IFRS overview
2017

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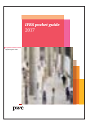

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1. Introduction

This ‘IFRS overview’ provides a summary of the recognition and measurement requirements of International Financial Reporting Standards (IFRSs) issued by the International Accounting Standards Board (IASB) up to October 2017.

The information in this guide is arranged in six sections:

- Accounting principles.
- Income statement and related notes.
- Balance sheet and related notes.
- Consolidated and separate financial statements.
- Other subjects.
- Industry-specific topics.

More detailed guidance and information on these topics can be found on inform.pwc.com in the ‘Accounting topic home pages’ and in the ‘IFRS Manual of accounting’. Click on each heading to visit its topic home page on Inform.

Accounting rules and principles

2. Accounting principles and applicability of IFRS

The IASB has the authority to set IFRSs and to approve interpretations of those standards.

IFRSs are intended to be applied by profit-orientated entities. These entities' financial statements give information about performance, position and cash flow that is useful to a range of users in making financial decisions. These users include shareholders, creditors, employees and the general public. A complete set of financial statements includes:

- A balance sheet.
- A statement of comprehensive income.
- A cash flow statement.
- A statement of changes in equity.
- A description of accounting policies.
- Notes to the financial statements.

The concepts underlying accounting practices under IFRSs are set out in the IASB's 'Conceptual Framework for Financial Reporting' issued in September 2010 (the Framework). The Conceptual Framework covers:

- Objectives of general purpose financial reporting, including information about a reporting entity's economic resources and claims.
- The reporting entity (in the process of being updated).
- Qualitative characteristics of useful financial information (that is, of relevance and faithful representation), and the enhancing qualitative characteristics of comparability, verifiability, timeliness and understandability.
- The remaining text of the 1989 Framework (in the process of being updated), which includes:
- Underlying assumption, the going concern convention.
- Elements of financial statements, including financial position (assets, liabilities and equity) and performance (income and expenses).
- Recognition of elements, including probability of future benefit, reliability of measurement and recognition of assets, liabilities, income and expenses.
- Measurement of elements, including a discussion on historical cost and its alternatives.
- Concepts of capital and its maintenance.

The IASB issued an exposure draft on a revised Framework in May 2015 and it aims to publish the final revised Framework in 2017. In the exposure draft, the IASB focused on those areas that caused problems in practice or that needed updating to reflect concepts developed by the IASB in other projects. These include:

- Definition of assets, liabilities, income and expenses;
- Recognition and derecognition of assets and liabilities;
- Measurement;
- The distinction between equity and liabilities;
- Profit or loss and other comprehensive income (OCI);
- Providing information regarding management's stewardship and re-introducing the concept of prudence;
- Presentation and disclosure; and
- Fundamental concepts (including business model, unit of account, going concern and capital maintenance).

3. First-time adoption of IFRS – IFRS 1

An entity moving from national GAAP to IFRS should apply the requirements of IFRS 1. It applies to an entity's first IFRS financial statements and the interim reports presented under IAS 34, 'Interim financial reporting', that are part of that period. It also applies to entities under 'repeated first-time application'. The basic requirement is for full retrospective application of all IFRSs effective at the reporting date. However, there are a number of optional exemptions and mandatory exceptions to the requirement for retrospective application.

The optional exemptions cover standards for which the IASB considers that retrospective application could prove too difficult or could result in a cost likely to exceed any benefits to users. Any, all or none of the optional exemptions could be applied.

The optional exemptions relate to:

- Business combinations;
- Deemed cost;
- Cumulative translation differences;
- Compound financial instruments;
- Assets and liabilities of subsidiaries, associates and joint ventures;
- Designation of previously recognised financial instruments;
- Share-based payment transactions;
- Insurance contracts;
- Fair value measurement of financial assets or financial liabilities at initial recognition;
- Decommissioning liabilities included in the cost of property, plant and equipment;
- Leases;
- Financial assets or intangible assets accounted for in accordance with IFRIC 12;
- Borrowing costs;
- Investments in subsidiaries, joint ventures and associates;
- Designation of contracts to buy or sell a non-financial item;
- Customer contracts;
- Extinguishing financial liabilities with equity instruments;
- Regulatory deferral accounts (IFRS 14);
- Severe hyperinflation;
- Joint arrangements; and
- Stripping costs in the production phase of a surface.

The mandatory exceptions cover areas in which retrospective application of the IFRS requirements is considered inappropriate. The following exceptions are mandatory, not optional:

- Estimates;
- Hedge accounting;
- Derecognition of financial assets and liabilities;
- Non-controlling interests;
- Classification and measurement of financial assets (IFRS 9);
- Embedded derivatives (IAS 39/IFRS 9);
- Impairment of financial assets; and
- Government loans.

