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International Financial Reporting Standards, their Interpretations and US GAAPS - An Overview

1. Introduction

The International Accounting Standards Board (IASB) was established in 2001 as part of the International Accounting Standards Committee (IASC) Foundation. In 2010 the IASC Foundation was renamed the IFRS Foundation. The governance of the IFRS Foundation rests with twenty-two Trustees. The Trustees' responsibilities include appointing the members of the IASB and associated councils and committees, as well as securing financing for the organisation.

The IASB comprises fifteen full-time members (the IFRS Foundation's Constitution provides for membership to raise to sixteen by 1 July 2012). Approval of International Financial Reporting Standards (IFRSs) and related documents, such as the Conceptual Framework for Financial Reporting, exposure drafts, and other discussion documents, is the responsibility of the IASB.

The IFRS Interpretations Committee comprises fourteen voting members and a non-voting Chairman, all appointed by the Trustees. The role of the Committee is to prepare interpretations of IFRSs for approval by the IASB and, in the context of the Conceptual Framework, to provide timely guidance on financial reporting issues. The Committee (then called the International Financial Reporting Interpretations Committee) replaced the former Standing Interpretations Committee (SIC) in 2002.

The IFRS Advisory Council is appointed by the Trustees. It provides a formal vehicle for participation by organisations and individuals with an interest in international financial reporting. The participants have diverse geographical and functional backgrounds. The Council's objective is to give advice to the IASB on priorities, agenda decisions and on major standard-setting projects.

The IASB was preceded by the Board of IASC, which came into existence on 29 June 1973 as a result of an agreement by professional accountancy bodies in Australia, Canada, France, Germany, Japan, Mexico, the Netherlands, the United Kingdom and Ireland, and the United States of America. A revised Agreement and Constitution were signed in November 1982.The constitution was further revised revised in October 1992 and May 2000 by the IASC Board. Under the May 2000 Constitution, the professional accountancy bodies adopted a mechanism enabling the appointed Trustees to put the May 2000 Constitution into force. The Trustees activated the new Constitution in January 2001, and revised it in March 2002.

At its meeting on 20 April 2001 the IASB passed the following resolution:

"*All Standards and Interpretations issued under previous Constitutions continue to beapplicable unless and until they are amended or withdrawn. The International Accounting Standards Board may amend or withdraw International Accounting Standards and SIC Interpretations issued under previous Constitutions of IASC as well as issue new Standards and Interpretations*."

When the term IFRSs is used i, it includes standards and Interpretations approved by the IASB, and International Accounting Standards (IASs) and SIC Interpretations issued under previous Constitution.

2. Objectives of the IASB

The objectives of the IASB are:

(a) to develop, in the public interest, a single set of high quality, understandable, enforceable and globally accepted financial reporting standards based on clearly articulated principles. These standards should require high quality, transparent and comparable information in financial statements and other financial reporting to help investors, other participants in the various capital markets of the world and other users of financial information make economic decisions;

(b) to promote the use and rigorous application of those standards;

(c) in fulfilling the objectives associated with (a) and (b), to take account of, as appropriate, the needs of a range of sizes and types of entities in diverse economic settings;

(d) to promote and facilitate the adoption of IFRSs, being the standards and interpretations issued by the IASB, through the convergence of national accounting standards and IFRSs.

3. Scope and Authority of International Financial Reporting Standards

The IASB achieves its objectives primarily by developing and publishing IFRSs and promoting the use of those standards in general purpose financial statements and other financial reporting. Other financial reporting comprises information provided outside financial statements that assists in the interpretation of a complete set of financial statements or improves users' ability to make efficient economic decisions. In developing IFRSs, the IASB works with national standard-setters to promote and facilitate adoption of IFRSs through convergence of national accounting standards and IFRSs.

IFRSs set out recognition, measurement, presentation and disclosure requirements dealing with transactions and events that are important in general purpose financial statements. They may also set out such requirements for transactions and events that arise mainly in specific industries. IFRSs are based on the Conceptual Framework, which addresses the concepts underlying the information presented in general purpose financial statements. Although the Conceptual Framework was not issued until September 2010, it was developed from the previous Framework for the Preparation and Presentation of Financial Statements, which the IASB adopted in 2001.

The objective of the Conceptual Framework is to facilitate the consistent and logical formulation of IFRSs. The Conceptual Framework also provides a basis for the use of judgment in resolving accounting issues.

IFRSs are designed to apply to the general purpose financial statements and other financial reporting of profit-oriented entities. Profit-oriented entities include those engaged in commercial, industrial, financial and similar activities, whether organised in corporate or in other forms. They include organisations such as mutual insurance companies and other mutual co-operative entities that provide dividends or other economic benefits directly and proportionately to their owners, members or participants. Although IFRSs are not designed to apply to not-for-profit activities in the private sector, public sector or government, entities with such activities may find them appropriate. The International Public Sector Accounting Standards Board (IPSASB) prepares accounting standards for governments and other public sector entities, other than government business entities, based on IFRSs.

IFRSs apply to all general purpose financial statements. Such financial statements are directed towards the common information needs of a wide range of users, for example, shareholders, creditors, employees and the public at large. The objective of financial statements is to provide information about the financial position, performance and cash flows of an entity that is useful to those users in making economic decisions.

A complete set of financial statements includes a statement of financial position, a statement of comprehensive income, a statement of changes in equity, a statement of cash flows, and accounting policies and explanatory notes. When a separate income statement is presented in accordance with IAS 1 Presentation of Financial Statements (as revised in 2007), it is part of that complete set. In the interest of timeliness and cost considerations and to avoid repeating information previously reported, an entity may provide less information in its interim financial statements than in its annual financial statements. IAS 34 Interim Financial Reporting prescribes the minimum content of complete or condensed financial statements for an interim period. The term 'financial statements' includes a complete set of financial statements prepared for an interim or annual period, and condensed financial statements for an interim period.

Some IFRSs permit different treatments for given transactions and events. The IASB's objective is to require like transactions and events to be accounted for and reported in a like way and unlike transactions and events to be accounted for and reported differently, both within an entity over time and among entities. Consequently, the IASB intends not to permit choices in accounting treatment. Also, the IASB has reconsidered, and will continue to reconsider, those transactions and events for which IFRSs permit a choice of accounting treatment, with the objective of reducing the number of those choices.

Standards approved by the IASB include paragraphs in bold type and plain type, which have equal authority. Paragraphs in bold type indicate the main principles. An individual standard should be read in the context of the objective stated in that standard and the Preface of IFRS

Interpretations of IFRSs are prepared by the Interpretations Committee to give authoritative guidance on issues that are likely to receive divergent or unacceptable treatment, in the absence of such guidance.

An entity whose financial statements comply with IFRSs shall make an explicit andunreserved statement of such compliance in the notes. An entity shall not describe financial statements as complying with IFRSs unless they comply with all the requirements of IFRSs.

Any limitation of the scope of an IFRS is made clear in the standard

4. Due Process

IFRSs are developed through an international due process that involves accountants, financial analysts and other users of financial statements, the business community, stock exchanges, regulatory and legal authorities, academics and other interested individuals and organisations from around the world. The IASB consults, in public meetings, the Advisory Council on major projects, agenda decisions and work priorities, and discusses technical matters in meetings that are open to public observation. Due process for projects normally, but not necessarily, involves the following steps

(a) the staff are asked to identify and review all the issues associated with the topic and to consider the application of the Conceptual Framework to the issues;

(b) study of national accounting requirements and practice and an exchange of views about the issues with national standard-setters;

(c) consulting the Trustees and the Advisory Council about the advisability of adding the topic to the IASB's agenda;

(d) formation of an advisory group to give advice to the IASB on the project;

(e) publishing for public comment a discussion document;

(f) publishing for public comment an exposure draft (including any dissenting opinions held by IASB members) approved by at least nine votes of the IASB if there are fewer than sixteen members, or by ten of its members if there are sixteen members;

(g) normally publishing with an exposure draft a basis for conclusions and the alternative views of any IASB member who opposes(h) consideration of all comments received within the comment period on discussion documents and exposure drafts;

(i) consideration of the desirability of holding a public hearing and of the desirability of conducting field tests and, if considered desirable, holding such hearings and conducting such tests;

(j) approval of a standard by at least nine votes of the IASB if there are fewer than sixteen members, or by ten of its members if there are sixteen members; and

(k) publishing with a standard (i) a basis for conclusions, explaining, among other things, the steps in the IASB's due process and how the IASB dealt with public comments on the exposure draft, and (ii) the dissenting opinion of any IASB member.

Interpretations of IFRSs are developed through an international due process that involves accountants, financial analysts and other users of financial statements, the business community, stock exchanges, regulatory and legal authorities, academics and other interested individuals and organisations from around the world. The Interpretations Committee discusses technical matters in meetings that are open to public observation. The due process for each project normally, but not necessarily, involves the following steps

(a) the staff are asked to identify and review all the issues associated with the topic and to consider the application of the Conceptual Framework to the issues;

(b) consideration of the implications for the issues of the hierarchy of IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors;

(c) publication of a draft Interpretation for public comment if no more than four Committee members have voted against the proposal;

(d) consideration of all comments received within the comment period on a draft Interpretation;

(e) approval by the Interpretations Committee of an Interpretation if no more than four Committee members have voted against the Interpretation after considering public comments on the draft Interpretation; and

(f) approval of the Interpretation by at least nine votes of the IASB if there are fewer than sixteen members, or by ten of its members if there are sixteen members.

5. Timing of Application of International Financial Reporting Standards

IFRSs apply from a date specified in the document. New or revised IFRSs set out transitional provisions to be applied on their initial application.

The IASB has no general policy of exempting transactions occurring before a specific date from the requirements of new IFRSs. When financial statements are used to monitor compliance with contracts and agreements, a new IFRS may have consequences that were not foreseen when the contract or agreement was finalised. For example, covenants contained in banking and loan agreements may impose limits on measures shown in a borrower's financial statements. The IASB believes the fact that financial reporting requirements evolve and change over time is well understood and would be known to the parties when they entered into the agreement. It is up to the parties to determine whether the agreement should be insulated from the effects of a future IFRS, or, if not, the manner in which it might be renegotiated to reflect changes in reporting rather than changes in the underlying financial condition.

Exposure drafts are published for comment and their proposals are subject to revision. Until the effective date of an IFRS, the requirements of any IFRS that would be affected by proposals in an exposure draft remain in force.

6. Conceptual Framework

6.1 Introduction

Financial statements are prepared and presented for external users by many entities around the world. Although such financial statements may appear similar from country to country, there are differences which have probably been caused by a variety of social, economic and legal circumstances and by different countries having in mind the needs of different users of financial statements when setting national requirements.

These different circumstances have led to the use of a variety of definitions of the elements of financial statements: for example, assets, liabilities, equity, income and expenses. Theyhave also resulted in the use of different criteria for the recognition of items in the financial statements and in a preference for different bases of measurement. The scopes of the financial statements and the disclosures made in them have also been affected.

The International Accounting Standards Board is committed to narrowing these differences by seeking to harmonise regulations, accounting standards and procedures relating to the preparation and presentation of financial statements. It believes that further harmonisation can best be pursued by focusing on financial statements that are prepared for the purpose of providing information that is useful in making economic decisions.

The Board believes that financial statements prepared for this purpose meet the commonneeds of most users. This is because nearly all users are making economic decisions, for example:

(a) to decide when to buy, hold or sell an equity investment.

(b) to assess the stewardship or accountability of management.

(c) to assess the ability of the entity to pay and provide other benefits to its employees.

(d) to assess the security for amounts lent to the entity.

(e) to determine taxation policies.

(f) to determine distributable profits and dividends.

(g) to prepare and use national income statistics.

(h) to regulate the activities of entities.

The Board recognises, however, that governments, in particular, may specify different oradditional requirements for their own purposes. These requirements should not, however, affect financial statements published for the benefit of other users unless they also meetthe needs of those other users.

Financial statements are most commonly prepared in accordance with an accounting model based on recoverable historical cost and the nominal financial capital maintenance concept. Other models and concepts may be more appropriate in order to meet the objective of providing information that is useful for making economic decisions although there is at present

no consensus for change. The Conceptual Framework has been developed so that it is applicable to a range of accounting models and concepts of capital and capital maintenance.

6.2 Purpose and Status

This Conceptual Framework sets out the concepts that underlie the preparation and presentation of financial statements for external users. The purpose of the Conceptual Framework is:

(a) to assist the Board in the development of future IFRSs and in its review of existing IFRSs;

(b) to assist the Board in promoting harmonisation of regulations, accounting standards and procedures relating to the presentation of financial statements by providing a basis for reducing the number of alternative accounting treatments permitted by IFRSs;

(c) to assist national standard-setting bodies in developing national standards;

(d) to assist preparers of financial statements in applying IFRSs and in dealing with topics that have yet to form the subject of an IFRS;

(e) to assist auditors in forming an opinion on whether financial statements comply with IFRSs;

(f) to assist users of financial statements in interpreting the information contained in financial statements prepared in compliance with IFRSs; and

(g) to provide those who are interested in the work of the IASB with information about its approach to the formulation of IFRSs.

The Conceptual Framework is not an IFRS and hence does not define standards for any particular measurement or disclosure issue. Nothing in this Conceptual Framework overrides any specific IFRS.

The Board recognises that in a limited number of cases there may be a conflict between the Conceptual Framework and an IFRS. In those cases where there is a conflict, the requirements of the IFRS prevail over those of the Conceptual Framework. As, however, the Board is guided by the Conceptual Framework in the development of future IFRSs and in its review of existing IFRSs, the number of cases of conflict between the Conceptual Framework and IFRSs will diminish through time.

The Conceptual Framework is revised from time to time on the basis of the Board's experience of working with it.

6.3 Scope

The Conceptual Framework deals with:

(a) the objective of financial reporting;

(b) the qualitative characteristics of useful financial information;

(c) the definition, recognition and measurement of the elements from which financial statements are constructed; and

(d) concepts of capital and capital maintenance.

7. International Financial Reporting Standards

International Financial Reporting Standards in a broad sense comprise:

- *Framework for the Preparation and Presentation of Financial Statements*—stating basic principles and grounds of IFRS
- *IAS*—standards issued before 2001
- *IFRS*—standards issued after 2001
- *SIC*—interpretations of accounting standards, giving specific guidance on unclear issues
- *IFRIC*—newer interpretations, issued after 2001

IFRS, IAS, IFRIC and SIC in force as on …….

IFRSs

IFRS 1: First time Adoption of International Financial Reporting Standards

IFRS 2: Share-based Payment

IFRS 3: Business Combinations

IFRS 4: Insurance Contracts

IFRS 5: Non-current Assets Held for Sale and Discontinued Operations

IFRS 6: Exploration for and Evaluation of Mineral Resources

IFRS 7: Financial Instruments: Disclosures

IFRS 8: Operating Segments

IFRS 9: Financial Instruments

IFRS 10: Consolidated Financial Statements

IFRS 11: Joint Arrangements

IFRS 12: Disclosure of Interests in Other Entities

IFRS 13: Fair Value Measurement

IASs

IAS 1: Presentation of Financial Statements

IAS 2: Inventories

IAS 7: Statement of Cash Flows

IAS 8: Accounting Policies, Changes in Accounting Estimates and Errors

IAS 10: Events after the Reporting Period

IAS 11: Construction Contracts

IAS 12: Income Taxes

IAS 16: Property, Plant and Equipment

IAS 17: Leases

IAS 18: Revenue

IAS 19: Employee Benefits

IAS 20: Accounting for Government Grants and Disclosure of Government Assistance

IAS 21: The Effects of Changes in Foreign Exchange Rates

IAS 23: Borrowing Costs

IAS 24: Related Party Disclosures

IAS 26: Accounting and Reporting by Retirement Benefit Plans

IAS 27: Consolidated and Separate Financial Statements – Superseded by IFRS 10, IFRS 12 and IAS 27 (rev. 2011) effective 2013

IAS 28: Investments in Associates – Superseded by IAS 28 (rev. 2011) and IFRS 12 effective 2013

IAS 29: Financial Reporting in Hyperinflationary Economies

IAS 31: Interests in Joint Ventures – Superseded by IFRS 11 and IFRS 12 effective 2013

IAS 32: Financial Instruments: Presentation – Disclosure provisions superseded by IFRS 7 effective 2007

IAS 33: Earnings per Share

IAS 34: Interim Financial Reporting

IAS 36: Impairment of Assets

IAS 37: Provisions, Contingent Liabilities and Contingent Assets

IAS 38: Intangible Assets

IAS 39: Financial Instruments: Recognition and Measurement – Superseded by IFRS 9 effective 2013

IAS 40: Investment Property

IAS 41: Agriculture

Note: IAS 3, 4, 5, 6, 9, 13, 14, 15, 22, 25, 30, 35 have been superseded

IFRICs

IFRIC 1: Changes in Existing Decommissioning, Restoration and Similar Liabilities

IFRIC 2: Members' Shares in Co-operative Entities and Similar Instruments

IFRIC 4: Determining Whether an Arrangement Contains a Lease

IFRIC 5: Rights to Interests Arising from Decommissioning, Restoration and Environmental Rehabilitation Funds

IFRIC 6: Liabilities Arising from Participating in a Specific Market - Waste Electrical and Electronic Equipment

IFRIC 7: Applying the Restatement Approach under IAS 29 Financial Reporting in Hyperinflationary Economies

IFRIC 10: Interim Financial Reporting and Impairment

IFRIC 12: Service Concession Arrangements

IFRIC 13: Customer Loyalty Programmes

IFRIC 14: AS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction

IFRIC 15: Agreements for the Construction of Real Estate

IFRIC 16: Hedges of a Net Investment in a Foreign Operation

IFRIC 17: Distributions of Non-cash Assets to Owners

IFRIC 18: Transfers of Assets from Customers

IFRIC 19: Extinguishing Financial Liabilities with Equity Instruments

IFRIC 20: Stripping Costs in the Production Phase of a Surface Mine

Note: IFRIC 3, 8, 9 & 11 have since been withdrawn

SICs

SIC 7: Introduction of the Euro

SIC 10: Government Assistance – No Specific Relation to Operating Activities

SIC 15: Operating Leases – Incentives

SIC 25: Income Taxes – Changes in the Tax Status of an Enterprise or its Shareholders

SIC 27: Evaluating the Substance of Transactions in the Legal Form of a Lease

SIC 29: Disclosure – Service Concession Arrangements

SIC 31: Revenue – Barter Transactions Involving Advertising Services

SIC 32: Intangible Assets – Web Site Costs

Note: SIC 1, 2, 3, 4, 5, 6, 8, 9, 11, 12, 13, 14, 16, 17, 18, 19, 20, 21, 22, 23, 24, 26, 28, 30, 33 have been superseded

8. Overview of International Financial Reporting Standards

8.1 IFRS 1: First-Time Adoption of International Financial Reporting Standards

The objective of this IFRS is to ensure that an entity's *first IFRS financial statements*, and its interim financial reports for part of the period covered by those financial statements, contain high quality information that:

(a) is transparent for users and comparable over all periods presented;

(b) provides a suitable starting point for accounting in accordance with *International Financial Reporting Standards (IFRSs)*; and

(c) can be generated at a cost that does not exceed the benefits.

An entity shall prepare and present an *opening IFRS statement of financial position* at the *date of transition to IFRSs*. This is the starting point for its accounting in accordance with IFRSs.

An entity shall use the same accounting policies in its opening IFRS statement of financial position and throughout all periods presented in its first IFRS financial statements. Those accounting policies shall comply with each IFRS effective at the end of its *first IFRS reporting period*.

In particular, the IFRS requires an entity to do the following in the opening IFRS statement of financial position that it prepares as a starting point for its accounting under IFRSs:

(a) recognise all assets and liabilities whose recognition is required by IFRSs;

(b) not recognise items as assets or liabilities if IFRSs do not permit such recognition;

(c) reclassify items that it recognised in accordance with previous GAAP as one type of asset, liability or component of equity, but are a different type of asset, liability or component of equity in accordance with IFRSs; and

(d) apply IFRSs in measuring all recognised assets and liabilities.

The IFRS grants limited exemptions from these requirements in specified areas where the cost of complying with them would be likely to exceed the benefits to users of financial statements. The IFRS also prohibits retrospective application of IFRSs in some areas, particularly where retrospective application would require judgements by management about past conditions after the outcome of a particular transaction is already known.

The IFRS requires disclosures that explain how the transition from previous GAAP to IFRSs affected the entity's reported financial position, financial performance and cash flows.

8.2 IFRS 2: Share-Based Payment

The objective of this IFRS is to specify the financial reporting by an entity when it undertakes a *share-based payment transaction*. In particular, it requires an entity to reflect in its profit or loss and financial position the effects of share-based payment transactions, including expenses associated with transactions in which *share options* are granted to employees.

The IFRS requires an entity to recognise share-based payment transactions in its financial statements, including transactions with employees or other parties to be settled in cash, other assets, or equity instruments of the entity. There are no exceptions to the IFRS, other than for transactions to which other Standards apply.

This also applies to transfers of equity instruments of the entity's parent, or equity instruments of another entity in the same group as the entity, to parties that have supplied goods or services to the entity.

The IFRS sets out measurement principles and specific requirements for three types of share-based payment transactions:

(a) equity-settled share-based payment transactions, in which the entity receives goods or services as consideration for equity instruments of the entity (including shares or share options);

(b) cash-settled share-based payment transactions, in which the entity acquires goods or services by incurring liabilities to the supplier of those goods or services for amounts that are based on the price (or value) of the entity's shares or other equity instruments of the entity; and

(c) transactions in which the entity receives or acquires goods or services and the terms of the arrangement provide either the entity or the supplier of those goods or services with a choice of whether the entity settles the transaction in cash or by issuing equity instruments.

For equity-settled share-based payment transactions, the IFRS requires an entity to measure the goods or services received, and the corresponding increase in equity, directly, at the fair value of the goods or services received, unless that fair value cannot be estimated reliably. If the entity cannot estimate reliably the fair value of the goods or services received, the entity is required to measure their value, and the corresponding increase in equity, indirectly, by reference to the fair value of the equity instruments granted. Furthermore:

(a) for transactions with employees and others providing similar services, the entity is required to measure the fair value of the equity instruments granted, because it is typically not possible to estimate reliably the fair value of employee services received. The fair value of the equity instruments granted is measured at grant date.

(b) for transactions with parties other than employees (and those providing similar services), there is a rebuttable presumption that the fair value of the goods or services received can be estimated reliably. That fair value is measured at the date the entity obtains the goods or the counterparty renders service. In rare cases, if the presumption is rebutted, the transaction is

measured by reference to the fair value of the equity instruments granted, measured at the date the entity obtains the goods or the counterparty renders service.

(c) for goods or services measured by reference to the fair value of the equity instruments granted, the IFRS specifies that vesting conditions, other than market conditions, are not taken into account when estimating the fair value of the shares or options at the relevant measurement date (as specified above). Instead, vesting conditions are taken into account by adjusting the number of equity instruments included in the measurement of the transaction amount so that, ultimately, the amount recognised for goods or services received as consideration for the equity instruments granted is based on the number of equity instruments that eventually vest. Hence, on a cumulative basis, no amount is recognised for goods or services received if the equity instruments granted do not vest because of failure to satisfy a vesting condition (other than a market condition).

(d) the IFRS requires the fair value of equity instruments granted to be based on market prices, if available, and to take into account the terms and conditions upon which those equity instruments were granted. In the absence of market prices, fair value is estimated, using a valuation technique to estimate what the price of those equity instruments would have been on the measurement date in an arm's length transaction between knowledgeable, willing parties.

(e) the IFRS also sets out requirements if the terms and conditions of an option or share grant are modified (eg an option is repriced) or if a grant is cancelled, repurchased or replaced with another grant of equity instruments. For example, irrespective of any modification, cancellation or settlement of a grant of equity instruments to employees, the IFRS generally requires the entity to recognise, as a minimum, the services received measured at the grant date fair value of the equity instruments granted.

For cash-settled share-based payment transactions, the IFRS requires an entity to measure the goods or services acquired and the liability incurred at the fair value of the liability. Until the liability is settled, the entity is required to remeasure the fair value of the liability at each reporting date and at the date of settlement, with any changes in value recognised in profit or loss for the period.

For share-based payment transactions in which the terms of the arrangement provide either the entity or the supplier of goods or services with a choice of whether the entity settles the transaction in cash or by issuing equity instruments, the entity is required to account for that transaction, or the components of that transaction, as a cash-settled share-based payment transaction if, and to the extent that, the entity has incurred a liability to settle in cash (or other assets), or as an equity-settled share-based payment transaction if, and to the extent that, no such liability has been incurred.

The IFRS prescribes various disclosure requirements to enable users of financial statements to understand:

(a) the nature and extent of share-based payment arrangements that existed during the period;

(b) how the fair value of the goods or services received, or the fair value of the equity instruments granted, during the period was determined; and

(c) the effect of share-based payment transactions on the entity's profit or loss for the period and on its financial position.

8.3 IFRS 3: Business Combinations

The objective of the IFRS is to enhance the relevance, reliability and comparability of the information that a reporting entity provides in its financial statements about a business combination and its effects. It does that by establishing principles and requirements for how an acquirer:

(a) recognises and measures in its financial statements the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquiree;

(b) recognises and measures the goodwill acquired in the business combination or a gain from a bargain purchase; and

(c) determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination.

Core principle

An acquirer of a business recognises the assets acquired and liabilities assumed at their acquisition-date fair values and discloses information that enables users to evaluate the nature and financial effects of the acquisition.

Applying the acquisition method

A business combination must be accounted for by applying the acquisition method, unless it is a combination involving entities or businesses under common control. One of the parties to a business combination can always be identified as the acquirer, being the entity that obtains control of the other business (the acquiree).

Formations of a joint venture or the acquisition of an asset or a group of assets that does not constitute a business are not business combinations.

The IFRS establishes principles for recognising and measuring the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquiree. Any classifications or designations made in recognising these items must be made in accordance with the contractual terms, economic conditions, acquirer's operating or accounting policies and other factors that exist at the acquisition date.

Each identifiable asset and liability is measured at its acquisition-date fair value. Any non-controlling interest in an acquiree is measured at fair value or as the non-controlling interest's proportionate share of the acquiree's net identifiable assets.

The IFRS provides limited exceptions to these recognition and measurement principles:

(a) Leases and insurance contracts are required to be classified on the basis of the contractual terms and other factors at the inception of the contract (or when the terms have changed) rather than on the basis of the factors that exist at the acquisition date.

(b) Only those contingent liabilities assumed in a business combination that are a present obligation and can be measured reliably are recognised.

(c) Some assets and liabilities are required to be recognised or measured in accordance with other IFRSs, rather than at fair value. The assets and liabilities affected are those falling within the scope of IAS 12 *Income Taxes*, IAS 19 *Employee Benefits*, IFRS 2 *Share-based Payment* and IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*.

(d) There are special requirements for measuring a reacquired right.

(e) Indemnification assets are recognised and measured on a basis that is consistent with the item that is subject to the indemnification, even if that measure is not fair value.

The IFRS requires the acquirer, having recognised the identifiable assets, the liabilities and any non-controlling interests, to identify any difference between:

(a) the aggregate of the consideration transferred, any non-controlling interest in the acquiree and, in a business combination achieved in stages, the acquisition-date fair value of the acquirer's previously held equity interest in the acquiree; and

(b) the net identifiable assets acquired.

The difference will, generally, be recognised as goodwill. If the acquirer has made a gain from a bargain purchase that gain is recognised in profit or loss.

The consideration transferred in a business combination (including any contingent consideration) is measured at fair value.

In general, an acquirer measures and accounts for assets acquired and liabilities assumed or incurred in a business combination after the business combination has been completed in accordance with other applicable IFRSs. However, the IFRS provides accounting requirements for reacquired rights, contingent liabilities, contingent consideration and indemnification assets.

Disclosure

The IFRS requires the acquirer to disclose information that enables users of its financial statements to evaluate the nature and financial effect of business combinations that occurred during the current reporting period or after the reporting date but before the financial statements are authorised for issue. After a business combination, the acquirer must disclose any adjustments recognised in the current reporting period that relate to business combinations that occurred in the current or previous reporting periods.

8.4 IFRS 4 : Insurance Contracts

The objective of this IFRS is to specify the financial reporting for *insurance contracts* by any entity that issues such contracts (described in this IFRS as an *insurer*) until the Board completes the second phase of its project on insurance contracts. In particular, this IFRS requires:

(a) limited improvements to accounting by insurers for insurance contracts.

(b) disclosure that identifies and explains the amounts in an insurer's financial statements arising from insurance contracts and helps users of those financial statements understand the amount, timing and uncertainty of future cash flows from insurance contracts.

An *insurance contract* is a contract under which one party (the insurer) accepts significant insurance risk from another party (the policyholder) by agreeing to compensate the policyholder if a specified uncertain future event (the insured event) adversely affects the policyholder.

The IFRS applies to all insurance contracts (including reinsurance contracts) that an entity issues and to reinsurance contracts that it holds, except for specified contracts covered by other IFRSs. It does not apply to other assets and liabilities of an insurer, such as financial assets and financial liabilities within the scope of IFRS 9 *Financial Instruments*. Furthermore, it does not address accounting by policyholders.

The IFRS exempts an insurer temporarily (ie during phase I of this project) from some requirements of other IFRSs, including the requirement to consider the *Framework* in selecting accounting policies for insurance contracts. However, the IFRS:

(a) prohibits provisions for possible claims under contracts that are not in existence at the end of the reporting period (such as catastrophe and equalisation provisions).

(b) requires a test for the adequacy of recognised insurance liabilities and an impairment test for reinsurance assets.

(c) requires an insurer to keep insurance liabilities in its statement of financial position until they are discharged or cancelled, or expire, and to present insurance liabilities without offsetting them against related reinsurance assets.

The IFRS permits an insurer to change its accounting policies for insurance contracts only if, as a result, its financial statements present information that is more relevant and no less reliable, or more reliable and no less relevant. In particular, an insurer cannot introduce any of the following practices, although it may continue using accounting policies that involve them:

(a) measuring insurance liabilities on an undiscounted basis.

(b) measuring contractual rights to future investment management fees at an amount that exceeds their fair value as implied by a comparison with current fees charged by other market participants for similar services.

(c) using non-uniform accounting policies for the insurance liabilities of subsidiaries.

The IFRS permits the introduction of an accounting policy that involves remeasuring designated insurance liabilities consistently in each period to reflect current market interest rates (and, if the insurer so elects, other current estimates and assumptions). Without this permission, an insurer would have been required to apply the change in accounting policies consistently to all similar liabilities.

The IFRS requires disclosure to help users understand:

(a) the amounts in the insurer's financial statements that arise from insurance contracts.

(b) the nature and extent of risks arising from insurance contracts.

8.5 IFRS 5 : Non-Current Assets held for Sale and Discontinued Operations

The objective of this IFRS is to specify the accounting for assets held for sale, and the presentation and disclosure of discontinued operations. In particular, the IFRS requires:

(a) assets that meet the criteria to be classified as held for sale to be measured at the lower of carrying amount and fair value less costs to sell, and depreciation on such assets to cease;

(b) an asset classified as held for sale and the assets and liabilities included within a disposal group classified as held for sale to be presented separately in the statement of financial position; and

(c) the results of discontinued operations to be presented separately in the statement of comprehensive income.

The IFRS:

(a) adopts the classification 'held for sale'.

(b) introduces the concept of a disposal group, being a group of assets to be disposed of, by sale or otherwise, together as a group in a single transaction, and liabilities directly associated with those assets that will be transferred in the transaction.

(c) classifies an operation as discontinued at the date the operation meets the criteria to be classified as held for sale or when the entity has disposed of the operation.

An entity shall classify a non-current asset (or disposal group) as held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use.

For this to be the case, the asset (or disposal group) must be available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such assets (or disposal groups) and its sale must be *highly probable*.

For the sale to be highly probable, the appropriate level of management must be committed to a plan to sell the asset (or disposal group), and an active programme to locate a buyer and complete the plan must have been initiated. Further, the asset (or disposal group) must be actively marketed for sale at a price that is reasonable in relation to its current fair value. In addition, the sale should be expected to qualify for recognition as a completed sale within one year from the date of classification, except as permitted by paragraph 9, and actions required to complete the plan should indicate that it is unlikely that significant changes to the plan will be made or that the plan will be withdrawn.

A discontinued operation is a component of an entity that either has been disposed of, or is classified as held for sale, and

(a) represents a separate major line of business or geographical area of operations,

(b) is part of a single co-ordinated plan to dispose of a separate major line of business or geographical area of operations or

(c) is a subsidiary acquired exclusively with a view to resale.

A component of an entity comprises operations and cash flows that can be clearly distinguished, operationally and for financial reporting purposes, from the rest of the entity. In other words, a component of an entity will have been a cash-generating unit or a group of cash-generating units while being held for use.

An entity shall not classify as held for sale a non-current asset (or disposal group) that is to be abandoned.

This is because its carrying amount will be recovered principally through continuing use.

8.6 IFRS 6 Exploration for and Evaluation of Mineral Resources

The objective of this IFRS is to specify the financial reporting for the exploration for and evaluation of mineral resources.

Exploration and evaluation expenditures are expenditures incurred by an entity in connection with the exploration for and evaluation of mineral resources before the technical feasibility and commercial viability of extracting a mineral resource are demonstrable. *Exploration for and evaluation of mineral resources* is the search for mineral resources, including minerals, oil, natural gas and similar non-regenerative resources after the entity has obtained legal rights to explore in a specific area, as well as the determination of the technical feasibility and commercial viability of extracting the mineral resource.

Exploration and evaluation assets are exploration and evaluation expenditures recognised as assets in accordance with the entity's accounting policy.

The IFRS:

(a) permits an entity to develop an accounting policy for exploration and evaluation assets without specifically considering the requirements of paragraphs 11 and 12 of IAS 8. Thus, an entity adopting IFRS 6 may continue to use the accounting policies applied immediately before adopting the IFRS. This includes continuing to use recognition and measurement practices that are part of those accounting policies.

(b) requires entities recognising exploration and evaluation assets to perform an impairment test on those assets when facts and circumstances suggest that the carrying amount of the assets may exceed their recoverable amount.

(c) varies the recognition of impairment from that in IAS 36 but measures the impairment in accordance with that Standard once the impairment is identified.

An entity shall determine an accounting policy for allocating exploration and evaluation assets to cashgenerating units or groups of cash-generating units for the purpose of assessing such assets for impairment.

Each cash-generating unit or group of units to which an exploration and evaluation asset is allocated shall not be larger than an operating segment determined in accordance with IFRS 8 *Operating Segments*.

Exploration and evaluation assets shall be assessed for impairment when facts and circumstances suggest that the carrying amount of an exploration and evaluation asset may exceed its

recoverable amount. When facts and circumstances suggest that the carrying amount exceeds the recoverable amount, an entity shall measure, present and disclose any resulting impairment loss in accordance with IAS 36.

One or more of the following facts and circumstances indicate that an entity should test exploration and evaluation assets for impairment (the list is not exhaustive):

(a) the period for which the entity has the right to explore in the specific area has expired during the period or will expire in the near future, and is not expected to be renewed.

(b) substantive expenditure on further exploration for and evaluation of mineral resources in the specific area is neither budgeted nor planned.

(c) exploration for and evaluation of mineral resources in the specific area have not led to the discovery of commercially viable quantities of mineral resources and the entity has decided to discontinue such activities in the specific area.

(d) sufficient data exist to indicate that, although a development in the specific area is likely to proceed, the carrying amount of the exploration and evaluation asset is unlikely to be recovered in full from successful development or by sale.

An entity shall disclose information that identifies and explains the amounts recognised in its financial statements arising from the exploration for and evaluation of mineral resources.

8.7 IFRS 7 : Financial Instruments: Disclosures

The objective of this IFRS is to require entities to provide disclosures in their financial statements that enable users to evaluate:

(a) the significance of financial instruments for the entity's financial position and performance; and

(b) the nature and extent of risks arising from financial instruments to which the entity is exposed during the period and at the end of the reporting period, and how the entity manages those risks. The qualitative disclosures describe management's objectives, policies and processes for managing those risks. The quantitative disclosures provide information about the extent to which the entity is exposed to risk, based on information provided internally to the entity's key management personnel. Together, these disclosures provide an overview of the entity's use of financial instruments and the exposures to risks they create.

The IFRS applies to all entities, including entities that have few financial instruments (eg a manufacturer whose only financial instruments are accounts receivable and accounts payable) and those that have many financial instruments (eg a financial institution most of whose assets and liabilities are financial instruments).

When this IFRS requires disclosures by class of financial instrument, an entity shall group financial instruments into classes that are appropriate to the nature of the information disclosed and that take into account the characteristics of those financial instruments. An entity shall provide sufficient information to permit reconciliation to the line items presented in the statement of financial position.

The principles in this IFRS complement the principles for recognising, measuring and presenting financial assets and financial liabilities in IAS 32 *Financial Instruments: Presentation* and IFRS 9 *Financial Instruments*.

8.8 IFRS 8 : Operating Segments

Core principle—An entity shall disclose information to enable users of its financial statements to evaluate the nature and financial effects of the business activities in which it engages and the economic environments in which it operates.

This IFRS shall apply to:

(a) the separate or individual financial statements of an entity:

  (i) whose debt or equity instruments are traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets), or

  (ii) that files, or is in the process of filing, its financial statements with a securities commission or other regulatory organisation for the purpose of issuing any class of instruments in a public market; and

(b) the consolidated financial statements of a group with a parent:

  (i) whose debt or equity instruments are traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets), or

  (ii) that files, or is in the process of filing, the consolidated financial statements with a securities commission or other regulatory organisation for the purpose of issuing any class of instruments in a public market.

The IFRS specifies how an entity should report information about its operating segments in annual financial statements and, as a consequential amendment to IAS 34 *Interim Financial Reporting*, requires an entity to report selected information about its operating segments in interim financial reports. It also sets out requirements for related disclosures about products and services, geographical areas and major customers.

The IFRS requires an entity to report financial and descriptive information about its reportable segments.

Reportable segments are operating segments or aggregations of operating segments that meet specified criteria.

Operating segments are components of an entity about which separate financial information is available that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance. Generally, financial information is required to be reported on the same basis as is used internally for evaluating operating segment performance and deciding how to allocate resources to operating segments.

The IFRS requires an entity to report a measure of operating segment profit or loss and of segment assets.

It also requires an entity to report a measure of segment liabilities and particular income and expense items if such measures are regularly provided to the chief operating decision maker. It requires reconciliations of total reportable segment revenues, total profit or loss, total assets, liabilities and other amounts disclosed for reportable segments to corresponding amounts in the entity's financial statements.

The IFRS requires an entity to report information about the revenues derived from its products or services (or groups of similar products and services), about the countries in which it earns revenues and holds assets, and about major customers, regardless of whether that information is used by management in making operating decisions. However, the IFRS does not require an entity to report information that is not prepared for internal use if the necessary information is not available and the cost to develop it would be excessive.

The IFRS also requires an entity to give descriptive information about the way the operating segments were determined, the products and services provided by the segments, differences between the measurements used in reporting segment information and those used in the entity's financial statements, and changes in the measurement of segment amounts from period to period.

8.9 IFRS 9 : Financial Instruments

On 12th November 2009, the International Accounting Standards Board issued IFRS 9 Financial Instruments. IASB reissued IFRS 9 *Financial Instruments*, on 28th October, 2010, incorporating new requirements on accounting for financial liabilities and carrying over from IAS 39 the requirements for derecognition of financial assets and financial liabilities. Effective date of IFRS 9 is 1st January, 2013, with early adoption permitted starting in 2009.

