Foundation

Introduction

- An associate is any entity over which the investor has significant influence.
- Significant influence is the power to participate in the financial and operating policy decisions of the investee.
  - significant influence is not control (which indicates a subsidiary)
  - significant influence is not joint control (which indicates an interest in a joint arrangement).

Significant influence

- Significant influence might come from:
  - representation on the board of directors;
  - participation in policy making, including decisions about dividends;
  - a close relationship involving transactions between investor and investee;
  - interchange of managerial personnel; or
  - provision of essential technical information.

Measurement rule

- Associates are accounted for using the equity method.

Exception

- A venture capital organisation or similar entity can elect to measure its investments in associates or joint ventures at fair value through profit or loss in accordance with IFRS 9.

Equity method

- Associates are accounted for using the equity method.
- The equity method involves recognising the investment initially at cost, then adjusting for the post-acquisition change in the investor's share of net assets of the associate.
- A one-line entry in the statement of comprehensive income presents the investor's share of the associate's profit or loss.
- There is also a one-line adjustment to the investment in the statement of financial position.

Equity method continued

- If the associate has losses, equity accounting reduces the carrying amount of the investor’s investment.
- Equity accounting continues until the investment is reduced to zero.
- The ‘investment’ includes not only shares in the associate, but also some non-equity interests such as some long-term receivables.

Business Implications

- There is no exemption from equity accounting when severe long-term restrictions impair the associate's ability to transfer funds to the investor.
  - However, the investor should consider whether such restrictions, taken with other factors, indicate that the investor does not have significant influence.

International Financial Reporting Standards

IAS 32
Financial Instruments: Presentation

The views expressed in this presentation are those of the presenter,
not necessarily those of the IASB or IFRS Foundation

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Introduction

- IAS 32 specifies presentation for financial instruments.
  - The recognition and measurement and the disclosure of financial instruments are the subjects of IAS 39 *Financial Instruments: Recognition and Measurement* and IFRS 7 *Financial Instruments: Disclosures respectively*.
- It establishes principles for presenting financial instruments as liabilities or equity and for offsetting financial assets and financial liabilities.

Liabilities and equity

- Differentiation between a financial liability and equity depends on whether there is an obligation to deliver cash (or some other financial asset).
    - But note the exception for certain puttable instruments
- When a transaction will be settled in the issuer's own shares, classification depends on whether the number of shares to be issued is fixed or variable.

Compound financial instruments

- A compound financial instrument, such as a convertible note, is split into equity and liability components.
- When the instrument is issued, the equity component is measured as the difference between the fair value of the compound instrument and the fair value of the liability component.

Offsetting

- Financial assets and financial liabilities are offset only when the entity:
  - has a legally enforceable right to set off the recognised amounts; and
  - intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

Business Implications

- Classification of a financial instrument as a financial liability or equity determines the treatment of the interest, dividends, losses or gains on the financial instrument as items of income or expense, or as changes in equity.
- Dividends on shares classified as liabilities are recognised as expenses, and affect profit or loss.

International Financial Reporting Standards

IAS 33
Earnings per Share

The views expressed in this presentation are those of the presenter, not necessarily those of the IASB or IFRS Foundation

IFRS™

Introduction

- IAS 33 deals with the calculation and presentation of earnings per share (EPS).
- It applies to entities whose ordinary shares or potential ordinary shares (for example, convertibles, options and warrants) are publicly traded.
- An entity must present basic EPS and diluted EPS with equal prominence in the statement of comprehensive income.

Dilution

- Dilution is a notional reduction in EPS or a notional increase in loss per share resulting from the assumption that convertible instruments are converted, options or warrants are exercised, or ordinary shares are issued upon the satisfaction of specified conditions.

Earnings

- The ‘earnings’ of two entities subject to identical transactions and events could differ because they have adopted different accounting policies. These differences are not adjusted for when calculating EPS.
- The numerators used in the calculation of basic and diluted EPS must be reconciled to profit or loss attributable to the ordinary equity holders of the parent.

Shares

- The denominators used in the calculation of basic and diluted EPS might be affected by:
  - share issues during the year
  - shares to be issued upon conversion of a convertible instrument
  - contingently issuable or returnable shares;
  - bonus issues
  - share splits and share consolidation
  - the exercise of options and warrants
  - contracts that may be settled in shares
  - written put options

International Financial Reporting Standards

IAS 34
Interim Financial Reporting

Introduction

- IAS 34 specifies the minimum content of an interim financial report and prescribes the principles for recognition and measurement in complete or condensed financial statements for an interim period.
- IAS 34 does not specify which entities must publish an interim financial report. That is generally a matter for securities regulation. IAS 34 applies if an entity publishes an interim financial report.