Certain reconciliations from previous GAAP to IFRS are also required.

4. Presentation of financial statements – IAS 1

The objective of financial statements is to provide information that is useful in making economic decisions. IAS 1's objective is to ensure comparability of presentation of that information with the entity's financial statements of previous periods and with the financial statements of other entities.

Financial statements are prepared on a going concern basis, unless management intends either to liquidate the entity or to cease trading, or has no realistic alternative but to do so. Management prepares its financial statements, except for cash flow information, under the accrual basis of accounting.

There is no prescribed format for the financial statements, but there are minimum presentation and disclosure requirements. The implementation guidance to IAS 1 contains illustrative examples of acceptable formats.

Financial statements disclose corresponding information for the preceding period (comparatives), unless a standard or interpretation permits or requires otherwise.

Statement of financial position (balance sheet)

The statement of financial position presents an entity's financial position at a specific point in time. Subject to meeting certain minimum presentation and disclosure requirements, management uses its judgement regarding the form of presentation, such as whether to use a vertical or a horizontal format, which sub-classifications to present, and which information to disclose on the face of the statement or in the notes.

The following items, as a minimum, are presented on the face of the balance sheet:

- Assets – Property, plant and equipment; investment property; intangible assets; financial assets; investments accounted for using the equity method; biological assets; deferred tax assets; current tax assets; inventories; trade and other receivables; and cash and cash equivalents.
- Equity – Issued capital and reserves attributable to the parent's owners; and non-controlling interest.
- Liabilities – Deferred tax liabilities; current tax liabilities; financial liabilities; provisions; and trade and other payables.
- Assets and liabilities held for sale – The total of assets classified as held for sale and assets included in disposal groups classified as held for sale; and liabilities included in disposal groups classified as held for sale in accordance with IFRS 5.

Current and non-current assets, and current and non-current liabilities, are presented as separate classifications in the statement, unless presentation based on liquidity provides information that is reliable and more relevant.

Statement of comprehensive income

The statement of comprehensive income presents an entity's performance over a specific period. An entity presents profit or loss, total other comprehensive income and comprehensive income for the period. [IAS 1 para 81A].

Entities have a choice of presenting the statement of comprehensive income in a single statement or as two statements. The statement of comprehensive income under the single-statement approach includes all items of income and expense, and it includes each component of other comprehensive income classified by nature. Under the two-statement approach, all components of profit or loss are presented in an income statement. The income statement is followed immediately by a statement of comprehensive income, which begins with the total profit or loss for the period and displays all components of other comprehensive income.

Items to be presented in statement of comprehensive income

The following items of profit or loss are, as a minimum, presented in the statement of comprehensive income:

- Revenue, *presenting separately interest revenue calculated using the effective interest method.*[1]
- *Gains and losses arising from the de-recognition of financial assets measured at amortised cost.*
- Finance costs.
- *Impairment losses (including reversals of impairment losses or impairment gains) determined in accordance with Section 5.5 of IFRS 9.*
- Share of the profit and loss of associates and joint ventures accounted for using the equity method.
- *If a financial asset is reclassified out of the amortised cost measurement category so that it is measured at fair value through profit or loss, any gain arising from a difference between the previous amortised cost of the financial asset and its fair value at the reclassification date (as defined in IFRS 9).*
- *If a financial asset is reclassified out of the fair value through other comprehensive income measurement category so that it is measured at fair value through profit or loss, any cumulative gain or loss previously recognised in other comprehensive income that is reclassified to profit or loss.*
- Tax expense
- A single amount for the total of discontinued operations. This comprises the total of:
  - The post-tax profit or loss of discontinued operations; and
  - The post-tax gain or loss recognised on the measurement to fair value less costs to sell or on the disposal of the assets or disposal group(s) constituting the discontinued operation.

[IAS 1 para 82].

Additional line items or sub-headings are presented in this statement where such presentation is relevant to an understanding of the entity's financial performance.

An entity presents each component of other comprehensive income in the statement either (i) net of its related tax effects, or (ii) before its related tax effects, with the aggregate tax effect of these components shown separately.

Material items

The nature and amount of items of income and expense are disclosed separately, where they are material. Disclosure could be in the statement or in the notes. Such income and expenses might include: restructuring costs; write-downs of inventories or property, plant and equipment; litigation settlements; and gains or losses on disposals of non-current assets.