IFRS 9 specifies how an entity should classify and measure financial assets and financial liabilities, including some hybrid contracts. It is the first part of Phase 1 of the Board's project to replace IAS 39. The main phases are: Phase 1: Classification and measurement. Phase 2: Impairment methodology. Phase 3: Hedge accounting.

The Board aims to have replaced IAS 39 in its entirety. Therefore the objective of this IFRS is to establish principles for the financial reporting of financial assets and financial liabilities that will present relevant and useful information to users of financial statements for their assessment of the amounts, timing and uncertainty of an entity's future cash flows.

Recognition and initial measurement: An entity shall recognise a financial asset or a financial liability in its statement of financial position when, and only when, the entity becomes party to the contractual provisions of the instrument. At initial recognition, an entity shall measure a financial asset or financial liability at its fair value plus or minus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability.

Financial assets – classification, reclassification and subsequent measurement

When an entity first recognises a financial asset, it shall classify it based on the entity's business model for managing the financial assets and the contractual cash flow characteristics of the financial asset.

A financial asset shall be measured at amortised cost if both of the following conditions are met:

(a) The asset is held within a business model whose objective is to hold assets in order to collect contractual cash flows.

(b) The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

However, an entity may, at initial recognition, irrevocably designate a financial asset as measured at fair value through profit or loss if doing so eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as an 'accounting mismatch') that would otherwise arise from measuring assets or liabilities or recognising the gains and losses on them on different bases.

A financial asset shall be measured at fair value unless it is measured at amortised cost.

When, and only when, an entity changes its business model for managing financial assets it shall reclassify all affected financial assets.

Financial liabilities – classification, reclassification and subsequent measurement

An entity shall classify all financial liabilities as subsequently measured at amortised cost using the effective interest method, except for:

(a) financial liabilities at fair value through profit or loss. Such liabilities, including derivatives that are liabilities, shall be subsequently measured at fair value.

(b) financial liabilities that arise when a transfer of a financial asset does not qualify for derecognition or when the continuing involvement approach applies.

(c) financial guarantee contracts as defined in Appendix A. After initial recognition, an issuer of such a contract shall (unless paragraph 4.2.1(a) or (b) applies) subsequently measure it at the higher of:

    (i) the amount determined in accordance with IAS 37 Provisions, Contingent Liabilities and Contingent Assets and

    (ii) the amount initially recognised less, when appropriate, cumulative amortisation recognised in accordance with IAS 18 Revenue.

(d) commitments to provide a loan at a below-market interest rate. After initial recognition, an issuer of such a commitment shall (unless paragraph 4.2.1(a) applies) subsequently measure it at the higher of:

    (i) the amount determined in accordance with IAS 37 and

(ii) the amount initially recognised less, when appropriate, cumulative amortisation recognised in accordance with IAS 18.

However, an entity may, at initial recognition, irrevocably designate a financial liability as measured at fair value through profit or loss when permitted or when doing so results in more relevant information.

An entity shall not reclassify any financial liability.

8.10 IFRS 10: Consolidated Financial Statements

Objective

The objective of IFRS 10 is to establish principles for the presentation and preparation of consolidated financial statements when an entity controls one or more other entities.

The Standard:

- requires a parent entity (an entity that controls one or more other entities) to present consolidated financial statements
- defines the principle of control, and establishes control as the basis for consolidation
- set out how to apply the principle of control to identify whether an investor controls an investee and therefore must consolidate the investee
- sets out the accounting requirements for the preparation of consolidated financial statements.

Key definitions

Consolidated financial statements	The financial statements of a group in which the assets, liabilities, equity, income, expenses and cash flows of the parent and its subsidiaries are presented as those of a single economic entity
Control of an investee	An investor controls an investee when the investor is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee
Parent	An entity that controls one or more entities
Power	Existing rights that give the current ability to direct the relevant activities
Protective rights	Rights designed to protect the interest of the party holding those rights without giving that party power over the entity to which those rights relate
Relevant activities	Activities of the investee that significantly affect the investee's returns

Control

An investor determines whether it is a parent by assessing whether it controls one or more investees. An investor considers all relevant facts and circumstances when assessing whether it controls an investee. An investor controls an investee when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee.

An investor controls an investee if and only if the investor has all of the following elements:

- power over the investee, i.e. the investor has existing rights that give it the ability to direct the relevant activities (the activities that significantly affect the investee's returns)
- exposure, or rights, to variable returns from its involvement with the investee
- the ability to use its power over the investee to affect the amount of the investor's returns.

Power arises from rights. Such rights can be straightforward (e.g. through voting rights) or be complex (e.g. embedded in contractual arrangements). An investor that holds only protective rights cannot have power over an investee and so cannot control an investee.

An investor must be exposed, or have rights, to variable returns from its involvement with an investee to control the investee. Such returns must have the potential to vary as a result of the investee's performance and can be positive, negative, or both.

A parent must not only have power over an investee and exposure or rights to variable returns from its involvement with the investee, a parent must also have the ability to use its power over the investee to affect its returns from its involvement with the investee.

When assessing whether an investor controls an investee an investor with decision-making rights determines whether it acts as principal or as an agent of other parties. A number of factors are considered in making this assessment. For instance, the remuneration of the decision-maker is considered in determining whether it is an agent.

Accounting requirements

Preparation of consolidated financial statements

A parent prepares consolidated financial statements using uniform accounting policies for like transactions and other events in similar circumstances.

However, a parent need not present consolidated financial statements if it meets all of the following conditions:

- it is a wholly-owned subsidiary or is a partially-owned subsidiary of another entity and its other owners, including those not otherwise entitled to vote, have been informed about, and do not object to, the parent not presenting consolidated financial statements
- its debt or equity instruments are not traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets)
- it did not file, nor is it in the process of filing, its financial statements with a securities commission or other regulatory organisation for the purpose of issuing any class of instruments in a public market, and
- its ultimate or any intermediate parent of the parent produces consolidated financial statements available for public use that comply with IFRSs.

Furthermore, post-employment benefit plans or other long-term employee benefit plans to which IAS 19 *Employee Benefits* applies are not required to apply the requirements of IFRS 10.

Consolidation procedures

Consolidated financial statements:

- combine like items of assets, liabilities, equity, income, expenses and cash flows of the parent with those of its subsidiaries
- offset (eliminate) the carrying amount of the parent's investment in each subsidiary and the parent's portion of equity of each subsidiary (IFRS 3 *Business Combinations* explains how to account for any related goodwill)
- eliminate in full intragroup assets and liabilities, equity, income, expenses and cash flows relating to transactions between entities of the group (profits or losses resulting from intragroup transactions that are recognised in assets, such as inventory and fixed assets, are eliminated in full).

A reporting entity includes the income and expenses of a subsidiary in the consolidated financial statements from the date it gains control until the date when the reporting entity ceases to control the subsidiary. Income and expenses of the subsidiary are based on the amounts of the assets and liabilities recognised in the consolidated financial statements at the acquisition date.

The parent and subsidiaries are required to have the same reporting dates, or consolidation based on additional financial information prepared by subsidiary, unless impracticable. Where impracticable, the most recent financial statements of the subsidiary are used, adjusted for the effects of significant transactions or events between the reporting dates of the subsidiary and consolidated financial statements. The difference between the date of the subsidiary's financial statements and that of the consolidated financial statements shall be no more than three months.

Non-Controlling Interests (NCIs)

A parent presents non-controlling interests in its consolidated statement of financial position within equity, separately from the equity of the owners of the parent.

A reporting entity attributes the profit or loss and each component of other comprehensive income to the owners of the parent and to the non-controlling interests. The proportion allocated to the parent and non-controlling interests are determined on the basis of present ownership interests.

The reporting entity also attributes total comprehensive income to the owners of the parent and to the non-controlling interests even if this results in the non-controlling interests having a deficit balance.

Changes in ownership interests

Changes in a parent's ownership interest in a subsidiary that do not result in the parent losing control of the subsidiary are equity transactions (i.e. transactions with owners in their capacity as owners). When the proportion of the equity held by non-controlling interests changes, the carrying amounts of the controlling and non-controlling interests area adjusted to reflect the changes in their relative interests in the subsidiary. Any difference between the amount by which the non-controlling

interests are adjusted and the fair value of the consideration paid or received is recognised directly in equity and attributed to the owners of the parent.

If a parent loses control of a subsidiary, the parent:

- derecognises the assets and liabilities of the former subsidiary from the consolidated statement of financial position
- recognises any investment retained in the former subsidiary at its fair value when control is lost and subsequently accounts for it and for any amounts owed by or to the former subsidiary in accordance with relevant IFRSs. That fair value is regarded as the fair value on initial recognition of a financial asset in accordance with IFRS 9 *Financial Instruments* or, when appropriate, the cost on initial recognition of an investment in an associate or joint venture
- recognises the gain or loss associated with the loss of control attributable to the former controlling interest.

Investment entities consolidation exemption

[Note: The investment entity consolidation exemption was introduced by Investment Entities, issued on 31 October 2012 and effective for annual periods beginning on or after 1 January 2014.]

IFRS 10 contains special accounting requirements for investment entities. Where an entity meets the definition of an 'investment entity' (see above), it does not consolidate its subsidiaries, or apply IFRS 3 Business Combinations when it obtains control of another entity.

An entity is required to consider all facts and circumstances when assessing whether it is an investment entity, including its purpose and design. IFRS 10 provides that an investment entity should have the following typical characteristics:

- *it has more than one investment*
- *it has more than one investor*
- *it has investors that are not related parties of the entity*
- *it has ownership interests in the form of equity or similar interests.*

The absence of any of these typical characteristics does not necessarily disqualify an entity from being classified as an investment entity.

An investment entity is required to measure an investment in a subsidiary at fair value through profit or loss in accordance with IFRS 9 Financial Instruments or IAS 39 Financial Instruments: Recognition and Measurement. However, an investment entity is still required to consolidate a subsidiary where that subsidiary provides services that relate to the investment entity's investment activities.

Because an investment entity is not required to consolidate its subsidiaries, intragroup related party transactions and outstanding balances are not eliminated.

Special requirements apply where an entity becomes, or ceases to be, an investment entity.

The exemption from consolidation only applies to the investment entity itself. Accordingly, a parent of an investment entity is required to consolidate all entities that it controls, including those controlled through an investment entity subsidiary, unless the parent itself is an investment entity.

Disclosure

There are no disclosures specified in IFRS 10. Instead, IFRS 12 *Disclosure of Interests in Other Entities* outlines the disclosures required.

Applicability and early adoption

IFRS 10 is applicable to annual reporting periods beginning on or after 1 January 2013.

Retrospective application is generally required in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. However, an entity is not required to make adjustments to the accounting for its involvement with entities that were previously consolidated and continue to be consolidated, or entities that were previously unconsolidated and continue not to be consolidated.

Furthermore, an entity is not required to present the quantitative information required by paragraph 28(f) of IAS 8 for the annual period immediately preceding the date of initial application of the standard (the beginning of the annual reporting period for which IFRS 10 is first applied). However, an entity may choose to present adjusted comparative information for earlier reporting periods, any must clearly identify any unadjusted comparative information and explain the basis on which the comparative information has been prepared.

IFRS 10 prescribes modified accounting on its first application in the following circumstances:

- an entity consolidates an entity not previously consolidated
- an entity no longer consolidates an entity that was previously consolidated
- in relation to certain amendments to IAS 27 made in 2008 that have been carried forward into IFRS 10.

8.11 IFRS 11: Joint Arrangements

IFRS 11 is applicable to annual reporting periods beginning on or after 1 January 2013.

Core principle

The core principle of IFRS 11 is that a party to a joint arrangement determines the type of joint arrangement in which it is involved by assessing its rights and obligations and accounts for those rights and obligations in accordance with that type of joint arrangement.

Key definitions

Joint arrangement	An arrangement of which two or more parties have joint control
Joint control	The contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control
Joint operation	A joint arrangement whereby the parties that have joint control of the arrangement have rights to the assets, and obligations for the liabilities, relating to the arrangement
Joint venture	A joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement
Joint venturer	A party to a joint venture that has joint control of that joint venture
Party to a joint arrangement	An entity that participates in a joint arrangement, regardless of whether that entity has joint control of the arrangement
Separate vehicle	A separately identifiable financial structure, including separate legal entities or entities recognised by statute, regardless of whether those entities have a legal personality

Joint arrangements

A joint arrangement is an arrangement of which two or more parties have joint control.

A joint arrangement has the following characteristics:

- the parties are bound by a contractual arrangement, and
- the contractual arrangement gives two or more of those parties joint control of the arrangement.

A joint arrangement is either a joint operation or a joint venture.

Joint control

Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control.

Before assessing whether an entity has joint control over an arrangement, an entity first assesses whether the parties, or a group of the parties, control the arrangement (in accordance with the definition of control in IFRS 10 *Consolidated Financial Statements*).

After concluding that all the parties, or a group of the parties, control the arrangement collectively, an entity shall assess whether it has joint control of the arrangement. Joint control exists only when decisions about the relevant activities require the unanimous consent of the parties that collectively control the arrangement.

The requirement for unanimous consent means that any party with joint control of the arrangement can prevent any of the other parties, or a group of the parties, from making unilateral decisions (about the relevant activities) without its consent.

Types of joint arrangements

Joint arrangements are either joint operations or joint ventures:

- A **joint operation** is a joint arrangement whereby the parties that have joint control of the arrangement have rights to the assets, and obligations for the liabilities, relating to the arrangement. Those parties are called joint operators.
- A **joint venture** is a joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement. Those parties are called joint venturers.

Classifying joint arrangements

The classification of a joint arrangement as a joint operation or a joint venture depends upon the rights and obligations of the parties to the arrangement. An entity determines the type of joint arrangement in which it is involved by considering the structure and form of the arrangement, the terms agreed by the parties in the contractual arrangement and other facts and circumstances.

Regardless of the purpose, structure or form of the arrangement, the classification of joint arrangements depends upon the parties' rights and obligations arising from the arrangement.

A joint arrangement in which the assets and liabilities relating to the arrangement are held in a separate vehicle can be either a joint venture or a joint operation.

A joint arrangement that is not structured through a separate vehicle is a joint operation. In such cases, the contractual arrangement establishes the parties' rights to the assets, and obligations for the liabilities, relating to the arrangement, and the parties' rights to the corresponding revenues and obligations for the corresponding expenses.

Financial statements of parties to a joint arrangement

Joint operations

A joint operator recognises in relation to its interest in a joint operation:

- its assets, including its share of any assets held jointly;
- its liabilities, including its share of any liabilities incurred jointly;
- its revenue from the sale of its share of the output of the joint operation;
- its share of the revenue from the sale of the output by the joint operation; and
- its expenses, including its share of any expenses incurred jointly.

A joint operator accounts for the assets, liabilities, revenues and expenses relating to its involvement in a joint operation in accordance with the relevant IFRSs.

A party that participates in, but does not have joint control of, a joint operation shall also account for its interest in the arrangement in accordance with the above if that party has rights to the assets, and obligations for the liabilities, relating to the joint operation.

Joint ventures

A joint venturer recognises its interest in a joint venture as an investment and shall account for that investment using the equity method in accordance with IAS 28 *Investments in Associates and Joint Ventures* unless the entity is exempted from applying the equity method as specified in that standard.

A party that participates in, but does not have joint control of, a joint venture accounts for its interest in the arrangement in accordance with IFRS 9 *Financial Instruments* unless it has significant influence over the joint venture, in which case it accounts for it in accordance with IAS 28 (as amended in 2011).

Separate Financial Statements

The accounting for joint arrangements in an entity's separate financial statements depends on the involvement of the entity in that joint arrangement and the type of the joint arrangement:

- If the entity is a joint operator or joint venturer it shall account for its interest in
  - a joint operation in accordance with paragraphs 20-22;
  - a joint venture in accordance with paragraph 10 of IAS 27 *Separate Financial Statements*.
- If the entity is a party that participates in, but does not have joint control of, a joint arrangement shall account for its interest in:
  - a joint operation in accordance with paragraphs 23;
  - a joint venture in accordance with IFRS 9, unless the entity has significant influence over the joint venture, in which case it shall apply paragraph 10 of IAS 27 (as amended in 2011).

Disclosure

There are no disclosures specified in IFRS 11. Instead, IFRS 12 *Disclosure of Interests in Other Entities* outlines the disclosures required.

Special transitional provisions are included for:

- transition from proportionate consolidation to the equity method for joint ventures
- transition from the equity method to accounting for assets and liabilities for joint operations
- transition in an entity's separate financial statements for a joint operation previously accounted for as an investment at cost.

8.12 IFRS 12: Disclosure of Interests in other Entities

IFRS 12 is applicable to annual reporting periods beginning on or after 1 January 2013. Early application is permitted.

Objective and scope

The objective of IFRS 12 is to require the disclosure of information that enables users of financial statements to evaluate:

- the nature of, and risks associated with, its interests in other entities
- the effects of those interests on its financial position, financial performance and cash flows.

Where the disclosures required by IFRS 12, together with the disclosures required by other IFRSs, do not meet the above objective, an entity is required to disclose whatever additional information is necessary to meet the objective.

IFRS 12 is required to be applied by an entity that has an interest in any of the following:

- subsidiaries
- joint arrangements (joint operations or joint ventures)
- associates
- unconsolidated structured entities

IFRS 12 does not apply to certain employee benefit plans, separate financial statements to which IAS 27 *Separate Financial Statements* applies (except in relation to unconsolidated structured entities in some cases), certain interests in joint ventures held by an entity that does not share in joint control, and the majority of interests in another entity accounted for in accordance with IFRS 9 *Financial Instruments*.

Key definitions

Interest in another entity	Refers to contractual and non-contractual involvement that exposes an entity to variability of returns from the performance of the other entity. An interest in another entity can be evidenced by, but is not limited to, the holding of equity or debt instruments as well as other forms of involvement such as the provision of funding, liquidity support, credit enhancement and guarantees. It includes the means by which an entity has control or joint control of, or significant influence over, another entity. An entity does not necessarily have an interest in another entity solely because of a typical customer supplier relationship.
Structured entity	An entity that has been designed so that voting or similar rights are not the dominant factor in deciding who controls the entity, such as when any voting rights relate to administrative tasks only and the relevant activities are directed by means of contractual arrangements.

Disclosures required

Important note: The summary of disclosures that follows is a high-level summary of the main requirements of IFRS 12. It does not list every specific disclosure required by the standard, but instead highlights the broad objectives, categories and nature of the disclosures required. IFRS 12 lists specific examples and additional disclosures which further expand upon the disclosure objectives, and includes other guidance on the disclosures required. Accordingly,

readers should not consider this to be a comprehensive or complete listing of the disclosure requirements of IFRS 12.

Significant judgements and assumptions

An entity discloses information about significant judgements and assumptions it has made (and changes in those judgements and assumptions) in determining:

- that it controls another entity
- that it has joint control of an arrangement or significant influence over another entity
- the type of joint arrangement (i.e. joint operation or joint venture) when the arrangement has been structured through a separate vehicle.

Interests in subsidiaries

An entity shall disclose information that enables users of its consolidated financial statements to:

- understand the composition of the group
- understand the interest that non-controlling interests have in the group's activities and cash flows
- evaluate the nature and extent of significant restrictions on its ability to access or use assets, and settle liabilities, of the group
- evaluate the nature of, and changes in, the risks associated with its interests in consolidated structured entities
- evaluate the consequences of changes in its ownership interest in a subsidiary that do not result in a loss of control
- evaluate the consequences of losing control of a subsidiary during the reporting period.

Interests in unconsolidated subsidiaries

[Note: The investment entity consolidation exemption referred to in this section was introduced by Investment Entities, issued on 31 October 2012 and effective for annual periods beginning on or after 1 January 2014.]

In accordance with IFRS 10 Consolidated Financial Statements, an investment entity is required to apply the exception to consolidation and instead account for its investment in a subsidiary at fair value through profit or loss.

Where an entity is an investment entity, IFRS 12 requires additional disclosure, including:

- *the fact the entity is an investment entity*
- *information about significant judgements and assumptions it has made in determining that it is an investment entity, and specifically where the entity does not have one or more of the 'typical characteristics' of an investment entity*

- *details of subsidiaries that have not been consolidated (name, place of business, ownership interests held)*
- *details of the relationship and certain transactions between the investment entity and the subsidiary (e.g. restrictions on transfer of funds, commitments, support arrangements, contractual arrangements)*
- *information where an entity becomes, or ceases to be, an investment entity*

An entity making these disclosures are not required to provide various other disclosures required by IFRS 12

Interests in joint arrangements and associates

An entity shall disclose information that enables users of its financial statements to evaluate:

- the nature, extent and financial effects of its interests in joint arrangements and associates, including the nature and effects of its contractual relationship with the other investors with joint control of, or significant influence over, joint arrangements and associates
- the nature of, and changes in, the risks associated with its interests in joint ventures and associates.

Interests in unconsolidated structured entities

An entity shall disclose information that enables users of its financial statements to:

- understand the nature and extent of its interests in unconsolidated structured entities
- evaluate the nature of, and changes in, the risks associated with its interests in unconsolidated structured entities.

8.13 IFRS 13 : Fair Value Measurement

IFRS 13:

(a) defines fair value;

(b) sets out in a single IFRS a framework for measuring fair value; and

(c) requires disclosures about fair value measurements.

The IFRS applies to IFRSs that require or permit fair value measurements or disclosures about fair value measurements (and measurements, such as fair value less costs to sell, based on fair value or disclosures about those measurements), except in specified circumstances.

The measurement and disclosure requirements of the IFRS do not apply to the following:

(a) share-based payment transactions within the scope of IFRS 2 Share-based Payment;

(b) leasing transactions within the scope of IAS 17 Leases; and

(c) measurements that have some similarities to fair value but are not fair value, such as net realisable value in IAS 2 Inventories or value in use in IAS 36 Impairment of Assets.

The disclosures required by the IFRS are not required for the following:

(a) plan assets measured at fair value in accordance with IAS 19 Employee Benefits;

(b) retirement benefit plan investments measured at fair value in accordance with IAS 26 Accounting and Reporting by Retirement Benefit Plans; and

(c) assets for which recoverable amount is fair value less costs of disposal in accordance with IAS 36.

IFRS 13 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (ie an exit price). That definition of fair value emphasises that fair value is a market-based measurement, not an entity-specific measurement.

When measuring fair value, an entity uses the assumptions that market participants would use when pricing the asset or liability under current market conditions, including assumptions about risk. As a result, an entity's intention to hold an asset or to settle or otherwise fulfil a liability is not relevant when measuring fair value.

The IFRS explains that a fair value measurement requires an entity to determine the following:

(a) the particular asset or liability being measured;

(b) for a non-financial asset, the highest and best use of the asset and whether the asset is used in combination with other assets or on a stand-alone basis;

(c) the market in which an orderly transaction would take place for the asset or liability; and

(d) the appropriate valuation technique(s) to use when measuring fair value. The valuation technique(s) used should maximise the use of relevant observable inputs and minimise unobservable inputs. Those inputs should be consistent with the inputs a market participant would use when pricing the asset or liability.

Application to liabilities and an entity's own equity instruments

A fair value measurement assumes that a financial or non-financial liability or an entity's own equity instrument (eg equity interests issued as consideration in a business combination) is transferred to a market participant at the measurement date. The transfer of a liability or an entity's own equity instrument assumes the following:

(a) A liability would remain outstanding and the market participant transferee would be required to fulfil the obligation. The liability would not be settled with the counterparty or otherwise extinguished on the measurement date.

(b) An entity's own equity instrument would remain outstanding and the market participant transferee would take on the rights and responsibilities associated with the instrument. The instrument would not be cancelled or otherwise extinguished on the measurement date.

Fair value hierarchy

To increase consistency and comparability in fair value measurements and related disclosures, the IFRS establishes a fair value hierarchy that categorises into three levels the inputs to valuation techniques used to measure fair value. The fair value hierarchy gives the highest priority to quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1 inputs) and the lowest priority to unobservable inputs (Level 3 inputs).

Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the entity can access at the measurement date. Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. Level 3 inputs are unobservable inputs for the asset or liability.

Disclosure

An entity shall disclose information that helps users of its financial statements assess both of the following:

(a) for assets and liabilities that are measured at fair value on a recurring or non-recurring basis in the statement of financial position after initial recognition, the valuation techniques and inputs used to develop those measurements.

(b) for recurring fair value measurements using significant unobservable inputs (Level 3), the effect of the measurements on profit or loss or other comprehensive income for the period.

9. Overview of International Accounting Standards

9.1 IAS 1 (Revised): Presentation of Financial Statements

This Standard prescribes the basis for presentation of general purpose financial statements to ensure comparability both with the entity's financial statements of previous periods and with the financial statements of other entities. It sets out overall requirements for the presentation of financial statements, guidelines for their structure and minimum requirements for their content.

A complete set of financial statements comprises:

(a) a statement of financial position as at the end of the period;

(b) a statement of comprehensive income for the period;

(c) a statement of changes in equity for the period;

(d) a statement of cash flows for the period;

(e) notes, comprising a summary of significant accounting policies and other explanatory information; and

(f) a statement of financial position as at the beginning of the earliest comparative period when an entity applies an accounting policy retrospectively or makes a retrospective

restatement of items in its financial statements, or when it reclassifies items in its financial statements.

An entity whose financial statements comply with IFRSs shall make an explicit and unreserved statement of such compliance in the notes. An entity shall not describe financial statements as complying with IFRSs unless they comply with all the requirements of IFRSs. The application of IFRSs, with additional disclosure when necessary, is presumed to result in financial statements that achieve a fair presentation.

When preparing financial statements, management shall make an assessment of an entity's ability to continue as a going concern. An entity shall prepare financial statements on a going concern basis unless management either intends to liquidate the entity or to cease trading, or has no realistic alternative but to do so. When management is aware, in making its assessment, of material uncertainties related to events or conditions that may cast significant doubt upon the entity's ability to continue as a going concern, the entity shall disclose those uncertainties.

An entity shall present separately each material class of similar items. An entity shall present separately items of a dissimilar nature or function unless they are immaterial.

An entity shall not offset assets and liabilities or income and expenses, unless required or permitted by an IFRS.

An entity shall present a complete set of financial statements (including comparative information) at least annually.

Except when IFRSs permit or require otherwise, an entity shall disclose comparative information in respect of the previous period for all amounts reported in the current period's financial statements. An entity shall include comparative information for narrative and descriptive information when it is relevant to an understanding of the current period's financial statements.

When the entity changes the presentation or classification of items in its financial statements, the entity shall reclassify comparative amounts unless reclassification is impracticable.

An entity shall clearly identify the financial statements and distinguish them from other information in the same published document.

IAS 1 requires an entity to present, in a statement of changes in equity, all owner changes in equity. All nonowner changes in equity (ie comprehensive income) are required to be presented in one statement of comprehensive income or in two statements (a separate income statement and a statement of comprehensive income). Components of comprehensive income are not permitted to be presented in the statement of changes in equity.

An entity shall recognise all items of income and expense in a period in profit or loss unless an IFRS requires or permits otherwise.

The notes shall:

(a) present information about the basis of preparation of the financial statements and the specific accounting policies used in accordance with paragraphs 117–124;

(b) disclose the information required by IFRSs that is not presented elsewhere in the financial statements; and

(c) provide information that is not presented elsewhere in the financial statements, but is relevant to an understanding of any of them.

An entity shall disclose, in the summary of significant accounting policies or other notes, the judgements, apart from those involving estimations (see paragraph 125), that management has made in the process of applying the entity's accounting policies and that have the most significant effect on the amounts recognised in the financial statements.

An entity shall disclose information about the assumptions it makes about the future, and other major sources of estimation uncertainty at the end of the reporting period, that have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

An entity shall disclose information that enables users of its financial statements to evaluate the entity's objectives, policies and processes for managing capital. An entity shall also provide additional disclosures on puttable financial instruments classified as equity instruments.

9.2 IAS 2 (Revised): Inventories

The objective of this Standard is to prescribe the accounting treatment for inventories. A primary issue in accounting for inventories is the amount of cost to be recognised as an asset and carried forward until the related revenues are recognised. This Standard provides guidance on the determination of cost and its subsequent recognition as an expense, including any write-down to net realisable value. It also provides guidance on the cost formulas that are used to assign costs to inventories.

Inventories shall be measured at the lower of cost and net realisable value.

Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

The cost of inventories shall comprise all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

The cost of inventories shall be assigned by using the first-in, first-out (FIFO) or weighted average cost formula. An entity shall use the same cost formula for all inventories having a similar nature and use to the entity. For inventories with a different nature or use, different cost formulas may be justified. However, the

cost of inventories of items that are not ordinarily interchangeable and goods or services produced and segregated for specific projects shall be assigned by using specific identification of their individual costs.

When inventories are sold, the carrying amount of those inventories shall be recognised as an expense in the period in which the related revenue is recognised. The amount of any write-down of inventories to net realisable value and all losses of inventories shall be recognised as an expense in the period the write-down or loss occurs. The amount of any reversal of any write-down of

inventories, arising from an increase in net realisable value, shall be recognised as a reduction in the amount of inventories recognised as an expense in the period in which the reversal occurs.

9.3 IAS 7: Statement of Cash Flows

The objective of this Standard is to require the provision of information about the historical changes in cash and cash equivalents of an entity by means of a statement of cash flows which classifies cash flows during the period from operating, investing and financing activities.

Cash flows are inflows and outflows of cash and cash equivalents. *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 which are subject to an insignificant risk of changes in value.

Information about the cash flows of an entity is useful in providing users of financial statements with a basis to assess the ability of the entity to generate cash and cash equivalents and the needs of the entity to utilise those cash flows. The economic decisions that are taken by users require an evaluation of the ability of an entity to generate cash and cash equivalents and the timing and certainty of their generation.

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

Operating activities

Operating activities are the principal revenue-producing activities of the entity and other activities that are not investing or financing activities. Cash flows from operating activities are primarily derived from the principal revenue-producing activities of the entity. Therefore, they generally result from the transactions and other events that enter into the determination of profit or loss.

The amount of cash flows arising from operating activities is a key indicator of the extent to which the operations of the entity have generated sufficient cash flows to repay loans, maintain the operating capability of the entity, pay dividends and make new investments without recourse to external sources of financing.

An entity shall report cash flows from operating activities using either:

(a) the direct method, whereby major classes of gross cash receipts and gross cash payments are disclosed; or

(b) the indirect method, whereby profit or loss is adjusted for the effects of transactions of a non-cash nature, any deferrals or accruals of past or future operating cash receipts or payments, and items of income or expense associated with investing or financing cash flows.

Investing activities

Investing activities are the acquisition and disposal of long-term assets and other investments not included in cash equivalents. The separate disclosure of cash flows arising from investing activities is important because the cash flows represent the extent to which expenditures have been made for resources intended to generate future income and cash flows.

The aggregate cash flows arising from obtaining and losing control of subsidiaries or other businesses shall be presented separately and classified as investing activities.

Financing activities

Financing activities are activities that result in changes in the size and composition of the contributed equity and borrowings of the entity. The separate disclosure of cash flows arising from financing activities is important because it is useful in predicting claims on future cash flows by providers of capital to the entity.

An entity shall report separately major classes of gross cash receipts and gross cash payments arising from investing and financing activities.

Non-cash transactions

Investing and financing transactions that do not require the use of cash or cash equivalents shall be excluded from a statement of cash flows. Such transactions shall be disclosed elsewhere in the financial statements in a way that provides all the relevant information about these investing and financing activities.

Foreign currency cash flows

Cash flows arising from transactions in a foreign currency shall be recorded in an entity's functional currency by applying to the foreign currency amount the exchange rate between the functional currency and the foreign currency at the date of the cash flow.

The cash flows of a foreign subsidiary shall be translated at the exchange rates between the functional currency and the foreign currency at the dates of the cash flows.

Unrealised gains and losses arising from changes in foreign currency exchange rates are not cash flows.

However, the effect of exchange rate changes on cash and cash equivalents held or due in a foreign currency is reported in the statement of cash flows in order to reconcile cash and cash equivalents at the beginning and the end of the period.

Cash and cash equivalents

An entity shall disclose the components of cash and cash equivalents and shall present a reconciliation of the amounts in its statement of cash flows with the equivalent items reported in the statement of financial position.

An entity shall disclose, together with a commentary by management, the amount of significant cash and cash equivalent balances held by the entity that are not available for use by the group.

9.4 IAS 8 (Revised): Accounting Policies, Changes in Accounting Estimates and Errors

The objective of this Standard is to prescribe the criteria for selecting and changing accounting policies, together with the accounting treatment and disclosure of changes in accounting policies, changes in accounting estimates and corrections of errors. The Standard is intended to enhance the relevance and reliability of an entity's financial statements, and the comparability of those financial statements over time and with the financial statements of other entities.

Accounting policies

Accounting policies are the specific principles, bases, conventions, rules and practices applied by an entity in preparing and presenting financial statements. When an IFRS specifically applies to a transaction, other event or condition, the accounting policy or policies applied to that item shall be determined by applying the IFRS and considering any relevant Implementation Guidance issued by the IASB for the IFRS.

In the absence of a Standard or an Interpretation that specifically applies to a transaction, other event or condition, management shall use its judgement in developing and applying an accounting policy that results in information that is relevant and reliable. In making the judgement management shall refer to, and consider the applicability of, the following sources in descending order:

(a) the requirements and guidance in IFRSs dealing with similar and related issues; and

(b) the definitions, recognition criteria and measurement concepts for assets, liabilities, income and expenses in the *Conceptual Framework*.

An entity shall select and apply its accounting policies consistently for similar transactions, other events and conditions, unless an IFRS specifically requires or permits categorisation of items for which different policies may be appropriate. If an IFRS requires or permits such categorisation, an appropriate accounting policy shall be selected and applied consistently to each category.

An entity shall change an accounting policy only if the change:

(a) is required by an IFRS; or

(b) results in the financial statements providing reliable and more relevant information about the effects of transactions, other events or conditions on the entity's financial position, financial performance or cash flows.

An entity shall account for a change in accounting policy resulting from the initial application of an IFRS in accordance with the specific transitional provisions, if any, in that IFRS. When an entity changes an accounting policy upon initial application of an IFRS that does not include specific transitional provisions applying to that change, or changes an accounting policy voluntarily, it shall apply the change retrospectively.

However, a change in accounting policy shall be applied retrospectively except to the extent that it is impracticable to determine either the period-specific effects or the cumulative effect of the change.

Change in accounting estimate

The use of reasonable estimates is an essential part of the preparation of financial statements and does not undermine their reliability. A *change in accounting estimate* is an adjustment of the carrying amount of an asset or a liability, or the amount of the periodic consumption of an asset, that results from the assessment of the present status of, and expected future benefits and obligations associated with, assets and liabilities. Changes in accounting estimates result

from new information or new developments and, accordingly, are not corrections of errors. The effect of a change in an accounting estimate, shall be recognised prospectively by including it in profit or loss in:

(a) the period of the change, if the change affects that period only; or

(b) the period of the change and future periods, if the change affects both.

Prior period errors

Prior period errors are omissions from, and misstatements in, the entity's financial statements for one or more prior periods arising from a failure to use, or misuse of, reliable information that:

(a) was available when financial statements for those periods were authorised for issue; and

(b) could reasonably be expected to have been obtained and taken into account in the preparation and presentation of those financial statements.

Such errors include the effects of mathematical mistakes, mistakes in applying accounting policies, oversights or misinterpretations of facts, and fraud.

Except to the extent that it is impracticable to determine either the period-specific effects or the cumulative effect of the error, an entity shall correct material prior period errors retrospectively in the first set of financial statements authorised for issue after their discovery by:

(a) restating the comparative amounts for the prior period(s) presented in which the error occurred; or

(b) if the error occurred before the earliest prior period presented, restating the opening balances of assets, liabilities and equity for the earliest prior period presented.

Omissions or misstatements of items are material if they could, individually or collectively, influence the economic decisions of users taken on the basis of the financial statements. Materiality depends on the size and nature of the omission or misstatement judged in the surrounding circumstances. The size or nature of the item, or a combination of both, could be the determining factor.

9.5 IAS 10 (Revised): Events after the Repporting Period

The objective of this Standard is to prescribe:

(a) when an entity should adjust its financial statements for events after the reporting period; and

(b) the disclosures that an entity should give about the date when the financial statements were authorised for issue and about events after the reporting period.

The Standard also requires that an entity should not prepare its financial statements on a going concern basis if events after the reporting period indicate that the going concern assumption is not appropriate.

Events after the reporting period are those events, favourable and unfavourable, that occur between the end of the reporting period and the date when the financial statements are authorised for issue. Two types of events can be identified:

(a) those that provide evidence of conditions that existed at the end of the reporting period (*adjusting events after the reporting period*); and

(b) those that are indicative of conditions that arose after the reporting period (*non-adjusting events after the reporting period*).

An entity shall adjust the amounts recognised in its financial statements to reflect adjusting events after the reporting period.

An entity shall not adjust the amounts recognised in its financial statements to reflect non-adjusting events after the reporting period. If non-adjusting events after the reporting period are material, non-disclosure could influence the economic decisions of users taken on the basis of the financial statements. Accordingly, an entity shall disclose the following for each material category of non-adjusting event after the reporting period:

(a) the nature of the event; and

(b) an estimate of its financial effect, or a statement that such an estimate cannot be made.

If an entity receives information after the reporting period about conditions that existed at the end of the reporting period, it shall update disclosures that relate to those conditions, in the light of the new information.

9.6 IAS 11: Construction Contracts

The objective of this Standard is to prescribe the accounting treatment of revenue and costs associated with construction contracts. Because of the nature of the activity undertaken in construction contracts, the date at which the contract activity is entered into and the date when the activity is completed usually fall into different accounting periods. Therefore, the primary issue in accounting for construction contracts is the allocation of contract revenue and contract costs to the accounting periods in which construction work is performed.

This Standard shall be applied in accounting for construction contracts in the financial statements of contractors.

A *construction contract* is a contract specifically negotiated for the construction of an asset or a combination of assets that are closely interrelated or interdependent in terms of their design, technology and function or their ultimate purpose or use.

The requirements of this Standard are usually applied separately to each construction contract. However, in certain circumstances, it is necessary to apply the Standard to the separately identifiable components of a single contract or to a group of contracts together in order to reflect the substance of a contract or a group of contracts.

Contract revenue shall comprise:

(a) the initial amount of revenue agreed in the contract; and

(b) variations in contract work, claims and incentive payments:

(i) to the extent that it is probable that they will result in revenue; and

(ii) they are capable of being reliably measured

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

Contract costs shall comprise:

(a) costs that relate directly to the specific contract;

(b) costs that are attributable to contract activity in general and can be allocated to the contract; and

(c) such other costs as are specifically chargeable to the customer under the terms of the contract.

When the outcome of a construction contract can be estimated reliably, contract revenue and contract costs associated with the construction contract shall be recognised as revenue and expenses respectively by reference to the stage of completion of the contract activity at the end of the reporting period.

When the outcome of a construction contract cannot be estimated reliably:

(a) revenue shall be recognised only to the extent of contract costs incurred that it is probable will be recoverable; and

(b) contract costs shall be recognised as an expense in the period in which they are incurred.

When it is probable that total contract costs will exceed total contract revenue, the expected loss shall be recognised as an expense immediately.