Content

- The minimum content is a set of condensed financial statements,
  - ie statement of financial position, statement of comprehensive income, statement of cash flows, statement of changes in equity, and selected explanatory material.
- Generally, information available in the entity's most recent annual report is not repeated or updated in the interim report.
  - The interim report deals with changes since the end of the last annual reporting period.

Recognition and Measurement

- The same accounting policies are applied in the interim report as in the most recent annual report.
  – Assets and liabilities are recognised and measured for interim reporting on the basis of information available on a year-to-date basis.
- While measurements in both annual financial statements and interim financial reports are often based on reasonable estimates, the preparation of interim financial reports will generally require a greater use of estimation methods than annual financial statements.

International Financial Reporting Standards

IAS 36
Impairment of Assets

The views expressed in this presentation are those of the presenter,
not necessarily those of the IASB or IFRS Foundation

Introduction

- An asset must not be carried in the financial statements at more than the highest amount to be recovered through its use or sale.
  - The entity must reduce the carrying amount of the asset to its recoverable amount, and recognise an impairment loss.
- The standard also applies to groups of assets (cash-generating units).

Identifying an asset that may be impaired

- The recoverable amount of the following assets must be assessed each year:
  - intangible assets with indefinite useful lives
  - intangible assets not yet available for use
  - goodwill acquired in a business combination
- The recoverable amount of other assets is assessed only when there is an indication that the asset may be impaired.

Recoverable amount

- Recoverable amount is the higher of fair value less costs to sell and value in use.
  - Fair value less costs to sell is the arm's length sale price between knowledgeable, willing parties less the costs of disposal.
  - The value in use of an asset is the expected future cash flows the asset in its current condition will produce, discounted to present value using an appropriate pre-tax discount rate.

- Impairment might be indicated by, amongst others:
  - decline in an asset’s market value
  - adverse changes in the technological, market, economic or legal environment
  - increase in market interest rates
  - market capitalisation of the entity being less than net asset value
  - obsolescence or damage of an asset
  - plans to discontinue or restructure operations

Recognition and Measurement

- An impairment loss is recognised immediately in the statement of comprehensive income.
- When an impairment loss is recognised, the carrying amount of the asset (or cash-generating unit) is reduced.
- In a cash-generating unit, goodwill is reduced first, then other assets are reduced pro rata.
- The depreciation (amortisation) charge is adjusted in future periods to allocate the asset's revised carrying amount over its remaining useful life.

Reversing an impairment loss

- An impairment loss for goodwill is never reversed.
- For other assets, when the circumstances that caused the impairment loss are resolved, the reversal of the impairment loss is recognised immediately in the statement of comprehensive income.
- On reversal, the asset's carrying amount is increased, but it must not exceed the amount that it would have been had there been no impairment loss in prior years.
- Depreciation (amortisation) is adjusted in future periods.

International Financial Reporting Standards

IAS 37
Provisions, Contingent Liabilities and Contingent Assets

Introduction

- IAS 37 aims to ensure that appropriate recognition criteria and measurement bases are applied to provisions, contingent liabilities and contingent assets and that appropriate disclosures enable users to understand their nature, timing and amount.

Provisions

- A provision is a liability of uncertain timing or amount. A liability may be a legal obligation or a constructive obligation.
- A constructive obligation arises from the entity's actions, through which it has indicated to others that it will accept certain responsibilities, and as a result has created an expectation that it will discharge those responsibilities.

Provisions continued

- A provision is measured at the amount that the entity would rationally pay to settle the obligation at the end of the reporting period or to transfer it to a third party at that time.
- Risks and uncertainties are taken into account in the measurement of a provision.
- A provision is discounted to its present value.

Contingent liabilities

- Contingent liabilities are possible obligations whose existence will be confirmed by uncertain future events that are not wholly within the control of the entity.
- Contingent liabilities also include obligations that are not recognised because their amount cannot be measured reliably or settlement is not probable.
  - eg litigation against the entity when the occurrence of any wrongdoing by the entity is uncertain.