Other comprehensive income

An entity presents items of other comprehensive income grouped into those that will be reclassified subsequently to profit or loss, and those that will not be reclassified. An entity discloses reclassification adjustments relating to components of other comprehensive income. The IAS 1 amendments clarify that the entity's share of items of comprehensive income of associates and joint ventures is presented separately, analysed into those items that will not be reclassified subsequently to profit or loss and those that will be so reclassified when specific conditions are met.

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[1] *The text in italics is added by IFRS 9, 'Financial instruments'. IFRS 9 is effective for accounting periods beginning on or after 1 January 2018.*

An entity presents each component of other comprehensive income in the statement either (i) net of its related tax effects, or (ii) before its related tax effects, with the aggregate tax effect of these components shown separately.

Statement of changes in equity

The following items are presented in the statement of changes in equity:

- Total comprehensive income for the period, showing separately the total amounts attributable to the parent's owners and to non-controlling interest.
- For each component of equity, the effects of retrospective application or retrospective restatement recognised in accordance with IAS 8.
- For each component of equity, a reconciliation between the carrying amount at the beginning and the end of the period, separately disclosing changes resulting from:
  - Profit or loss;
  - Other comprehensive income; and
  - Transactions with owners in their capacity as owners, showing separately contributions by and distributions to owners and changes in ownership interests in subsidiaries that do not result in a loss of control.

The amounts of dividends recognised as distributions to owners during the period, and the related amount of dividends per share, should be disclosed.

Statement of cash flows

Cash flow statements are addressed in a separate summary dealing with the requirements of IAS 7.

Notes to the financial statements

The notes are an integral part of the financial statements. Notes provide information additional to the amounts disclosed in the 'primary' statements. They also include significant accounting policies, critical accounting estimates and judgements, and disclosures on capital and puttable financial instruments classified as equity.

5. Accounting policies, accounting estimates and errors – IAS 8

An entity follows the accounting policies required by IFRS that are relevant to the transactions, other events and conditions of the entity. Sometimes, standards offer a policy choice; there are other situations where no guidance is given by IFRSs. In these situations, management should develop and apply appropriate accounting policies.

Management uses judgement in developing and applying an accounting policy that results in information that is relevant and reliable. Reliable information demonstrates the following qualities: faithful representation, substance over form, neutrality, prudence and completeness. If there is no IFRS or interpretation that is specifically applicable, management considers the applicability of the requirements in IFRS on similar and related issues, and then the definitions, recognition criteria and measurement concepts for assets, liabilities, income and expenses in the Framework. Management can also consider the most recent pronouncements of other standard-setting bodies, other accounting literature and accepted industry practices, where these do not conflict with IFRS.

Accounting policies are applied consistently to similar items, transactions and events (unless a standard permits or requires otherwise).

Changes in accounting policies

Changes in accounting policies made on adoption of a new standard or interpretation are accounted for in accordance with the transitional provisions (if any) within that standard or interpretation. If a change in policy on initial application of a new standard does not include specific transitional provisions, or it is a voluntary change in policy, it should be accounted for retrospectively (that is, by restating all comparative figures presented), unless this is impracticable. There is also a specific exception for the initial adoption of a policy to measure property, plant and equipment or intangible assets by applying the revaluation model, which would be accounted for in the year in which the change is being made.

Issue of new/revised standards not yet effective

Standards are normally published in advance of the required implementation date. In the intervening period, where a new/revised standard that is relevant to an entity has been issued but is not yet effective, management discloses this fact. It also provides the known or reasonably estimable information relevant to assessing the impact that the application of the standard might have on the entity's financial statements in the period of initial recognition.

Changes in accounting estimates

An entity recognises changes in accounting estimates prospectively, by including the effects in profit or loss in the period that is affected (the period of the change and future periods, if applicable), except where the change in estimate gives rise to changes in assets, liabilities or equity. In this case, it is recognised by adjusting the carrying amount of the related asset, liability or equity in the period of the change.

Errors

Errors might arise from mistakes (mathematical or application of accounting policies), oversights or misinterpretation of facts, and fraud.

Errors that are discovered in a subsequent period are prior-period errors. Material prior-period errors are adjusted retrospectively (that is, by restating comparative figures), unless this is impracticable (that is, it cannot be done after '*making every reasonable effort to do so*').

6. Fair value – IFRS 13

IFRS 13, 'Fair value management', provides a common framework for measuring fair value where required or permitted by another IFRS.

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*'. [IFRS 13 para 9]. The key principle is that fair value is the exit price, from the perspective of market participants who hold the asset or owe the liability, at the measurement date. It is based on the perspective of market participants rather than the entity itself, so fair value is not affected by an entity's intentions towards the asset, liability or equity item that is being fair valued.