9.7 IAS 12: Income Taxes

The objective of this Standard is to prescribe the accounting treatment for income taxes. For the purposes of this Standard, income taxes include all domestic and foreign taxes which are based on taxable profits. Income taxes also include taxes, such as withholding taxes, which are payable by a subsidiary, associate or joint venture on distributions to the reporting entity.

The principal issue in accounting for income taxes is how to account for the current and future tax consequences of:

(a) the future recovery (settlement) of the carrying amount of assets (liabilities) that are recognised in an entity's statement of financial position; and

(b) transactions and other events of the current period that are recognised in an entity's financial statements.

Recognition

Current tax for current and prior periods shall, to the extent unpaid, be recognised as a liability. If the amount already paid in respect of current and prior periods exceeds the amount

due for those periods, the excess shall be recognised as an asset. Current tax liabilities (assets) for the current and prior periods shall be measured at the amount expected to be paid to (recovered from) the taxation authorities, using the tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period.

It is inherent in the recognition of an asset or liability that the reporting entity expects to recover or settle the carrying amount of that asset or liability. If it is probable that recovery or settlement of that carrying amount will make future tax payments larger (smaller) than they would be if such recovery or settlement were to have no tax consequences, this Standard requires an entity to recognise a deferred tax liability (deferred tax asset), with certain limited exceptions.

A deferred tax asset shall be recognised for the carryforward of unused tax losses and unused tax credits to the extent that it is probable that future taxable profit will be available against which the unused tax losses and unused tax credits can be utilised.

Measurement

Deferred tax assets and liabilities shall be measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period.

The measurement of deferred tax liabilities and deferred tax assets shall reflect the tax consequences that would follow from the manner in which the entity expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets and liabilities shall not be discounted.

The carrying amount of a deferred tax asset shall be reviewed at the end of each reporting period. An entity shall reduce the carrying amount of a deferred tax asset to the extent that it is no longer probable that sufficient taxable profit will be available to allow the benefit of part or all of that deferred tax asset to be utilised. Any such reduction shall be reversed to the extent that it becomes probable that sufficient taxable profit will be available.

Allocation

This Standard requires an entity to account for the tax consequences of transactions and other events in the same way that it accounts for the transactions and other events themselves. Thus, for transactions and other events recognised in profit or loss, any related tax effects are also recognised in profit or loss. For transactions and other events recognised outside profit or loss (either in other comprehensive income or directly in equity), any related tax effects are also recognised outside profit or loss (either in other comprehensive income or directly in equity, respectively). Similarly, the recognition of deferred tax assets and liabilities in a business combination affects the amount of goodwill arising in that business combination or the amount of the bargain purchase gain recognised.

9.8 IAS 16 (Revised): Property, Plant and Equipment

The objective of this Standard is to prescribe the accounting treatment for property, plant and equipment so that users of the financial statements can discern information about an entity's investment in its property, plant and equipment and the changes in such investment. The principal issues in accounting for property, plant and equipment are the recognition of the assets, the determination of their carrying amounts and the depreciation charges and impairment losses to be recognised in relation to them.

Property, plant and equipment are tangible items that:

(a) are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes; and

(b) are expected to be used during more than one period.

The cost of an item of property, plant and equipment shall be recognised as an asset if, and only if:

(a) it is probable that future economic benefits associated with the item will flow to the entity; and

(b) the cost of the item can be measured reliably.

Measurement at recognition: An item of property, plant and equipment that qualifies for recognition as an asset shall be measured at its cost. The cost of an item of property, plant and equipment is the cash price equivalent at the recognition date. If payment is deferred beyond normal credit terms, the difference between the cash price equivalent and the total payment is recognised as interest over the period of credit unless such interest is capitalised in accordance with IAS 23.

The cost of an item of property, plant and equipment comprises:

(a) its purchase price, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates.

(b) any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management.

(c) the initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located, the obligation for which an entity incurs either when the item is acquired or as a consequence of having used the item during a particular period for purposes other than to produce inventories during that period.

Measurement after recognition: An entity shall choose either the cost model or the revaluation model as its accounting policy and shall apply that policy to an entire class of property, plant and equipment.

Cost model: After recognition as an asset, an item of property, plant and equipment shall be carried at its cost less any accumulated depreciation and any accumulated impairment losses.

Revaluation model: After recognition as an asset, an item of property, plant and equipment whose fair value can be measured reliably shall be carried at a revalued amount, being its fair value at the date of the revaluation less any subsequent accumulated depreciation and subsequent accumulated impairment losses. Revaluations shall be made with sufficient regularity to ensure

that the carrying amount does not differ materially from that which would be determined using fair value at the end of the reporting period.

If an asset's carrying amount is increased as a result of a revaluation, the increase shall be recognised in other comprehensive income and accumulated in equity under the heading of revaluation surplus. However, the increase shall be recognised in profit or loss to the extent that it reverses a revaluation decrease of the same asset previously recognised in profit or loss. If an asset's carrying amount is decreased as a result of a revaluation, the decrease shall be recognised in profit or loss. However, the decrease shall be recognised in other comprehensive income to the extent of any credit balance existing in the revaluation surplus in respect of that asset.

Depreciation is the systematic allocation of the depreciable amount of an asset over its useful life. *Depreciable amount* is the cost of an asset, or other amount substituted for cost, less its residual value. Each part of an item of property, plant and equipment with a cost that is significant in relation to the total cost of the item shall be depreciated separately. The depreciation charge for each period shall be recognised in profit or loss unless it is included in the carrying amount of another asset. The depreciation method used shall reflect the pattern in which the asset's future economic benefits are expected to be consumed by the entity.

The *residual value* of an asset is the estimated amount that an entity would currently obtain from disposal of the asset, after deducting the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life.

To determine whether an item of property, plant and equipment is impaired, an entity applies IAS 36 *Impairment of Assets*.

The carrying amount of an item of property, plant and equipment shall be derecognised:

(a) on disposal; or

(b) when no future economic benefits are expected from its use or disposal.

9.9 IAS 17: Leases

The objective of this Standard is to prescribe, for lessees and lessors, the appropriate accounting policies and disclosure to apply in relation to leases.

The classification of leases adopted in this Standard is based on the extent to which risks and rewards incidental to ownership of a leased asset lie with the lessor or the lessee.

A lease is classified as a finance lease if it transfers substantially all the risks and rewards incidental to ownership. A lease is classified as an operating lease if it does not transfer substantially all the risks and rewards incidental to ownership.

Leases in the financial statements of lessees

Operating Leases

Lease payments under an operating lease shall be recognised as an expense on a straight-line basis over the lease term unless another systematic basis is more representative of the time pattern of the user's benefit.

Finance Leases

At the commencement of the lease term, lessees shall recognise finance leases as assets and liabilities in their statements of financial position at amounts equal to the fair value of the leased property or, if lower, the present value of the minimum lease payments, each determined at the inception of the lease. The discount rate to be used in calculating the present value of the minimum lease payments is the interest rate implicit in the lease, if this is practicable to determine; if not, the lessee's incremental borrowing rate shall be used. Any initial direct costs of the lessee are added to the amount recognised as an asset.

Minimum lease payments shall be apportioned between the finance charge and the reduction of the outstanding liability. The finance charge shall be allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability. Contingent rents shall be charged as expenses in the periods in which they are incurred.

A finance lease gives rise to depreciation expense for depreciable assets as well as finance expense for each accounting period. The depreciation policy for depreciable leased assets shall be consistent with that for depreciable assets that are owned, and the depreciation recognised shall be calculated in accordance with IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets*. If there is no reasonable certainty that the lessee will obtain ownership by the end of the lease term, the asset shall be fully depreciated over the shorter of the lease term and its useful life.

Leases in the financial statements of lessors

Operating Leases

Lessors shall present assets subject to operating leases in their statements of financial position according to the nature of the asset. The depreciation policy for depreciable leased assets shall be consistent with the lessor's normal depreciation policy for similar assets, and depreciation shall be calculated in accordance with IAS 16 and IAS 38. Lease income from operating leases shall be recognised in income on a straight-line basis over the lease term, unless another systematic basis is more representative of the time pattern in which use benefit derived from the leased asset is diminished.

Finance Leases

Lessors shall recognise assets held under a finance lease in their statements of financial position and present them as a receivable at an amount equal to the net investment in the lease. The recognition of finance income shall be based on a pattern reflecting a constant periodic rate of return on the lessor's net investment in the finance lease.

Manufacturer or dealer lessors shall recognise selling profit or loss in the period, in accordance with the policy followed by the entity for outright sales. If artificially low rates of interest are quoted, selling profit shall be restricted to that which would apply if a market rate of interest were charged. Costs incurred by manufacturer or dealer lessors in connection with negotiating and arranging a lease shall be recognised as an expense when the selling profit is recognised.

Sale and leaseback transactions

A sale and leaseback transaction involves the sale of an asset and the leasing back of the same asset. The lease payment and the sale price are usually interdependent because they are negotiated as a package.

The accounting treatment of a sale and leaseback transaction depends upon the type of lease involved.

9.10 IAS 18: Revenue

The primary issue in accounting for revenue is determining when to recognise revenue. Revenue is recognized when it is probable that future economic benefits will flow to the entity Tand these benefits can be measured reliably. This Standard identifies the circumstances in which these criteria will be met and, therefore, revenue will be recognised. It also provides practical guidance on the application of these criteria.

Revenue is the gross inflow of economic benefits during the period arising in the course of the ordinary activities of an entity when those inflows result in increases in equity, other than increases relating to contributions from equity participants.

This Standard shall be applied in accounting for revenue arising from the following transactions and events:

(a) the sale of goods;

(b) the rendering of services; and

(c) the use by others of entity assets yielding interest, royalties and dividends.

The recognition criteria in this Standard are usually applied separately to each transaction. However, in certain circumstances, it is necessary to apply the recognition criteria to the separately identifiable components of a single transaction in order to reflect the substance of the transaction. For example, when the selling price of a product includes an identifiable amount for subsequent servicing, that amount is deferred and recognised as revenue over the period during which the service is performed. Conversely, the recognition criteria are applied to two or more transactions together when they are linked in such a way that the commercial effect cannot be understood without reference to the series of transactions as a whole. For example, an entity may sell goods and, at the same time, enter into a separate agreement to repurchase the goods at a later date, thus negating the substantive effect of the transaction; in such a case, the two transactions are dealt with together.

Revenue shall be measured at the fair value of the consideration received or receivable. *Fair value* is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

The amount of revenue arising on a transaction is usually determined by agreement between the entity and the buyer or user of the asset. It is measured at the fair value of the consideration received or receivable taking into account the amount of any trade discounts and volume rebates allowed by the entity.

Sale of goods

Revenue from the sale of goods shall be recognised when all the following conditions have been satisfied:

(a) the entity has transferred to the buyer the significant risks and rewards of ownership of the goods;

(b) the entity retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold;

(c) the amount of revenue can be measured reliably;

(d) it is probable that the economic benefits associated with the transaction will flow to the entity; and

(e) the costs incurred or to be incurred in respect of the transaction can be measured reliably.

Rendering of services

When the outcome of a transaction involving the rendering of services can be estimated reliably, revenue associated with the transaction shall be recognised by reference to the stage of completion of the transaction at the end of the reporting period. The outcome of a transaction can be estimated reliably when all the following conditions are satisfied:

(a) the amount of revenue can be measured reliably;

(b) it is probable that the economic benefits associated with the transaction will flow to the entity;

(c) the stage of completion of the transaction at the end of the reporting period can be measured reliably; and

(d) the costs incurred for the transaction and the costs to complete the transaction can be measured reliably.

The recognition of revenue by reference to the stage of completion of a transaction is often referred to as the percentage of completion method. Under this method, revenue is recognised in the accounting periods in which the services are rendered. The recognition of revenue on this basis provides useful information on the extent of service activity and performance during a period.

When the outcome of the transaction involving the rendering of services cannot be estimated reliably, revenue shall be recognised only to the extent of the expenses recognised that are recoverable.

Interest, royalties and dividends

Revenue shall be recognised on the following bases:

(a) interest shall be recognised using the effective interest method as set out in IAS 39, paragraphs 9 and AG5–AG8;

(b) royalties shall be recognised on an accrual basis in accordance with the substance of the relevant agreement; and

(c) dividends shall be recognised when the shareholder's right to receive payment is established.

9.11 IAS 19: Employee Benefits

Employee benefits are all forms of consideration given by an entity in exchange for service rendered by employees.

The objective of this Standard is to prescribe the accounting and disclosure for employee benefits. The Standard requires an entity to recognise:

(a) a liability when an employee has provided service in exchange for employee benefits to be paid in the future; and

(b) an expense when the entity consumes the economic benefit arising from service provided by an employee in exchange for employee benefits.

This Standard shall be applied by an employer in accounting for all employee benefits, except those to which IFRS 2 *Share-based Payment* applies.

Short-term employee benefits

Short-term employee benefits are employee benefits (other than termination benefits) that are due to be settled within twelve months after the end of the period in which the employees render the related service.

When an employee has rendered service to an entity during an accounting period, the entity shall recognise the undiscounted amount of short-term employee benefits expected to be paid in exchange for that service:

(a) as a liability (accrued expense), after deducting any amount already paid. If the amount already paid exceeds the undiscounted amount of the benefits, an entity shall recognise that excess as an asset (prepaid expense) to the extent that the prepayment will lead to, for example, a reduction in future payments or a cash refund; and

(b) as an expense, unless another Standard requires or permits the inclusion of the benefits in the cost of an asset (see, for example, IAS 2 *Inventories* and IAS 16 *Property, Plant and Equipment*).

Post-employment benefits

Post-employment benefits are employee benefits (other than termination benefits) which are payable after the completion of employment. *Post-employment benefit plans* are formal or informal arrangements under which an entity provides post-employment benefits for one or more employees. Post-employment benefit plans are classified as either defined contribution plans or defined benefit plans, depending on the economic substance of the plan as derived from its principal terms and conditions.

Post-employment benefits: defined contribution plans

Defined contribution plans are post-employment benefit plans under which an entity pays fixed contributions into a separate entity (a fund) and will have no legal or constructive obligation to pay further contributions if the fund does not hold sufficient assets to pay all employee benefits relating to employee service in the current and prior periods. Under defined contribution plans:

(a) the entity's legal or constructive obligation is limited to the amount that it agrees to contribute to the fund. Thus, the amount of the post-employment benefits received by the employee is determined by the amount of contributions paid by an entity (and perhaps also the employee) to a post-employment benefit plan or to an insurance company, together with investment returns arising from the contributions; and

(b) in consequence, actuarial risk (that benefits will be less than expected) and investment risk (that assets invested will be insufficient to meet expected benefits) fall on the employee.

When an employee has rendered service to an entity during a period, the entity shall recognise the contribution payable to a defined contribution plan in exchange for that service:

(a) as a liability (accrued expense), after deducting any contribution already paid. If the contribution already paid exceeds the contribution due for service before the end of the reporting period, an entity shall recognise that excess as an asset (prepaid expense) to the extent that the prepayment will lead to, for example, a reduction in future payments or a cash refund; and

(b) as an expense, unless another Standard requires or permits the inclusion of the contribution in the cost of an asset (see, for example, IAS 2 *Inventories* and IAS 16 *Property, Plant and Equipment*).

Post-employment benefits: defined benefit plans

Defined benefit plans are post-employment benefit plans other than defined contribution plans. Under defined benefit plans:

(a) the entity's obligation is to provide the agreed benefits to current and former employees; and

(b) actuarial risk (that benefits will cost more than expected) and investment risk fall, in substance, on the entity. If actuarial or investment experience are worse than expected, the entity's obligation may be increased.

Accounting by an entity for defined benefit plans involves the following steps:

(a) using actuarial techniques to make a reliable estimate of the amount of benefit that employees have earned in return for their service in the current and prior periods. This requires an entity to determine how much benefit is attributable to the current and prior periods (see paragraphs 67–71) and to make estimates (actuarial assumptions) about demographic variables (such as employee turnover and mortality) and financial variables

(such as future increases in salaries and medical costs) that will influence the cost of the benefit (see paragraphs 72–91);

(b) discounting that benefit using the Projected Unit Credit Method in order to determine the present value of the defined benefit obligation and the current service cost (see paragraphs 64–66);

(c) determining the fair value of any plan assets (see paragraphs 102–104);

(d) determining the total amount of actuarial gains and losses and the amount of those actuarial gains and losses to be recognised (see paragraphs 92–95);

(e) where a plan has been introduced or changed, determining the resulting past service cost (see paragraphs 96–101); and

(f) where a plan has been curtailed or settled, determining the resulting gain or loss (see paragraphs 109–115).

Where an entity has more than one defined benefit plan, the entity applies these procedures for each material plan separately.

Other long-term employee benefits

Other long-term employee benefits are employee benefits (other than post-employment benefits and termination benefits) that are not due to be settled within twelve months after the end of the period in which the employees render the related service.

The Standard requires a simpler method of accounting for other long-term employee benefits than for postemployment benefits: actuarial gains and losses and past service cost are recognised immediately.

Termination benefits

Termination benefits are employee benefits payable as a result of either:

(a) an entity's decision to terminate an employee's employment before the normal retirement date; or

(b) an employee's decision to accept voluntary redundancy in exchange for those benefits.

An entity shall recognise termination benefits as a liability and an expense when, and only when, the entity is demonstrably committed to either:

(a) terminate the employment of an employee or group of employees before the normal retirement date; or

(b) provide termination benefits as a result of an offer made in order to encourage voluntary redundancy.

Where termination benefits fall due more than 12 months after the reporting period, they shall be discounted.

In the case of an offer made to encourage voluntary redundancy, the measurement of termination benefits should be based on the number of employees expected to accept the offer.

9.12 IAS 20 : Accounting for Government Grants and Disclosure of Government Assistance

This Standard shall be applied in accounting for, and in the disclosure of, government grants and in the disclosure of other forms of government assistance.

Government grants are assistance by government in the form of transfers of resources to an entity in return for past or future compliance with certain conditions relating to the operating activities of the entity. They exclude those forms of government assistance which cannot reasonably have a value placed upon them and transactions with government which cannot be distinguished from the normal trading transactions of the entity.

Government assistance is action by government designed to provide an economic benefit specific to an entity or range of entities qualifying under certain criteria. Government assistance for the purpose of this Standard does not include benefits provided only indirectly through action affecting general trading conditions, such as the provision of infrastructure in development areas or the imposition of trading constraints on competitors.

In this Standard, government assistance does not include the provision of infrastructure by improvement to the general transport and communication network and the supply of improved facilities such as irrigation or water reticulation which is available on an ongoing indeterminate basis for the benefit of an entire local community.

A government grant may take the form of a transfer of a non-monetary asset, such as land or other resources, for the use of the entity. In these circumstances it is usual to assess the fair value of the non-monetary asset and to account for both grant and asset at that fair value.

Government grants, including non-monetary grants at fair value, shall not be recognised until there is reasonable assurance that:

(a) the entity will comply with the conditions attaching to them; and

(b) the grants will be received.

Government grants shall be recognised in profit or loss on a systematic basis over the periods in which the entity recognises as expenses the related costs for which the grants are intended to compensate.

A government grant that becomes receivable as compensation for expenses or losses already incurred or for the purpose of giving immediate financial support to the entity with no future related costs shall be recognised in profit or loss of the period in which it becomes receivable.

Grants related to assets are government grants whose primary condition is that an entity qualifying for them should purchase, construct or otherwise acquire long-term assets. Subsidiary conditions may also be attached restricting the type or location of the assets or the periods during which they are to be acquired or held.

Government grants related to assets, including non-monetary grants at fair value, shall be presented in the statement of financial position either by setting up the grant as deferred income or by deducting the grant in arriving at the carrying amount of the asset.

Grants related to income are government grants other than those related to assets. Grants related to income are sometimes presented as a credit in the statement of comprehensive income, either separately or under a general heading such as 'Other income'; alternatively, they are deducted in reporting the related expense.

A government grant that becomes repayable shall be accounted for as a change in accounting estimate (see IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*). Repayment of a grant related to income shall be applied first against any unamortised deferred credit recognised in respect of the grant. To the extent that the repayment exceeds any such deferred credit, or when no deferred credit exists, the repayment shall be recognised immediately in profit or loss. Repayment of a grant related to an asset shall be recognised by increasing the carrying amount of the asset or reducing the deferred income balance by the amount repayable.

The cumulative additional depreciation that would have been recognised in profit or loss to date in the absence of the grant shall be recognised immediately in profit or loss.

The following matters shall be disclosed:

(a) the accounting policy adopted for government grants, including the methods of presentation adopted in the financial statements;

(b) the nature and extent of government grants recognised in the financial statements and an indication of other forms of government assistance from which the entity has directly benefited; and

(c) unfulfilled conditions and other contingencies attaching to government assistance that has been recognised.

9.13 IAS 21 (Revised): The Effects of Changes in Foreign Exchange Rates

An entity may carry on foreign activities in two ways. It may have transactions in foreign currencies or it may have foreign operations. In addition, an entity may present its financial statements in a foreign currency.

The objective of this Standard is to prescribe how to include foreign currency transactions and foreign operations in the financial statements of an entity and how to translate financial statements into a presentation currency. The principal issues are which exchange rate(s) to use and how to report the effects of changes in exchange rates in the financial statements.

This Standard does not apply to hedge accounting for foreign currency items, including the hedging of a net investment in a foreign operation. IAS 39 applies to hedge accounting.

This Standard does not apply to the presentation in a statement of cash flows of the cash flows arising from transactions in a foreign currency, or to the translation of cash flows of a foreign operation (see IAS 7 *Statement of Cash Flows*).

Functional currency

Functional currency is the currency of the primary economic environment in which the entity operates.

The primary economic environment in which an entity operates is normally the one in which it primarily generates and expends cash.

An entity considers the following factors in determining its functional currency:

(a) the currency:

  (i) that mainly influences sales prices for goods and services (this will often be the currency in which sales prices for its goods and services are denominated and settled); and

  (ii) of the country whose competitive forces and regulations mainly determine the sales prices of its goods and services.

(b) the currency that mainly influences labour, material and other costs of providing goods or services (this will often be the currency in which such costs are denominated and settled).

Reporting foreign currency transactions in the functional currency

Foreign currency is a currency other than the functional currency of the entity. *Spot exchange rate* is the exchange rate for immediate delivery.

Exchange difference is the difference resulting from translating a given number of units of one currency into another currency at different exchange rates.

Net investment in a foreign operation is the amount of the reporting entity's interest in the net assets of that operation.

A foreign currency transaction shall be recorded, on initial recognition in the functional currency, by applying to the foreign currency amount the spot exchange rate between the functional currency and the foreign currency at the date of the transaction.

At the end of each reporting period:

(a) foreign currency monetary items shall be translated using the closing rate;

(b) non-monetary items that are measured in terms of historical cost in a foreign currency shall be translated using the exchange rate at the date of the transaction; and

(c) non-monetary items that are measured at fair value in a foreign currency shall be translated using the exchange rates at the date when the fair value was determined.

Exchange differences arising on the settlement of monetary items or on translating monetary items at rates different from those at which they were translated on initial recognition during the period or in previous financial statements shall be recognised in profit or loss in the period in which they arise.

However, exchange differences arising on a monetary item that forms part of a reporting entity's net investment in a foreign operation shall be recognised in profit or loss in the separate financial statements of the reporting entity or the individual financial statements of the foreign operation, as appropriate. In the financial statements that include the foreign operation and the reporting entity (eg consolidated financial statements when the foreign operation is a subsidiary), such exchange differences shall be recognised initially in other comprehensive income and reclassified from equity to profit or loss on disposal of the net investment.

Furthermore, when a gain or loss on a non-monetary item is recognised in other comprehensive income, any exchange component of that gain or loss shall be recognised in other comprehensive income. Conversely, when a gain or loss on a non-monetary item is recognised in profit or loss, any exchange component of that gain or loss shall be recognised in profit or loss.

Translation to the presentation currency/Translation of a foreign operation The Standard permits an entity to present its financial statements in any currency (or currencies). For this purpose, an entity could be a stand-alone entity, a parent preparing consolidated financial statements or a parent, an investor or a venturer preparing separate financial statements in accordance with IAS 27 *Consolidated and Separate Financial Statements*. If the presentation currency differs from the entity's functional currency, it translates its results and financial position into the presentation currency. For example, when a group contains individual entities with different functional currencies, the results and financial position of each entity are expressed in a common currency so that consolidated financial statements may be presented.

An entity is required to translate its results and financial position from its functional currency into a presentation currency (or currencies) using the method required for translating a foreign operation for inclusion in the reporting entity's financial statements.

The results and financial position of an entity whose functional currency is not the currency of a hyperinflationary economy shall be translated into a different presentation currency using the following procedures:

(a) assets and liabilities for each statement of financial position presented (ie including comparatives) shall be translated at the closing rate at the date of that statement of financial position;

(b) income and expenses for each statement of comprehensive income or separate income statement presented (ie including comparatives) shall be translated at exchange rates at the dates of the transactions; and

(c) all resulting exchange differences shall be recognised in other comprehensive income.

Any goodwill arising on the acquisition of a foreign operation and any fair value adjustments to the carrying amounts of assets and liabilities arising on the acquisition of that foreign operation shall be treated as assets and liabilities of the foreign operation. *Foreign operation* is an entity that is a subsidiary, associate, joint venture or branch of a reporting entity, the

activities of which are based or conducted in a country or currency other than those of the reporting entity.

On the disposal of a foreign operation, the cumulative amount of the exchange differences relating to that foreign operation, recognised in other comprehensive income and accumulated in the separate component of equity, shall be reclassified from equity to profit or loss (as a reclassification adjustment) when the gain or loss on disposal is recognised (see IAS 1 *Presentation of Financial Statements* (as revised in 2007)).

On the partial disposal of a subsidiary that includes a foreign operation, the entity shall re-attribute the proportionate share of the cumulative amount of the exchange differences recognised in other comprehensive income to the non-controlling interests in that foreign operation. In any other partial disposal of a foreign operation the entity shall reclassify to profit or loss only the proportionate share of the cumulative amount of the exchange differences recognised in other comprehensive income.

When there is a change in an entity's functional currency, the entity shall apply the translation procedures applicable to the new functional currency prospectively from the date of the change.

If the functional currency is the currency of a hyperinflationary economy, the entity's financial statements are restated in accordance with IAS 29 *Financial Reporting in Hyperinflationary Economies.*

The results and financial position of an entity whose functional currency is the currency of a hyperinflationary economy shall be translated into a different presentation currency using the following procedures:

(a) all amounts (ie assets, liabilities, equity items, income and expenses, including comparatives) shall be translated at the closing rate at the date of the most recent statement of financial position, except that

(b) when amounts are translated into the currency of a non-hyperinflationary economy, comparative amounts shall be those that were presented as current year amounts in the relevant prior year financial statements (ie not adjusted for subsequent changes in the price level or subsequent changes in exchange rates).

9.14 IAS 23 (Revised 1993) : Borrowing Costs

Core principle

Borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset form part of the cost of that asset. Other borrowing costs are recognised as an expense.

Borrowing costs are interest and other costs that an entity incurs in connection with the borrowing of funds.

Recognition

An entity shall capitalise borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset as part of the cost of that asset. An entity shall recognise other borrowing costs as an expense in the period in which it incurs them.

A *qualifying asset* is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale.

To the extent that an entity borrows funds specifically for the purpose of obtaining a qualifying asset, the entity shall determine the amount of borrowing costs eligible for capitalisation as the actual borrowing costs incurred on that borrowing during the period less any investment income on the temporary investment of those borrowings.

To the extent that an entity borrows funds generally and uses them for the purpose of obtaining a qualifying asset, the entity shall determine the amount of borrowing costs eligible for capitalisation by applying a capitalisation rate to the expenditures on that asset. The capitalisation rate shall be the weighted average of the borrowing costs applicable to the borrowings of the entity that are outstanding during the period, other than borrowings made specifically for the purpose of obtaining a qualifying asset. The amount of borrowing costs that an entity capitalises during a period shall not exceed the amount of borrowing costs it incurred during that period.

An entity shall begin capitalising borrowing costs as part of the cost of a qualifying asset on the commencement date. The commencement date for capitalisation is the date when the entity first meets all of the following conditions:

(a) it incurs expenditures for the asset;

(b) it incurs borrowing costs; and

(c) it undertakes activities that are necessary to prepare the asset for its intended use or sale.

An entity shall suspend capitalisation of borrowing costs during extended periods in which it suspends active development of a qualifying asset.

An entity shall cease capitalising borrowing costs when substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are complete.

Disclosure

An entity shall disclose:

(a) the amount of borrowing costs capitalised during the period; and

(b) the capitalisation rate used to determine the amount of borrowing costs eligible for capitalisation.

9.15 IAS 24 (Revised): Related Party Disclosures

The objective of this Standard is to ensure that an entity's financial statements contain the disclosures necessary to draw attention to the possibility that its financial position and profit or loss may have been affected by the existence of related parties and by transactions and outstanding balances, including commitments, with such parties.

A *related party* is a person or entity that is related to the entity that is preparing its financial statements (in this Standard referred to as the 'reporting entity').

(a) A person or a close member of that person's family is related to a reporting entity if that person:

  (i) has control or joint control over the reporting entity;

  (ii) has significant influence over the reporting entity; or

  (iii) is a member of the key management personnel of the reporting entity or of a parent of the reporting entity.

(b) An entity is related to a reporting entity if any of the following conditions applies:

  (i) The entity and the reporting entity are members of the same group (which means that each parent, subsidiary and fellow subsidiary is related to the others).

  (ii) One entity is an associate or joint venture of the other entity (or an associate or joint venture of a member of a group of which the other entity is a member).

  (iii) Both entities are joint ventures of the same third party.

  (iv) One entity is a joint venture of a third entity and the other entity is an associate of the third entity.

  (v) The entity is a post-employment benefit plan for the benefit of employees of either the reporting entity or an entity related to the reporting entity. If the reporting entity is itself such a plan, the sponsoring employers are also related to the reporting entity.

  (vi) The entity is controlled or jointly controlled by a person identified in (a).

  (vii) A person identified in (a)(i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity).

A *related party transaction* is a transfer of resources, services or obligations between a reporting entity and a related party, regardless of whether a price is charged.

Close members of the family of a person are those family members who may be expected to influence, or be influenced by, that person in their dealings with the entity and include:

(a) that person's children and spouse or domestic partner;

(b) children of that person's spouse or domestic partner; and

(c) dependants of that person or that person's spouse or domestic partner.

Relationships between a parent and its subsidiaries shall be disclosed irrespective of whether there have been transactions between them. An entity shall disclose the name of its parent and, if different, the ultimate controlling party. If neither the entity's parent nor the ultimate controlling party produces consolidated financial statements available for public use, the name of the next most senior parent that does so shall also be disclosed.

An entity shall disclose key management personnel compensation in total and for each of the following categories:

(a) short-term employee benefits;

(b) post-employment benefits;

(c) other long-term benefits;

(d) termination benefits; and

(e) share-based payment.

If an entity has had related party transactions during the periods covered by the financial statements, it shall disclose the nature of the related party relationship as well as information about those transactions and outstanding balances, including commitments, necessary for users to understand the potential effect of the relationship on the financial statements. These disclosure requirements are in addition to those in paragraph 17.

At a minimum, disclosures shall include:

(a) the amount of the transactions;

(b) the amount of outstanding balances, including commitments, and:

  (i) their terms and conditions, including whether they are secured, and the nature of the consideration to be provided in settlement; and

  (ii) details of any guarantees given or received;

(c) provisions for doubtful debts related to the amount of outstanding balances; and

(d) the expense recognised during the period in respect of bad or doubtful debts due from related parties. (c) [paragraph 18]

The disclosures required by paragraph 18 shall be made separately for each of the following categories:

(a) the parent;

(b) entities with joint control or significant influence over the entity;

(c) subsidiaries;

(d) associates;

(e) joint ventures in which the entity is a venturer;

(f) key management personnel of the entity or its parent; and

(g) other related parties.

Items of a similar nature may be disclosed in aggregate except when separate disclosure is necessary for an understanding of the effects of related party transactions on the financial statements of the entity.

A reporting entity is exempt from the disclosure requirements of paragraph 18 in relation to related party transactions and outstanding balances, including commitments, with:

(a) a government that has control, joint control or significant influence over the reporting entity; and

(b) another entity that is a related party because the same government has control, joint control or significant influence over both the reporting entity and the other entity. [paragraph 25]

If a reporting entity applies the exemption in paragraph 25, it shall disclose the following about the transactions and related outstanding balances referred to in paragraph 25:

(a) the name of the government and the nature of its relationship with the reporting entity (ie control, joint control or significant influence);

(b) the following information in sufficient detail to enable users of the entity's financial statements to understand the effect of related party transactions on its financial statements:

   (i) the nature and amount of each individually significant transaction; and

   (ii) for other transactions that are collectively, but not individually, significant, a qualitative or quantitative indication of their extent. Types of transactions include those listed in paragraph 21.

9.16 IAS 26: Accounting and Reporting by Retirement Benefit Plans

This Standard shall be applied in the financial statements of retirement benefit plans where such financial statements are prepared.

Retirement benefit plans are arrangements whereby an entity provides benefits for employees on or after termination of service (either in the form of an annual income or as a lump sum) when such benefits, or the contributions towards them, can be determined or estimated in advance of retirement from the provisions of a document or from the entity's practices.

Some retirement benefit plans have sponsors other than employers; this Standard also applies to the financial statements of such plans.

Defined contribution plans

Defined contribution plans are retirement benefit plans under which amounts to be paid as retirement benefits are determined by contributions to a fund together with investment earnings thereon.

The financial statements of a defined contribution plan shall contain a statement of net assets available for benefits and a description of the funding policy.

Defined benefit plans

Defined benefit plans are retirement benefit plans under which amounts to be paid as retirement benefits are determined by reference to a formula usually based on employees' earnings and/or years of service.

The objective of reporting by a defined benefit plan is periodically to provide information about the financial resources and activities of the plan that is useful in assessing the relationships between the accumulation of resources and plan benefits over time.

The financial statements of a defined benefit plan shall contain either:

(a) a statement that shows:

  (i) the net assets available for benefits;

  (ii) the actuarial present value of promised retirement benefits, distinguishing between vested benefits and non-vested benefits; and

  (iii) the resulting excess or deficit; or

(b) a statement of net assets available for benefits including either:

  (i) a note disclosing the actuarial present value of promised retirement benefits, distinguishing between vested benefits and non-vested benefits; or

  (ii) a reference to this information in an accompanying actuarial report.

If an actuarial valuation has not been prepared at the date of the financial statements, the most recent valuation shall be used as a base and the date of the valuation disclosed. [Paragraph 17]

For the purposes of paragraph 17, the actuarial present value of promised retirement benefits shall be based on the benefits promised under the terms of the plan on service rendered to date using either current salary levels or projected salary levels with disclosure of the basis used. The effect of any changes in actuarial assumptions that have had a significant effect on the actuarial present value of promised retirement benefits shall also be disclosed.

The financial statements shall explain the relationship between the actuarial present value of promised retirement benefits and the net assets available for benefits, and the policy for the funding of promised benefits.

All plans

Retirement benefit plan investments shall be carried at fair value. In the case of marketable securities fair value is market value. Where plan investments are held for which an estimate of fair value is not possible disclosure shall be made of the reason why fair value is not used.

The financial statements of a retirement benefit plan, whether defined benefit or defined contribution, shall also contain the following information:

(a) a statement of changes in net assets available for benefits;

(b) a summary of significant accounting policies; and

(c) a description of the plan and the effect of any changes in the plan during the period.

9.17 IAS 27 (Revised): Consolidated and Separate Financial Statements

The objective of IAS 27 is to enhance the relevance, reliability and comparability of the information that a parent entity provides in its separate financial statements and in its consolidated financial statements for a group of entities under its control. The Standard specifies:

(a) the circumstances in which an entity must consolidate the financial statements of another entity (being a subsidiary);

(b) the accounting for changes in the level of ownership interest in a subsidiary;

(c) the accounting for the loss of control of a subsidiary; and

(d) the information that an entity must disclose to enable users of the financial statements to evaluate the nature of the relationship between the entity and its subsidiaries.

Consolidated financial statements are the financial statements of a group presented as those of a single economic entity. A *group* is a parent and all its subsidiaries. A *subsidiary* is an entity, including an unincorporated entity such as a partnership, that is controlled by another entity (known as the parent). *Control* is the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

Presentation of consolidated financial statements

A parent must consolidate its investments in subsidiaries. There is a limited exception available to some nonpublic entities. However, that exception does not relieve venture capital organisations, mutual funds, unit trusts and similar entities from consolidating their subsidiaries.

Consolidation procedures

A group must use uniform accounting policies for reporting like transactions and other events in similar circumstances. The consequences of transactions, and balances, between entities within the group must be eliminated.

In preparing consolidated financial statements, an entity combines the financial statements of the parent and its subsidiaries line by line by adding together like items of assets, liabilities, equity, income and expenses.

In order that the consolidated financial statements present financial information about the group as that of a single economic entity, the following steps are then taken:

(a) the carrying amount of the parent's investment in each subsidiary and the parent's portion of equity of each subsidiary are eliminated (see IFRS 3, which describes the treatment of any resultant goodwill);

(b) non-controlling interests in the profit or loss of consolidated subsidiaries for the reporting period are identified; and

(c) non-controlling interests in the net assets of consolidated subsidiaries are identified separately from the parent's ownership interests in them. Non-controlling interests in the net assets consist of:

  (i) the amount of those non-controlling interests at the date of the original combination calculated in accordance with IFRS 3; and

  (ii) the non-controlling interests' share of changes in equity since the date of the combination.

Non-controlling interests

Non-controlling interests must be presented in the consolidated statement of financial position within equity, separately from the equity of the owners of the parent. Total comprehensive income must be attributed to the owners of the parent and to the non-controlling interests even if this results in the non-controlling interests having a deficit balance.

Changes in the ownership interests

Changes in a parent's ownership interest in a subsidiary that do not result in the loss of control are accounted for within equity.

When an entity loses control of a subsidiary it derecognises the assets and liabilities and related equity components of the former subsidiary. Any gain or loss is recognised in profit or loss. Any investment retained in the former subsidiary is measured at its fair value at the date when control is lost.

Separate financial statements

When an entity elects, or is required by local regulations, to present separate financial statements, investments in subsidiaries, jointly controlled entities and associates must be accounted for at cost or in accordance with IFRS 9 *Financial Instruments*.

Disclosure

An entity must disclose information about the nature of the relationship between the parent entity and its subsidiaries.

9.18 IAS 28 (Revised): Investments in Associates

This Standard shall be applied in accounting for investments in associates. However, it does not apply to investments in associates held by:

(a) venture capital organisations, or

(b) mutual funds, unit trusts and similar entities including investment-linked insurance funds that are measured at fair value through profit or loss and accounted for in accordance with IFRS 9 *Financial Instruments*. Such investments shall be measured at fair value in accordance with IFRS 9, with changes in fair value recognised in profit or loss in the period of the change.

An *associate* is an entity, including an unincorporated entity such as a partnership, over which the investor has significant influence and that is neither a subsidiary nor an interest in a joint venture. *Significant influence* is the power to participate in the financial and operating policy decisions of the investee but is not control or joint control over those policies.