Contingent assets

- Contingent assets are possible assets the existence of which will be confirmed by the occurrence or non-occurrence of uncertain future events that are not wholly within the control of the entity.
- Contingent assets are not recognised in the statement of financial position.
- Contingent assets are disclosed when it is more likely than not that an inflow of benefits will occur.
  - However, when the inflow of benefits is virtually certain an asset is recognised in the statement of financial position, because that asset is no longer considered to be contingent.

IAS 37: Provisions, Contingent Liabilities and Contingent Assets

Business Implications

- IAS 37 restricts the circumstances in which a provision can be recognised. It does not allow a provision to be created for the possibility of something occurring in future.
  - there must be a present obligation (a liability) at the end of the reporting period.
- When disclosure of some or all information normally required by IAS 37 can be expected to prejudice seriously the position of the entity in a dispute then disclose only general nature of the dispute and reason why alternative disclosures made. Note: no recognition and measurement alternative.

International Financial Reporting Standards

IAS 38
Intangible Assets

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not necessarily those of the IASB or IFRS Foundation

Introduction

- IAS 38 sets out criteria for the recognition and measurement of intangible assets, and requires disclosures about them.
- Goodwill acquired in a business combination is accounted for in accordance with IFRS 3 *Business Combinations* and is outside the scope of IAS 38.

Intangible assets

- An intangible asset is an identifiable non-monetary asset without physical substance.
- Such an asset is identifiable when it is separable, or when it arises from contractual or other legal rights.
- Separable assets can be sold, transferred, licensed etc.
- eg computer software, licences, trademarks, patents, films, copyrights and import quotas

Recognition

- Expenditure for an intangible item is recognised as an expense, unless the item meets the definition of an intangible asset, and:
  - it is probable that there will be future economic benefits from the asset; and
  - the cost of the asset can be reliably measured.
- Intangible assets are measured initially at cost.

Measurement

- An entity usually measures an intangible asset at cost less accumulated amortisation.
- It may choose to measure the asset at fair value, if fair value can be determined by reference to an active market.
- If an intangible asset is revalued, all assets within that class of intangible assets must be revalued.
- Valuations must be updated regularly.
- Revaluation increases are usually credited to other comprehensive income (ie outside profit or loss) in the statement of comprehensive income.

Measurement continued

- An intangible asset with a finite useful life is amortised.
- An intangible asset with an indefinite useful life is not amortised, but is tested annually for impairment.

International Financial Reporting Standards

IAS 39
Financial Instruments: Recognition and Measurement

Introduction

- IAS 39 establishes principles for recognising and measuring financial assets, financial liabilities and some contracts to buy or sell non-financial items.
- The presentation and the disclosure of financial instruments are the subjects of IAS 32 *Financial Instruments: Presentation* and IFRS 7 *Financial Instruments: Disclosures* respectively.

Recognition and derecognition

- A financial instrument is recognised in the financial statements when the entity becomes a party to the financial instrument contract.
- An entity removes a financial liability from its statement of financial position when its obligation is extinguished.

Recognition and derecognition continued

- An entity removes a financial asset from its statement of financial position when
  - its contractual rights to the asset's cash flows expire,
  - it has transferred the asset and substantially all the risks and rewards of ownership, or
  - it has transferred the asset, and has retained some substantial risks and rewards of ownership, but the other party may sell the asset. The risks and rewards retained are recognised as an asset.

Measurement

- A financial asset or liability is measured initially at fair value.
- Subsequent measurement depends on the category of financial instrument. Some categories are measured at amortised cost, and some at fair value.

Measurement continued

- At amortised cost:
  - ‘Held to maturity’. Non-derivative financial assets that the entity has the positive intention and ability to hold to maturity.
  - ‘Loans and receivables’. Non derivative financial assets with fixed or determinable payments that are not quoted in an active market.
  - Financial liabilities that are not carried at fair value through profit or loss or otherwise required to be measured in accordance with another measurement basis.

Measurement continued

- At fair value:
  - ‘At fair value through profit or loss’. This category includes financial assets and financial liabilities held for trading, including derivatives not designated as hedging instruments and financial assets and financial liabilities that the entity has designated for measurement at fair value. All changes in fair value are reported in profit or loss.
  - ‘Available for sale’. All financial assets that do not fall within one of the other categories. These are measured at fair value. Unrealised changes in fair value are reported in other comprehensive income. Realised changes in fair value (from sale or impairment) are reported in profit or loss at the time of realisation.