A fair value measurement requires management to determine four things: the particular asset or liability that is the subject of the measurement (consistent with its unit of account); the highest and best use for a non-financial asset; the principal (or, in its absence, the most advantageous) market; and the valuation technique. [IFRS 13 para B2].

IFRS 13 addresses how to measure fair value, but it does not stipulate when fair value can or should be used.

7. Financial instruments

7.1. Introduction to financial instruments – Objectives, definitions and scope – IAS 32, IAS 39, IFRS 9 and IFRS 7

The objective of the four financial instruments standards (IAS 32, IAS 39, IFRS 9 and IFRS 7) is to establish requirements for all aspects of accounting for financial instruments, including distinguishing debt from equity, balance sheet offsetting, recognition, derecognition, measurement, hedge accounting and disclosure.

The standards' scope is broad. The standards cover all types of financial instruments, including receivables, payables, investments in bonds and shares, borrowings and derivatives. They also apply to certain contracts to buy or sell non-financial assets (such as commodities) that can be net-settled in cash or another financial instrument. Financial instruments are recognised and measured according to IAS 39/IFRS 9's requirements and are disclosed in accordance with IFRS 7.

For annual reporting periods beginning on or after 1 January 2018 IFRS 9 replaces IAS 39. However for some preparers IAS 39 will remain relevant (for example insurers that apply the IFRS 4 deferral of IFRS 9). On transition to IFRS 9 entities may also continue to apply IAS 39 hedge accounting.

In addition, requirements for fair value measurement and disclosures are covered by IFRS 13.

IAS 32 establishes principles for presenting financial instruments as financial liabilities or equity, and for offsetting financial assets and financial liabilities.

Financial instruments represent contractual rights or obligations to receive or pay cash or other financial assets.

A financial asset is cash; a contractual right to receive cash or another financial asset; a contractual right to exchange financial assets or liabilities with another entity under conditions that are potentially favourable; or an equity instrument of another entity.

A financial liability is a contractual obligation to deliver cash or another financial asset; or to exchange financial instruments with another entity under conditions that are potentially unfavourable.

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

A derivative is a financial instrument that derives its value from an underlying price or index; requires little or no initial net investment; and is settled at a future date.

7.2. Classification and measurement – IFRS 9

The publication of IFRS 9 in July 2014 was the culmination of the IASB's efforts to replace IAS 39. IFRS 9 was released in phases from 2009 to 2014. The final standard was issued in July 2014, with a proposed mandatory effective date of periods beginning on or after 1 January 2018. Early application of IFRS 9 is permitted. The Board also amended the transitional provisions to provide relief from restating comparative information, and it introduced new disclosures to help users of financial statements to understand the effect of moving to the IFRS 9 classification and measurement model. The amendment, above, to prepayment features with negative compensation is effective on or after 1 January 2019, with early application permitted.

Classification and measurement

IFRS 9 replaces the multiple classification and measurement models for financial assets in IAS 39 with a single model that has three classification categories: amortised cost; fair value through other comprehensive income (OCI); and fair value through profit and loss. Classification under IFRS 9 is driven by the entity's business model for managing the financial assets and whether the contractual characteristics of the financial assets represent solely payments of principal and interest. However, at initial recognition an entity can irrevocably designate a financial asset as measured at fair value through profit and loss, if doing so eliminates or significantly reduces an accounting mismatch.

The new standard removes the requirement to separate embedded derivatives from financial asset hosts. It requires a hybrid contract to be classified, in its entirety, at either amortised cost or fair value if the contractual cash flows do not represent solely payments of principal and interest. IFRS 9 prohibits reclassifications, except in rare circumstances when the entity's business model changes. There is specific guidance for contractually linked instruments that leverage credit risk, which is often the case with investment tranches in a securitisation.

IFRS 9's classification principles indicate that all equity investments should be measured at fair value through profit and loss. However, an entity has the ability to make an irrevocable election, on an instrument-by-instrument basis, to present changes in fair value in other comprehensive income (OCI) rather than profit or loss, provided that the instrument is not held for trading. IFRS 9 removes the cost exemption for unquoted equities and derivatives on unquoted equities, but it provides guidance on when cost might be an appropriate estimate of fair value.

Under IFRS 9, financial liabilities continue to be measured at amortised cost, unless they are required to be measured at fair value through profit or loss or an entity has opted to measure a liability at fair value through profit or loss. However, IFRS 9 changes the accounting for those financial liabilities where the fair value option has been elected. For such liabilities, changes in fair value related to changes in own credit risk are presented separately in OCI.