If an investor holds, directly or indirectly (eg through subsidiaries), 20 per cent or more of the voting power of the investee, it is presumed that the investor has significant influence, unless it can be clearly demonstrated that this is not the case. Conversely, if the investor holds, directly or indirectly (eg through subsidiaries), less than 20 per cent of the voting power of the investee, it is presumed that the investor does not have significant influence, unless such influence can be clearly demonstrated. A substantial or majority ownership by another investor does not necessarily preclude an investor from having significant influence.

Under the equity method, the investment in an associate is initially recognised at cost and the carrying amount is increased or decreased to recognise the investor's share of the profit or loss of the investee after the date of acquisition. The investor's share of the profit or loss of the investee is recognised in the investor's profit or loss. Distributions received from an investee reduce the carrying amount of the investment. Adjustments to the carrying amount may also be necessary, for changes in the investor's proportionate interest in the investee, arising from changes in the investee's other comprehensive income. Such changes include those arising from the revaluation of property, plant and equipment and from foreign exchange translation differences. The investor's share of those changes is recognised in other comprehensive income of the investor (see IAS 1 *Presentation of Financial Statements* (as revised in 2007)).

The investor's financial statements shall be prepared using uniform accounting policies for like transactions and events in similar circumstances.

After application of the equity method, including recognising the associate's losses, the investor applies the requirements of IAS 39 to determine whether it is necessary to recognise any additional impairment loss with respect to the investor's net investment in the associate.

9.19 IAS 29: Financial Reporting in Hyperinflationary Economies

This Standard shall be applied to the financial statements, including the consolidated financial statements, of any entity whose functional currency is the currency of a hyperinflationary economy.

This Standard does not establish an absolute rate at which hyperinflation is deemed to arise. It is a matter of judgement when restatement of financial statements in accordance with this Standard becomes necessary.

Hyperinflation is indicated by characteristics of the economic environment of a country which include, but are not limited to, the following:

(a) 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 immediately invested to maintain purchasing power;

(b) 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 that currency;

(c) 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;

(d) interest rates, wages and prices are linked to a price index; and

(e) the cumulative inflation rate over three years is approaching, or exceeds, 100%.

The financial statements of an entity whose functional currency is the currency of a hyperinflationary economy shall be stated in terms of the measuring unit current at the end of the reporting period. The corresponding figures for the previous period required by IAS 1 *Presentation of Financial Statements* and any information in respect of earlier periods shall also be stated in terms of the measuring unit current at the end of the reporting period. For the purpose of presenting comparative amounts in a different presentation currency, paragraphs 42(b) and 43 of IAS 21 *The Effects of Changes in Foreign Exchange Rates* (as revised in 2003) apply.

The restatement of financial statements in accordance with this Standard requires the application of certain procedures as well as judgement. The consistent application of these procedures and judgements from period to period is more important than the precise accuracy of the resulting amounts included in the restated financial statements.

The restatement of financial statements in accordance with this Standard requires the use of a general price index that reflects changes in general purchasing power. It is preferable that all entities that report in the currency of the same economy use the same index.

When an economy ceases to be hyperinflationary and an entity discontinues the preparation and presentation of financial statements prepared in accordance with this Standard, it shall treat the amounts expressed in the measuring unit current at the end of the previous reporting period as the basis for the carrying amounts in its subsequent financial statements.

9.20 IAS 31 (Revised): Interest in Joint Ventures

This Standard shall be applied in accounting for interests in joint ventures and the reporting of joint venture assets, liabilities, income and expenses in the financial statements of venturers and investors, regardless of the structures or forms under which the joint venture activities take place. However, it does not apply to venturers' interests in jointly controlled entities held by:

(a) venture capital organisations, or

(b) mutual funds, unit trusts and similar entities including investment-linked insurance funds that are measured at fair value through profit or loss in accordance with IFRS 9 *Financial Instruments*.

A *joint venture* is a contractual arrangement whereby two or more parties undertake an economic activity that is subject to joint control. *Joint control* is the contractually agreed sharing of control over an economic activity, and exists only when the strategic financial and

operating decisions relating to the activity require the unanimous consent of the parties sharing control (the venturers). *Control* is the power to govern the financial and operating policies of an economic activity so as to obtain benefits from it.

A *venturer* is a party to a joint venture and has joint control over that joint venture.

Joint ventures take many different forms and structures. This Standard identifies three broad types—jointly controlled operations, jointly controlled assets and jointly controlled entities—that are commonly described as, and meet the definition of, joint ventures.

Jointly controlled operations

The operation of some joint ventures involves the use of the assets and other resources of the venturers rather than the establishment of a corporation, partnership or other entity, or a financial structure that is separate from the venturers themselves. Each venturer uses its own property, plant and equipment and carries its own inventories. It also incurs its own expenses and liabilities and raises its own finance, which represent its own obligations.

In respect of its interests in jointly controlled operations, a venturer shall recognise in its financial statements:

(a) the assets that it controls and the liabilities that it incurs; and

(b) the expenses that it incurs and its share of the income that it earns from the sale of goods or services by the joint venture.

Jointly controlled assets

Some joint ventures involve the joint control, and often the joint ownership, by the venturers of one or more assets contributed to, or acquired for the purpose of, the joint venture and dedicated to the purposes of the joint venture. The assets are used to obtain benefits for the venturers. Each venturer may take a share of the output from the assets and each bears an agreed share of the expenses incurred.

In respect of its interest in jointly controlled assets, a venturer shall recognise in its financial statements:

(a) its share of the jointly controlled assets, classified according to the nature of the assets;

(b) any liabilities that it has incurred;

(c) its share of any liabilities incurred jointly with the other venturers in relation to the joint venture;

(d) any income from the sale or use of its share of the output of the joint venture, together with its share of any expenses incurred by the joint venture; and

(e) any expenses that it has incurred in respect of its interest in the joint venture.

Jointly controlled entities

A jointly controlled entity is a joint venture that involves the establishment of a corporation, partnership or other entity in which each venturer has an interest. The entity operates in the

same way as other entities, except that a contractual arrangement between the venturers establishes joint control over the economic activity of the entity.

A venturer shall recognise its interest in a jointly controlled entity using proportionate consolidation or the equity method.

Proportionate consolidation is a method of accounting whereby a venturer's share of each of the assets, liabilities, income and expenses of a jointly controlled entity is combined line by line with similar items in the venturer's financial statements or reported as separate line items in the venturer's financial statements.

The *equity method* is a method of accounting whereby an interest in a jointly controlled entity is initially recorded at cost and adjusted thereafter for the post-acquisition change in the venturer's share of net assets of the jointly controlled entity. The profit or loss of the venturer includes the venturer's share of the profit or loss of the jointly controlled entity.

Transactions between a venturer and a joint venture

When a venturer contributes or sells assets to a joint venture, recognition of any portion of a gain or loss from the transaction shall reflect the substance of the transaction. While the assets are retained by the joint venture, and provided the venturer has transferred the significant risks and rewards of ownership, the venturer shall recognise only that portion of the gain or loss that is attributable to the interests of the other venturers.

The venturer shall recognise the full amount of any loss when the contribution or sale provides evidence of a reduction in the net realisable value of current assets or an impairment loss.

When a venturer purchases assets from a joint venture, the venturer shall not recognise its share of the profits of the joint venture from the transaction until it resells the assets to an independent party. A venturer shall recognise its share of the losses resulting from these transactions in the same way as profits except that losses shall be recognised immediately when they represent a reduction in the net realisable value of current assets or an impairment loss.

9.21 IAS 32 (Revised): Financial Instruments: Presentation

The objective of this Standard is to establish principles for presenting financial instruments as liabilities or equity and for offsetting financial assets and financial liabilities. It applies to the classification of financial instruments, from the perspective of the issuer, into financial assets, financial liabilities and equity instruments; the classification of related interest, dividends, losses and gains; and the circumstances in which financial assets and financial liabilities should be offset.

The principles in this Standard complement the principles for recognising and measuring financial assets and financial liabilities in IFRS 9 *Financial Instruments*, and for disclosing information about them in IFRS 7 *Financial Instruments: Disclosures*.

The issuer of a financial instrument shall classify the instrument, or its component parts, on initial recognition as a financial liability, a financial asset or an equity instrument in accordance

with the substance of the contractual arrangement and the definitions of a financial liability, a financial asset and an equity instrument.

The issuer of a non-derivative financial instrument shall evaluate the terms of the financial instrument to determine whether it contains both a liability and an equity component. Such components shall be classified separately as financial liabilities, financial assets or equity instruments.

A *financial instrument* is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity.

A *financial asset* is any asset that is:

(a) cash;

(b) an equity instrument of another entity;

(c) a contractual right:

  (i) to receive cash or another financial asset from another entity; or

  (ii) to exchange financial assets or financial liabilities with another entity under conditions that are potentially favourable to the entity; or

(d) a contract that will or may be settled in the entity's own equity instruments and is:

  (i) a non-derivative for which the entity is or may be obliged to receive a variable number of the entity's own equity instruments; or

  (ii) a derivative that will or may be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the entity's own equity instruments. For this purpose the entity's own equity instruments do not include puttable financial instruments classified as equity instruments in accordance with paragraphs 16A and 16B, instruments that impose on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation and are classified as equity instruments in accordance with paragraphs 16C and 16D, or instruments that are contracts for the future receipt or delivery of the entity's own equity instruments.

A *financial liability* is any liability that is:

(a) a contractual obligation:

  (i) to deliver cash or another financial asset to another entity; or

  (ii) to exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavourable to the entity; or

(b) a contract that will or may be settled in the entity's own equity instruments and is:

  (i) a non-derivative for which the entity is or may be obliged to deliver a variable number of the entity's own equity instruments; or

(ii) a derivative that will or may be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the entity's own equity instruments. For this purpose the entity's own equity instruments do not include puttable financial instruments that are classified as equity instruments in accordance with paragraphs 16A and 16B, instruments that impose on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation and are classified as equity instruments in accordance with paragraphs 16C and 16D, or instruments that are contracts for the future receipt or delivery of the entity's own equity instruments.

As an exception, an instrument that meets the definition of a financial liability is classified as an equity instrument if it has all the features and meets the conditions in paragraphs 16A and 16B or paragraphs 16C and 16D.

An *equity instrument* is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities.

A financial instrument may require the entity to deliver cash or another financial asset, or otherwise to settle it in such a way that it would be a financial liability, in the event of the occurrence or non-occurrence of uncertain future events (or on the outcome of uncertain circumstances) that are beyond the control of both the issuer and the holder of the instrument, such as a change in a stock market index, consumer price index, interest rate or taxation requirements, or the issuer's future revenues, net income or debt-to-equity ratio. The issuer of such an instrument does not have the unconditional right to avoid delivering cash or another financial asset (or otherwise to settle it in such a way that it would be a financial liability). Therefore, it is a financial liability of the issuer unless:

(a) the part of the contingent settlement provision that could require settlement in cash or another financial asset (or otherwise in such a way that it would be a financial liability) is not genuine;

(b) the issuer can be required to settle the obligation in cash or another financial asset (or otherwise to settle it in such a way that it would be a financial liability) only in the event of liquidation of the issuer; or

(c) The instrument has all the features and meets the conditions in paragraphs 16A and 16B.

When a derivative financial instrument gives one party a choice over how it is settled (eg the issuer or the holder can choose settlement net in cash or by exchanging shares for cash), it is a financial asset or a financial liability unless all of the settlement alternatives would result in it being an equity instrument.

If an entity reacquires its own equity instruments, those instruments ('treasury shares') shall be deducted from equity. No gain or loss shall be recognised in profit or loss on the purchase, sale, issue or cancellation of an entity's own equity instruments. Such treasury shares may be acquired and held by the entity or by other members of the consolidated group. Consideration paid or received shall be recognised directly in equity.

Interest, dividends, losses and gains relating to a financial instrument or a component that is a financial liability shall be recognised as income or expense in profit or loss. Distributions to holders of an equity instrument shall be debited by the entity directly to equity, net of any related income tax benefit. Transaction costs of an equity transaction shall be accounted for as a deduction from equity, net of any related income tax benefit.

A financial asset and a financial liability shall be offset and the net amount presented in the statement of financial position when and only when, an entity:

(a) currently has a legally enforceable right to set off the recognised amounts; and

(b) intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

9.22 IAS 33 (Revised): Earnings per Share

The objective of this Standard is to prescribe principles for the determination and presentation of earnings per share, so as to improve performance comparisons between different entities in the same reporting period and between different reporting periods for the same entity. The focus of this Standard is on the denominator of the earnings per share calculation.

This Standard shall be applied by entities whose ordinary shares or potential ordinary shares are publicly traded and by entities that are in the process of issuing ordinary shares or potential ordinary shares in public markets. An entity that discloses earnings per share shall calculate and disclose earnings per share in accordance with this Standard.

An *ordinary share* is an equity instrument that is subordinate to all other classes of equity instruments.

A *potential ordinary share* is a financial instrument or other contract that may entitle its holder to ordinary shares.

An entity shall present in the statement of comprehensive income basic and diluted earnings per share for profit or loss from continuing operations attributable to the ordinary equity holders of the parent entity and for profit or loss attributable to the ordinary equity holders of the parent entity for the period for each class of ordinary shares that has a different right to share in profit for the period. An entity shall present basic and diluted earnings per share with equal prominence for all periods presented.

An entity that reports a discontinued operation shall disclose the basic and diluted amounts per share for the discontinued operation either in the statement of comprehensive income or in the notes.

Basic earnings per share

Basic earnings per share shall be calculated by dividing profit or loss attributable to ordinary equity holders of the parent entity (the numerator) by the weighted average number of ordinary shares outstanding (the denominator) during the period.

For the purpose of calculating basic earnings per share, the amounts attributable to ordinary equity holders of the parent entity in respect of:

(a) profit or loss from continuing operations attributable to the parent entity; and

(b) profit or loss attributable to the parent entity shall be the amounts in (a) and (b) adjusted for the after-tax amounts of preference dividends, differences arising on the settlement of preference shares, and other similar effects of preference shares classified as equity.

For the purpose of calculating basic earnings per share, the number of ordinary shares shall be the weighted average number of ordinary shares outstanding during the period. [Paragraph 19] The weighted average number of ordinary shares outstanding during the period and for all periods presented shall be adjusted for events, other than the conversion of potential ordinary shares, that have changed the number of ordinary shares outstanding without a corresponding change in resources. [Paragraph 26]

Diluted earnings per share

For the purpose of calculating diluted earnings per share, an entity shall adjust profit or loss attributable to ordinary equity holders of the parent entity, and the weighted average number of shares outstanding, for the effects of all dilutive potential ordinary shares.

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

For the purpose of calculating diluted earnings per share, the number of ordinary shares shall be the weighted average number of ordinary shares calculated in accordance with paragraphs 19 and 26, plus the weighted average number of ordinary shares that would be issued on the conversion of all the dilutive potential ordinary shares into ordinary shares.

Potential ordinary shares shall be treated as dilutive when, and only when, their conversion to ordinary shares would decrease earnings per share or increase loss per share from continuing operations.

An entity uses profit or loss from continuing operations attributable to the parent entity as the control number to establish whether potential ordinary shares are dilutive or antidilutive. In determining whether potential ordinary shares are dilutive or antidilutive, each issue or series of potential ordinary shares is considered separately rather than in aggregate.

Retrospective adjustments

If the number of ordinary or potential ordinary shares outstanding increases as a result of a capitalisation, bonus issue or share split, or decreases as a result of a reverse share split, the calculation of basic and diluted earnings per share for all periods presented shall be adjusted retrospectively.

9.23 IAS 34: Interim Financial Reporting

The objective of this Standard is to prescribe the minimum content of an interim financial report and to prescribe the principles for recognition and measurement in complete or condensed financial statements for an interim period. Timely and reliable interim financial reporting improves the ability of investors, creditors, and others to understand an entity's capacity to generate earnings and cash flows and its financial condition and liquidity.

This Standard applies if an entity is required or elects to publish an interim financial report in accordance with International Financial Reporting Standards.

Interim financial report means a financial report containing either a complete set of financial statements (as described in IAS 1 *Presentation of Financial Statements* (as revised in 2007)) or a set of condensed financial statements (as described in this Standard) for an interim period. *Interim period* is a financial reporting period shorter than a full financial year.

In the interest of timeliness and cost considerations and to avoid repetition of information previously reported, an entity may be required to or may elect to provide less information at interim dates as compared with its annual financial statements. This Standard defines the minimum content of an interim financial report as including condensed financial statements and selected explanatory notes. The interim financial report is intended to provide an update on the latest complete set of annual financial statements. Accordingly, it focuses on new activities, events, and circumstances and does not duplicate information previously reported.

Nothing in this Standard is intended to prohibit or discourage an entity from publishing a complete set of financial statements (as described in IAS 1) in its interim financial report, rather than condensed financial statements and selected explanatory notes. If an entity publishes a complete set of financial statements in its interim financial report, the form and content of those statements shall conform to the requirements of IAS 1 for a complete set of financial statements.

An interim financial report shall include, at a minimum, the following components:

(a) condensed statement of financial position;

(b) condensed statement of comprehensive income, presented as either;

  (i) a condensed single statement; or

  (ii) a condensed separate income statement and a condensed statement of comprehensive income;

(c) condensed statement of changes in equity;

(d) condensed statement of cash flows; and

(e) selected explanatory notes.

If an entity publishes a set of condensed financial statements in its interim financial report, those condensed statements shall include, at a minimum, each of the headings and subtotals that were included in its most recent annual financial statements and the selected explanatory notes as required by this Standard. Additional line items or notes shall be included if their omission would make the condensed interim financial statements misleading.

In deciding how to recognise, measure, classify, or disclose an item for interim financial reporting purposes, materiality shall be assessed in relation to the interim period financial data. In making assessments of materiality, it shall be recognised that interim measurements may rely on estimates to a greater extent than measurements of annual financial data.

An entity shall apply the same accounting policies in its interim financial statements as are applied in its annual financial statements, except for accounting policy changes made after the date of the most recent annual financial statements that are to be reflected in the next annual financial statements. To achieve that objective, measurements for interim reporting purposes shall be made on a year-to-date basis.

The measurement procedures to be followed in an interim financial report shall be designed to ensure that the resulting information is reliable and that all material financial information that is relevant to an understanding of the financial position or performance of the entity is appropriately disclosed. While measurements in both annual and interim financial reports are often based on reasonable estimates, the preparation of interim financial reports generally will require a greater use of estimation methods than annual financial reports.

9.24 IAS 36: Impairment of Assets

The objective of this Standard is to prescribe the procedures that an entity applies to ensure that its assets are carried at no more than their recoverable amount. An asset is carried at more than its recoverable amount if its carrying amount exceeds the amount to be recovered through use or sale of the asset. If this is the case, the asset is described as impaired and the Standard requires the entity to recognise an impairment loss.

The Standard also specifies when an entity should reverse an impairment loss and prescribes disclosures.

Identifying an asset that may be impaired

An entity shall assess at the end of each reporting period whether there is any indication that an asset may be impaired. If any such indication exists, the entity shall estimate the recoverable amount of the asset.

Irrespective of whether there is any indication of impairment, an entity shall also:

(a) test an intangible asset with an indefinite useful life or an intangible asset not yet available for use for impairment annually by comparing its carrying amount with its recoverable amount. This impairment test may be performed at any time during an annual period, provided it is performed at the same time every year. Different intangible assets may be tested for impairment at different times. However, if such an intangible asset was initially recognised during the current annual period, that intangible asset shall be tested for impairment before the end of the current annual period.

(b) test goodwill acquired in a business combination for impairment annually in accordance with paragraphs 80-99.

If there is any indication that an asset may be impaired, recoverable amount shall be estimated for the individual asset. If it is not possible to estimate the recoverable amount of the individual asset, an entity shall determine the recoverable amount of the cash-generating unit to which the asset belongs (the asset's cash-generating unit).

A *cash-generating unit* is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets.

Measuring recoverable amount

The *recoverable amount* of an asset or a cash-generating unit is the higher of its fair value less costs to sell and its value in use.

It is not always necessary to determine both an asset's fair value less costs to sell and its value in use. If either of these amounts exceeds the asset's carrying amount, the asset is not impaired and it is not necessary to estimate the other amount.

Fair value less costs to sell is the amount obtainable from the sale of an asset or cash-generating unit in an arm's length transaction between knowledgeable, willing parties, less the costs of disposal.

Value in use is the present value of the future cash flows expected to be derived from an asset or cashgenerating unit.

The following elements shall be reflected in the calculation of an asset's value in use:

(a) an estimate of the future cash flows the entity expects to derive from the asset;

(b) expectations about possible variations in the amount or timing of those future cash flows;

(c) the time value of money, represented by the current market risk-free rate of interest;

(d) the price for bearing the uncertainty inherent in the asset; and

(e) other factors, such as illiquidity, that market participants would reflect in pricing the future cash flows the entity expects to derive from the asset.

Estimates of future cash flows shall include:

(a) projections of cash inflows from the continuing use of the asset;

(b) projections of cash outflows that are necessarily incurred to generate the cash inflows from continuing use of the asset (including cash outflows to prepare the asset for use) and can be directly attributed, or allocated on a reasonable and consistent basis, to the asset; and

(c) net cash flows, if any, to be received (or paid) for the disposal of the asset at the end of its useful life.

Future cash flows shall be estimated for the asset in its current condition. Estimates of future cash flows shall not include estimated future cash inflows or outflows that are expected to arise from:

(a) a future restructuring to which an entity is not yet committed; or

(b) improving or enhancing the asset's performance.

Estimates of future cash flows shall not include:

(a) cash inflows or outflows from financing activities; or

(b) income tax receipts or payments.

Recognising and measuring an impairment loss

If, and only if, the recoverable amount of an asset is less than its carrying amount, the carrying amount of the asset shall be reduced to its recoverable amount. That reduction is an impairment loss.

An impairment loss shall be recognised immediately in profit or loss, unless the asset is carried at revalued amount in accordance with another Standard (for example, in accordance with the revaluation model in IAS 16 *Property, Plant and Equipment*). Any impairment loss of a revalued asset shall be treated as a revaluation decrease in accordance with that other Standard.

An impairment loss shall be recognised for a cash-generating unit (the smallest group of cash-generating units to which goodwill or a corporate asset has been allocated) if, and only if, the recoverable amount of the unit (group of units) is less than the carrying amount of the unit (group of units). The impairment loss shall be allocated to reduce the carrying amount of the assets of the unit (group of units) in the following order:

(a) first, to reduce the carrying amount of any goodwill allocated to the cash-generating unit (group of units); and

(b) then, to the other assets of the unit (group of units) pro rata on the basis of the carrying amount of each asset in the unit (group of units).

However, an entity shall not reduce the carrying amount of an asset below the highest of:

(a) its fair value less costs to sell (if determinable);

(b) its value in use (if determinable); and

(c) zero.

The amount of the impairment loss that would otherwise have been allocated to the asset shall be allocated pro rata to the other assets of the unit (group of units).

Goodwill

For the purpose of impairment testing, goodwill acquired in a business combination shall, from the acquisition date, be allocated to each of the acquirer's cash-generating units, or groups of cash-generating units, that is expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units or groups of units.

The annual impairment test for a cash-generating unit to which goodwill has been allocated may be performed at any time during an annual period, provided the test is performed at the same time every year. Different cashgenerating units may be tested for impairment at different times. However, if some or all of the goodwill allocated to a cash-generating unit was acquired in a business combination during the current annual period, that unit shall be tested for impairment before the end of the current annual period.

The Standard permits the most recent detailed calculation made in a preceding period of the recoverable amount of a cash-generating unit (group of units) to which goodwill has been allocated to be used in the impairment test for that unit (group of units) in the current period, provided specified criteria are met.

Reversing an impairment loss

An entity shall assess at the end of each reporting period whether there is any indication that an impairment loss recognised in prior periods for an asset other than goodwill may no longer exist or may have decreased.

If any such indication exists, the entity shall estimate the recoverable amount of that asset.

An impairment loss recognised in prior periods for an asset other than goodwill shall be reversed if, and only if, there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised. A reversal of an impairment loss for a cash-generating unit shall be allocated to the assets of the unit, except for goodwill, pro rata with the carrying amounts of those assets. The increased carrying amount of an asset other than goodwill attributable to a reversal of an impairment loss shall not exceed the carrying amount that would have been determined (net of amortisation or depreciation) had no impairment loss been recognised for the asset in prior years.

A reversal of an impairment loss for an asset other than goodwill shall be recognised immediately in profit or loss, unless the asset is carried at revalued amount in accordance with another IFRS (for example, the revaluation model in IAS 16 *Property, Plant and Equipment*). Any reversal of an impairment loss of a revalued asset shall be treated as a revaluation increase in accordance with that other IFRS.

An impairment loss recognised for goodwill shall not be reversed in a subsequent period.

9.25 IAS 37: Provisions, Contingent Liabilities and Contingent Assets

The objective of this Standard is to ensure that appropriate recognition criteria and measurement bases are applied to provisions, contingent liabilities and contingent assets and that sufficient information is disclosed in the notes to enable users to understand their nature, timing and amount.

IAS 37 prescribes the accounting and disclosure for all provisions, contingent liabilities and contingent assets, except:

(a) those resulting from financial instruments that are carried at fair value;

(b) those resulting from executory contracts, except where the contract is onerous. Executory contracts are contracts under which neither party has performed any of its obligations or both parties have partially performed their obligations to an equal extent;

(c) those arising in insurance entities from contracts with policyholders; or

(d) those covered by another Standard.

Provisions

A *provision* is a liability of uncertain timing or amount.

Recognition

A provision should be recognised when:

(a) an entity has a present obligation (legal or constructive) as a result of a past event;

(b) it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and

(c) a reliable estimate can be made of the amount of the obligation.

If these conditions are not met, no provision shall be recognised.

In rare cases it is not clear whether there is a present obligation. In these cases, a past event is deemed to give rise to a present obligation if, taking account of all available evidence, it is more likely than not that a present obligation exists at the end of the reporting period.

Measurement

The amount recognised as a provision shall be the best estimate of the expenditure required to settle the present obligation at the end of the reporting period. The best estimate of the expenditure required to settle the present obligation is the amount that an 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.

Where the provision being measured involves a large population of items, the obligation is estimated by weighting all possible outcomes by their associated probabilities. Where a single obligation is being measured, the individual most likely outcome may be the best estimate of the liability. However, even in such a case, the entity considers other possible outcomes.

Contingent liabilities

A *contingent liability* is:

(a) a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity; or

(b) a present obligation that arises from past events but is not recognised because:

  (i) it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation; or

  (ii) the amount of the obligation cannot be measured with sufficient reliability.

An entity should not recognise a contingent liability. An entity should disclose a contingent liability, unless the possibility of an outflow of resources embodying economic benefits is remote.

Contingent assets

A *contingent asset* is a possible asset that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity.

An entity shall not recognise a contingent asset. However, when the realisation of income is virtually certain, then the related asset is not a contingent asset and its recognition is appropriate.

9.26 IAS 38: Intangible Assets

The objective of this Standard is to prescribe the accounting treatment for intangible assets that are not dealt with specifically in another Standard. This Standard requires an entity to recognise an intangible asset if, and only if, specified criteria are met. The Standard also specifies how to measure the carrying amount of intangible assets and requires specified disclosures about intangible assets.

An *intangible asset* is an identifiable non-monetary asset without physical substance.

Recognition and measurement

The recognition of an item as an intangible asset requires an entity to demonstrate that the item meets:

(a) the definition of an intangible asset; and

(b) the recognition criteria.

This requirement applies to costs incurred initially to acquire or internally generate an intangible asset and those incurred subsequently to add to, replace part of, or service it.

An asset is identifiable if it either:

(a) is separable, ie is capable of being separated or divided from the entity and sold, transferred, licensed, rented or exchanged, either individually or together with a related contract, identifiable asset or liability, regardless of whether the entity intends to do so; or

(b) arises from contractual or other legal rights, regardless of whether those rights are transferable or separable from the entity or from other rights and obligations.

An intangible asset shall be recognised if, and only if:

(a) it is probable that the expected future economic benefits that are attributable to the asset will flow to the entity; and

(b) the cost of the asset can be measured reliably.

The probability recognition criterion is always considered to be satisfied for intangible assets that are acquired separately or in a business combination.

An intangible asset shall be measured initially at cost.

The cost of a separately acquired intangible asset comprises:

(a) its purchase price, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates; and

(b) any directly attributable cost of preparing the asset for its intended use.

In accordance with IFRS 3 *Business Combinations*, if an intangible asset is acquired in a business combination, the cost of that intangible asset is its fair value at the acquisition date. If an asset acquired in a business combination is separable or arises from contractual or other legal rights, sufficient information exists to measure reliably the fair value of the asset.

In accordance with this Standard and IFRS 3 (as revised in 2008), an acquirer recognises at the acquisition date, separately from goodwill, an intangible asset of the acquiree, irrespective of whether the asset had been recognised by the acquiree before the business combination. This means that the acquirer recognises as an asset separately from goodwill an in-process research and development project of the acquiree if the project meets the definition of an intangible asset.

Internally generated intangible assets

Internally generated goodwill shall not be recognised as an asset.

No intangible asset arising from research (or from the research phase of an internal project) shall be recognised. Expenditure on research (or on the research phase of an internal project) shall be recognised as an expense when it is incurred.

An intangible asset arising from development (or from the development phase of an internal project) shall be recognised if, and only if, an entity can demonstrate all of the following:

(a) the technical feasibility of completing the intangible asset so that it will be available for use or sale.

(b) its intention to complete the intangible asset and use or sell it.

(c) its ability to use or sell the intangible asset.

(d) how the intangible asset will generate probable future economic benefits. Among other things, the entity can demonstrate the existence of a market for the output of the intangible asset or the intangible asset itself or, if it is to be used internally, the usefulness of the intangible asset.

(e) the availability of adequate technical, financial and other resources to complete the development and to use or sell the intangible asset.

(f) its ability to measure reliably the expenditure attributable to the intangible asset during its development.

Internally generated brands, mastheads, publishing titles, customer lists and items similar in substance shall not be recognised as intangible assets.

The cost of an internally generated intangible asset for the purpose of paragraph 24 is the sum of expenditure incurred from the date when the intangible asset first meets the recognition criteria in paragraphs 21, 22 and 57. Paragraph 71 prohibits reinstatement of expenditure previously recognised as an expense.

Expenditure on an intangible item shall be recognised as an expense when it is incurred unless:

(a) it forms part of the cost of an intangible asset that meets the recognition criteria; or

(b) the item is acquired in a business combination and cannot be recognised as an intangible asset. If this is the case, it forms part of the amount recognised as goodwill at the acquisition date (see IFRS 3).

Measurement after recognition

An entity shall choose either the cost model or the revaluation model as its accounting policy. If an intangible asset is accounted for using the revaluation model, all the other assets in its class shall also be accounted for using the same model, unless there is no active market for those assets.

Cost model: After initial recognition, an intangible asset shall be carried at its cost less any accumulated amortisation and any accumulated impairment losses.

Revaluation model: After initial recognition, an intangible asset shall be carried at a revalued amount, being its fair value at the date of the revaluation less any subsequent accumulated amortisation and any subsequent accumulated impairment losses. For the purpose of revaluations under this Standard, fair value shall be determined by reference to an active market. Revaluations shall be made with such regularity that at the end of the reporting period the carrying amount of the asset does not differ materially from its fair value.

An *active market* is a market in which all the following conditions exist:

(a) the items traded in the market are homogeneous;

(b) willing buyers and sellers can normally be found at any time; and

(c) prices are available to the public.

If an intangible asset's carrying amount is increased as a result of a revaluation, the increase shall be recognised in other comprehensive income and accumulated in equity under the heading of revaluation surplus.

However, the increase shall be recognised in profit or loss to the extent that it reverses a revaluation decrease of the same asset previously recognised in profit or loss. If an intangible asset's carrying amount is decreased as a result of a revaluation, the decrease shall be recognised in profit or loss. However, the decrease shall be recognised in other comprehensive income to the extent of any credit balance in the revaluation surplus in respect of that asset.

Useful life

Useful life is:

(a) the period over which an asset is expected to be available for use by an entity; or

(b) the number of production or similar units expected to be obtained from the asset by an entity.

An entity shall assess whether the useful life of an intangible asset is finite or indefinite and, if finite, the length of, or number of production or similar units constituting, that useful life. An intangible asset shall be regarded by the entity as having an indefinite useful life when, based on an analysis of all of the relevant factors, there is no foreseeable limit to the period over which the asset is expected to generate net cash inflows for the entity.

The useful life of an intangible asset that arises from contractual or other legal rights shall not exceed the period of the contractual or other legal rights, but may be shorter depending on the period over which the entity expects to use the asset. If the contractual or other legal rights are conveyed for a limited term that can be renewed, the useful life of the intangible asset shall include the renewal period(s) only if there is evidence to support renewal by the entity without significant cost.

To determine whether an intangible asset is impaired, an entity applies IAS 36 *Impairment of Assets*.

Intangible assets with finite useful lives

The depreciable amount of an intangible asset with a finite useful life shall be allocated on a systematic basis over its useful life. *Depreciable amount* is the cost of an asset, or other amount substituted for cost, less its residual value. Amortisation shall begin when the asset is available for use, ie when it is in the location and condition necessary for it to be capable of operating in the manner intended by management. Amortisation shall cease at the earlier of the date that the asset is classified as held for sale (or included in a disposal group that is classified as held for sale) in accordance with IFRS 5 *Non-current Assets Held for Sale and*

Discontinued Operations and the date that the asset is derecognised. The amortisation method used shall reflect the pattern in which the asset's future economic benefits are expected to be consumed by the entity.

If that pattern cannot be determined reliably, the straight-line method shall be used. The amortisation charge for each period shall be recognised in profit or loss unless this or another Standard permits or requires it to be included in the carrying amount of another asset.

The *residual value* of an intangible asset is the estimated amount that an entity would currently obtain from disposal of the asset, after deducting the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life. The residual value of an intangible asset with a finite useful life shall be assumed to be zero unless:

(a) there is a commitment by a third party to purchase the asset at the end of its useful life; or

(b) there is an active market for the asset and:

(i) residual value can be determined by reference to that market; and

(ii) it is probable that such a market will exist at the end of the asset's useful life.

The amortisation period and the amortisation method for an intangible asset with a finite useful life shall be reviewed at least at each financial year-end. If the expected useful life of the asset is different from previous estimates, the amortisation period shall be changed accordingly. If there has been a change in the expected pattern of consumption of the future economic benefits embodied in the asset, the amortisation method shall be changed to reflect the changed pattern. Such changes shall be accounted for as changes in accounting estimates in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.

Intangible assets with indefinite useful lives

An intangible asset with an indefinite useful life shall not be amortised.

In accordance with IAS 36 *Impairment of Assets,* an entity is required to test an intangible asset with an indefinite useful life for impairment by comparing its recoverable amount with its carrying amount

(a) annually, and

(b) whenever there is an indication that the intangible asset may be impaired.

The useful life of an intangible asset that is not being amortised shall be reviewed each period to determine whether events and circumstances continue to support an indefinite useful life assessment for that asset. If they do not, the change in the useful life assessment from indefinite to finite shall be accounted for as a change in an accounting estimate in accordance with IAS 8.

9.27 IAS 39: Financial Instruments: Recognition and Measurement

The International Accounting Standards Board has decided to replace IAS 39 *Financial Instruments:*

Recognition and Measurement over a period of time. The first instalment, dealing with classification and measurement of financial assets, was issued as IFRS 9 *Financial Instruments* in November 2009. The requirements for classification and measurement of financial liabilities and derecognition of financial assets and liabilities were added to IFRS 9 in October 2010. As a consequence, parts of IAS 39 are being superseded and will become obsolete for annual periods beginning on or after 1 January 2013–earlier application is permitted in 2010. The remaining requirements of IAS 39 continue in effect until superseded by future instalments of IFRS 9. The Board expects to replace IAS 39 in its entirety.

Impairment and uncollectibility of financial assets measured at amortised cost

An entity shall assess at the end of each reporting period whether there is any objective evidence that a financial asset or group of financial assets measured at amortised cost is impaired. If there is objective evidence that an impairment loss on financial assets measured

at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (ie the effective interest rate computed at initial recognition).

The carrying amount of the asset shall be reduced either directly or through use of an allowance account. The amount of the loss shall be recognised in profit or loss.

Hedging

A hedging relationship qualifies for hedge accounting under paragraphs 89–102 if, and only if, all of the following conditions are met.

(a) At the inception of the hedge there is formal designation and documentation of the hedging relationship and the entity's risk management objective and strategy for undertaking the hedge. That documentation shall include identification of the hedging instrument, the hedged item or transaction, the nature of the risk being hedged and how the entity will assess the hedging instrument's effectiveness in offsetting the exposure to changes in the hedged item's fair value or cash flows attributable to the hedged risk.

(b) The hedge is expected to be highly effective in achieving offsetting changes in fair value or cash flows attributable to the hedged risk, consistently with the originally documented risk management strategy for that particular hedging relationship.

(c) For cash flow hedges, a forecast transaction that is the subject of the hedge must be highly probable and must present an exposure to variations in cash flows that could ultimately affect profit or loss.

(d) The effectiveness of the hedge can be reliably measured, ie the fair value or cash flows of the hedged item that are attributable to the hedged risk and the fair value of the hedging instrument can be reliably measured.

(e) The hedge is assessed on an ongoing basis and determined actually to have been highly effective throughout the financial reporting periods for which the hedge was designated. [paragraph 88]

Hedging relationships are of three types:

(a) *fair value hedge*: a hedge of the exposure to changes in fair value of a recognised asset or liability or an unrecognised firm commitment, or an identified portion of such an asset, liability or firm commitment, that is attributable to a particular risk and could affect profit or loss.

(b) *cash flow hedge*: a hedge of the exposure to variability in cash flows that (i) is attributable to a particular risk associated with a recognised asset or liability (such as all or some future interest payments on variable rate debt) or a highly probable forecast transaction and (ii) could affect profit or loss.

(c) *hedge of a net investment in a foreign operation* as defined in IAS 21.

If a fair value hedge meets the conditions in paragraph 88 during the period, it shall be accounted for as follows:

(a) the gain or loss from remeasuring the hedging instrument at fair value (for a derivative hedging instrument) or the foreign currency component of its carrying amount measured in accordance with IAS 21 (for a nonderivative hedging instrument) shall be recognised in profit or loss; and

(b) the gain or loss on the hedged item attributable to the hedged risk shall adjust the carrying amount of the hedged item and be recognised in profit or loss. This applies if the hedged item is otherwise measured at cost. Recognition of the gain or loss attributable to the hedged risk in profit or loss applies if the hedged item is an available-for-sale financial asset.

If a cash flow hedge meets the conditions in paragraph 88 during the period, it shall be accounted for as follows:

(a) the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge (see paragraph 88) shall be recognised in other comprehensive income; and

(b) the ineffective portion of the gain or loss on the hedging instrument shall be recognised in profit or loss.

Hedges of a net investment in a foreign operation, including a hedge of a monetary item that is accounted for as part of the net investment (see IAS 21), shall be accounted for similarly to cash flow hedges:

(a) the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge (see paragraph 88) shall be recognised in other comprehensive income; and

(b) the ineffective portion shall be recognised in profit or loss.

9.28 IAS 40 (Revised): Investment Property

The objective of this Standard is to prescribe the accounting treatment for investment property and related disclosure requirements.

Investment property is property (land or a building—or part of a building—or both) held (by the owner or by the lessee under a finance lease) to earn rentals or for capital appreciation or both, rather than for:

(a) use in the production or supply of goods or services or for administrative purposes; or

(b) sale in the ordinary course of business.