Hedge accounting

- Hedge accounting recognises the offsetting effects of changes in the fair values or the cash flows of the hedging instrument and the hedged item. Strict conditions must be met before hedge accounting is possible:
  - There must be formal designation and documentation of a hedge, including the risk management strategy for the hedge.
  - The hedging instrument must be expected to be highly effective in achieving offsetting changes in fair value or cash flows of the hedged item that are attributable to the hedged risk.

Hedge accounting continued

- For cash flow hedges, a forecast transaction being hedged must be highly probable.
- Hedge effectiveness must be reliably measurable—ie the fair value or cash flows of the hedged item and the fair value of the hedging instrument can be reliably measured.
- The hedge must be assessed on an ongoing basis and be highly effective.

International Financial Reporting Standards

IAS 40
Investment Property

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not necessarily those of the IASB or IFRS Foundation

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Introduction

- Investment property is land or a building (including part of a building) or both, held to earn rentals or for capital appreciation or both.
  - It is not owner-occupied, and is not used in the production or supply of goods and services, or for administration.
  - It is not property that is for sale in the ordinary course of business.

Initial measurement

- An investment property is measured initially at cost.
- The cost of a property interest held under a lease is measured in accordance with IAS 17 *Leases* at the lower of the fair value of the property interest and the present value of the minimum lease payments.

Subsequent measurement

- For subsequent measurement an entity must adopt either the fair value model or the cost model for all investment properties.
- All entities must estimate the fair value of investment property, either for measurement (if the entity uses the fair value model) or for disclosure (if it uses the cost model).
- Measure fair value in accordance with IFRS 13 *Fair Value Measurement*.

Fair value model

- Investment property is remeasured to its fair value at the end of each reporting period.
- Changes in fair value are recognised in profit or loss in the period they occur.

Cost model

- Investment property is measured at cost less accumulated depreciation and any accumulated impairment losses (ie using the cost model in IAS 16 *Property, Plant and Equipment*).
- Must also disclose the fair value of investment property.

Judgement and estimates

- Sometimes it is difficult to identify investment property
  – eg, owner of a hotel transfers some responsibilities to third parties under a management contract (PPE or investment property?)
  – entity develops criteria so that it can exercise that judgement consistently
- In some cases measuring fair value (see IFRS 13)
- When cost model used measuring depreciation (eg estimate residual value, depreciation method and useful life)

Business Implications

- Users of IFRS financial statements are provided with relevant information about the entity's investment property.
- Difficult for management to justify a change in accounting policy from the fair value model to the cost model.

International Financial Reporting Standards

IAS 41
Agriculture

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not necessarily those of the IASB or IFRS Foundation

Introduction

- IAS 41 establishes the accounting treatment for:
  - biological assets (living plant or animal) whose biological transformation (growth, degeneration, production and procreation) and harvest is managed by an entity for sale or for conversion into agricultural produce or into additional biological assets.
  - the initial measurement of agricultural produce at the point of harvest.
- It does not address the processing of agricultural produce after harvest (eg processing grapes into wine, or wool into yarn).

Recognition and measurement

- Biological assets are measured at fair value less costs to sell.
- Agricultural produce at the point of harvest is also measured at fair value less costs to sell.
- Changes in the value of biological assets are included in profit or loss.
- Biological assets that are attached to land (eg trees in a plantation forest) are measured separately from the land.

Government grants

- IAS 41 differs from IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance* with regard to the recognition of government grants.
- Unconditional grants related to biological assets measured at fair value less costs to sell are recognised as income when the grant becomes receivable.
- Conditional grants are recognised as income only when the conditions attaching to the grant are met.

Judgement and estimates

- Sometimes it is difficult to determine whether or not particular biological assets are in the scope of IAS 41.
  - eg, exotic bird breeding zoo.
- In some cases measuring fair value (see IFRS 13)
  - eg separating the land (PPE) from the trees when measuring the fair value of some plantation.

Business Implications

- Users of IFRS financial statements are provided with relevant information about the entity’s biological assets in agricultural activity.

Questions or comments?

Expressions of individual views by members of the IASB and its staff are encouraged.
The views expressed in this presentation are those of the presenter. Official positions of the IASB on accounting matters are determined only after extensive due process and deliberation.