7.3. Embedded derivatives – IFRS 9

Some financial instruments and other contracts combine a derivative and a non-derivative host contract in a single contract. The derivative part of the contract is referred to as an 'embedded derivative'. Its effect is that some of the contract's cash flows vary in a similar way to a stand-alone derivative. For example, the principal amount of a bond might vary with changes in a stock market index. In this case, the embedded derivative is an equity derivative on the relevant stock market index.

Embedded derivatives that are not 'closely related' to the host contract are separated and accounted for as stand-alone derivatives (that is, measured at fair value, with changes in fair value recognised in profit or loss). An embedded derivative is not 'closely related' if its economic characteristics and risks are different from those of the rest of the contract. IFRS 9 sets out many examples to help determine when this test is (and is not) met.

Analysing contracts for potential embedded derivatives is one of the more challenging aspects of IFRS 9.

7.4. Financial liabilities and equity – IAS 32, IFRS 9

The classification of a financial instrument by the issuer as either a liability (debt) or equity can have a significant impact on an entity's gearing (debt-to-equity ratio) and reported earnings. It could also affect the entity's debt covenants.

The critical feature of a liability is that, under the terms of the instrument, the issuer is or can be required to deliver either cash or another financial asset to the holder; it cannot avoid this obligation. For example, a debenture under which the issuer is required to make interest payments and redeem the debenture for cash is a financial liability.

An instrument is classified as equity where it represents a residual interest in the issuer's assets after deducting all of its liabilities; or, put another way, where the issuer has no obligation under the terms of the instrument to deliver cash or other financial assets to another entity. Ordinary shares, where all of the payments are at the discretion of the issuer, are an example of equity of the issuer.

In addition, the following types of financial instrument are accounted for as equity, provided that they have particular features and meet specific conditions:

- Puttable financial instruments (for example, some shares issued by co-operative entities, funds and some partnership interests).
- Instruments or components of 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 (for example, some shares issued by limited-life entities).

The classification of the financial instrument as either debt or equity is based on the substance of the contractual arrangement of the instrument, rather than its legal form. This means, for example, that a redeemable preference share, which is economically the same as a bond, is accounted for in the same way as a bond. The redeemable preference share is therefore treated as a liability rather than equity, even though legally it is a share of the issuer.

Other instruments might not be as straightforward. An analysis of the terms of each instrument (in light of the detailed classification requirements) is necessary, particularly since some financial instruments contain both liability and equity features. Such instruments (such as bonds that are convertible into a fixed number of equity shares) are accounted for as separate components of liability and equity (being the option to convert if all of the criteria for equity are met).

The treatment of interest, dividends, losses and gains in the income statement follows the classification of the related instrument. If a preference share is classified as a liability, its coupon is shown as interest. However, the discretionary coupon on an instrument that is treated as equity is shown as a distribution within equity.

7.5. Recognition and derecognition –IAS 39, IFRS 9

Recognition

Recognition for financial assets and financial liabilities tends to be straightforward. An entity recognises a financial asset or a financial liability at the time when it becomes a party to a contract.

Derecognition

Derecognition is the term used for ceasing to recognise a financial asset or financial liability on an entity's statement of financial position. These rules are more complex.

Assets

An entity that holds a financial asset might raise finance using the asset as security for the finance, or as the primary source of cash flows from which to repay the finance. The derecognition requirements of IAS 39 and IFRS 9 determine whether the transaction is a sale of the financial assets (and therefore the entity ceases to recognise the assets), or whether finance has been secured on the assets (and the entity recognises a liability for any proceeds received). This evaluation might be straightforward. For example, it is clear, with little or no analysis, that a financial asset is derecognised in an unconditional transfer of it to a third party, with no risks and rewards of the asset being retained. Conversely, derecognition is not allowed where an asset has been transferred, but substantially all of the risks and rewards of the asset have been retained through the terms of the agreement. However, the analysis might be more complex in other cases. Securitisation and debt factoring are examples of more complex transactions where derecognition will need careful consideration.

Liabilities

An entity may only cease to recognise (derecognise) a financial liability when it is extinguished – that is, when the obligation is discharged, cancelled or expired, or when the debtor is legally released from the liability by law or by the creditor agreeing to such a release.

Entities frequently negotiate with bankers or bond-holders to amend or cancel existing debt and replace it with new debt with the same lender on different terms. IAS 39 and IFRS 9 provide guidance to distinguish between the settlement or extinguishment of debt that is replaced by new debt and the restructuring or modification of existing debt. The distinction is based on whether or not the new debt has substantially different terms from the old debt.