A property interest that is held by a lessee under an operating lease may be classified and accounted for as investment property provided that:

(a) the rest of the definition of investment property is met;

(b) the operating lease is accounted for as if it were a finance lease in accordance with IAS 17 *Leases*; and

(c) the lessee uses the fair value model set out in this Standard for the asset recognised.

Investment property shall be recognised as an asset when, and only when:

(a) it is probable that the future economic benefits that are associated with the investment property will flow to the entity; and

(b) the cost of the investment property can be measured reliably.

An investment property shall be measured initially at its cost. Transaction costs shall be included in the initial measurement.

The initial cost of a property interest held under a lease and classified as an investment property shall be as prescribed for a finance lease by paragraph 20 of IAS 17, ie the asset shall be recognised at the lower of the fair value of the property and the present value of the minimum lease payments. An equivalent amount shall be recognised as a liability in accordance with that same paragraph.

The Standard permits entities to choose either:

(a) a fair value model, under which an investment property is measured, after initial measurement, at fair value with changes in fair value recognised in profit or loss; or

(b) a cost model. The cost model is specified in IAS 16 and requires an investment property to be measured after initial measurement at depreciated cost (less any accumulated impairment losses). An entity that chooses the cost model discloses the fair value of its investment property.

The fair value of investment property is the price at which the property could be exchanged between knowledgeable, willing parties in an arm's length transaction.

An investment property shall be derecognised (eliminated from the statement of financial position) on disposal or when the investment property is permanently withdrawn from use and no future economic benefits are expected from its disposal.

Gains or losses arising from the retirement or disposal of investment property shall be determined as the difference between the net disposal proceeds and the carrying amount of the asset and shall be recognised in profit or loss (unless IAS 17 requires otherwise on a sale and leaseback) in the period of the retirement or disposal.

9.29 IAS 41: Agriculture

The objective of this Standard is to prescribe the accounting treatment and disclosures related to agricultural activity.

Agricultural activity is the management by an entity of the biological transformation and harvest of biological assets for sale or for conversion into agricultural produce or into additional biological assets. *Biological transformation* comprises the processes of growth,

degeneration, production, and procreation that cause qualitative or quantitative changes in a biological asset. A *biological asset* is a living animal or plant.

Agricultural produce is the harvested product of the entity's biological assets. *Harvest* is the detachment of produce from a biological asset or the cessation of a biological asset's life processes.

IAS 41 prescribes, among other things, the accounting treatment for biological assets during the period of growth, degeneration, production, and procreation, and for the initial measurement of agricultural produce at the point of harvest. It requires measurement at fair value less costs to sell from initial recognition of biological assets up to the point of harvest, other than when fair value cannot be measured reliably on initial recognition.

This Standard is applied to agricultural produce, which is the harvested product of the entity's biological assets, only at the point of harvest. Thereafter, IAS 2 *Inventories* or another applicable Standard is applied.

Accordingly, this Standard does not deal with the processing of agricultural produce after harvest; for example, the processing of grapes into wine by a vintner who has grown the grapes.

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. Costs to sell include commissions to brokers and dealers, levies by regulatory agencies and commodity exchanges, and transfer taxes and duties. Costs to sell exclude transport and other costs necessary to get assets to a market. Such transport and other costs are deducted in determining fair value (that is, fair value is a market price less transport and other costs necessary to get an asset to a market).

IAS 41 requires that a change in fair value less costs to sell of a biological asset be included in profit or loss for the period in which it arises. In agricultural activity, a change in physical attributes of a living animal or plant directly enhances or diminishes economic benefits to the entity.

IAS 41 does not establish any new principles for land related to agricultural activity. Instead, an entity follows IAS 16 *Property, Plant and Equipment* or IAS 40 *Investment Property*, depending on which standard is appropriate in the circumstances. IAS 16 requires land to be measured either at its cost less any accumulated impairment losses, or at a revalued amount. IAS 40 requires land that is investment property to be measured at its fair value, or cost less any accumulated impairment losses. Biological assets that are physically attached to land (for example, trees in a plantation forest) are measured at their fair value less costs to sell separately from the land.

IAS 41 requires that an unconditional government grant related to a biological asset measured at its fair value less costs to sell to be recognised in profit or loss when, and only when, the government grant becomes receivable. If a government grant is conditional, including when a government grant requires an entity not to engage in specified agricultural activity, an entity should recognise the government grant in profit or loss when, and only when, the conditions

attaching to the government grant are met. If a government grant relates to a biological asset measured at its cost less any accumulated depreciation and any accumulated impairment losses, IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance* is applied.

10. International Financial Reporting Interpretations Committee (IFRIC)

Interpretations of IASs and IFRSs are developed by the International Financial Reporting Interpretations Committee (IFRIC). IFRIC is the new name for the Standing Interpretations Committee (SIC) approved by the IASC Foundation Trustees in March 2002. SIC had been created in 1997 to enhance the rigorous application and worldwide comparability of financial statements that are prepared using International Accounting Standards (IAS) by interpreting potentially contentious accounting issues.

Interpretations are part of IASB's authoritative literature (see IAS 1, Presentation of Financial Statements). Therefore, financial statements may not be described as complying with International Accounting Standards unless they comply with all the requirements of each applicable Standard and each applicable Interpretation issued by the International Financial Reporting Interpretations Committee.

Interpretations are part of IASB's authoritative literature (see IAS 1, Presentation of Financial Statements). Therefore, financial statements may not be described as complying with International Accounting Standards unless they comply with all the requirements of each applicable Standard and each applicable Interpretation issued by the International Financial Reporting Interpretations Committee.

11. Overview of International Financial Reporting Interpretations

Interpretations of IASs and IFRSs are developed by the International Financial Reporting Interpretations Committee (IFRIC). IFRIC is the new name for the Standing Interpretations Committee (SIC) approved by the IASC Foundation Trustees in March 2002.

11.1 IFRIC 1: Changes in Existing Decommissioning, Restoration and Similar Liabilities

- Final Interpretation 1 issued on 27 May 2004
- Effective for annual periods beginning on or after 1 September 2004

Reference

IAS 37, Provisions, Contingent Liabilities and Contingent Assets

Summary

IFRIC contains guidance on accounting for changes in decommissioning, restoration and similar liabilities that have previously been recognised both as part of the cost of an item of

property, plant and equipment under IAS 16 and as a provision (liability) under IAS 37. An example would be a liability that was recognised by the operator of a nuclear power plant for costs that it expects to incur in the future when the plant is shut down (decommissioned). The interpretation addresses subsequent changes to the amount of the liability that may arise from (a) a revision in the timing or amount of the estimated decommissioning or restoration costs or from (b) a change in the current market-based discount rate.

IAS 37 requires the amount recognised as a provision to be the best estimate of the expenditure required to settle the obligation at the balance sheet date. This is measured at its present value, which IFRIC 1 confirms should be measured using a current market-based discount rate. The Interpretation deals with three kinds of change in an existing liability for such costs.

The two main kinds of change dealt with in the Interpretation are those that arise from:

(a) the revision of estimated outflows of resources embodying economic benefits. For example, the estimated costs of decommissioning a nuclear power plant may vary significantly both in timing and amount; and

(b) revisions to the current market-based discount rate.

Most entities account for their property, plant and equipment using the cost model. Where this is so, these changes are required to be capitalised as part of the cost of the item and depreciated prospectively over the remaining life of the item to which they relate. This is consistent with the treatment under IAS 16 of other changes in estimate relating to property, plant and equipment.

In the spirit of convergence, the IFRIC considered the US GAAP approach in Statement of Financial Accounting Standards No. 143 Accounting for Asset Retirement Obligations. The Interpretation treats changes in estimated cash flows in a similar way to SFAS 143. However, SFAS 143 does not require any adjustment to the cost of the item, or to the provision, to reflect the effect of a change in the current market-based discount rate. The IFRIC did not choose this approach because IAS 37, unlike US GAAP, requires provisions to be measured at the current best estimate, which should reflect current discount rates. Also, the IFRIC considered it important that both kinds of change should be dealt with in the same way.

Where entities account for their property, plant and equipment using the fair value model, a change in the liability does not affect the valuation of the item for accounting purposes. Instead, it alters the revaluation surplus or deficit on the item, which is the difference between its valuation and what would be its carrying amount under the cost model. The effect of the change is treated consistently with other revaluation surpluses or deficits. Any cumulative deficit is taken to profit or loss, but any cumulative surplus is credited to equity.

The third kind of change dealt with by the Interpretation is an increase in the liability that reflects the passage of time – also referred to as the unwinding of the discount. This is recognised in profit or loss as a finance cost as it occurs.

11.2 IFRIC 2: Members' Shares in Co-Operative Entities and Similar Instruments

- Final Interpretation 2 issued 25 November 2004
- Effective for annual periods beginning on or after 1 January 2005

Reference

- IAS 32 Financial Instruments: Disclosure and Presentation

Summary

Members' shares in co-operative entities have some characteristics of equity. They also give the holder the right to request redemption for cash, although that right may be subject to certain limitations. IFRIC 2 gives guidance on how those redemption terms should be evaluated in determining whether the shares should be classified as financial liabilities or as equity. Under IFRIC 2, shares for which the member has the right to request redemption are normally liabilities. However, they are equity if:

- the entity has an unconditional right to refuse redemption, or
- local law, regulation, or the entity's governing charter imposes prohibitions on redemption. But the mere existence of law, regulation, or charter provisions that would prohibit redemption only if conditions (such as liquidity constraints) are met, or are not met, does not result in members' shares being equity.

11.3 IFRIC 4 : Determining Whether an Arrangement contains a Lease

- IFRIC 4 Issued 2 December 2004
- Effective for annual periods beginning on or after 1 January 2006

Reference

- IAS 17, Leases

Summary

In recent years arrangements have developed that do not take the legal form of a lease but which convey rights to use assets in return for a payment or series of payments. Examples of such arrangements include:

- outsourcing arrangements;
- telecommunication contracts that provide rights to capacity; and

- take-or-pay and similar contracts, in which purchasers must make specified payments regardless of whether they take delivery of the contracted products or services.

The Interpretation specifies that an arrangement that meets the following criteria is, or contains, a lease that should be accounted for in accordance with IAS 17 Leases:

- Fulfilment of the arrangement depends upon a specific asset. The asset need not be explicitly identified by the contractual provisions of the arrangement. Rather it may be implicitly specified because it is not economically feasible or practical for the supplier to fulfil the arrangement by providing use of alternative assets.
- The arrangement conveys a right to control the use of the underlying asset. This is the case if any of the following conditions is met:
  - (i) the purchaser in the arrangement has the ability or right to operate the asset or direct others to operate the asset (while obtaining more than an insignificant amount of the output of the asset).
  - (ii) the purchaser has the ability or right to control physical access to the asset (while obtaining more than an insignificant amount of the output of the asset).
  - (iii) there is only a remote possibility that parties other than the purchaser will take more than an insignificant amount of the output of the asset and the price that the purchaser will pay is neither fixed per unit of output nor equal to the current market price at the time of delivery.

11.4 IFRIC 5 : Rights to Interests Arising from Decommissioning, Restoration and Environmental Funds

IFRIC 5 issued on 16 December 2004 and is effective for annual periods beginning on or after 1 January 2006

References

IAS 8, IAS 27, IAS 28, IAS 31, IAS 37, IAS 39 and SIC 12

Summary

Some entities have obligations to decommission assets or to perform environmental restoration or rehabilitation. Some such entities contribute to a fund established to reimburse the decommissioning, restoration or rehabilitation costs when they are incurred. The fund may be set up to meet the decommissioning costs of a single contributor or for many contributors.

The issues addressed in IFRIC 5 are:

- How should a contributor account for its interest in a fund?
- When a contributor has an obligation to make additional contributions, how should that obligation be accounted for?

Under IFRIC 5:

- If an entity recognises a decommissioning obligation under IFRSs and contributes to a fund to segregate assets to pay for the obligation, it should apply IAS 27, Consolidated and Separate Financial Statements, SIC-12, Consolidation—Special Purpose Entities, IAS 28, Investments in Associates, and IAS 31, Interests in Joint Ventures, to determine whether decommissioning funds should be consolidated, proportionately consolidated or accounted for under the equity method.
- When a fund is not consolidated, proportionately consolidated, or accounted for under the equity method, and that fund does not relieve the contributor of its obligation to pay decommissioning costs, the contributor should recognise:
  - its obligation to pay decommissioning costs as a liability, and
  - its rights to receive reimbursement from the fund as a reimbursement under IAS 37.
- A right to reimbursement should be measured at the lower of (i) the amount of the decommissioning obligation recognised and (ii) the contributor's share of the fair value of the net assets of the fund. Changes in the carrying amount of this right (other than contributions to and payments from the funds) should be recognised in profit or loss.
- When a contributor has an obligation to make potential additional contributions to the fund, that obligation is a contingent liability within the scope of IAS 37. When it becomes probable that the additional contributions will be made, a provision should be recognised.

IFRIC 5 amends IAS 39 Financial Instruments: Recognition and Measurement to exclude from its scope rights to reimbursement for expenditure required to settle a liability recognised as a provision. Such rights will be accounted for in accordance with IAS 37 Provisions, Contingent Liabilities and Contingent Assets.

11.5 IFRIC 6 : Liabilities Arising from Participating in A Specific Market - Waste Electrical and Electronic Equipment

IFRIC 6 Issued on 1st September and Effective Date of IFRIC 6 is financial periods beginning on or after 1 December 2005.

References

IAS 37 Provisions, Contingent Liabilities and Contingent Assets

Summary

IFRIC 6 clarifies when certain producers of electrical goods are required to recognise a liability under IAS 37 for the cost of waste management relating to the decommissioning of waste electrical and electronic equipment supplied to private households.

The European Union's Directive on Waste Electrical and Electronic Equipment (WE&EE) has raised questions about when the liability of certain electrical goods manufacturers for the decommissioning of such waste should be recognised. The Directive prescribes that the cost of waste management for equipment that has been sold to private households before 13 August 2005 should be borne by producers of that type of equipment that are in the market during the period specified in the applicable legislation of the individual member state (the measurement period). The manufcturers have to contribute to costs in proportion to their respective share of the market by type of equipment.

The issue that IFRIC 6 addresses is: if an entity has an obligation to contribute to waste management costs based on its share of the market in a measurement period, what is the event under paragraph 14(a) of IAS 37 that gives rise to a liability:

- the manufacture or sale of the historical household equipment?
- participation in the market during the measurement period?
- the incurrence of costs in the performance of waste management activities?

IFRIC 6 concludes that the event that triggers liability recognition is participation in the market during the measurement period. The measurement period is a period in which market shares are determined for the purposes of allocating waste management costs. IFRIC 6 states that it is this date, rather than the date of production of the equipment or incurrence of costs, that is the triggering event for liability recognition.

Examples

2. Company Z began operations in September 2005 and manufactures domestic washing machines. Even though it was not responsible for producing any 'historical' WE&EE, because it participates in the market currently it will contribute to the cost of recycling historical WE&EE in proportion to its market share during the measurement period.
3. Company T ceased to produce domestic refrigerators in 2004. Because T no longer produces domestic refrigerators (i.e., its market share is zero), it has no obligation to fund the collection and recycling of historical WE&EE it produced.

The IFRIC's conclusion on this issue is a pragmatic one. The WE&EE Directive attaches the liability for the disposal of historical waste to currently active producers and distributors on the basis of their current market share – irrespective of the extent of their participation in the market at the time the equipment was produced. To apply the Directive retrospectively was not thought practicable. Working with this result, the IFRIC determined that the only workable 'past event' (required by IAS 37 for recognising a liability) was current participation in the market, evidenced by sales in that market.

IFRIC 6 is effective for financial periods beginning on or after 1 December 2005. Earlier application is encouraged.

11.6 IFRIC 7 : Applying the Restatement Approach Under IAS 29 Financial Reporting in Hyperinflationary Economies

IFRIC 7 Issued on 24 November 2005 and effective Date of IFRIC 7 is annual periods beginning on or after 1 March 2006

References

IAS 29 Financial Reporting in Hyperinflationary Economies

Summary

IAS 29 Financial Reporting in Hyperinflationary Economies requires that the financial statements of an entity that reports in the currency of a hyperinflationary economy should be stated in terms of the measuring unit current at the balance sheet date. Comparative figures for prior period(s) should be restated into the same current measuring unit. IFRIC 7 contains guidance on how an entity would restate its financial statements in the first year it identifies the existence of hyperinflation in the economy of its functional currency.

The restatement approach on which IAS 29 is based distinguishes between monetary and non-monetary items. However, in practice there has been uncertainty about how an entity goes about restating its financial statements for the first time, especially deferred tax balances and comparatives.

The main requirements of the Interpretation are:

- In the period in which the economy of an entity's functional currency becomes hyperinflationary, the entity shall apply the requirements of IAS 29 as though the economy had always been hyperinflationary. The effect of this requirement is that restatements of non-monetary items carried at historical cost are made from the dates at which those items were first recognised; for other non-monetary items the restatements are made from the dates at which revised current values for those items were established.
- Deferred tax amounts in the opening balance sheet are determined in two stages:
  - Deferred tax items are remeasured in accordance with IAS 12 after restating the nominal carrying amounts of the non-monetary items in the opening balance sheet by applying the measuring unit at that date.
  - The deferred tax items remeasured in this way are restated for the change in the measuring unit from the date of the opening balance sheet to the date of the closing balance sheet.

IFRIC 7 is effective for annual periods beginning on or after 1 March 2006. Earlier application is encouraged.

11.7 IFRIC 10 : Interim Financial Reporting and Impairment

IFRIC Interpretation 10 *Interim Financial Reporting and Impairment* issued on 20 July 2006 and its effective date is annual periods beginning on or after 1 November 2006

References

IAS 34 Interim Financial Reporting

Summary

The Interpretation addresses an apparent conflict between the requirements of IAS 34 Interim Financial Reporting and those in other standards on the recognition and reversal in financial statements of impairment losses on goodwill and certain financial assets. IFRIC 10 concludes that:

An entity shall not reverse an impairment loss recognised in a previous interim period in respect of goodwill or an investment in either an equity instrument or a financial asset carried at cost.

An entity shall not extend this consensus by analogy to other areas of potential conflict between IAS 34 and other standards.

IFRIC 10 is effective for annual periods beginning on or after 1 November 2006. Earlier application is encouraged.

11.8 IFRIC 12 : Service Concession Arrangements

IFRIC Interpretation 12 *IFRS 12: Service Concession Arrangements* was issued on 30 November 2006 and its effective date is annual periods beginning on or after 1 January 2008.

References:

IFRS 1 First-time Adoption of International Financial Reporting Standards

IFRS 7 Financial Instruments: Disclosures

Framework for the Preparation and Presentation of Financial Statements

IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors

IAS 11 Construction Contracts

IAS 16 Property, Plant and Equipment

IAS 17 Leases

IAS 18 Revenue

IAS 20 Government Grants

IAS 23 Borrowing Costs

IAS 32 Financial Instruments: Disclosure and Presentation

IAS 36 Impairment of Assets

IAS 37 Provisions, Contingent Liabilities and Contingent Assets

IAS 38 Intangible Assets

IAS 39 Financial Instruments: Recognition and Measurement

IFRIC 4 Determining whether an Arrangement contains a Lease

SIC-29 Disclosure - Service Concession Arrangements

Summary

Service Concession Arrangements Defined

Service concession arrangements are arrangements whereby a government or other body grants contracts for the supply of public services – such as roads, energy distribution, prisons or hospitals – to private operators. The objective of this project of the IFRIC is to clarify how certain aspects of existing IASB literature are to be applied to service concession arrangements.

Two Types of Service Concession Arrangements

IFRIC 12 draws a distinction between two types of service concession arrangement.

- In one, the operator receives a financial asset, specifically an unconditional contractual right to receive cash or another financial asset from the government in return for constructing or upgrading the public sector asset.
- In the other, the operator receives an intangible asset – a right to charge for use of the public sector asset that it constructs or upgrades. A right to charge users is not an unconditional right to receive cash because the amounts are contingent on the extent to which the public uses the service.

IFRIC 12 allows for the possibility that both types of arrangement may exist within a single contract: to the extent that the government has given an unconditional guarantee of payment for the construction of the public sector asset, the operator has a financial asset; to the extent that the operator has to rely on the public using the service in order to obtain payment, the operator has an intangible asset.

Accounting – Financial asset model

The operator recognises a financial asset to the extent that it has an unconditional contractual right to receive cash or another financial asset from or at the direction of the grantor for the construction services. The operator has an unconditional right to receive cash if the grantor contractually guarantees to pay the operator

(a) specified or determinable amounts or

(b) the shortfall, if any, between amounts received from users of the public service and specified or determinable amounts, even if payment is contingent on the operator ensuring that the infrastructure meets specified quality or efficiency requirements.

The operator measures the financial asset at fair value.

Accounting – Intangible asset model

The operator recognises an intangible asset to the extent that it receives a right (a licence) to charge users of the public service. A right to charge users of the public service is not an unconditional right to receive cash because the amounts are contingent on the extent that the public uses the service.

The operator measures the intangible asset at fair value.

Operating revenue

The operator of a service concession arrangement recognises and measures revenue in accordance with IASs 11 and 18 for the services it performs.

Accounting by the Government (Grantor)

IFRIC 12 does not address accounting for the government side of service concession arrangements. IFRSs are not designed to apply to not-for-profit activities in the private sector or the public sector. However, the International Public Sector Accounting Standards Board (IPSASB) has started its own project on service concession arrangements, which will give serious consideration to accounting by grantors. The principles applied in IFRIC 12 will be considered as part of the project.

11.9 IFRIC 13: Customer Loyalty Programmes

IFRIC Interpretation 13 *IFRS 13 Customer Loyalty Programmes* was issued 28 June 2007 and its effective date is annual periods beginning on or after 1 July 2008.

References:

IAS 18 Revenue

IAS 37 Provisions, Contingent Liabilities and Contingent Assets

IAS 38 Intangible Assets

Summary

IFRIC 13 Customer Loyalty Programmes addresses accounting by entities that grant loyalty award credits (such as 'points' or travel miles) to customers who buy other goods or services. Specifically, it explains how such entities should account for their obligations to provide free or discounted goods or services ('awards') to customers who redeem award credits.

Key Provisions:

- An entity that grants loyalty award credits shall allocate some of the proceeds of the initial sale to the award credits as a liability (its obligation to provide the awards). In effect, the award is accounted for as a separate component of the sale transaction.
- The amount of proceeds allocated to the award credits is measured by reference to their fair value, that is, the amount for which the award credits could have been sold separately.
- The entity shall recognise the deferred portion of the proceeds as revenue only when it has fulfilled its obligations. It may fulfil its obligations either by supplying the awards itself or by engaging (and paying) a third party to do so.
- If at any time the expected costs of meeting the obligation exceed the consideration received, the entity has an onerous contract for which IAS 37 would require recognition of a liability.
- If IFRIC 13 causes an entity to change its accounting policy for customer loyalty awards, IAS 8 applies.

11.10 IFRIC 14: IAS 19 – The Limit on A Defined Benefit Asset, Minimum Funding Requirements and Their Interaction

IFRIC 14 was issued 4 July 2007.and its Effective Date of IFRIC 14: Annual periods beginning on or after 1 January 2008. Earlier application permitted.

References

IAS 19 Employee Benefits

Summary

In many countries, laws or contractual terms require employers to make minimum funding payments for their pension or other employee benefit plans. This enhances the security of the retirement benefit promise made to members of an employee benefit plan.

Normally, such statutory or contractual funding requirements would not affect the measurement of the defined benefit asset or liability. This is because the contributions, once paid, become plan assets and the additional net liability would be nil. However, paragraph 58 of IAS 19 Employee Benefits limits the measurement of the defined benefit asset to the 'present value of economic benefits available in the form of refunds from the plan or reductions in future contributions to the plan.' IFRIC 14 addresses the interaction between a minimum funding requirement and the limit placed by paragraph 58 of IAS 19 on the measurement of the defined benefit asset or liability.

When determining the limit on a defined benefit asset in accordance with IAS 19.58, under IFRIC 14 entities are required to measure any economic benefits available to them in the form

of refunds or reductions in future contributions at the maximum amount that is consistent with the terms and conditions of the plan and any statutory requirements in the jurisdiction of the plan. The entity's intentions on how to use a surplus (for instance, whether the entity intends to improve benefits rather than reduce contributions or get a refund) must be disregarded.

Such economic benefits are regarded as available to an entity if the entity has an unconditional right to realise them at some point during the life of the plan or when the plan is settled, even if they are not realisable immediately at the balance sheet date. Such an unconditional right would not exist when the availability of the refund or the reduction in future contribution would be contingent upon factors beyond the entity's control (for example, approval by third parties such as plan trustees). To the extent the right is contingent, no asset would be recognised.

Economic benefits available as a refund

If an entity has an unconditional right to a refund

(a) during the life of the plan, without assuming that the plan liabilities must be settled in order to obtain the refund, or

(b) assuming the gradual settlement of the plan liabilities over time until all members have left the plan, or

(c) assuming the full settlement of the plan liabilities in a single event (i.e. as a plan wind-up),

it shall recognise an asset measured as the amount of the surplus at the balance sheet date that it has a right to receive as a refund. This is the fair value of the plan assets less the present value of the defined benefit obligation, less any associated costs, such as taxes.

If the refund is determined as the full amount or a proportion of the surplus, rather than a fixed amount, the amount shall be calculated without further adjustment for the time value of money, even if the refund is realisable only at a future date, as both the defined benefit obligation and the fair value of plan assets are already measured on a present value basis.

Economic benefits available as a reduction in contributions

In the absence of a minimum funding requirement, IFRIC 14 requires entities to determine economic benefits available as a reduction in future contributions as:

- the present value of the future service cost to the entity (excluding costs borne by employees) over:
- the shorter of the expected life of the plan; and
- the expected life of the entity;
- determined using assumptions consistent with those used to determine the defined benefit obligation (including the discount rate); and

- based on conditions that exist at the balance sheet date.
- This means, an entity shall assume
- no change to the benefits provided by a plan in the future until the plan is amended, and
- a stable workforce unless it is demonstrably committed at the balance sheet date to make a reduction in the number of employees covered by the plan.

IFRIC 14 contains illustrative examples that outline the accounting treatments under a number of different scenarios.

Effective date and transition

IFRIC 14 is effective for annual periods beginning on or after 1 January 2008. Earlier application is permitted.

The Interpretation is to be applied from the beginning of the first period presented in the financial statements for annual periods beginning on or after the effective date. The IFRIC had initially proposed full retrospective application, but decided to amend the transitional provisions reflecting concerns from constituents.

11.11 IFRIC 15: Agreements for the Construction of Real Estate

IFRIC 15 standardises accounting practice across jurisdictions for the recognition of revenue by real estate developers for sales of units, such as apartments or houses, 'off plan' – that is, before construction is complete.

Fundamental issue

The fundamental issue is whether the developer is selling a product (goods) – the completed apartment or house – or is selling a service – a construction service as a contractor engaged by the buyer. Revenue from selling products is normally recognised at delivery. Revenue from selling services is normally recognised on a percentage-of-completion basis as construction progresses.

IAS 11 or IAS 18?

IFRIC 15 provides guidance on how to determine whether an agreement for the construction of real estate is within the scope of IAS 11 Construction Contracts or IAS 18 Revenue and, accordingly, when revenue from the construction should be recognised:

- An agreement for the construction of real estate is a construction contract within the scope of IAS 11 only when the buyer is able to specify the major structural elements of the design of the real estate before construction begins and/or specify major structural changes once construction is in progress (whether it exercises that ability or not).
- If the buyer has that ability, IAS 11 applies.
- If the buyer does not have that ability, IAS 18 applies.

If IAS 11 applies, what is the accounting?

If IAS 11 applies, revenue is recognised on a percentage-of-completion basis provided that reliable estimates of construction progress and future costs can be made.

If IAS 18 applies, service or goods?

Even if IAS 18 applies, the agreement may be to provide construction services rather than goods. This would likely be the case, for instance, if the entity is not required to acquire and supply construction materials. If the entity is required to provide services together with construction materials in order to perform its contractual obligation to deliver real estate to the buyer, the agreement is accounted for as the sale of goods under IAS 18.

Impact of IFRIC 15

The main expected change in practice is a shift for some entities from recognising revenue as construction progresses to recognising revenue at a single time – at completion upon or after delivery. Agreements that will be affected will be mainly those currently accounted for in accordance with IAS 11 that do not meet the definition of a construction contract as interpreted by the IFRIC and do not transfer to the buyer control and the significant risks and rewards of ownership of the work in progress in its current state as construction progresses.

Effective Date

IFRIC 15 is effective for annual periods beginning on or after 1 January 2009 and must be applied retrospectively. Earlier application is permitted.

11.12 IFRIC 16: Hedges of a Net Investment in a Foreign Operation

IFRIC 16 clarifies three main issues:

Whether risk arises from (a) the foreign currency exposure to the functional currencies of the foreign operation and the parent entity, or from (b) the foreign currency exposure to the functional currency of the foreign operation and the presentation currency of the parent entity's consolidated financial statements.

IFRIC 16 concludes that the presentation currency does not create an exposure to which an entity may apply hedge accounting. Consequently, a parent entity may designate as a hedged risk only the foreign exchange differences arising from a difference between its own functional currency and that of its foreign operation.

Which entity within a group can hold a hedging instrument in a hedge of a net investment in a foreign operation and in particular whether the parent entity holding the net investment in a foreign operation must also hold the hedging instrument.

IFRIC 16 concludes that the hedging instrument(s) may be held by any entity or entities within the group.

How an entity should determine the amounts to be reclassified from equity to profit or loss for both the hedging instrument and the hedged item when the entity disposes of the investment.

IFRIC 16 concludes that while IAS 39 must be applied to determine the amount that needs to be reclassified to profit or loss from the foreign currency translation reserve in respect of the hedging instrument, IAS 21 must be applied in respect of the hedged item.

Effective Date

IFRIC 16 is effective for annual periods beginning on or after 1 October 2008. An entity may choose to apply IFRIC 16 retrospectively or prospectively. Earlier application is permitted.

On 16 April 2009 the IASB amended IFRIC 16 to allow entities to designate as a hedging instrument in a net investment in a foreign operation an instrument that is held by the foreign operation that is being hedged. Effective date is 1 July 2009. The amendment was part of the IASB's annual improvements for 2009.

11.13 IFRIC 17: Distributions of Non-Cash Assets to Owners

IFRIC 17 *Distributions of Non-cash Assets to Owners* applies to the entity making the distribution, not to the recipient. It applies when non-cash assets are distributed to owners or when the owner is given a choice of taking cash in lieu of the non-cash assets.

IFRIC 17 clarifies that:

- a dividend payable should be recognised when the dividend is appropriately authorised and is no longer at the discretion of the entity
- an entity should measure the dividend payable at the fair value of the net assets to be distributed
- an entity should remeasure the liability at each reporting date and at settlement, with changes recognised directly in equity
- an entity should recognise the difference between the dividend paid and the carrying amount of the net assets distributed in profit or loss, and should disclose it separately
- an entity should provide additional disclosures if the net assets being held for distribution to owners meet the definition of a discontinued operation

IFRIC 17 applies to pro rata distributions of non-cash assets (all owners are treated equally) but does not apply to common control transactions.

Effective Date and Transition

- IFRIC 17 is to be applied prospectively.
- IFRIC 17 is effective for annual periods beginning on or after 1 July 2009. Earlier application is permitted, with some restrictions.

11.14 IFRIC 18: Transfers of Assets from Customers

IFRIC 18 clarifies the requirements of IFRSs for agreements in which an entity receives from a customer an item of property, plant, and equipment that the entity must then use either to connect the customer to a network or to provide the customer with ongoing access to a supply of goods or services (such as a supply of electricity, gas or water). In some cases, the entity

receives cash from a customer that must be used only to acquire or construct the item of property, plant, and equipment in order to connect the customer to a network or provide the customer with ongoing access to a supply of goods or services (or to do both).

The basic principle of IFRIC 18 is that when the item of property, plant and equipment transferred from a customer meets the definition of an asset under the IASB Framework from the perspective of the recipient, the recipient must recognise the asset in its financial statements. If the customer continues to control the transferred item, the asset definition would not be met even if ownership of the asset is transferred to the utility or other recipient entity.

The deemed cost of that asset is its fair value on the date of the transfer.

If there are separately identifiable services received by the customer in exchange for the transfer, then the recipient should split the transaction into separate components as required by IAS 18. If there is only one component identified, revenue is recognised when the service is performed (which could, for example, be as soon as access to a utility network is provided). IFRIC 18 provides guidance on how to identify the entity's obligation to provide one or more separately identifiable services in exchange for the transferred asset – and, therefore, how to recognise revenue:

- If the entity has only one service obligation, it would recognise revenue when the service is performed.
- If the entity has more than one separately identifiable service obligation, it should allocate the fair value of the total consideration received to each service and recognise revenue from each service separately in accordance with IAS 18.
- If the entity has an obligation to provide ongoing services, the period over which revenue is recognised is generally determined by the terms of the agreement with the customer. If the agreement does not specify a period, the revenue shall be recognised over a period no longer than the useful life of the transferred asset used to
- provide the ongoing service.

IFRIC 18 also provides guidance on how to account for transfers of cash from customers.

While IFRIC 18 is particularly relevant for entities in the utility sector, it applies to all entities that prepare IFRS financial statements.

Effective Date

IFRIC 18 must be applied prospectively to transfers of assets from customers received on or after 1 July 2009. Earlier application is permitted provided the valuations and other information needed to apply to the Interpretation to past transfers were obtained at the time those transfers were made.

11.15 IFRIC 19 : Extinguishing Financial Liabilities with Equity Instruments

- If a debtor issues equity instruments to a creditor to extinguish all or part of a financial liability, those equity instruments are 'consideration paid' in accordance with IAS 39.41. Accordingly, the debtor should derecognise the financial liability fully or partly.
- The debtor should measure the equity instruments issued to the creditor at fair value, unless fair value is not reliably determinable, in which case the equity instruments issued are measured at the fair value of the liability extinguished.
- If only part of a liability is extinguished, the debtor must determine whether any part of the consideration paid relates to modification of the terms of the remaining liability. If it does, the debtor must allocate the fair value of the consideration paid between the liability extinguished and the liability retained.
- The debtor recognises in profit or loss the difference between the carrying amount of the financial liabiilty (or part) extinguished and the measurement of the equity instruments issued.
- When only part of the liability is extinguished, the debtor must determine whether the terms of the remaining debt have been substantially modified (taking into account any portion of the consideration paid that was allocated to the remaining debt). If there has been a substantial modification, the debtor should account for an extinguishment of the old remaining liabiilty and the recognition of a new liability (see IAS 39.40).

IFRIC 19 addresses only the accounting by the entity that issues equity instruments in order to settle, in full or in part, a financial liability. It does not address the accounting by the creditor (lender).

The following situations are explicitly excluded from the scope of IFRIC 19:

- the creditor is also a direct or indirect shareholder and is acting in its capacity as direct or indirect shareholder;
- the creditor and the entity are controlled by the same party or parties before and after the transaction, and the substance of the transaction includes an equity distribution from, or contribution to, the entity; or
- extinguishing the financial liability by issuing equity shares is in accordance with the original terms of the financial liability.

IFRIC 19 must be applied in annual periods beginning on or after 1 July 2010. Earlier application is permitted. It must be applied retrospectively from the beginning of the earliest comparative period presented.

11.16 IFRIC 20 : Stripping Costs in the Production Phase of a Surface Mine

In surface mining operations, entities may find it necessary to remove mine waste materials ('overburden') to gain access to mineral ore deposits. This waste removal activity is known as 'stripping'. There can be two benefits accruing to the entity from the stripping activity: usable

ore that can be used to produce inventory and improved access to further quantities of material that will be mined in future periods.

IFRIC 20 considers when and how to account separately for these two benefits arising from the stripping activity, as well as how to measure these benefits both initially and subsequently.

IFRIC 20 only deals with waste removal costs that are incurred in surface mining activity during the production phase of the mine ('production stripping costs').

IFRIC 20 requires:

- The costs of stripping activity to be accounted for in accordance with the principles of IAS 2 *Inventories* to the extent that the benefit from the stripping activity is realised in the form of inventory produced
- The costs of stripping activity which provides a benefit in the form of improved access to ore is recognised as a non-current 'stripping activity asset' where the following criteria are met:
    - it is probable that the future economic benefit (improved access to the ore body) associated with the stripping activity will flow to the entity
    - the entity can identify the component of the ore body for which access has been improved
    - the costs relating to the stripping activity associated with that component can be measured reliably
- When the costs of the stripping activity asset and the inventory produced are not separately identifiable, production stripping costs are allocated between the inventory produced and the stripping activity asset by using an allocation basis that is based on a relevant production measure
- A stripping activity asset is accounted for as an addition to, or as an enhancement of, an existing asset and classified as tangible or intangible according to the nature of the existing asset of which it forms part
- A stripping activity asset is initially measured at cost and subsequently carried at cost or its revalued amount less depreciation or amortisation and impairment losses
- A stripping activity asset is depreciated or amortised on a systematic basis, over the expected useful life of the identified component of the ore body that becomes more accessible as a result of the stripping activity. The units of production method is used unless another method is more appropriate.

Application and transition

IFRIC 20 applies to annual periods beginning on or after 1 January 2013. Earlier application is permitted.

The Interpretation applies to production stripping costs incurred on or after the beginning of the earliest period presented. Any 'predecessor stripping asset' at that date is required to be

reclassified as a part of the existing asset to which the stripping activity is related (to the extent there remains an identifiable component of the ore body to which it can be associated), or otherwise recognised in opening retained earnings at the beginning of the earliest period presented.

12. Standing Interpretations Committee – An Overview

SIC had been created in 1997 to enhance the rigorous application and worldwide comparability of financial statements that are prepared using International Accounting Standards (IAS) by interpreting potentially contentious accounting issues.

12.1 SIC 7 : Introduction of the Euro

This SIC has been Revised in December 2003 and is effective from 1 January 2005,

References

IAS 21 *The Effects of Changes in Foreign Exchange Rates*

Summary

This Interpretation addresses how the introduction of the Euro, resulting from the European Economic and Monetary Union (EMU), affects the application of IAS 21 *The Effects of Changes in Foreign Exchange Rates*. SIC 7 states that the requirements of IAS 21 should be strictly applied when a country joins the EU's Economic and Monetary Union. Therefore:

- foreign currency monetary assets and liabilities resulting from transactions continue to be translated into the functional currency at the closing rate. Any resulting exchange differences are recognised as income or expense immediately, except that an entity continues to apply its existing accounting policy for exchange gains and losses related to hedges of the currency risk of a forecast transaction.
- cumulative exchange differences relating to the translation of financial statements of foreign operations continue to be classified as equity and are recognised as income or expense only on the disposal of the net investment in the foreign operation; and
- exchange differences resulting from translating liabilities denominated in participating currencies are not included in the carrying amount of related assets.

12.2 SIC 10: Government Assistance - No Specific Relation to Operating Activities

SIC 10 has been issued on July 1998 and is effective from 1 August 1998.

References

IAS 20, Accounting for Government Grants and Disclosure of Government Assistance

Summary

In some countries, government assistance to enterprises can be aimed at encouragement or long-term support of business activities either in certain regions or industry sectors. Conditions to receive such assistance may not be specifically related to the operating activities of the enterprise. The issue is whether such government assistance is "a government grant" within the scope of IAS 20 and should therefore be accounted for in accordance with this Standard.

Under SIC 10, government assistance to enterprises that is aimed at encouragement or long-term support of business activities either in certain regions or industry sectors meets the definition of government grants in IAS 20. Such grants should therefore not be credited directly to shareholders' interests.

12.3 SIC 15: Operating Leases - Incentives

SIC 15 has been issued on July 1999 and is effective from Lease terms beginning on or after 1 January 1999.

References

IAS 17, Leases

Summary

In SIC-15, the SIC clarifies the recognition of incentives related to operating leases by both the lessee and lessor. The Interpretation indicates that lease incentives (such as rent-free periods or contributions by the lessor to the lessee's relocation costs) should be considered an integral part of the consideration for the use of the leased asset. IAS 17.24 and .42 (rev. 1997) require an enterprise to treat incentives as a reduction of lease income or lease expense. As they are an integral part of the net consideration agreed for the use of the leased asset, incentives should be recognised by both the lessor and the lessee over the lease term, with each party using a single amortisation method applied to the net consideration.

12.4 SIC 25: Income Taxes - Changes in the Tax Status of an Enterprise or Its Shareholders

SIC 25 has been issued on July 2000 and is effective from 15 July 2000

References

IAS 12, Income Taxes

Summary

A change in the tax status of an enterprise or its shareholders does not give rise to increases or decreases in the pre-tax amounts recognised directly in equity. Therefore, SIC 25 concludes that the current and deferred tax consequences of the change in tax status should be included in net profit or loss for the period. However, where a transaction or event does

result in a direct credit or charge to equity, for example the revaluation of property, plant or equipment under IAS 16, the related tax consequence would still be recognised directly in equity.

12.5 SIC 27: Evaluating the Substance of Transactions in the Legal Form of A Lease

SIC 27 is effective from 31 December 2001

References

IAS 1, Presentation of Financial Statements, IAS 17, Leases, and IAS 18, Revenue.

Summary

SIC 27 addresses issues that may arise when an arrangement between an enterprise and an investor involves the legal form of a lease. Among the provisions of SIC 27:

- Accounting for arrangements between an enterprise and an investor should reflect the substance of the arrangement. All aspects of the arrangement should be evaluated to determine its substance, with weight given to those aspects and implications that have an economic effect. In this respect, SIC 27 includes a list of indicators that individually demonstrate that an arrangement may not, in substance, involve a lease under IAS 17, Leases.
- If an arrangement does not meet the definition of a lease, SIC 27 addresses whether a separate investment account and lease payment obligation that might exist represent assets and liabilities of the enterprise; how the enterprise should account for other obligations resulting from the arrangement; and how the enterprise should account for a fee it might receive from an Investor. SIC 27 includes a list of indicators that collectively demonstrate that, in substance, a separate investment account and lease payment obligations do not meet the definitions of an asset and a liability and should not be recognised by the enterprise. Other obligations of an arrangement, including any guarantees provided and obligations incurred upon early termination, should be accounted for under IAS 37 or IAS 39, depending on the terms. Further, it agreed that the criteria in IAS 18.20 should be applied to the facts and circumstances of each arrangement in determining when to recognise a fee as income that an Enterprise might receive.
- A series of transactions that involve the legal form of a lease is linked, and therefore should be accounted for as one transaction, when the overall economic effect cannot be understood without reference to the series of transactions as a whole.

12.6 SIC 29: Disclosure – Service Concession Arrangements

SIC 29 is effective from 31 December 2001

References

An Interpretation of IAS 1, Presentation of Financial Statements

Summary

SIC 29 prescribes the information that should be disclosed in the notes to the financial statements of a concession operator and a concession provider when the two parties are joined by a service concession arrangement. A service concession arrangement exists when an enterprise (the concession operator) agrees with another enterprise (the concession provider) to provide services that give the public access to major economic and social facilities.

Examples of service concession arrangements involve water treatment and supply facilities, motorways, car parks, tunnels, bridges, airports and telecommunication networks. Examples of arrangements that are not service concession arrangements include an enterprise outsourcing the operation of its internal services (for instance, employee cafeteria, building maintenance, and accounting or information technology functions).

Under SIC 29, the following should be disclosed in each period:

- a description of the arrangement;
- significant terms of the arrangement that may affect the amount, timing, and certainty of future cash flows (such as the period of the concession, re-pricing dates, and the basis on which re-pricing or re-negotiation is determined);
- the nature and extent (quantity, time period, or amount, as appropriate) of:
  - rights to use specified assets;
  - obligations to provide or rights to expect provision of services;
  - obligations to acquire or build items of property, plant and equipment;
  - obligations to deliver or rights to receive specified assets at the end of the concession period;
  - renewal and termination options; and
  - other rights and obligations (for instance, major overhauls); and
- changes in the arrangement occurring during the period.

12.7 SIC 31: Revenue - Barter Transactions Involving Advertising Services

SIC 31 is effective from 31 December 2001.

References

IAS 18, Revenue

Summary

Under IAS 18, revenue cannot be recognised if the amount of revenue is not reliably measurable. SIC 31 deals with the circumstances in which a seller can reliably measure

revenue at the fair value of advertising services received or provided in a barter transaction. Under SIC 31, revenue from a barter transaction involving advertising cannot be measured reliably at the fair value of advertising services received. However, a seller can reliably measure revenue at the fair value of the advertising services it provides in a barter transaction by reference only to non-barter transactions that:

- involve advertising similar to the advertising in the barter transaction;
- occur frequently;
- represent a predominant number of transactions and amount when compared to all transactions to provide advertising that is similar to the advertising in the barter transaction;
- involve cash and/or another form of consideration (such as marketable securities, non-monetary assets, and other services) that has a reliably measurable fair value; and
- do not involve the same counter party as in the barter transaction.

12.8 SIC 32: Intangible Assets - Website Costs

SIC 32 is effective from 25 March 2002

References

IAS 38, Intangible Assets

Summary

SIC 32 concludes that a website developed by an enterprise using internal expenditure, whether for internal or external access, is an internally generated intangible asset that is subject to the requirements of IAS 38, Intangible Assets.

SIC 32 identifies the following stages of website development:

- Planning
- Application and infrastructure development
- Content development
- Operating

SIC 32 addresses the appropriate accounting treatment for internal expenditure on each of those stages of development and operation:

(a) A website arising from development should be recognised as an intangible asset if, and only if, in addition to complying with the general requirements described in IAS 38.19 for recognition and initial measurement, an enterprise can satisfy the requirements in IAS 38.45. In particular, an enterprise may be able to satisfy the requirement to demonstrate how its website will generate probable future economic benefits under IAS 38.45(d)

when, for example, the website is capable of generating revenues, including direct revenues from enabling orders to be placed. An enterprise is not able to demonstrate how a website developed solely or primarily for promoting and advertising its own products and services will generate probable future economic benefits, and consequently all expenditure on developing such a website should be recognised as an expense when incurred.

(b) Any internal expenditure on the development and operation of an enterprise's own website should be accounted for in accordance with IAS 38. The nature of each activity for which expenditure is incurred (eg training employees and maintaining the website) and the website's stage of development or post-development should be evaluated to determine the appropriate accounting treatment. For example:

- Planning. The Planning stage is similar in nature to the research phase in IAS 38.42-.44. Expenditure incurred in this stage should be recognised as an expense when it is incurred.
- Application and Infrastructure Development. The Application and Infrastructure Development stage, the Graphical Design stage and the Content Development stage, to the extent that content is developed for purposes other than to advertise and promote an enterprise's own products and services, are similar in nature to the development phase in IAS 38.45-.52. Expenditure incurred in these stages should be included in the cost of a website recognised as an intangible asset in accordance with this Interpretation when the expenditure can be directly attributed, or allocated on a reasonable and consistent basis, to preparing the website for its intended use. For example, expenditure on purchasing or creating content (other than content that advertises and promotes an enterprise's own products and services) specifically for a website, or expenditure to enable use of the content (such as a fee for acquiring a licence to reproduce) on the website, should be included in the cost of development when this condition is met. However, in accordance with IAS 38.59, expenditure on an intangible item that was initially recognised as an expense in previous financial statements should not be recognised as part of the cost of an intangible asset at a later date (for instance, when the costs of a copyright have been fully amortised, and the content is subsequently provided on a website).
- Content Development. Expenditure incurred in the Content Development stage, to the extent that content is developed to advertise and promote an enterprise's own products and services (such as digital photographs of products) should be recognised as an expense when incurred in accordance with IAS 38.57(c). For example, when accounting for expenditure on professional services for taking digital photographs of an enterprise's own products and for enhancing their display, expenditure should be recognised as an expense as the professional services are

received during the process, not when the digital photographs are displayed on the website.

- Operating. The Operating stage begins once development of a website is complete. Expenditure incurred in this stage should be recognised as an expense when it is incurred unless it meets the criteria in IAS 38.60.

(c) A website that is recognised as an intangible asset under SIC 32 should be measured after initial recognition by applying the requirements of IAS 38.63-.78. The best estimate of a website's useful life should be short.

13. US GAAPS

GAAP refers to accounting policies and procedures that are widely used in practice. Unlike India where accounting has its basis in law, US GAAP has evolved to be a collection of pronouncements issued by particular accounting organisation. US GAAPs are the accounting rules used to prepare financial statements for publicly traded companies and many private companies in the United States. Generally accepted accounting principles for local and state governments operates under a different set of assumptions, principles, and constraints, as determined by the Governmental Accounting Standards Board (GASB).

In the United States, as well as in other countries practicing under the English common law system, the government does not set accounting standards, in the belief that the private sector has better knowledge and resources. The Securities and Exchange Commission (SEC) has the ultimate authority to set US accounting and financial reporting standards for public (listed) companies. The SEC has delegated this responsibility to the private sector led by the Financial Accounting Standards Board (FASB). Other private sector bodies including the American Institute of Certified Public Accountants (AICPA) and the FASB's Emerging Issues Task Force (EITF) also establish authoritative accounting standards in the United States. Interpretations of the Financial Accounting Standard Board (FIN) also provide implementation and interpretation guidance. The SEC has the statutory authority to establish GAAP for filings made with it. While allowing most of the standard settings to be done in the private sector, the SEC is still very active in both its oversight responsibility as well as establishing guidance and interpretations, as it believes appropriate. US GAAP have the reputation around the world of being more prescriptive and detailed than accounting standards in other countries. In order to organise and make clear what is meant by US GAAP, a GAAP hierarchy has been established which contains four categories of accounting principles. The sources in the higher category carry more weight and must be followed when conflicts arise. The table given below summarises the current GAAP hierarchy for financial statements of non-governmental entities.

Established Accounting Principles in the US

Category (a)	Financial Accounting Standards Board (FASB) Statements and Interpretations, American Institute of Certified Public Accountants

	(AICPA), Accounting Principles Board (APB) Opinions, and AICPA Accounting Research Bulletins (ARB).
Category (b)	FASB Technical Bulletins, cleared AICPA Industry Audit and Accounting Guides, and cleared AICPA Statement of Position (SOPs).
Category (c)	Consensus positions of the FASB Emerging Issues Task Force (EITF) and cleared Accounting Standards Executive Committee of the AICPA (ACSEC) Practice Bulletins.
Category (d)	AICPA Accounting Interpretations, FASB Implementation Guides (QSAs), and widely recognised and prevalent industry practices.
Other Accounting	Other accounting literature, including FASB concepts statements,
Literature	APB Statements; AICPA Issues Papers; International Accounting Standards Committee Statements; Pronouncements of other professional associations or regulatory agencies; AICPA Technical Practice Aids; and accounting textbooks, handbooks, and articles.

The US GAAP provisions differ somewhat from International Financial Reporting Standards though efforts are underway to reconcile the differences so that reports created under international standards will be acceptable to the SEC for companies listed on US markets.

13.1 AICPA

The AICPA sets *generally accepted* professional and technical standards for CPAs in many areas. Until the 1970's, the AICPA held a monopoly in this field. In the 1970's, however, it transferred its responsibility for setting generally accepted accounting principles (GAAP) to the newly formed Financial Accounting Standards Board (FASB.) Following this, it retained its standards setting function in areas such as financial statement auditing, professional ethics, attest services, CPA firm quality control, CPA tax practice and financial planning practice. Before passage of the Sarbanes-Oxley law, AICPA standards in these areas were considered "generally accepted" for all CPA practitioners.

Accounting Principles Board (APB) Opinions were published by Accounting Principles Board (APB). APB was the main organization setting the US GAAP and its opinions are still an important part of it.

13.2 FASB

The Financial Accounting Standards Board (FASB) is a private, not-for-profit organization whose primary purpose is to develop generally accepted accounting principles in the United States (US GAAP). The FASB's mission for the private sector is similar to that of the Governmental Accounting Standards Board (GASB) for local and state governments in the United States. The FASB was created in 1973, replacing the Accounting Principles Board of the American Institute of Certified Public Accountants (AICPA). The FASB's mission is "to

establish and improve standards of financial accounting and reporting for the guidance and education of the public, including issuers, auditors, and users of financial information."

The U.S. Securities and Exchange Commission (SEC) has statutory authority to establish financial accounting and reporting standards for publicly held companies under the Securities Exchange Act of 1934. The SEC designated the FASB as the organization responsible for setting accounting standards for public companies in the U.S.

FASB has so far issued 158 Statements of Financial Accounting Standards (FAS).

13.3 COMPONENTS OF US GAAP

Given below are important components of US GAAP:

- FASB Statement of Financial Accounting Standards (FAS).
- FASB Interpretations (FIN).
- FASB Statements of Financial Accounting Concepts(FAS Conc.).
- FASB Technical Bulletins (FTB).
- AICPA Accounting Research Bulletins (ARB).
- AICPA Accounting Principles Board Opinions (APB Opinions)
- AICPA Accounting Interpretations (AIN).

Not only there are an extremely large number of different standards under US GAAP, the volume and complexity is also increasing. This complexity of US GAAP makes it critically important that the independent accountants that are assisting a company in filing with the SEC are knowledgeable and experts in US GAAP.

14. Financial Statements as per US GAAP

14.1 Basic Objectives

Financial reporting prepared on the basis of US GAAP should provide information:

- useful to present to potential investors and creditors and other users in making rational investment, credit, and other financial decisions.
- helpful to present to potential investors and creditors and other users in assessing the amounts, timing, and uncertainty of prospective cash receipts.
- about economic resources, the claims to those resources, and the changes in them.

14.2 Financial Statement Requirements

14.2.1 For US GAAP Financial Statements: US GAAP Financial Statements comprise of (i) Statements of income with comparatives of the preceding two accounting periods; (ii) statements of cash flows with comparatives of the preceding two accounting periods; (iii) statements of changes in shareholders' equity with comparatives of the preceding two accounting periods; (iv) statements of comprehensive income with comparatives of the

preceding two accounting periods and (v) Balance Sheet with comparatives of one preceding accounting period.

14.2.2 For Non-US GAAP Financial Statements: The basic financial statements for a non-US company are the same as that of a US company: three years of statements of income, statements of cash flows, statements of changes in shareholders' equity and statements of comprehensive income and two years of balance sheets.

Some companies have not registered with the SEC due to the so-called "reconciliation requirement." Non-US companies are allowed to prepare their financial statements using any comprehensive basis of generally accepted accounting principles (GAAP). However, if US GAAP is not used, a reconciliation from the foreign GAAP to US GAAP must be included as a part of the audited financial statements

14.3 Reconciliation Requirements

US Securities and Exchange Commission has prescribed Form 20-F, Item 17 of which requires:

- Description of differences between foreign GAAP and US GAAP
- Reconciliation of net income from foreign GAAP to US GAAP
- Reconciliation of the balance sheet i.e., differences in each asset/liability between foreign GAAP and US GAAP – usually presented in the form of a reconciliation of shareholders' equity.
- Reconciliation of a statement of cash flows between foreign GAAP to US GAAP.
- Disclosure of earnings per share under US GAAP

Item 18 of Form 20-F requires

The same information as required by Item 17 plus all the disclosures required by US GAAP and Regulation S-X – e.g., information on segments, pensions, taxes, fair value of financial instruments, etc.

Companies are required to comply with Item 18 in all capital raising transactions of non-investment grade securities. Item 17 can be used in many other situations including annual reports. As a matter of practice, however, most companies elect to use Item 18 for all filings. Compliance with item 18 allows the company to have continued access to the US market without a delay that could result from preparing the required US GAAP disclosures.

Currently, non-US companies have the option of preparing the statement of comprehensive income using either Foreign GAAP or US GAAP. If the company elects to present this statement using Foreign GAAP, the staff encourages, but does not require, the disclosure of comprehensive income under US GAAP.

15. Major Issues Discussed by Various US GAAPS - An Overview

Before a set of US GAAP financial statements is presented, it is intended to discuss certain basic concepts, which are followed in the preparation of US GAAP financial statements.

15.1 Balance Sheet Classification

For a proper classified balance sheet, an enterprise should classify the balance sheet items into current and non-current items. This type of classified balance sheet helps to determine the working capital readily. For accounting purposes, current assets are those assets, which are reasonably expected to be realized in cash, or sold or consumed during the normal operating cycle of the business i.e. normally a year. The term 'current liabilities' is used principally to designate obligations whose liquidation is reasonably expected to require the use of existing resources (properly classifiable as current assets) or the creation of other current liabilities.

However, enterprises in several specialized industries including broker dealers, real estate, life insurance companies for which current / non-current classification has not much relevance may prepare unclassified balance sheet.

Given below are the concepts of current assets, current liabilities and operating cycle:

Items of Current Assets

(a) Trade Accounts, notes, and acceptances receivable;

(b) Cash available for current operations and items which are the equivalent of cash;

(c) Inventories of merchandise, raw materials, goods in process, finished goods, operating suppliers and ordinary maintenance materials and parts;

(d) Receivables from officers, employees, affiliates, and others if collectible in the ordinary course of business within a year;

(e) Marketable securities representing the investment of cash available for current operations;

(f) Instalment of deferred accounts and notes receivable if they conform generally to normal trade practices and terms within the business; and

(g) Pre-paid expenses such as insurance, interests, rents, taxes unused royalties, current paid advertising service not yet received and operating suppliers.

Prepaid expenses are not current assets in that sense that they will be converted into cash within normal operating cycle. But, they represent use of current assets during the operating cycle, if not paid in advance.

Items excluded from Current Assets

(a) Land and other natural resources.

(b) Depreciable assets

(c) Receivables arising from unusual transactions such as sale of capital assets, or loans or advances to affiliates, officers or employees which are not expected to be collected within a period of twelve months.

(d) Cash surrender value of insurance policies.

(e) Investments in securities (whether marketable or not) or advances which have been made for the purposes of control, affiliation, or other continuing business advantage.

(f). Cash and claims to cash which are restricted as to withdrawal or use for other than current operations. They are designated for expenditure in the acquisition or construction of non-current assets or used for liquidation of long term debts.

(g) Long term pre-payments which are fairly chargeable to the operations of several years, or deferred charges such as unamortised debt discount and expense, bonus payments under a long term lease, costs of management of factory lay out or removal to a new location, and certain types of research and development expenses.

Meaning of Operating Cycle

The ordinary operations of a business involved a circulation of capital within the current asset group. The average time intervening between the acquisition of materials or services entering the process and the final cash realization constitutes an operating cycle. In case several operating cycles occurring within a year, a one-year period is to be used as a basis for the segregation of current assets.

However, the period of operating cycle is more than twelve months, the longer period should be used. Where a particular business has not clearly defined operating cycle, the one year rule should govern.

Items of Current Liabilities	(a)	Collections received as advance of the delivery of goods or performance of services.
	(b)	Debts, which arise from operations directly, related to the operating cycle, such as accruals for wages, salaries, commissions, rentals, royalties and income and other taxes
	(c).	Payable incurred in the acquisition of materials or supplies to be used in the production of goods or in providing services to be offered for sale.
	(d)	Other liabilities whose regular and ordinary liquidation is expected to occur within a relatively short period of time, usually twelve months. For example short term debt arising from acquisition of capital assets, serial maturities of long term obligations, amount required to be expected within one year under sinking fund provisions.
	(e)	Estimated or accrued amounts which are expected to be required to cover expenditures within the year for known obligations, i.e., provision for bonus, provision for product warranty.
Items excluded from current liabilities	(a)	Contractual obligation falling at an early date which is expected to be refunded.
	(b)	Debts to be liquidated by funds which have been accumulated in accounts of a type not properly classified as current assets.

It also includes long term obligations that are or will be callable by the creditor either because the debtor's violation of provision of the debt agreement at the balance sheet date makes the obligation callable or because the violation, if not cured within a specified grace period, will make the obligation callable. Such callable obligations are to be classified as current liabilities unless one of the following conditions is met:

(a) The creditor has waived or subsequently lost the right to demand repayment for more than one year (or operating cycle, if longer) from the balance sheet date;

(b) For long term obligations containing a grace period within which the debtor may cure the violation, it is probable that the violation will be cured within that period, thus preventing the obligation from becoming callable.

Classification of Short Term Obligations Expected to be Refinanced [FAS 6]: Some short term obligations that are expected to be refinanced on a long term basis are not expected to use enterprise's working capital. Examples include commercial paper, construction loan, etc. Refinancing a short obligation on a long term basis means either replacing it with a long term obligation or with equity securities or renewing, extending or replacing it with short term obligations for an uninterrupted period extending beyond one year from the date of an enterprise's balance sheet.

15.2 Balance Sheet Display

The offsetting of related assets and liabilities in the balance sheet is permitted only when there is a right to set off.

A right to set off is debtor's local right, by contract or otherwise, to discharge all or a portion of the debt owed to another party by applying against the debt an amount that the other party owes to the debtor. A right to set off exists when these four conditions are met:

- Each of the two parties owes the other determinable amount;
- The reporting party has the right to set off the amount owed by the other party;
- The reporting party intends to set off;
- The right of set off is enforceable in law [Para 5, FIN 39].

Generally debts may be set off if they exist between mutual debtors each, acting in the capacity as both debtor and creditor. However, State laws about the right to set off may be different from those normally provided by the contract or as a matter of common law. Legal constraint should be taken into account to determine whether right to set off exists.

Offsetting Government Securities Against Tax Payable: Generally, tax payable is not an offset against cash or other assets. Most of the government securities are not by their terms designed for the payment of tax. In exceptional circumstances the purchase of government securities may be acceptable for the payment of taxes. Only in those cases off-set is allowed.

Offsetting Forward, Interest Rate Swap, Currency Swap, Option and Other Conditional or Exchange Contracts: Fair value of those contracts or an accrued receivable or payable arising from those contracts, rather than the notional amount or amounts to be exchanged, is recognized in the balance sheet. Unless the four conditions stated in Para 5, FIN 39 are met, the fair value of contracts in loss position should not be offset against the fair value of contracts in a gain position. Similarly, amounts recognized as accrued receivables should not be off-set against amounts recognized as accrued payable unless a right to setoff exists.

There is special Guidance for master netting arrangement. It means existence of multiple contracts, whether for the same type of conditional or exchange contract or for different types of contracts, with a single counterparty that are subject to a contractual agreement. Such an agreement provides for the net settlement of all contracts through a single payment in single currency in the event of default or on termination of any one contract.

When fair value amounts recognised for forward, interest rate swap, currency swap, option and other conditional or exchange contracts are executed with same counterparty under a master netting arrangement, they are offset items. The reporting entity has to find out net fair value of the position under master netting arrangement and report it as an asset or liability in the Balance Sheet.

15.3 Comprehensive Income

One important feature of US GAAP financial statements is the computation of comprehensive income. Items of income statement can be classified into two categories – (i) those which are included in computing current operating performance (or dirty surplus) and (ii) those which are included in computing all-inclusive performance of the current period (clean surplus). For the measurement of current operating performance extraordinary and non-operating gains and losses are excluded from income. On the contrary, for the purpose of measurement of all-inclusive performance all revenues, expenses, gains and losses are recognized during the period and included in income regardless of whether they are considered to be result of operations of the period.

Generally, all inclusive income measurement is followed in the US GAAP with the exceptions that certain changes in assets and liabilities are not reported in the income statement. Such changes are included in the separate component of equity in the Balance Sheet.

FAS 130 discusses how to report and display comprehensive income and its components. Given below are the important features of FAS 6:

Issues	*Para References to FAS 130*	*Description*
Definition	8-10	The change in equity of a business enterprise during a period from transactions and other events and circumstances from non-owner sources. It includes all changes in equity during a period except those resulting from investments by owners and distributions to owners. Comprehensive income includes net income and other items. Net income means a measurement of financial performance resulting from the aggregation of revenues, expenses, gains and losses that are not items of other comprehensive income. Other comprehensive income means revenues, expenses, gains and losses that under generally accepted accounting principles are included in comprehensive income but excluded from net income.
Classifications within net income	16	Items classified under net income are displayed under various classifications: (i) Income from continuing operations; (ii) Income discontinuing operations; (iii) Extraordinary Items; and

		(iv) Cumulative effects of changes in accounting principle.
Classifications within net income	17	Items under other comprehensive income are classified by their nature. for example: (i) Foreign currency items; (ii) Minimum pension liability adjustments; (iii) Unrealized Gains and Losses on Certain Investments in debt and equity securities. Additional classification may arise from future accounting standards.
Classifications within comprehensive income	15	Comprehensive income is divided into two components (i) Net Income and (ii) Other Comprehensive Income. If an enterprise that does not have any item of other comprehensive income in any period presented is not required to report comprehensive income. All components of comprehensive income is reported in the financial statements in the period in which they are recognized.
Reclassification adjustments	18-21	Adjustments are made to avoid double counting comprehensive income. For example, when an investment security is realized, realized gain or loss occurs. There may be unrealized gain or loss already recognized against this income in other comprehensive income in any of the prior periods. So when realized gain/loss on realization of an investment security is recognized in the net income, appropriate portion of the unrealized gain/loss should eliminated from other comprehensive income. This adjustment is termed as "reclassification adjustment". No reclassification adjustment is determined for minimum pension liability. Reclassification adjustment for foreign currency translation is limited to translation gains/losses realized upon sale or complete/substantially complete liquidation of an investment in a foreign entity. An enterprise may display reclassification adjustments in the face of the financial statements in which comprehensive income is presented or by notes.

Other comprehensive income – This term refers to revenues, expenses, gains or losses that are excluded in the net income under generally accepted accounting principles but included in the comprehensive income. Under current accounting standards, items of other comprehensive income are-

- *Foreign currency translation adjustments:* If an entity's functional currency is a foreign currency, translation adjustments result from the process of translating that entity's financial statements into reporting currency. Translation adjustments shall not be included in determining net income but shall be reported in other comprehensive income. [FAS 52, Para 13].
- Gains and losses on foreign currency transactions that are designated as, and are effective as, economic hedges of a net investment in a foreign entity, commencing as of the designation date. Such gains or losses shall not be included in determining net income but shall be reported in other comprehensive income.
- Gains or losses on inter-company foreign currency transactions that are of a long term investment nature (i.e., settlement is not planned or anticipated in the foreseeable future), when the entities to the transaction are consolidated, combined, or accounted for by the equity method in the reporting enterprise's financial statements. Such gains or losses shall not be included in determining net income but shall be reported in other comprehensive income.
- The effective portion of the gain or loss on derivative instruments designated and qualifying as cash flow hedging instrument is reported as a component of other comprehensive income. [Para 30(b)(2), FAS 133]/
- Unrealized gains or losses for trading securities shall be included in earnings. Unrealized holding gains or losses for "available for sale" securities shall be excluded from earnings and reported in other comprehensive income until realized [Para 13, FAS 115].
- However, all or a portion of the unrealized holding gain or loss of an "available for sale" securities that is designated as being hedged in a fair value hedge are recognized in earnings for the period.
- For a debt security transferred into the "available for sale" category from the "held to maturity" category, the unrealized holding gain or loss at the date of transfer is reported in other comprehensive income [Para 33 (b), FAS 130].
- For individual securities classified as either "available for sale" or "held to maturity", it is necessary to determine whether a decline in fair value below amortized cost is "other than temporary". If it is probable that the investor will be unable to collect all amounts due according to the contractual terms of debt security not impaired at acquisition, it is considered that "other than temporary" impairment has occurred. In case the decline is

"other than temporary" in nature, individual security will be written down to fair value and such a fair value is taken on new cost basis.

- Subsequently, if fair value increases, net cost basis is not changed. Subsequent increase in fair value for "available for sale" securities is included in other comprehensive income. [Para 534(d), FAS 133. Para 16, FAS 115 and Para 33(d), FAS 130].
- Net loss recognized pursuant to pension cost as per para 36, FAS 87 as an additional pension liability not yet recognized as net periodic pension cost is included in other comprehensive income

15.4 Results of Operations

Financial Accounting Standards Board concludes that the results of continuing operations should be reported separately from discontinued operations. Also gain or loss from disposal of a segment of a business is included along with the results of discontinued operations. Presentation of an Income Statement distinguishing continuing and discontinuing operations would appear as follows:

Particulars		
Income from continuing operations before income taxes	XXXX	
Provision for Income Taxes	XXX	
Income from Continuing Operations		XXXX
Discontinued Operations:		
Income (Loss) from Operations of Discontinued Division	XXXX	
Loss on Disposal of Division X, including provision for Operating Losses during phase out period less	XXX	
Net Income		XXXX

Extraordinary items should be separately presented in the Income Statement:

In the absence of discontinuing operations and changes in accounting principles, the following main captions should appear in the Income Statement if extraordinary items are reported:

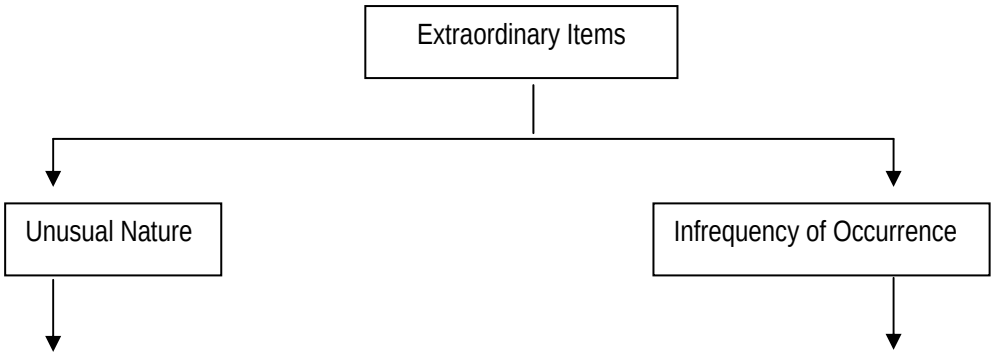
Particulars	
Income before Extraordinary Items	XXXX
Extraordinary items less applicable Income Taxes	XXX
Net Income	XXXX

- The caption extraordinary items should be used to identify separately the effects of events and transactions and other disposal of business.

- Descriptive captions and amounts for individual extraordinary events and transactions should be presented preferably on the face of the income statement. Alternatively, amount and nature of different extraordinary items should be disclosed by way of notes.
- Income tax applicable to extraordinary items should be presented preferably on the face of the income statement. Alternatively, amount of income tax effect on extraordinary items should be disclosed by way of notes.

15.5 Extraordinary Items

Extraordinary items are events and transactions that are distinguishing by their unusual nature and infrequency of occurrence. Two criteria for the identification of extraordinary items are (i) unusual nature and (ii) infrequency of occurrence.



Transaction should possess a high degree of abnormality and be of a type clearly unrelated to, or only incidentally related to, the ordinary and typical activities of the entity.

What should be considered to determine unusual nature of a transaction?

Type of scope of operations

The environment in which an enterprise operates is the primary consideration to determine whether a transaction or event is abnormal.

Environment includes industry in which the enterprise operates, it s geographical locations and government regulation within which it operates

Identification criteria should not include a factor whether transaction or event is beyond the control of the management.

Events of transactions should be of a type that would not reasonably be expected to recur in the foreseeable future.

Probability of occurrence of an event or transactions should be taken into consideration.

Same transaction or event may have different probability of occurrence to different enterprises.

Mere infrequency of occurrence should not be sole criteria for identifying extraordinary items.

On the other hand, a transaction or event although of unusual nature, but frequently occurs in the environment in which an enterprise operates. So that item cannot be identified as extraordinary item.

Examples of Extraordinary Items – The following items should not be reported as extraordinary items:

(a) Write down or write off of receivables, inventories, equipment leased to others, deferred research and development costs or other intangible assets.

(b) Gains or losses from exchange or translation of foreign currencies, including those relating to major devaluations or revaluations.

(c) Gains or losses on disposal of business segment.

(d) Other gains or losses from sale or abandonment of property, plant or equipment used in the business.

(e) Effect of a strike.

(f) Adjustment of accruals on long term contracts.

In rare situations an event or transaction may meet both the criteria of unusual nature and infrequency of occurrence and gains or losses may arise therefrom. Such gains and losses include gains or losses stated in items (a) to (d) above. When such items occur in the ordinary course of valuation, they are not regarded as extraordinary items but when the circumstance is different, they may be regarded as extraordinary items. For example, when such gains or losses occur as direct result of major casualty like an earthquake, an expropriation, or a prohibition under a newly enacted law or regulation that clearly meets the two criteria specified above, it is treated as an extraordinary item.

Materiality and Aggregation: Individual extraordinary item should be material in relation to income before extraordinary item. If an extraordinary item is material in relation to income before extraordinary item or to the trend of annual earning before extraordinary item, it should be separately disclosed on the face of the income statement as an extraordinary item. Materiality of extraordinary items is evaluated item-wise. However, the effect of series of related transactions arising from a single specific unusual event of infrequent nature should be aggregated to test the materiality.

A material event or transaction that is either of unusual nature or of infrequent nature shouldbe disclosed on the face of income statement separately as a component of income from continuing operations. Such an event or transaction should not be classified as an extraordinary item.

15.6 Disposal of Business Segment

Disposal may be by way of sale or abandonment. The plan of disposal should include to the minimum-

- Identification of the major assets to be disposed of;
- Expected method of disposal;

- period expected to be required for completion of disposal;
- An active programme to find a buyer if disposal is by sale;
- The estimated results of operations of the segment from the measurement date to the disposaldate;
- Estimated proceeds or salvage to be realized by disposal.

Disposal date is the date on which sale is closed if the disposal is by sale. If the disposal is by abandonment, it is the date on which operation ceases.

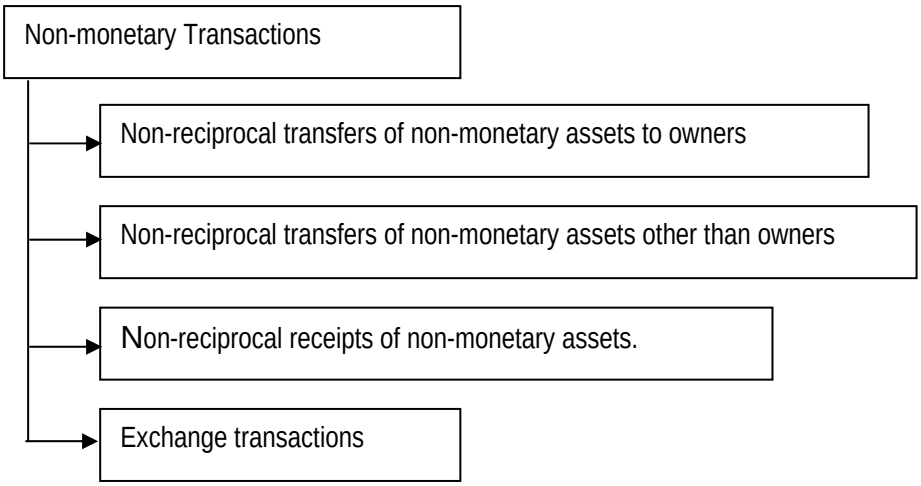
How to measure gain or loss on disposal of a business segment?

Issues	Description
Step 1: Estimate net realizable value	Estimates are made at the measurement date about the net realizable value of the business segment which is to be disposed of.
Find out loss/gain on disposal	Expenses to be incurred for the disposal is considered while determining the net realizable value. Determine the loss comparing net realizable value with the carrying amount of net assets. Provision is created for such loss. Gain is not recognized until realized.
Step 2: If the plant of disposal is to be carried out over a period of time and business is to be continued during that period.	(a) There may be estimated loss taking into account revenues and expenses for continuing operations between the measurement date and disposal date. Such loss is included in lthe loss computed in Step 1. (b) There may be estimated gain arising out of continuing business during the measurement date and the disposal date. Such gain should be taken into account to the extent of loss estimated in Step 1. Any gain above that should be recognized as and when realized.
General Principle	Gain or loss should be limited to those amounts that can be projected with reasonable accuracy.
Costs and expenses directly associated with disposal	Generally, it is expected that the plan of disposal will be carried out within a period of one year from the measurement date.

	Includes- ♦ Severance pay ♦ Additional pension cost ♦ Employee relocation expenses Future rentals on long term leases.
Disclosures by way of notes	This is in addition to provision for estimated loss on disposal shown in the income statement as component of discontinued operations: ♦ Identity of the business segment to be disposed of; ♦ Expected disposal date, if known; ♦ Expected manner of disposal; ♦ A description of the remaining assets and liabilities of the segment planned to be disposed of; ♦ Income or loss from thesegment between the measurement date and the balance sheet date. Such information should accompany data of prior estimates.

15.7 Non-Monetary Transactions

APB Opinion No.29 is the principal document in this regard. Let us first understand the meaning of the term non-monetary transactions. Such transactions are classified into four types:



Monetary assets are assets whose amounts are fixed in terms of units of currency. Examples are cash, receivables, notes payable in cash, etc. Non-monetary assets are, on the contrary, which are not monetary assets.

Non-reciprocal transfer means transfer of assets or services in one direction. This may be from the enterprise to the owner or any other entity. On the other hand, this may be from the owner or other entity to the enterprise.

Non-reciprocal transfers with owners	Examples: Distribution of non-monetary assets to stockholders as dividends; Distribution of non-monetary assets to stockholders for redemption or acquisition of outstanding capital stock; Distribution of non-monetary assets to a group of stockholders pursuant to a plan of rescission or other settlements relating to a prior business combination.
Non-reciprocal transfers with other than owners	Example: Contribution of non-monetary assets by an enterprise to a charitable organization.
Non-reciprocal receipts of non-monetary assets from other than owners	Example: Land received from Government free of cost.
Exchange Transactions	Exchange of non-monetary assets between the enterprise and another entity other than stockholders.

Measurement and accounting-

- In general, accounting for non-monetary transactions should be based on the fair values of the assets (services) involved. This is same basis as is used for monetary transactions. This means cost of a non-monetary asset acquired in exchange of another non-monetary asset between an enterprise and another entity is the fair value of assets surrendered. For example, X Ltd. wants to exchange a Building A carried at cost less depreciation ₹ 10 lacs for another Building B. The fair value of the Building a to be surrendered is ₹ 25 lacs. So the cost of the Building B should be taken at ₹ 25 lacs and gain of ₹ 15 lacs should be recognized.
- Fair value of the asset received should be adopted as the basis if that is more clearly evident than the fair value of asset surrendered. In case fair value of Building A is not available, whereas fair value of Building B is available through competitive quotations. Fair value of Building B is ₹ 22 lacs. In such a case, the transaction should be recorded at fair value of non-monetary asset received.