Alternatively, an entity might negotiate with its third party lenders to exchange existing debt for equity. In these circumstances, the difference between the carrying amount of the financial liability extinguished and the fair value of the equity issued is recognised in the income statement.

7.6. Impairment – IFRS 9

The impairment rules of IFRS 9 introduce a new, forward-looking, expected credit loss ('ECL') impairment model which will generally result in earlier recognition of losses compared to IAS 39. These changes are likely to have a significant impact on entities that have significant financial assets (in particular, financial institutions).

The new impairment model introduces a three-stage approach. Stage 1 includes financial instruments that have not had a significant increase in credit risk since initial recognition or that have low credit risk at the reporting date. For these assets, 12-month ECL (that is, expected losses arising from the risk of default in the next 12 months) are recognised, and interest revenue is calculated on the gross carrying amount of the asset (that is, without deduction for credit allowance). Stage 2 includes financial instruments that have had a significant increase in credit risk since initial recognition (unless they have low credit risk at the reporting date) but are not credit-impaired. For these assets, lifetime ECL (that is, expected losses arising from the risk of default over the life of the financial instrument) are recognised, and interest revenue is still calculated on the gross carrying amount of the asset. Stage 3 consists of financial assets that are credit-impaired, which is where one or more events that have a detrimental impact on the estimated future cash flows of the financial asset have occurred. For these assets, lifetime ECL are also recognised, but interest revenue is calculated on the net carrying amount (that is, net of the ECL allowance).

For trade receivables or contract assets that do not contain a significant financing component, the loss allowance should be measured, at initial recognition and throughout the life of the receivable, at an amount equal to lifetime ECL. As an exception to the general model, if the credit risk of a financial instrument is low at the reporting date, management can measure impairment using 12-month ECL, and so it does not have to assess whether a significant increase in credit risk has occurred.

In many cases, application of the new requirements will require significant judgement – in particular, when assessing whether there has been a significant increase in credit risk (triggering a move from stage 1 to stage 2, and a consequential increase from 12-month ECL to lifetime ECL) and in estimating ECL, including the effect of forward-looking information. IFRS 9 also introduces significant new disclosure requirements.

7.7. Hedge accounting – IFRS 9

'Hedging' is a risk management activity. More specifically, it is the process of using a financial instrument (usually a derivative) to mitigate all or some of the risk of a hedged item. 'Hedge accounting' changes the timing of recognition of gains and losses on either the hedged item or the hedging instrument, so that both are recognised in profit or loss in the same accounting period, in order to record the economic substance of the combination of the hedged item and hedging instrument.

To qualify for hedge accounting, IFRS 9 includes the following requirements:

- An entity should formally designate and document the hedging relationship at the inception of the hedge. This includes identifying the hedging instrument, the hedged item or transaction, the nature of the risk being hedged and how the entity will assess hedge effectiveness, identification of sources of ineffectiveness, how the hedge ratio will be determined, and the entity's risk management objective and strategy for undertaking the hedge.
- There must be an economic relationship between the hedging instrument and the hedged item. There must be an expectation that the value of the hedging instrument and the value of the hedged item will move in the opposite direction as a result of the common underlying or hedged risk.
- Credit risk should not dominate value changes. Even if there is an economic relationship, a change in the credit risk of the hedging instrument or the hedged item must not be of such magnitude that it dominates the value changes that result from that economic relationship.

- The designated hedge ratio should be consistent with the risk management strategy. The hedge ratio is defined as the relationship between the quantity of the hedging instrument and the quantity of the hedged item, in terms of their relative weighting.

There is no 80–125% effectiveness 'bright line'. As such, a retrospective effectiveness test is no longer required to prove that the effectiveness was between 80% and 125%. However, all ineffectiveness should still be calculated and recorded in the income statement.

There are three types of hedge relationship:

- Fair value hedge – A hedge of the exposure to changes in the fair value of a recognised asset or liability, or a firm commitment.
- Cash flow hedge – A hedge of the exposure to variability in cash flows of a recognised asset or liability, a firm commitment or a highly probable forecast transaction.
- Net investment hedge – A hedge of the foreign currency risk on a net investment in a foreign operation.

For a fair value hedge, the hedged item is adjusted for the gain or loss attributable to the hedged risk. That element is included in the income statement, where it will offset the gain or loss on the hedging instrument.

For a cash flow hedge, gains and losses on the hedging instrument are initially included in other comprehensive income. The amount included in other comprehensive income is the lower of the fair value change of the hedging instrument and that of the hedged item. Where the hedging instrument has a fair value change greater than the hedged item, the excess is recorded within profit or loss as ineffectiveness. Gains or losses deferred in other comprehensive income are reclassified to profit or loss when the hedged item affects the income statement. If the hedged item is the forecast acquisition of a non-financial asset or liability, the carrying amount of the non-financial asset or liability is adjusted for the hedging gain or loss at initial recognition.