- Similarly, a non-monetary asset received in a non-reciprocal transfer should be recorded at the fair value of asset received.
- A non-monetary asset transferred to stockholders or any other entity in a non-reciprocal transfer should be recorded at fair value of the asset transferred. Gain or loss is accordingly recognized taking the difference between the fair value and carrying amount.
- The fair value of an entity's own stock re-acquired may be a more clearly evident measure of the fair value of the non-monetary asset distributed to acquire stock for treasury or for retirement.
- Disclosure: Nature of non-monetary transactions should be disclosed in the financial statements.

However, in cases there may be a need for modification of the above stated principle:

- Accounting for non-monetary transaction should not be based on the fair values of the assets transferred unless those fair values are determinable within reasonable limits. Fair values are determined with reference to estimated realizable value in a cash transaction of the same or similar assets or services received in exchange. Fair value is regarded as not determinable within reasonable limits if major uncertainties exist about the realisability of the value of the asset.
- In case fair value of the non-monetary asset received or surrendered cannot be determined within a reasonable limit, then the transaction should be recorded at the carrying amount of the asset surrendered.
- That apart, if the exchange is not essentially the culmination of the earning process, accounting for an exchange of a non-monetary asset between the enterprise and another entity should be recorded at the carrying amount of the asset surrendered. Two examples are cited in APB Opinion No.29 to explain the exchanges that do not culminate in the earning process:

    1. An exchange of product or property held for sale in the ordinary course of business for a product or property to be sold in the same line of business to facilitate sales to customers other than the parties to exchange.
    2. An exchange of productive assets not held for sale in the ordinary course of business for a similar productive asset or an equivalent interest in the same or similar productive asset.

Involuntary Conversion – Sometimes non-monetary assets are converted involuntarily to monetary assets. Example is acquisition of land by Government. The gain or loss on such a conversion is the difference between the carrying amount of the non-monetary asset and the amount received. However, when an involuntary conversion takes place and subsequently, the monetary asset is used to acquire another non-monetary asset, these two sets of transactions although linked but for accounting purposes they are separate and independent transactions. Accordingly, they should be regarded as two sets of monetary transactions.

15.8 Transactions with Related Parties

Related parties include transactions between (a) parent company and subsidiary, (b) subsidiaries of a common parent; (c) an enterprise and trust for the benefit of common parent; (d) an enterprise and its principal owners, management, or members of their immediate families and (e) affiliates.

Important terms are defined as follows:

Terms	Definition
Principal Owners	Owners of more than 10% of the voting interest of the enterprise.
Management	Persons who are responsible for achieving objectives of the enterprise and who have authority to establish policies and make decisions by which the objectives are achieved. Management normally includes board of directors, the chief executive officer, chief operating officer, vice president in charge of principal business functions and other persons who perform similar policy making functions.
Immediate family	Family members who the principal owner or member of management may control or influence or get controlled or influenced because of family relationship
Control	The possession, direct or indirect, of the power to direct or cause the direction of the management and policies of an enterprise through ownership, by contract or otherwise.
Affiliate	A party that, directly or indirectly through one or more intermediaries, controls or is controlled by, or is under common control with an enterprise.

Related party transactions – Transactions between related parties occur in the normal course of business. Some examples of common type of related party transactions are-

- Sales, purchases and transfers of personal property;
- Services received or furnished, [Accounting, management, engineering and legal services];
- use of property and equipment by lease or otherwise;
- Borrowings and lending;
- Guarantees;
- Maintenance of bank balances as compensating balances for another;
- Inter-company billing based on allocations of common costs;
- Filing of consolidated tax returns.

Transactions with related parties are considered even if there is accounting recognition. If a parent renders some service to its subsidiary free of cost, which both the parties do not recognize, still the transaction should be considered as related party transaction.

Disclosures – Related party transactions should be disclosed in the financial statements except for those which are eliminated for the purpose of consolidation.

Disclosures include:

(a) Nature of related party relationship;

(b) Description of the transactions including the transactions in which no amounts or nominal amounts are ascribed;

(c) Amount of the transaction; and

(d) Amount due from or to related parties.

When there exists common ownership or common control that affect the operating results or financial position of the enterprise as compared to a situation wherein control exists, it is necessary to disclose such relationship even if no transaction occurred between the parties.

15.9 Consolidation

Consolidated financial statements are primarily presented for the benefit of the shareholders and creditors of the parent company, the results of operations and the financial position of a parent company and its subsidiaries essentially as if the group were a single enterprise with one or more branches or division. Consolidated financial statements are prepared when there is ownership of majority interest characterized by direct or indirect ownership of more than fifty per cent voting shares. However, there are exceptions to this general rule:

- A subsidiary is not consolidated where control is likely to be temporary;
- A subsidiary is not consolidated where it does not rent with the majority owners (for example, if the subsidiary is in legal reorganization or in bankruptcy);
- There may be a situation wherein minority interest is so large in relation to the equity of the shareholders of the parent in the consolidated net assets, that the presentation of separate financial statements of the two companies are more meaningful and useful (withdrawn by FAS 94).

In deciding the consolidation policy, the aim should be to make the financial presentation meaningful. The user should be given information, which is suitable for decision making. Even though a group of companies is heterogeneous in character, it may be better to make full consolidation than to present large number of separate statements. On the other hand, separate statements may be preferable for a banking/insurance/finance subsidiary of a manufacturing company. This was the original position of the ARB 51. However, there was

an increasing tendency of "non-homogeneity" exception to avoid consolidation. This led to introduction of FAS 94 that demands consolidation of all majority owned subsidiaries except:

- A subsidiary is not consolidated where control is likely to be temporary;
- A subsidiary is not consolidated where it does not ret with the majority owners (for example, if the subsidiary is in legal re-organization or in brankruptcy);
- A subsidiary in which there are governmentally imposed uncertainties which cast significant doubt about the ability of the parent to control subsidiary.

In those exceptional cases, investment in subsidiaries is accounted for under cost method. Equity method accounting is followed for investments in common stock of corporate joint venture and investment in common stock for an investor that give rise to significant influence. Unincorporated joint venture and/or partnership are directly consolidated. EITF 85-28 explains that a special purpose subsidiary created to originate collateralized mortgage debt (which the parent company did itself) must be consolidated.

A difference in fiscal period of the parent and the subsidiary company does not justify the exclusion of consolidation. It is possible for a subsidiary to follow a fiscal year which is close to the fiscal year of the parent company. Generally, the difference in the fiscal year ending of the parent and the subsidiary should not be more than three months. in case it is more than three months, a disclosure should be made about the significant events which materially affect the financial position or results of operations.

Every consolidated financial statement should disclose the consolidation policy. It is possible to make it apparent by headings or other information, but in other cases it is given by way of footnotes.

Consolidation Procedure

Explained below is US GAAP consolidation procedure:

- Consolidation financial statements are prepared in a similar way for a pooling of interest as for a purchase.
- Stage by stage acquisition: When the parent purchases a subsidiary in more than one block, each acquisition is on a step-by-step basis. Consolidation is not done until control exists. Any goodwill or negative goodwill is determined at each step.
- Elimination of inter-company balances: Examples of inter-company balances are inter-company open account balances, security holdings, sales and purchases, interest, dividend, etc.
- Elimination of profit or loss on inter company transaction: This is applicable for assets remaining within the group. Complete elimination of profit or loss arising out of inter-company transactions on the assets remaining on the balance sheet date, which are consolidated, is required.

- Minority interest: It is the portion of minority stockholders' equity in the subsidiary. In the consolidated balance sheet minority interest is presented between the liability section and the stockholders' equity section. In case minority interest is insignificant, it is often included in other liabilities. Elimination of profit or loss in inter-company transaction is not affected by the existence of minority interest. In other words, unrealized profit in assets in the consolidated balance sheet arising out of inter-company transactions should be eliminated in full not to the extent of majority interest.
- If income tax has been paid on inter-company profit on assets remaining within the group, such taxes should be deferred. Alternatively, elimination of inter-company profit should be reduced appropriately.
- Unincorporated Subsidiaries: FAS 94 eliminated the requirement of pursuance of equity method accounting for unincorporated subsidiaries. When a majority owned subsidiary is not consolidated, equity method is considered to be the appropriate choice.

15.10 Cash Flow Statement

FAS 95 explains that information about cash flow is required to-

- Assess the enterprise's ability to generate positive future net cash flows;
- Assess the enterprise's ability to meet its obligation, its ability to pay dividend, and its needs for external financing;
- Assess the effects on an enterprise's financial position of both its cash and non-cash investing and financing transactions during the period. [Para 5, FAS 95].

Cash and Cash Equivalents

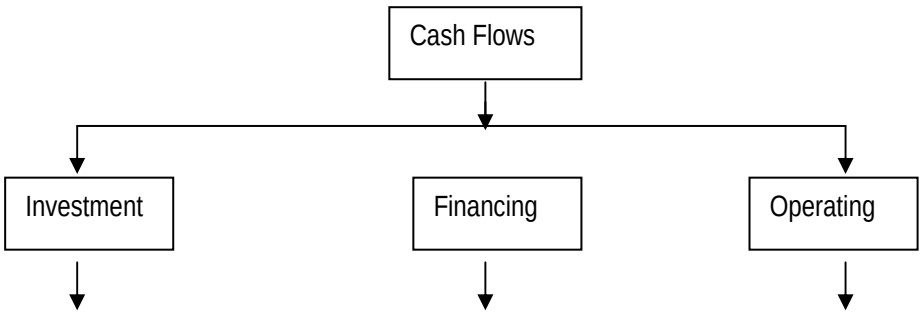
A statement of cash flow explains cash a nd cash equivalents rather than ambiguous term such as fund. Para 8, FAS 95 defined cash equivalents as short term highly liquid investments that are (a) readily convertible to known amounts of cash and (b) having insignificant risk of changes in value because of interest rate change as their maturity is very near. Generally, investments with original maturities of t here months or less qualify under this definition to be classified as cash equivalents. Examples are treasury bills, commercial paper, money market funds. Cash purchases and sales of these securities are part of the enterprise's cash management activities than classifying them as operating, financing or investment activities.

However, an enterprise is required to adopt a policy regarding classification of cash equivalents. it is not necessary to include all items that qualify the definition stated in Para 8, FAS 95 as cash equivalents for the purpose of preparation of cash flow statement. For example, a banking company may decide to classify all qualified investments as cash equivalents whereas a finance company, which largely invests in short-term securities, may like to classify such investments as investment activities. So, it is necessary to disclose the

policy adopted for classifying cash equivalents. Any change in such policy should be treated as change in accounting principles that shall be affected by restating financial statements for earlier years.

Cash Flow Classifications

In a statement of cash flow, various items of cash receipts and payment are classified into cash flows from investing, financing and operating activities.



Investment	Financing	Operating
It includes (i) making and collecting loans, (ii) acquiring and disposing of debt or equity instruments of other enterprise and (iii) acquiring and disposing of property, plant and equipment and other productive assets, i.e., assets held for use in the production of goods or services by the enterprise.	It includes (i) obtaining resources from owners and providing them with return on or return of their investments; (ii) borrowing money and repaying amounts borrowed or otherwise settling the obligations; and (iii) obtaining and paying for other resources obtained from creditors on long-term credit.	It includes (i) all transactions and other events that are not defined as investing or financing activities. It generally involves producing and delivering goods or services. Cash flows from operating activities are generally the cash effect of transactions and other events that enter into the determination of net income.
Cash Inflows: (i) Receipts from collections or sales of loans made by the enterprise; (ii) Receipts from collections or sales of other enterprise's debt instruments (other than cash equivalents) that were purchased by the enterprise; (iii) Receipts from sale of	Cash Inflows: (i) Proceeds from issuing equity instruments; (ii) Proceeds from issuing bonds, mortgages, notes, and from other short/long-term borrowings.	

property, plant and equipment and other productive assets;		
Cash flow from investing activities	Cash flow from financing activities	Cash flow from operating activities.
Cash outflows:	Cash Outflows:	Cash Outflows:
(i) Disbursements for loans made by the enterprise; (ii) Payments to acquire debt instruments of other entities;	(i) Payments of dividends and other distributions to owners, including outlays to reacquire the enterprise's equity instruments; (ii) Repayment of amounts borrowed; (iii) Other principal payments to creditors who have extended long-term credit.	(i) Cash payments to acquire materials for manufacturing or goods for resale, including principal payments on accounts and both short and long term notes payable to suppliers for those materials or goods; (ii) Cash payments to other suppliers and employees for goods and services; (iii) Cash payments to governments for taxes, duties, fines, other fees or penalties; (iv) Cash payments to lenders and other creditors for interest; (v) All other cash payments that do not stem from transactions defined as investing or financing activities such as payments to settle lawsuits, cash contributions to charities, and cash refunds to customers.

The following items qualify for net reporting (as their turnover is quick, amounts are large and the maturities are short):

- Investments other than cash equivalents;
- Loans receivables and
- Debt whose original maturities are three months or less. [Para 13, FAS 95].

15.11 Earnings per Share (EPS)

EPS is an important measure of corporate performance for investors and other users of financial statements. They generally are believed to be of value to investors in weighing the significance of a corporation's net income and of changes in its net income from period to period in relation to the shares the investors holds or may acquire. FAS 128 requires EPS information to be presented in the income statement of publicly held companies. An investment company or a wholly owned subsidiary company is not required to presents information regarding EPS.

Types of EPS

When potential reduction, called dilution, of EPS figures is inherent in a company's capital structure, a dual presentation of EPS is required namely:

1. Basic Earnings Per Share

$$\frac{\text{Income available to common stockholders}}{\text{Weighted average no. of common shares outstanding}}$$

Shares issued during the period and shares re-acquired during the period shall be weighted for the period they remained outstanding.

Income Available to Common Stockholders=

Continuing Operations	*Total*
Income from continuing operations	Net Income
Less: Dividends declared on preferred stock	*Less:* Dividends declared on preferred stock
Less: Dividend Accumulated on cumulative preferred stock	*Less:* Dividend Accumulated on cumulative preferred stock
Loss from continuing operations	Net Loss
Add: Dividend declared on preferred stock	*Add:* Dividends declared on preferred stock
Add: Dividend Accumulated on cumulative preferred stock	*Add:* Dividend Accumulated on cumulative preferred stock

Weighted average number of shares used as denominator of earning per share is simple average number of shares.

No. of shares outstanding	X	No. of Days outstanding
Si	X	Di

Weighted average No. of shares = $[\sum Si \times \sum Di] / \sum Di$

2. Diluted Earnings Per Share

When there are potential common shares in the capital structure of an enterprise, it requires to present diluted the earning share. For thep urpose of "diluted earning per share" computation, income is increased by dividend on convertible preferred stock and after tax interest cost on convertible debentures. Determination of diluted earning per share involves increases in denominator, as if the convertible instruments are outstanding from the beginning for the full year of convertible. Adjustments should be made certain contracts that give the issuer or holder with a choice of settlement method. Diluted EPS should be based on most advantageous conversion rate from the standpoint of the holders.

$$\frac{\text{Income Available to Common Stockholders} + \text{Effect of Assumed Conversions}}{\text{Weighted Average Shares} + \text{Dilutive Potential Common Shares}}$$

The computation of diluted earning per share does not cinlude assumed conversion of any securities that have antidilutive effect on the earning per share. For this purpose all potential common shares are tested separately for the impact of diluteness and those potential common shares are arranged from most dilutive and least dilutive. See Example 66.1.

15.12 Segment Reporting

Scope, Objectives and Basic Principles

FAS 131 requires public business enterprises to report certain information about operating segments in complete sets of financial statements of the enterprise and in condensed interim financial reports issued to the shareholders. Public business enterprises are those which have issued debt or equity securities that are traded in a public market (a domestic or foreign stock exchange or an over the counter market including local or regional markets) and that are required to file financial statements with the SEC or that provide financial statements for the purpose of issuing any class of securities in a public market.

It is not applicable to parent companies, subsidiaries, joint ventures or investees accounted for by the equity method if those enterprises' "separate company" statements are also consolidated or combined in a combined set of financial statements. Also both the separate financial statements and the consolidated/combined financial statements are included in the same financial report. However, FAS 131 is not applicable to those enterprises if they are public enterprises and their financial statements are issued separately.

Objectives: Disclosure of segments and related information is to provide information about the different types of business activities in which an enterprise engages and the different economic environments in which it operates to help users of financial statements:

- Better understand the enterprise's performance;
- Better assess its prospects for future net cash flows; and
- Make an informed judgement about the enterprise as a whole.

An enterprise might meet these objectives by providing a complete set of financial statements that are disaggregated in several different ways, for example, by products and services, by geography, by legal entity or by type of customers. However, it is not feasible to provide all such various types of information. Accordingly, FAS 131 suggests to adopt "management approach".

Under "management approach" is based on the way that management organizes a segment within the enterprise for the purpose of operating decision and assessing performance. So the segments become evident from the internal organizational structure of the enterprise. Therefore, it is possible to provide the information in a cost effective and timely manner.

FAS 131 requires that an enterprise should report measure of segment profit or loss and certain items included in determining segment profit or loss, segment assets, and certain related items. It does not require that an enterprise reports segment cash flow.

As per FAS 131 reportable segment is "operating segment" which should be identified in accordance with paras 1—15, FAS 131 or that results from aggregating two or more segments in accordance with para 17, FAS 131 and that exceeds quantitative thresholds mentioned in para 18, FAS 131. There is no such concept of primary segment and secondary segment as stated in the IAS 14. However, FAS 131 requires information about major customers (Paras 39, FAS 131).

Segment Report

Operating Segment`Other Information

Information

Information about Products and Services

Information about Geographic Areas

Information about Major Customers

Reportable Segments

Operating segment is the reportable segment for the purpose of FAS 131. An enterprise is required to identify operating segment in accordance with paras 10-15 of FAS 31.

Given below are identification criteria of an operating segment:

Issues and Para reference to FAS 131	Description
Para 10: Definition	Operating segment is a component of an enterprise: (a) that engages in business activities from which it may earn revenues and incur expenses; (b) whose operating results are regularly reviewed by the enterprise's chief operating decision maker to

	make decisions about decisions about resources to be allocated to the segment and assess its performance; (c) for which discrete financial information is available. An operating segment may engage in business activities for which it has yet to earn revenues. For example, start up segment maybe an operating segment before earning revenues.
Para 11: Part of the business enterprise which is not operating segment	Parts of the business enterprise which do not earn revenue are not classified as operating segment. For example, corporate headquarters or certain functional departments that earn revenue which is only incidental, pension and retirement benefit plans, etc., are not operating segments.
Para 12: Chief operating decision maker	This signifies a function not an officer. The function is to (i) allocate resources to a segment, and (ii) assess performance of the segment. Often this may signify the Chief Executive Officer or Chief Operating Officer. It may also signify a committee comprising of enterprise's President, Vice-President and others.
Para 13: Factors to be considered for identification	Three factors are stated in Para 10, namely, revenue earning capability, review of operating results and availability of discrete financial information. When the chief operating officer uses more than one set of segment information, other factors may identify a single set of components as constituting an enterprise's operating segments. These may include nature of business activities, existence of manager responsible for them and information presented to the board of directors. This means it is possible to identify an operating segment on the basis of nature of activities.
Para 14: Identify segment by function of the segment manager	Generally, an enterprise operates through a segment manager. Even the chief decision maker may a segment manager. It again signifies by function. The function is the over responsibility of running a particular set of activities. Segment manager is accountable for such activities and has to maintain regular contract with the chief operating decision maker to discuss operating results, financial results, forecasts, or plan for the segment.

	In case three characteristics specified in Para 10 is applicable to more than one components of an enterprise, but there is only one set for which the segment manager is responsible, that set of components are identified as operating segment.
Para 14: Identify segment by function of the segment manager	Generally, an enterprise operates through a segment manager. Even the chief decision maker may a segment manager. it again signifies by function. The function is the over responsibility of running a particular set of activities. Segment manager is accountable for such activities and has to maintain regular contact with the chief operating decision maer to discuss operating results, financial results, forecasts, or plan for the segment. In case three characteristics specified in Para 10 is applicable to more than one components of an enterprise, but there is only one set for which the segment manager is responsible, that set of components are identified as operating segment.
Para 15: Segment identification in a matrix organization	In matrix organization, a segment manager is responsible for managing a different product or service lines world-wide and others are responsible for managing only certain geographical locations. Characteristics stated in Para 10 are then identified with reference to a set of overlapping components. The chief decision maker uses both set of information for managing the business. In such a case, the components based on products and services should be the operating segment.
Para 17: Aggregation criteria	Two more operating segments are aggregated when into a single operating segment when they have same economic characteristics and similar in the following areas as well: ♦ the nature of products and services; ♦ the nature of the production processes; ♦ the type or class of customer for their products and services; ♦ the methods used to distribute their products or provide their services; and ♦ if applicable, the nature of regulatory environment.

Para 18: Quantitative thresholds Check whether a segment fulfils any of these criteria. If yes, select them as reportable segment.	Separate information about an operating segment is necessary when a segment meets any of the quantitative thresholds: (i) Reported revenue (including sales or external customers and inter-segment transfers) is 10% or more of the combined revenue (internal and external) of all reported operating segments. (ii) Absolute amount of its reported profit or loss is 10% or more of the greater of (a) the combined reported profit of all operating segments that did not report a loss or (b) the combined reported loss of all operating segments that did report a loss. (iii) Its assets are 10% or more of the combined assets of all operating segments.
Para 19: Combine other segments that do not satisfy the criteria specified in Para 18, but satisfies aggregation criteria stated in Para 17.	An enterprise may combine information about operating segments that meets the quantitative thresholds in case a segment does not meet the criteria stated in Para 18, but meets majority of the aggregation criteria.
Paras 20: Separate Operating segments should cover at least 75% of consolidated Revenue.	Check the total of revenue of the segments identified applying the criteria stated in Para 18 and para 19. Combined revenue of all those segments should cover 75% of the consolidated revenue. In case this threshold limit is not reached new operating segment should be identified ignoring threshold stated in para 18. The process should continue until aggregate revenue of all ide4ntified segments exceeds 75% of the consolidated revenue.
Para 21: All other segment category	Remaining segments are aggregated into “all other” segment category.
Para 22: Reportable segment of the immediately preceding period	Management judged an operating segment as reportable segment in the immediately preceding year. That segment does not meet the quantitative thresholds during the current year. Still that segment shall be continued to be reportable segment even if it no longer meets the criteria stated in Para 18.
Para 23: New segment identified during the current period and re-arrangement of the comparative data.	For the new segment identified during the current period due to fulfillment of the quantitative thresholds stated in Para 18, it is necessary to restate prior period segment data presented for comparative

	purposes unless it is impracticable to do so.
Para 24: Limit to number of segments to be reported to avoid information overload.	Although no precise limit has been determined as the number of segments to be identified as reportable in accordance with paras 18-23, when reportable segment reaches above 10, the enterprise needs to consider whether a practical limit has been reached.

15.13 Accounting Policies, Accounting Changes and Adjustments of Financial Statements for Prior Periods

Accounting Policies

Accounting policies are specific accounting principles and the methods of applying those principles that are judged by the management of the enterprises to be the most appropriate in the circumstances.

Information about accounting policies adopted by the enterprise is essential for providing fair view of financial position [Para 5, APB 22], cash flows [Para 152(b), FAS 95], and results of operations. Those statements are prepared in accordance with generally accepted accounting principles. Para 8, APB Opinion 22 requires that a description of all significant accounting policies of the reporting should be included as an integral part of the financial statements.

The disclosure of accounting policies should cover-

- Basis of conslidation;
- Depreciation methods;
- Amortization of intangibles;
- Inventory pricing;
- Accounting for Research and Development costs including basis for amortization;
- Translation of foreign currencies;
- Recognition of profit on a long term construction type contracts;
- Recognition of revenue from franchising and leasing ooperations;

Disclosure of accounting policies should not repeat details presented elsewhere as part of financial statements.

There is flexibility in disclosure of significant accounting policies. the disclosure is particularly useful if given in a separate Summary of Significant Accounting Policies preceding the notes to financial statements or as the initial note. FASB Interpretation 40 requires mutual Life Insurance enterprises to disclose significant accounting policies used in the preparation of financial statements.

Accounting Change

Accounting change is a change in (a) an accounting principle, (b) an accounting estimate or (c) the reporting enterprise. The correction of an error in previously issued financial statements is not deemed to be an accounting change. APB Opinion 20 discusses the issues relating to accounting changes. It applies to financial statements that purport to present financial position [Para 3, APB 20], Cash flows [Para 152(a), FAS 95] and results of operations in conformity with the generally accepted accounting principles.

Change in accounting principle - A change in accounting principles results from adoption of generally accepted accounting principles different from the one used previously for reporting purposes. The term accounting principles includes "not only accounting principles and practices but also methods of applying them". The following are not considered as changes in accounting principle:

- Initial adoption of accounting principle for the recognition of events or transactions occurring for the first time or that previously was immaterial in effect.
- Adoption or modification of an accounting principle in recognition of an accounting principle necessitated by transactions or events that are clearly different in substance from those previously occurred.

Examples of change in accounting principles are-

- A change in the method of inventory pricing;
- A change in depreciation policy;
- A change in accounting method for long term construction type contracts;
- A change in accounting for research and development costs.

Change in Accounting Estimates – Changes in accounting estimates are necessary consequences of periodic presentation of financial statements. Preparing financial statements require estimating the effects of future events. Examples of estimates are – uncollectible receivables, inventory obsolescence, service life and salvage value of depreciable assets, warranty costs, periods benefited by deferred costs etc. Changes in accounting estimates occur as new events occur, more experience is acquired, or as additional information is obtained.

Change in Reporting Entity – One special type of change in accounting principles results in financial statements which in effect are those of a different reporting entity. This type is limited mainly to (a) presenting consolidated financial statements in place of individual financial statements; (b) changing specific subsidiaries comprising group companies; (c) changing companies included in the combined financial statements. A different group of companies comprise the reporting entity after each change.

In the preparation of financial statements there is presumption that an accounting principle once adopted will not be changed in accounting for events and transactions of similar kinds. Consistent use of accounting principles over the period enhances the utility of the financial statements by facilitating the users in understanding comparative data.

In case there is a change in accounting principle, the justification of change should clearly explain why the newly adopted accounting principle is preferable. The nature of and justification for a change in accounting principle shall be disclosed in the financial statements.

In case previous period's data are restated, the public confidence in financial statements gets affected. On the other hand, if the previous year's data are not restated the quality of the comparative data and their utility in users' decision making gets minimized. To make a balance between the two, the US GAAP requires to present cumulative effect of accounting change on the face of the income statement of the period in which the change is effected. In addition, it is required that a set of proforma information should be included showing effect of change if carried in the previous periods presented.

That apart, summaries of financial information for a number of periods are commonly included in the financial reports. The summaries often show condensed income statements, including related earning per share amounts for five years or more. In summary financial information that includes an accounting period in which a change in accounting principle was made, the amount of cumulative effect of change that was included in net income of the period of the change shall be shown separately along with net income and related per share amounts.

For effecting change in accounting principles the following steps are followed:

- Financial statements for prior periods included for comparative purposes shall be presented as previously reported;
- The cumulative effect of changing to a new accounting principle on the amount of retained earnings at the beginning of the period in which change has been made is computed and presented in the income statement.
- The effect of change in income before extraordinary items a nd net income should be disclosed.
- Income before extraordinary items and net income are computed on proforma basis giving effect to the change in accounting policy and this is shown on the face of the income statement.

The above-stated steps aren ot applicable to (i) adjustments for prior period items which is discussed in Para 68.3 separately, (ii) other changes stated in items (1) to (3) below:

(1) Certain changes in accounting principles are such that advantage or retroactive effect outweighs disadvantages. In such cases prior period data should be restated, examples are-

   (a) a change from LIFO method of inventory pricing to another method;

(b) a change in method of accounting for long term construction type contracts;

(c) a change to or from the full cost method of accounting that is used in the extractive industries and

(d) a change from retirement, replacement, betterment accounting to depreciation accounting.

(2) *Initial public distribution*: It is possible to change accounting principles in connection with forthcoming public offerings with a view to present better financial information for current period. This is possible when effect of accounting change is favourable. Therefore, in such cases prior periods data should be restated.

(3) When a change in accounting principle is effected to conform with the recommendations of the AICPA statement of position [Para 5, FIN 20] or FASB Technical Bulletin or a consensus of the FASB EITF, such change should be accounted for in accordance with requirement of Para 5, FIN 20. This Para explains "For the purpose of applying APB Opinion No.20, an enterprise making a change in accounting principle to conform with the recommendations of an AICPA statement of position does not specify the manner of reporting a change in accounting principle to conform with its recommendations, an enterprise making a change in accounting principle to conform with the recommendations of the statement shall follow the change as specified by Opinion No.20."

15.14 Business Combination

Overview

A business combination occurs when two or more entities combine to form a single entity. An asset combination results when one company acquires the assets of one or more other companies, or when a new company is formed to acquire the assets of two or more existing companies. In an asset combination, the target companies cease to exist as operating entities and may be liquidated or become investment companies. An acquisition of stock combination occurs when one company acquires 50% of the outstanding voting common stock of one or more target companies, or when a new company is formed to acquire controlling interest in the outstanding voting common stock of two or more target companies.

Until 2001m two basic methods of accounting existed for business combinations: (1) the purchase method and (2) the pooling-of-interests method. In 2001, the FASB issued FAS 0141 (Business Combinations), which eliminated the pooling-of-interests method.

In a purchase method combination, the combined entity reports the assets and liabilities of the target company a t fair market value on the date of acquisition. Any excess of the fair market value of the consideration given over the fair market value of the net assets acquired is reported as goodwill. If the fair market value of the consideration given is less than the fair market value of the net assets acquired, the resulting excess of fair value of acquired net assets over the cost of the acquired entity is allocated, on a pro rata basis, against certain

assets acquired in the business combination. If any excess over cost remains after reducing certain assets to zero, the remaining excess is recognized as an extraordinary gain. The operating statements for purchase method combinations report combined results only for the period subsequent to the combination.

GAAP for business combinations are found in the following authoritative pronouncements:

Background

For many years, GAAP for business combinations was included in APB-16 and allowed two significantly different methods – the purchase method and the pooling-of-interests method. The purchase method, as the name implies, was based on the assumption that a purchase transaction had occurred (i.e., one entity has purchased the other). This type of transaction was usually executed via the transfer of cash or other assets or through a capital stock transfer. A new cost basis for the assets acquired and the liabilities assumed arose, and goodwill often was established as a result of the business combination. The pooling-of-interests method, on the other hand, was intended for business combinations in which the shareholders of the combining entities became shareholders of a combined company. The essence of a pooling was that the shareholders of the combining companies neither withdrew nor invested assets, but exchanged shares in accordance with a ratio that preserved their interests in the combining companies.

APB-16 was based on an assumption that a business combination was a purchase unless 12 very specific criteria were met, in which case the business combination was a pooling-of-interests. For business combinations initiated after June 30, 2001, the pooling-of-interests method is no longer available and, therefore, that method is not covered in this *Guide* other than for historical reference.

While the primary source of authoritative guidance on business combinations is FAS-141, other pronouncements also address issues related to business combinations. For example:

- FAS-109 (Accounting for Income Taxes) requires that a liability or asset be recognized for the deferred tax consequences of differences between the assigned values and the tax bases of the assets and liabilities (other than non-deductible goodwill and leveraged leases) recognized in a purchase business combination.
- FAS-87 (Employers' Accounting for Pensions) requires that assets and liabilities recorded under the purchase method include a liability for the projected benefit obligation in excess of plan assets or an asset for plant assets in excess of the projected benefit obligation, thereby eliminating any previously existing unrecognized net gain or loss, unrecognized prior service cost, or unrecognized net obligation or net asset existing prior to the business combination.

Each of the above issues relating to business combinations is addressed in this chapter.

The Purchase Method of Accounting for Business Combinations

Scope

For the purposes of applying FAS-141, a business combination occurs when an entity acquires net assets that constitute a business or acquires equity interests of one or more other entities and obtains control over that (or those) other entity (or entities). FAS-141 applies to combinations involving either incorporated or unincorporated entities. Business combinations may take a variety of forms, such as:

- One or more entities are merged or become subsidiaries.
- One entity transfers net assets or its owners transfe4r their interests to another.
- All entities transfer net assets or the owners of those entities transfer their equity interests to a newly formed entity.

The acquisition of some or all of the non-controlling interests in a subsidiary is not a business combination, although that type of transaction is covered in FAS-141. FAS-141 does not apply to combinations between not-for-profit organizations. Similarly, FAS-141 does not apply to the acquisition of a for profit organization by a not-for-profit organization.

Method of Accounting

All business combinations subject to the requirements of FAS-141 are to be accounted for by the purchase method.

The purchase of some or all the non-controlling interests in a subsidiary is also required to be accounted for by the purchase method, whether acquired by the parent, the subsidiary itself, or another affiliate.

Applying the Purchase Method

Determining the Acquiring Entity

A first step in applying the purchase method is to determine the acquiring entity. In a business combination effected through an exchange of equity interests, the entity that issues the equity interests is generally the acquiring entity. Typically the acquiring entity is the larger entity. Often, the combined entity uses the name of the acquiring entity. Circumstances differ, however, and all pertinent facts and circumstances should be considered in determining the acquiring entity.

Following are several factors that are particularly important in determining the acquiring entity:

1. *The relative voting rights in the combined entity after the combination* – The acquiring entity is the entity whose owners retain or receive the larger portion of the voting rights.
2. *The existence of a large minority voting interest when no other owner or organized group of owners has a significant voting interest* – The acquiring entity is typically the

combining entity whose single owner or organized group of owners holds the largest minority voting interest in the combined entity.

3. *The composition of the governing body of the combined entity*- The acquiring entity is the combining entity whose owners or governing body has the ability to elect or appoint a voting majority of the governing body of the combined entity.
4. *The composition of the senior management of the combined entity*- The acquiring entity is the combining entity whose senior management dominates that of the combined entity.
5. *The terms of the exchange of equity securities* – The acquiring entity is the combining entity that pays a premium over market value of the equity securities of the other combining entity or entities.

Determining Cost

Determining the cost of the acquisition is similar to determining the cost of assets acquired individually. Cash payment shall be used to measure the cost of an acquired entity. Similarly, the fair value of other assets distributed as consideration and the fair values of liabilities incurred are used to measure the cost of an acquired entity.

The fair value of securities traded is generally more clearly evident than the fair value of an acquired entity and, thus, generally should be used to determine cost in a business combination. If the quoted market price is not the fair value of the equity securities, the consideration received shall be estimated even though measuring directly the fair value of net assets received is difficult. Both the net assets received, including goodwill, and th the extent of the adjustment of the quoted market price of the shares issued shall be weighed in determining the amount to be recorded. Independent appraisals may be used to aid in determining fair values of securities. Indirectly and general expenses associated with a business combination should be expensed as incurred.

A business combination may include contingent consideration. Cash and other assets distributed, securities issued unconditionally, and amounts of contingent consideration that a re determinable at the date of acquisition shall be included in the cost of an acquired entity and recorded a t that date. Contingent consideration shall be recorded when the contingency is resolved and consideration is issued or becomes issuable. In general, the issuance of additional securities or distribution of other consideration when contingencies are resolved result in an additional element of cost of an acquired entity.

Allocating Cost

An acquiring entity shall allocate the cost of an acquired entity to the assets acquired and liabilities assumed based on their estimated fair values at date of acquisition. Following are general guidelines for the recording of assets acquired and liabilities assumed, except goodwill:

- Marketable securities- fair value
- Receivables-present value of amounts to be received.

- Inventories (finished goods and merchandise) – estimated selling prices less the costs of disposal and a reasonable profit allowance.
- Inventories (work-in-process)- estimated selling prices less the costs to complete, costs of disposal, and reasonable profit margin
- Inventories (raw materials)- current replacement cost.
- Plant and equipment (to be used) – current replacement cost
- Plant and equipment (to be sold) – fair value less cost to sell
- Intangible assets-estimated fair values
- Other assets (e.g., land, natural resources, nonmarketable securities)- appraised values.
- Accounts and notes payable, long-term debt, and other claims payable-present values of amounts to be paid determined at appropriate current interest rates.
- Liability for the projected benefit obligation in excess of plan assets (or vice versa)- amounts determined in accordance with FAS-87 (Employers' Accounting for Pensions).
- Liability for accumulated postretirement benefit obligation in excess of the fair value of plan assets (or vice versa)- amounts determined in accordance with FAS-106 (Employers' Accounting for Postretirement Benefits Other Than Pensions)
- Liabilities and accruals- present values of amounts to be paid determined at appropriate interest rates
- Other liabilities and commitments (e.g., unfavourable lease, contracts)-present value of amounts to be paid determined at appropriate current interest rates.

Intangible Assets

An intangible asset shall be recognized as an asset apart from goodwill if it arises from contractual or other legal rights. If this condition is not met, an intangible asset shall be recognized as an asset only if it is separable (i.e., is capable of being sold, transferred, licensed, rented, or exchanged). An assembled workforce cannot be recognized apart from goodwill.

The fair value of a preacquisition contingency shall be included in the allocation of the purchase price under the following circumstances:

- The fair value of the preacquisition contingency can be determined during the allocation period.
- Information available prior to the end of the allocation period indicates that it is probable that an asset exists, a liability has been incurred, or an asset has been impaired at the consummation of the business combination, and kthe asset or liability can be reasonably estimated.

Goodwill

Any excess of the cost of an acquired entity over the amounts assigned to assets acquired and liabilities assumed is recognized as goodwill. Goodwill so recorded is accounted for in accordance with FAS-142.

Excess of Fair Value over Cost

The sum of the amounts assigned to assets acquired and liabilities assumed may exceed the cost of the acquired entity. The excess shall be allocated as a pro rata reduction of the amounts that otherwise would have been assigned to the acquired assets except (a) financial assets other than investments accounted for by the equity method, (b) assets to be disposed of by sale, (c) deferred income taxes, (d) prepaid assets related to pension and other postretirement benefit plans, and (e) any other current assets. Any excess remaining after reducing to zero the amounts that otherwise would have been assigned to those assets is recognized as an extraordinary gain. That extraordinary gain generally is recognized in the period which the business combination is completed.

Financial Statement Disclosure

General Information

Notes to the financial statements shall include the following information in the period in which a business combination that has a material effect on the financial statements is completed:

1. The name and brief description of the acquired entity and the percentage of voting stock acquired.
2. The primary reasons for the acquisition.
3. The period for which the results of operations of the acquired entity are included in the income statement of the combined entity.
4. The cost of the acquired entity, the number of shares of equity interest issued or issuable, the value assigned to the interests, and the basis for determining that value.
5. A condensed balance sheet including the amount assigned to each major asset and liability caption of the acquired entity at the acquisition date.
6. Contingency payments, options, or commitments specified in the acquisition agreement and the accounting treatment of each.
7. The amount of purchased research and development assets acquired and written off in the period and the location of the write-off in the income statement.
8. For any purchase price allocation that is not final, that fact and the reasons therefore.

Intangible Asset Information

Notes to the financial statements shall include the following information regarding intangible assets and goodwill:

- For intangible assets subject to amortization:
  - Amount assigned to any major intangible asset class

- Amount of any significant residual value, in total a nd by major intangible asset class
- Weighted-average amortization period, in total and by major intangible asset class.

- For intangible assets not subject to amortization, the total amount assigned a nd the amounts assigned to any major intangible asset class.
- For goodwill:
  - Total amount of goodwill and the amount that is expected to be deductible for tax purposes.
  - The amount of goodwill by reportable segment (assuming the entity is required to disclose segment information in accordance with FAS-131 (Disclosures about Segments of an Enterprise and Related Information).

Special Disclosures for Public Companies

Notes to financial statements shall include the following supplemental information on a pro forma basis for the period in which a material business combinations occurs:

- Results of operations for the current period as though the combination had been completed at the beginning of the period.
- Results of operations for the comparable prior period as though the combination had been completed at the beginning of that period if comparative financial statements are presented.

These supplemental disclosures must include revenue, income before extraordinary items and the cumulative effect of accounting changes, net income,l and earnings per share.

In the period in which an extraordinary gain is recognized related to a business combination, the notes also shall disclose information consistent with paragraph 11 of APB-30 (Reporting the Results of Operations- Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions).

Interim Financial Statements

The summarized interim financial information of a public enterprise shall disclose the following information if a material business combination is completed during the current year:

1. The general disclosures described above.
2. Supplemental pro forma information that discloses the results of operations for the current interim period and the current year to date of the most recent interim statement of financial position presented as though the business combination had been completed at the beginning of the period being reported on.

3. The nature and amount of any material, nonrecurring items included in the reported pro forma results of operations.

Types of Purchase Business Combinations

A business combination may be accomplished in one of two ways. The acquiring company may purchase the assets (asset acquisition) of the target company. In this instance, normally the target company is liquidated and only one entity continues. Alternatively, the acquiring company may purchase more than 50% (upto 100%) of the outstanding voting common stock of the target company. In this instance, the financial statements of the two entities are consolidated in accordance with ARB-51 (Consolidated Financial Statements), as amended by FAS-94 (Consolidation of All Majority-owned Subsidiaries).

In an asset purchase, entrees are made to record the assets and assume the liabilities of the target company on the books of the acquiring company. If the purchase price exceeds the fair market value of the net assets, goodwill is recorded in the acquisition entry. If the fair market value of identifiable assets exceeds the purchase price, the resulting excess of fair value of acquired net assets over cost is a cated to reduce all of the acquired assets except (as) financial assets of than investments accounted for by the equity method, (b) assets to disposed of by sale, (c) deferred income taxes, (d) prepaid as related to pension and other postretirement benefit plans, and (e) other current assets. If an excess of fair value acquired net assets over cost remains unallocated, the resulting amount is treated as an extraordinary gain.

Goodwill is not necessarily the difference between cost and book value of an investment, unless the book value is equal to the fair value of the underlying assets. The underlying assets represented by an investment individually are assigned a fair value at the date of acquisition, and if the assigned fair values are less than the amount of the investment, the difference is goodwill. For consolidation purposes, the acquisition of a stock investment may be considered the purchase price paid for an interest in the underlying net assets of a business.

If any excess of cost over acquired book value is allocated to depreciable assets, the depreciation expense of subsequent periods must be increased to spread the amount of such excess over the remaining life of the assets.

Cost Determination

The recorded cost of an acquisition is equal to the determinable amount of cash and other net assets that are unconditionally surrendered at the date of acquisition. Contingent consideration is recorded if it is determinable at the date of the acquisition. Other contingent consideration, the amount of which is not determinable at the acquisition date, is disclosed.

Contingent consideration may be on the basis of maintaining or achieving specific earning levels over future periods, or on a security maintaining or achieving a specific market price.

When a contingent consideration based on earnings is achieved, the acquiring company records the current fair value of the additional consideration. At this juncture, it is more than likely that the increase in the cost of the acquisition will be in the form of goodwill.

When contingent consideration arises on the basis of maintaining or exceeding a specific market price for the securities issued to consummate the acquisition, the acquiring company will have to issue additional securities or transfer other assets in accordance with the contingency arrangements. The issuance of the additional contingency securities is based on their then-current fair value, but does not increase the overall cost of the acquisition because the recorded cost of the original securities issued is reduced by the same amount. The only item that changes is the total number of shares issued for the acquisition.

15.15 Issues in Inventory Valuation and Revenue Recognition

Basic Principles

The term "inventory" is used to designate the aggregate of those items of tangible personal property, that (a) are held for sale in the ordinary course of business (finished goods), (b) are in process of production for such sale (Work in Process), or (c) are tobe currently consumed either directly or indirectly in the production of goods and services to be available for sale (raw materials and supplies).

Inventories do not include long term assets which are subject to depreciation. Any depreciable assets retired from regular use and held for sale are not classified as inventory. Certain materials and supplies purchased for production may be used for the construction of long term assets. These items are not excluded from the inventory as they represent a small portion of the inventory.

Inventories are primarily valued at cost. A departure from cost basis of pricing is required when the utility of goods is no longer as great as its costs. If the utility of the goods is reduced by damage, deterioration, obsolescence, changes in price levels, or other causes, a loss should be recognized applying the rule of pricing inventories "at cost or market price whichever is lower".

The rule of "cost or market, whichever is lower" provides a means of measuring the residual usefulness of inventory expenditure. In applying this rule, however, judgment should always be exercised and no loss shall be recognized unless the evidence indicates clearly that a loss has been sustained. In case evidence provides that cost of the inventory will be recovered in the normal course of business, no loss shall be recognized even if the replaceme3nt or reproduction cost is lower. This might be true for production under firm sale contract.

As used in the phrase "cost or market" the term "market" means current replacement cost (by purchase or by reproduction) except that-

(a) Market shall not exceed net realizable value (estimated selling price in the ordinary course of business less reasonably predictable costs of completion and disposal);

(b) Market shall not be less than net realizable value reduced by an allowance for an approximate normal profit margin.

Say, cost of the inventory is ₹ 10 million, replacement cost ₹ 6 million selling price less cost of disposal ₹ 8 lacs. Normal profit margin is 10% of net sellingprice. In this case market cannot be less than ₹ 7.2 million.

In another case, cost of the inventory is ₹ 10 million, replacement cost of ₹ 9 million, selling price less cost of disposal ₹ 8 lacs. In this case market cannot be more than ₹ 8 million.

This is a major conceptual differenced in US GAAP inventory valuation.

The "lower of the cost or market" rule is applied separately for each item of inventory. But when raw materials or supplies are at less than cost, but when it enters into thye finished goods it is possible to recover its costs. In such "lower of the cost or market" rule is not applied.

If substantial and unusual losses result from the application of this "lower of the cost or market" rule, such loss should not be included in cost of goods sold. Such loss should be separately charged to income statement.

Basic Principles of Revenue Recognition

Profit is realized when a sale in the ordinary course of business is effected. Revenues shall be ordinarily recognized at the time transaction is completed with appropriate provision for uncollectible amounts [Para 12, APB 10].

Application of Instalment Method of Accounting – When collection of revenue is not reasonably assured, instalment method of revenue recognition is applied. As per this method revenue is recognized to the extent of cash collection. For example, Company A sold machinery by which the customers pay in instalment. Out of the sales during the year ₹ 10 million, instalments collected is ₹ 4 million and amount written off 0.5 million. The company earns gross profit of 20% on sales. So profit to be deferred is 20% of 3.5 million, i.e., 0.7 million.

Revenue recognition when Right to Return Exists – The product may be returned for refund of purchase price, for a credit applied to other purchases or in exchange for other products. Revenues from sale transactions that offer right to return is recognized if all of the following conditions are met:

- The seller's price to the buyer is substantially fixed at the date of sale;
- The buyer has paid the seller or the buyer is obligated to pay the seller, and obligation is not contingent on resale of the product;
- The buyer's obligation to the seller would not be changed in the event of theft or physical destruction or damage to the product;

- The buyer acquiring the product has economic substance apart from t6hat provided by the seller;
- The seller does not have significant obligation for future performance to directly bring about resale of the product by the buyer;
- The amount of the future return can be reasonably estimated.

If any portion of sales revenue is not recognized as any of the conditions are not met, such revenue should be recognized when the privilege to return expires.

Recognition of Franchise Revenue – A franchisee, a party who has been granted business rights to operate the franchise business, pays initial franchise fee and continuing franchise fee to the franchisor. Initial franchise fee is the consideration for establishing the franchise relationship and providing some initial services. Occasionally, the fee includes consideration for initially required equipment and inventory. Initial services include: (a) assistance in the site selection, (b) assistance in obtaining facilities including related financing and architectural and engineering services, (c) assistance in advertising, (d) training of the franchisee's personnel, (e) preparation and distribution of manuals, (f) book keeping and advertising services and (g) Inspection, testing and other quality control programmes.

Franchise fee is recognized as revenue when all the material services and conditions are satisfied by the franchisor. Substantial performance means the franchisor has no remaining obligation or intent, either by agreement or trade practice. Sometimes large initial franchise fees are agreed upon and continuing franchise fees are not sufficient to cover the cost of the continuing services, then a portion of the initial franchise fees should be deferred and amortized over the life of the franchise. The deferral should be based on cost of services and a reasonable profit.

Accounting for Product Financing Arrangements – In a product financing arrangement, the sponsor (the enterprise seeking the financing) sells the product to another entity and in related transaction it agrees to buy the product (or a substantial identical product). For example, in stock lending system, the seller gets back the same securities of different distinctive nos.

Company A sells 10000 units of goods to F @ ₹ 10 per unit with agreement to repurchase it @₹ 11 per unit after 15 days. Should the company a recognize ₹ 1,00,000 as sales and ₹ 1,10,000 as purchases?

The sponsor shall record sale. The amount received from F is recognized as a liability. The difference between the sale and purchase price is treated as financing cost and should be accounted for accordingly.

Other types of product financing arrangements are:

- Sponsor does not buy back the products. A third party buys back the product from which the sponsor buys back.

Important characteristics of product financing arrangement are-

- The product covered by the arrangement is stored in the sponsor's premises;

- The sponsor can use or sell the products;
- The debt of the entity that purchases the product is guaranteed by the sponsor.

The above-mentioned characteristics indicate that a sale transaction is in fact a financing arrangement.

Accounting for separately Priced Extended Product Warranty and Product Maintenance – Extended product warranty is an agreement to provide warranty protection in addition to the scope of coverage of the manufacturer's original warranty. A product maintenance contract is an agreement to perform certain agreed upon services to maintain a product for specified period of time. Such a contract is regarded as separately priced, if the customer has the option to purchase the services. For example, a machinery costs ₹ 10 million without warranty and the ₹ 11 million with warranty. In this case it is separately priced as the customer can chose with warranty or without war5ranty products.

Revenue from the separately priced warranty contract or maintenance contract is deferred and recognized as per straight line method over the period in which service is rendered. In case the historical data provide better evidence of the costs of services rendered under the contract, then revenue should be recognized in proportion to costs incurred in performing services under the contract.

15.16 Foreign Currency Translation

Background

This standard applies for (i) financial accounting and reporting for foreign currency transactions in financial statements of a reporting enterprise and for translating foreign currency financial statements that are incorporated in the financial statements of the reporting enterprise by consolidation, combination or other equity method of accounting.

Important terms that will help understanding FAS 52:

Foreign Entity	An operation (e.g., division, subsidiary, branchy, joint venture) whose financial statements are prepared in a currency other than the reporting currency of the reporting entity.
Foreign Currency Transactions	Transactions in which the terms are denominated in a currency other than; the entity's functional currency. Foreign currency transactions occur when a company: (1) purchases (imports) or sells (exports) on credit merchandise or services the prices being denominated in a foreign currency; (2) buys or sells assets or incurs or settles liabilities denominated in foreign currency; (3) takes out or gives international loans in which the amounts payable or receivable are denominated in a foreign currency; (4) is a participant in an unperformed forward exchange contract; and

	(5) borrows or lends money, and the amounts payable or receivable are expressed in a foreign currency.
Foreign Currency Translation	Conversion in a company's reporting currency those amounts denominated or measured in a different currency.
Foreign Currency Statements	Statements Financial statements using as the measuring unit a functional currency other than the reporting currency of the business.
Foreign Currency	A currency other than the functional currency of a business. For example, the dollar could be a foreign currency for a foreign entity. Composite of currencies (e.g., special drawing rights) may be used to establish prices or denominate amounts of loans.
Reporting Currency	The currency the business prepares its financial statements in typically U.S. dollars.
Local Currency	The currency of a particular foreign country.
Transaction gain or loss	Transaction gain or loss is produced from redeeming receivables/payables that a re fixed in terms of amounts of foreign currency received/paid. An example is a French subsidiary having a receivable denominated in francs from a Swiss customer. A transaction gain or loss takes place when there is a change in exchange rates between the funct5ional currency and the currency in which a foreign currency transaction is denominated. It constitutes an increase or decrease in (1) the actual functional currency cash flows realized upon settlement of foreign currency transactions and (2) the expected functional currency cash flows on unsettled foreign currency transactions. Adjustments derived from translating financial statements from the entity's functional currency into the reporting one.
Monetary assets and liabilities	Cash, receivables, and obligations to pay a fixed amount of debt.
Non-monetary Items	Items all balance sheet items except for cash, claims to cash, and cash obligations.
Currency swap	The exchange between two business entities of the currencies of two different countries in accordance with a contract to reexchange the two currencies at the same exchange rate a t an agreed upon future date.
Forward exchange contract	It is an agreement to exchange different currencies at a specified future date and at a specified rate.

Functional Currency

An entity's functional currency is the currency of the primary economic environmenht in which the entity operates. This is the currency of the environment in which the entity primarily generates and expends cash.

The assets, liabilities, and operations of a foreign entity shall be measured using functional currency [FAS 52].

Annex A to FAS 52 provides guidance for the determination of functional currency of a foreign entity.

Salient Economic Factors	*Para Reference to FAS 52*	*Use of Foreign currency*	*Use of Parent's currency*
Cash Flow Indicators	42a	Cash flows related to the foreign entity's individual assets and liabilities are primarily in foreign currency and do not directly impact the parent company's cash flows.	Cash flows related to the foreign entity's individual assets and liabilities directly impact the parent company's cash flows on a current basis and readily available for remittance to the parent company.
Sales Price Indicators	42b	Sales price for the foreign entity's products are not primarily responsive on short-term basis to changes in exchange rates but determined more by local competition or local government regulations	Sales price for the foreign entity's products are primarily responsive on short-term basis to changes in exchange rates and determined more by worldwide competition or by international; prices.
Sales Market Indicators	42c	Existence of significant local market even though exports are significant as well.	Sales market is mostly parent's currency.
Expense indicators	42d.	Expenses are primarily costs even though there are imports.	Costs are primarily obtained from the market wherein the parent company is located.
Financing Indicators	42e	Local financing or financing are primarily	Financing is primarily in the parent's currency.

		denominated in local currency.	
Inter-company transactions	421	Low volume of inter-company transactions. There is no extensive interrelationship between the operations of the foreign entity and the parent company.	High volume of inter-company transactions. There is extensive interrelationship between the operations of the foreign entity and the parent company.

Accounting for Foreign Currency Transactions

These principles a re applicable to both the parent company and foreign entity:

- Treatment of receivables and payables denominated in currency other than functional currency – Foreign currency transactions produce receivables or payables that are fixed in terms of amount of foreign currency that will be received or paid. A change in exchange rates between functional currency and currency in which the transactions are denominate3d increases or decreases the settlement cash flows.
  - Increase in settlement cash flows of debtors or decrease in settlement cash flows of creditors, gives rise to transaction gain;
  - Increase in settlement cash flows of creditors or decrease in settlement cash flows of debtors, gives rise to transaction loss;

A transaction gain or loss is included in the determination of net income for the period.

- Likewise, a transaction gain or loss may arise between the date of transaction and date of settlement of cash flows tha t occur before the balance sheet date. This is realized gain or loss.

  Other type of realized gain or loss is on the assets and liabilities denominated in currency other than functional currency outstanding on the previous balance sheet date which is settlement during the currency period.

This realized gain or loss is accounted for in the net income for the period.

- General principles to be followed in recognizing transactions that occur in currency other than functional currency:
  - Record all assets, liabilities, revenues, expenses,. Gain or loss arising from the transaction is measured and recorded in the functional currency of the entity using exchange rate in effect on the date of transaction.
  - At each balance sheet, recorded balances of assets and liabilities denominated in currency other than functional currency are restated to reflect exchange rate of the balance sheet date.

Transactions Gains or Losses to be excluded from the determination of Net Income

Gains or losses on the following foreign currency transactions are not included in the net income for the period but should be reported in the same manner as translation adjustments (stated in Para 13, FAS 52 arising out of translation from functional currency of foreign entity to the reporting currency, i.e., accounting in a separate section of equity):

- Foreign currency transactions that are designated as effective hedge of a net investment in a foreign entity.
- Inter-company foreign currency transactions that are of a long-term investment nature, when the entities to the transactions are consolidated, combined or accounted for by the equity method in the reporting enterprise's financial statements.
- Gain or loss on a forward contract or other foreign currency transactions that is intended to hedge an identifiable foreign currency commitment is deferred and included in the measurement of the related foreign currency transaction. However, loss is not deferred if such deferral leads to recognizing loss in a later period (s). A foreign currency transaction is considered a hedge of an identifiable foreign currency commitment on fulfillment of the following conditions:

  (a) the foreign currency transaction is designated and is effective as a hedge of a foreign currency commitment;

  (b) the foreign currency commitment is firm.

Deferral is applicable to the hedge portion only on an after-tax basis. A gain or loss so deferred shall be included as an offset to the related tax effects in the periods in which such tax effects are recognized. Gain or loss that arises from the portion of the transaction that is in excess of the amount required for hedge should be deferred.

Further, any gains or losses on a forward exchange contract applicable to a period subsequent to the transaction date of the related commitment cannot be deferred.

Deferred gain or loss on hedging a foreign currency commitment that is sold or terminated is not recorded until the associated identifiable transaction occurs, except if the transactions are likely to result in a loss.

A forward exchange contract may be entered into a hedge an identifiable foreign currency commitment. A gain or loss on a forward exchange contract that is intended to hedge a foreign currency commitment (such as an agreement to purchase or sell equipment) shall be deferred and included in the measurement of the related foreign currency transaction (i.e., the purchase or sale).

A forward exchange contract may be entered into a hedge exposure from a recognized receivable or payable denominated in a foreign currency. A gain or loss is recognized for

changes in the spot rate of the applicable currency; however, this gain or loss is offset by the transaction loss or gain recognized from the associated receivable or payable.

Forward exchange contracts

A company may enter into forward exchange contract to hedge a position or for speculation. Gains or losses on forward exchange contracts that are not for hedging are included in the determination of net income. Agreements that are essentially same as forward contracts are currency swaps. Accordingly, gains and losses of currency swap transactions are recorded in the same manner.

How to determine gain or loss on forward contract (other than speculative contracts)?

1. Find out the spot rate a t the balance sheet date.
2. Find out the forward rate at the inception of the contract.
3. Find out the spot rate at the date of inception of the forward contract.
4. Find out the amount of the contract.
5. Gain or loss on forward contract = (4)* [(1) – (3)].
6. Discount or premium on forward contract = (4)* [(2) – (3)].

16. Significant Differences and Similarities between Indian Accounting Standards, IFRS and US GAAPs

This table focuses on measurement similarities and differences most commonly found in practice. This summary, not necessarily justify the differences of details that exist among Indian Accounting Standards, IAS / IFRS and US GAAPs. Even if the summary given is similar, there can be differences in the detailed application, which could have a material impact on the financial statements. One should study this table with references to all relevant Accounting Standards, IAS / IFRS or US GAAPs where applicable in that country.

Topic	Indian Accounting Standards	IFRS / IAS	US GAAPs
Historical cost	Historical cost is used for valuing the assets. It is one of the accounting concept. However, property, plant and equipment may be revalued to fair value. Certain derivatives	For valuation purpose, in general, historical cost is used but some intangible assets; property plant and equipment and also investments may be revalued to fair value.	US GAAPs do not recommend revaluation of assets except for certain types of securities and derivatives to fair value.

	are carried at fair value but no accounting standards on derivatives and biological assets have been issued by the ICAI till date.	IFRS / IAS also requires tevaluation of Derivatives, biological assets and certain securities at fair value.	
First-time adoption of accounting frameworks	In India, there is no specific guidance on first time adoption of Accoutning frameworks.	There is a specific statement by IASB to apply IFRS for the first time. First time adoption of IFRS requires full retrospective application of IFRS effective at the reporting date for IFRS based financial statements of an entity. It has provided certain releifs, exemptions and imposes certain requirements and disclosures.	First-time adoption of US GAAP requires retrospective application. However, US GAAP does not give specific guidance on first time adoption of its accounting principles.
Constituents of financial statements	Required a company's standalone- two years' balance sheets, income statements, cash flow statements, and accounting policies and notes.	Two years' consolidated balance sheets, income statements, cash flow statements, changes in equity and accounting policies and notes. In some circumstances or on a voluntary basis, an entity may present standalone financial	For US Companies and SEC registrants (public companies) two years' balance sheet and three years income statements, cash flow statements, changes in equity statement and accounting policies and notes. However, in certain circumstances for foreign private issuers there is a relief from the three-year requirement. Non-US companies with

		statements along with its consolidated financial statements.	registered securities in US have an option to prepare their financial statements, either based on US GAAPs or on IFRS along with the reconciliation of net income and equity to US GAAPs, as a disclosure in the notes.
Balance sheet	Accounting standards do not prescribe a particular format of balance sheet. It accepts the format prescribed by the Companies Act or by other industry regulations like banking, insurance, as applicable. However, accounting Standard states certain items, which must be presented on the face of the balance sheet.	IFRS too do not prescribe any particular format of balance sheet. As per requirements of IFRS, certain items must be presented on the face of the balance sheet. There is a requirement of separate presentation of total assets and total liabilities. A liquidity presentation of assets and liabilities is used, instead of a current/non-current presentation, only when a liquidity presentation provides more relevant and reliable information. .	Entities may present either a classified or non-classified balance sheet. Decreasing order of liquidity is used for the presentation of the items on the face of the balance sheet. Public companies should follow SEC regulations.
Income statement	Accounting standards do not prescribe a particular format of income statement. Industry-specific formats are prescribed by	IFRS too do not prescribe any particular format of income statement. An entity selects the presentation of its expenses either by	US GAAP requires income statement to be presented in either of two formats - single-step or multiple-step format. Expenditures are presented by function. Public companies should

	industry regulations. However, accounting Standard states certain items, which must be presented on the face of the income statement.	function or nature. Expenses by nature are disclosed as afootnote if an entity selects functional presentation. However, IFRS requires certain items to be presented on the face of the income statement.	follow SEC regulations.
Extraordinary items	Events or transactions, clearly distinct from the ordinary activities of the entity, which are not expected to recur frequently and regularly, are termed as extra-ordinary items. Disclosure of the nature and amount of such item is required in the income statement to perceive the impact on current and future profits.	Not allowed.	Defined as being both infrequent and unusual, and are rare. Negative goodwill is presented as an extraordinary item.on the face of the income statement net of taxes. Disclosure of such is required either in the income statement or in the notes.
Statement of changes in share (stock) holders' equity	No separate statement is prepared for it. Separate schedules of 'Share capital' and 'Reserves and surplus' are prepared to show the changes in	It is a primary statement required to be prepared as a part of financial statements unless Statement of recognized income and expenses (SoRIE) is prepared as a primary	SEC rules allow certain information to be included in the notes and not in the primary statement.

	shareholders' equity.	statement. Statement shows capital transactions with owners, accumulated profits' movement and a reconciliation of all other components of equity.	
Cash flow statements –	Both indirect and direct method are used in the preparation of cash flow statement.. Cash flows are divided into three broad categories namely- operating, investing and financing. Cash includes cash equivalents with short-term maturities (typically less than three months) except that bank overdrafts are excluded.	Similar to Indian Accounting Standard. But cash includes cash equivalents like investments with short-term maturities (typically less than three months) and may include bank overdrafts repayable on demand but do not include short term borrowings as they are considered as financing item.	Similar to IFRS, but more specific guidance for items included in each category. Both direct and indirect method is used. However, a reconciliation of net income to cash flows from operating activities is disclosed if the direct method is used. Similar to Indian Accounting Standard.
Changes in accounting policy	In the year of change, the effect of change is included in income statement of that year and also the impact of change is disclosed.	Retrospective effect of the change in accounting policy is accounted. Also comparative figures are restated; where the effect of period(s) not presented is adjusted against opening retained earnings.	Similar to IFRS from the date of adoption of FAS 154.

Change in accounting estimates	Change is accounted in the income statement of the current year when identified. In general no retrospective effect is accounted for such change.	Similar to Indian Accounting Standard	Similar to Indian Accounting Standard
Definition of subsidiary	Based on voting control or control over the composition of the board of directors. The existence of currently exercisable potential voting rights is not taken into consideration.	Control is presumed to exist when parent owns, directly or indirectly through subsidiaries, more than one half of an entity's voting power. The existence of currently exercisable potential voting rights is also taken into considerations. A parent could have control over an entity in circumstances where it holds less than 50% of the voting rights of an entity.	Similar to IFRS. However, a bipolar consolidation model is used, which distinguishes between a variable interest model and a voting interest model. Control can be direct or indirect and may exist with a lesser percentage of ownership (voting interest model).
Definition of associate	Based on significant influence; presumed if 20% or greater interest or participation in entity's affairs.	Similar to Indian accouting Standard	Similar to IFRS, although the term 'equity investment is used instead of 'associate'.
Presentation of associate results	In consolidated financial statements; equity method is	In consolidated financial statements; equity method is	In consolidated financial statements; similar to IFRS.

	used. Share of post-tax results is shown. In standalone financials; at cost less impairment.	used. Share of post-tax results is shown. In standalone financial; at cost or at fair value in accordance with IAS 39.	
Definition of joint venture	Contractual arrangement whereby two or more parties undertake an economic activity, which is subject to joint control. Exclusion if it meets the definition of a subsidiary	Contractual arrangement whereby two or more parties undertake an economic activity, which is subject to joint control. Exclusion if investment is held-for-sale.	A corporation owned and operated by small group of businesses as a separate and specific business or project for the mutual benefit of the members of the group.
Presentation of jointly controlled entities (joint ventures)	In consolidated financial statements, proportional consolidation is used. In standalone financials; at cost less impairment.	In consolidated financial statements, both proportional consolidation and equity method is permitted. In standalone financials; at cost or at fair value in accordance with IAS 39.	In consolidated financial statements; equity method is required except in specific circumstances. In standalone financials; at cost or equity method is used.
Business combinations	No particular Standard has been issued by ICAI till date. However all business acquisitions are business combinations except pooling of interest	All business acquisitions are Combinations as per IFRS 3	All business acquisitions are Combinations.

	method for certain amalgamations		
Purchase method-values on acquisition	For an entity acquired and held as a subsidiary, the assets acquired and liabilities assumed are incorporated in their existing carrying amounts for consolidation purposes. On amalgamation, they may be incorporated at their existing carrying amounts or, alternatively, the consideration is allocated to individual identifiable assets and liabilities at their fair values. On business acquisition, they may be incorporated at their fair values or value of surrendered assets. No separate restructuring provision is recognized on acquisition.	Assets, liabilities and contingent liabilities of acquired entity are fair valued. If control is obtained in a partial acquisition of a subsidiary, the full fair value of assets, liabilities and contingent liabilities, including portion attributable to the minority (non-controlling) interest, is recorded on consolidated balance sheet. Goodwill is recognised as the residual between the consideration paid and the percentage of the business acquired. Liabilities for restructuring activities are recognized only when acquiree has an existing liability at acquisition date. Liabilities for future losses or other costs expected to be incurred as a result of the business combination cannot	Similar to IFRS, except minority interest is stated at pre-acquisition carrying value of net assets, and contingent liabilities of the acquiree are not recognised at the date of acquisition. Specific rules exist for acquired in-process research and development (generally expensed) and contingent liabilities. Some restructuring liabilities relating solely to the acquired entity may be recognized if specific criteria about restructuring plans are met.

		be recognized.	
Minority interests at acquisition	Stated at minority's share of pre-acquisition carrying value of net assets.	Stated at minority's share of the fair value of acquired identifiable assets, liabilities and contingent liabilities.	Similar of Indian Accounting Standard
Purchase method-goodwill and intangible assets with indefinite useful lives	Goodwill on consolidation and business acquisitions; no specific guidance-practice varies, between no amortization versus amortization over a period not exceeding 10 years; Goodwill on amalgamation is amortised over a period not exceeding 5 years, unless a longer period is justified; Goodwill is reviewed for impairment whenever an indication of impairment exists at the CGU level. Intangible assets are not classified into indefinite useful lives category. All intangible assets are amortised over a period not exceeding 10 years	Capitalised but not amortised. Goodwill and indefinite-lived intangible assets are reviewed for impairment at least annually at either the cash-generating unit (CGU) level or groups of CGUs, as applicable.	Similar to IFRS, although the level of impairment testing and the impairment test itself are different.

Purchase method-Capital Reserve	Negative goodwill is recorded in equity as capital reserve, which is not amortised to income. However, in case of an amalgamation, the fair value of intangible assets with no active market is reduced to the extent of capital reserve, if any, arising on the amalgamation.	The identification and measurement of acquiree's identifiable assets, liabilities and contingent liabilities are reassessed. Any excess remaining after reassessment is recgonised in Income statement immediately.	Any remaining excess after reassessment is used to reduce proportionately the fair values assigned to non-current assets (with certain exceptions). Any excess is recognized in the income statement immediately as an extraordinary gain.
Pooling of interests method	Required for certain amalgamations when all the specified conditions are met.	Prohibited.	Same as IFRS.
Revenue recognition	Indian Accounting Standard on revenue recognition does not give any guidance on revenue measurement. Revenue from services is recognized only on the completion of the services.	IFRS states that based on several criteria, which require the recognition of revenue when risks and rewards have been transferred and the revenue can be measured reliably. Revenue from services is recognized in proportion to the state of completion of the transaction at the balance sheet date.	Detailed guidance exists for specific types of transactions for the purpose of revenue recognition. US GAAP laid emphasis on persuasive evidence that an arrangement exists, and delivery has occurred or services have been rendered.

Construction contracts	Percentage of completion method is recommended if the outcome can be reliably measured. Expected loss to be recognized as an expense immediately.	Accounted for using percentage-of-completion method. Complete contract method is not allowed.	Similar to IFRS. However, completed contract method is permitted in rare circumstances when the extent of progress of completion cannot be measured reliably.
Employee share compensation	Guidance note issued by ICAI requires measurement of cost of benefits arising from employee share compensation plans on fair value. Alternatively, the guidance note allows use of the intrinsic value method.	Expense for services purchased is recognized. Corresponding amount recorded either as a liability or an increase in equity, depending on whether transaction is determined to be cash or equity-settled. Amount to be recorded is measured at fair value of shares or share options granted.	With the adoption of FAS 123R, similar model to IFRS. Compensation expense is generally recognized based on fair value of awards at grant date.
Acquired intangible assets	If recognition criterias are satisfied then it can be capitalized. all intangibles are amortised over useful life with a rebuttable presumption of not exceeding 10 years. Revaluations are not permitted.	If recognition criterias are satisfied then it can be capitalized. It is amortised over useful life. Intangibles assigned an indefinite useful life are not amortised but reviewed at least annually for impairment.	Similar to IFRS, except revaluations are not permitted.

		Revaluations are permitted in rare circumstances.	
Internally generated intangible assets	Research costs are expensed as incurred. Development cost is capitalized and amortised only when specific criteria are met.	Similar to Indian Accoutning Standard.	Research and development costs are expensed as incurred. Some software and website development costs are capitalized.
Property, plant and equipment	Historical cost is used. Revaluations are permitted, however, frequency of revaluation has not mentioned. On revaluation, an entire class of assets is revalued, or assets to be revalued are selected on systematic basis.	Historical cost or revalued amounts are used. On opting revaluation option, regular valuations of entire classes of assets are required.	Historical cost is used; revaluations are not permitted.
Non-current assets held for sale or disposal	There is no requirement to classify and present an asset as held for sale on the face of the balance sheet or in the notes.	Non-current asset is classified as held for sale if its carrying amount will be recovered through a sale transaction rather than through continuing use. A non-current asset classified as held for sale is measured at the lower of its carrying amount and fair value less costs to sell. Comparative	Similar to IFRS.

		balance sheet is not restated.	
Impairment of assets	Assets are impaired at higher of fair value less costs to sell and value in use based on discounted cash flows. Impairment test is to be conducted every year and if there is upward increase in the vaue of asset than reversal of impairment losses is required in certain circumstances. Assets are not separately classified or disclosed as held for sale on the face of the balance sheet.	Similar to Indian Accounting Standard. However, assets are classified and disclosed separately on the face of the balance sheet as held for sale or disposal.	Impairment is assessed on undiscounted cash flows for assets to be held and used. If less than carrying amount, impairment loss is measured using market value or discounted cash flows. Reversal of losses is prohibited.
Capitalisation of borrowing costs	There is no choice rather to capitalize the borrowing cost.	Permitted as a policy choice for all qualifying assets, but not required.	Required.
Investment property	Treated as a long-term investment and is carried at cost less impairment.. Revaluation of such property is not applicable.	IFRS gives the choice of measuring the investment property at depreciated cost or fair value, with changes in fair value recognized in the income statement. Regular revaluations should be made so that the carrying amount does not differ materially from	Treated the same as for other properties (depreciated cost). Industry-specific guidance applies to investor entities (for example investment entities)

		fair value	
Inventories	Carried at lower of cost and net realizable value. FIFO or weighted average method is used to determine cost. LIFO method is however, prohibited.	Carried at lower of cost and net realizable value. For cost determination, FIFO or weighted average method is used. LIFO basis of valuation is prohibited. Reversal is required for subsequent increase in value of previous write-downs.	Similar to IFRS; however, use of LIFO is permitted. Reversal of write-down is prohibited.
Biological assets	No specific guidance has been issued. Historical cost is used.in general.	Measured at fair value less estimated point-of-sale costs.	No specific guidance has been issued. Historical cost is used.in general.
Provisions – general	Provisions relating to present obligations from past events recorded if outflow of resources is probable and can be reliably estimated. Discounting of provision is not permitted.	Provisions relating to present obligations from past events recorded if outflow of resources is probable and can be reliably estimated. Provisions are discounted to present value where the effect of the time value of money is material.	Similar to IFRS, with rules for specific situations such as environmental liabilities. Loss contingencies, etc.
Contingencies	Contingent liabilities are disclosed unless the probability of outflows is remote. Contingent gains are	Unrecognised possible losses and probable gains are disclosed.	Similar to IFRS

	neither recognized nor disclosed.		
Government grants	Grants related to fixed assets are shown as deduction from the gross value of the assets concerned. Revenue related government grants are recognized on a systematic basis in the income statement over the periods to match them with the related costs. Grants in the nature of promoter's contribution are credited to capital reserve and treated as a part of shareholder's funds.	Revenue based grants are deferred in the balance sheet and released to the income statement to match the related expenditure that they are intended to compensate. Capital based grants are deferred and matched with the depreciation on the asset for which the grant arises. Grants related to recognized assets are either presented in the balance sheet as deferred income or amortised. Entities may offset capital grants against asset values.	Similar to IFRS, except when conditions are attached to grant. In this case, revenue recognition is delayed until such conditions are met. Long-lived asset contributions recorded as revenue in the period received.
Dividends on ordinary equity shares	Presented as an appropriation to the income statement. Dividends are accounted in the year when proposed.	Presented as a deduction in the statement of changes in shareholders' equity in the period when authorized by shareholders. Dividends are accounted in the year when declared.	Similar to IFRS.
Hyper-inflationary economy	No specific guidance.	Hyperinflation is indicated by characteristics of economic	Hyperinflation is generally indicated by cumulative three-year inflation rate of approximately 100% or more.

		environment of country, which include: Population's attitude towards local currency and prices linked to price index; and if cumulative inflation rate over three years is approaching, or exceeds, 100%. Entities of hyperinflationary economy have to restate their financial statements using a measurement unit current at balance sheet date.	Generally does not permit inflation-adjusted financial statements; instead requires use of reporting currency (US dollar) as functional currency.
Earnings per share – diluted	Weighted average potential dilutive shares are used as denominator for diluted EPS, except in certain circumstances where advance share application money received is treated as dilutive potential equity shares.	Weighted average potential dilutive shares are used as denominator for diluted EPS.	Similar to IFRS.
Related-party transactions	Determined by level of direct or indirect control, joint control and significant influence of one party over another or common control by another entity.	Determined by level of direct or indirect control, joint control and significant influence of one party over another or common control by another entity.	Similar to IFRS. Exemptions from disclosures are narrower than under IFRS.

	However, the determination may be based on legal form rather than substance. Hence, the scope of parties covered under the definition of related party could be less than under IFRS or US GAAP. Exemption from disclosure for certain SMEs having turnover or borrowings below certain limit. No exemption for separate financial statements of subsidiaries.	Name of the parent entity is disclosed and, if different, the ultimate controlling party, regardless of whether transactions occur. For related-party transactions, nature of relationship (seven categories), amount of transactions, outstanding balances, terms and types of transactions are disclosed. Some exemptions available for separate financial statements of subsidiaries.	
Segment reporting	Public entities: primary and secondary (business and geographic) segments are reported based on risks and returns and internal reporting structure. Exemption only for certain SMEs having turnover or borrowings below certain threshold. Group accounting policies or entity accounting policies apply.	Similar to Indian Accounting Standard	Reporting based on operating segments, and the manner in which chief operating decision-maker evaluates financial information for purposes of allocating resources and assessing performance. Internal financial reporting policies apply (even if accounting policies differ from group accounting policy). Disclosures of liabilities and geographical capex are not required.

	Disclosures for primary segment include revenues, results, capital expenditures (capex), total assets, total liabilities and other items. For secondary segment, revenues, total assets and capex are reported.		
Discontinued operations- definition and measurement	Operations and cash flows that can be clearly distinguished for financial reporting and represent a separate major line of business or geographical area of operations. Measurement of discontinued operations is based on AS 28 and 29	Simialr definition to Indian Accounting Standard. However, it also includes a subsidiary acquired exclusively with a view to resale. Measured at lower of carrying amount and fair value less costs to sell.	Wider definition than IFRS: Component that is clearly distinguishable operationally and for financial reporting can be: reporting segment, operating segment, reporting unit, subsidiary or asset grouping. Measurement is same as in IFRS.
Discontinued operations- presentation and main disclosures	At a minimum, separately from continuing operations, pre-tax profit or loss, related taxes, pre-tax gain or loss on disposal should be disclosed on the face of the income statement: Income and expenses line items separate from continuing and discontinued operations are disclosed in the	At a minimum, a single amount is disclosed on face of income statement, and further analysis disclosed in notes for current and prior periods. Assets and liabilities of discontinued operations are presented separately on balance sheet. No restatement of comparative balance	Similar to IFRS. Discontinued and held-for-sale operations are reported as separate line items on face of income statement before extraordinary items.

	notes; however, presented on a combined basis in the income sta tement. No separate presentation for balance sheet items. Exemption for certain SMEs having turnover or borrowings below certain threshold.	sheet.	
Events occurring after the balance sheet date	Financial statements are adjusted for events after the balance sheet date, providing evidence of conditions at balance sheet date and materially affecting amounts in financial statements (adjusting events) except non-adjusting events which are not required to be disclosed in financial statements but are disclosed in report of approving authority e.g., Director's Report.	Financial statements are adjusted for events after the balance sheet date, providing evidence of conditions at balance sheet date and materially affecting amounts in financial statements (adjusting events). Non-adjusting events are disclosed.	Similar to IFRS.

References / Sources:

Website of IASPLUS

Website of IFRS

Accounting Standards and Corporate Accounting Practices

Miller GAAP Guide Level A

Website of FASB