Hedges of a net investment in a foreign operation are accounted for similarly to cash flow hedges.

7.8. Disclosure – IFRS 7, IFRS 9

There have been significant developments in risk management concepts and practices in recent years. New techniques have evolved for measuring and managing exposures to risks arising from financial instruments. This, coupled with the significant volatility experienced in the financial markets, has increased the need for more relevant information and greater transparency about an entity's exposures arising from financial instruments and how those risks are managed. Financial statement users and other investors need such information to make more informed judgements about risks arising from entities' use of financial instruments and their associated returns.

IFRS 7 sets out disclosure requirements that are intended to enable users to evaluate the significance of financial instruments for an entity's financial position and performance, and to understand the nature and extent of risks arising from those financial instruments to which the entity is exposed. These risks include credit risk, liquidity risk and market risk. IFRS 13 requires disclosure of a three-level hierarchy for fair value measurement, and it requires some specific quantitative disclosures for financial instruments at the lowest level in the hierarchy.

The disclosure requirements do not just apply to banks and financial institutions. All entities that have financial instruments are affected – even simple instruments such as borrowings, accounts payable and receivable, cash and investments.

8. Foreign currencies – IAS 21, IAS 29

IAS 21

Many entities do business with overseas suppliers or customers, or have overseas operations. This gives rise to two main accounting issues:

- Some transactions (for example, those with overseas suppliers or customers) might be denominated in foreign currencies. These transactions are expressed in the entity's own currency ('functional currency') for financial reporting purposes.
- A parent entity might have foreign operations, such as overseas subsidiaries, branches or associates. The functional currency of these foreign operations might be different from the parent entity's functional currency, and therefore the accounting records might be maintained in different currencies. Because it is not possible to combine transactions measured in different currencies, the foreign operation's results and financial position are translated into a single currency, namely that in which the group's consolidated financial statements are reported ('presentation currency').

The methods required for each of the above circumstances are summarised below.

Expressing foreign currency transactions in the entity's functional currency

A foreign currency transaction is expressed in an entity's functional currency, using the exchange rate at the transaction date. Foreign currency balances representing cash or amounts to be received or paid in cash ('monetary items') are retranslated at the end of the reporting period, using the exchange rate on that date. Exchange differences on such monetary items are recognised as income or expense for the period. Non-monetary balances that are not remeasured at fair value and are denominated in a foreign currency are expressed in the functional currency, using the exchange rate at the transaction date. Where a non-monetary item is remeasured at fair value in the financial statements, the exchange rate at the date when fair value was determined is used.

Translating functional currency financial statements into a presentation currency

Assets and liabilities are translated from the functional currency to the presentation currency at the closing rate at the end of the reporting period. The income statement is translated at exchange rates at the dates of the transactions, or at the average rate if that approximates the actual rates. All resulting exchange differences are recognised in other comprehensive income.

The financial statements of a foreign operation that has the currency of a hyper-inflationary economy as its functional currency are first restated in accordance with IAS 29, 'Financial reporting in hyper-inflationary economies'. All components are then translated to the presentation currency at the closing rate at the end of the reporting period.

IAS 29

Conventional financial reporting is distorted by inflation. This is especially the case with hyper-inflation, where the measuring unit (the currency unit) is not stable. Adjustments to stabilise the unit of measurement – to measure items in units of constant purchasing power – make the financial statements more relevant and reliable. IAS 29 requires financial statements prepared in the currency of a hyper-inflationary economy to be stated in terms of the value of money at the end of the reporting period. This requirement relies on an understanding of complex economic concepts, a knowledge of the entity's financial and operating patterns, and a detailed series of procedures.

Prices change over time, as the result of political, economic and social factors. Two phenomena should be distinguished: (1) changes in supply and demand and technological changes might cause prices of individual items to increase or decrease independently of each other ('specific price changes'); and (2) other factors in the economy might result in changes in the general level of prices, and therefore in the general purchasing power of money ('general price changes'). The purchasing power of money declines as the level of prices of goods and services rises. The purchasing power of money in an inflationary environment and the price level are interdependent.

Financial statements, unadjusted for inflation in most countries, are prepared on the basis of historical cost, without regard either to changes in the general level of prices or to changes in specific prices of assets held. However, there are exceptions where the entity is required to, or chooses to, measure certain assets or liabilities at fair value. Examples are property, plant and equipment, which could be revalued to fair value under IAS 16, and biological assets, which are generally required to be measured at fair value by IAS 41. This produces a meaningful result, provided that there are no dramatic changes in the purchasing power of money. A small number of entities, however, present financial statements that are based on a current cost approach that reflects the effects of changes in the specific prices of assets held.

Significant changes in the purchasing power of money, particularly in a hyper-inflationary economy, mean that financial statements unadjusted for inflation are not useful and are likely to be misleading. Amounts are not comparable between periods, or even within a period, and the gain or loss in general purchasing power that arises in the reporting period is not recorded. Financial statements unadjusted for inflation do not properly reflect the company's position at the end of the reporting period, the results of its operations or its cash flows. In a hyper-inflationary economy, financial statements, whether they are based on an historical cost approach or a current cost approach, are useful only if they are expressed in terms of the measuring unit current at the end of the reporting period.

Inflation-adjusted financial statements are an extension to, and not a departure from, historical cost accounting. IAS 29 aims to overcome the limitations of historical cost financial reporting in hyper-inflationary environments, but it does not reflect specific price changes in assets and liabilities.

9. Insurance contracts – IFRS 4, IFRS 17

IFRS 4

Insurance contracts are contracts where an entity accepts significant insurance risk from another party (the policyholder) by agreeing to compensate the policyholder if the insured event adversely affects the policyholder. The risk transferred in the contract must be insurance risk, which is any risk except for financial risk.

IFRS 4 applies to all issuers of insurance contracts, whether or not the entity is legally an insurance company. It does not apply to accounting for insurance contracts by policyholders.

IFRS 4 was designed as an interim standard, pending completion of IFRS 17. It allows entities to continue with their existing accounting policies for insurance contracts if those policies meet certain minimum criteria. One of the minimum criteria is that the amount of the insurance liability is subject to a liability adequacy test. This test considers current estimates of all contractual and related cash flows. If the liability adequacy test identifies that the insurance liability is inadequate, the entire deficiency is recognised in the income statement.

Accounting policies modelled on IAS 37, 'Provisions, contingent liabilities and contingent assets', are appropriate in cases where the issuer is not an insurance company and where there is no specific local GAAP for insurance contracts (or the local GAAP is only directed at insurance companies).

Disclosure is particularly important for information relating to insurance contracts, because entities can continue to use local GAAP accounting policies for measurement. IFRS 4 has two main principles for disclosure. Entities should disclose information that:

- Identifies and explains the amounts in its financial statements arising from insurance contracts; and
- Enables users of its financial statements to evaluate the nature and extent of risks arising from insurance contracts.

IFRS 17

In May 2017, the IASB issued IFRS 17, 'Insurance contracts', and thereby started a new epoch of accounting for insurers. Whereas the current standard, IFRS 4, allows insurers to use their local GAAP, IFRS 17 defines clear and consistent rules that will significantly increase the comparability of financial statements. For insurers, the transition to IFRS 17 will have an impact on financial statements and on key performance indicators.

Under IFRS 17, the 'general model' requires entities to measure an insurance contract, at initial recognition, at the total of the fulfilment cash flows (comprising the estimated future cash flows, an adjustment to reflect the time value of money and an explicit risk adjustment for non-financial risk) and the contractual service margin. The fulfilment cash flows are remeasured on a current basis each reporting period. The unearned profit (contractual service margin) is recognised over the coverage period.

Aside from this general model, the standard provides, as a simplification, the 'premium allocation approach'. This simplified approach is applicable for certain types of contract, including those with a coverage period of one year or less.

For insurance contracts with direct participation features, the 'variable fee approach' applies. The variable fee approach is a variation on the general model. When applying the variable fee approach, the entity's share of the fair value changes of the underlying items is included in the contractual service margin. As a consequence, the fair value changes are not recognised in profit or loss in the period in which they occur but over the remaining life of the contract.

The new standard is applicable for annual periods beginning on or after 1 January 2021. Early application is permitted for entities that apply IFRS 9, 'Financial instruments', and IFRS 15, 'Revenue from contracts with customers', at or before the date of initial application of IFRS 17. The standard can be applied retrospectively in accordance with IAS 8, but it also contains a 'modified retrospective approach' and a 'fair value approach' for transition, depending on the availability of data.

10. Revenue and construction contracts – IAS 18, IFRS 15, IAS 11 and IAS 20

Revenue is the gross inflow of economic benefits arising in the ordinary course of an entity's activities, and it is measured at the fair value of the consideration received or receivable. Where the substance of a single transaction indicates that it includes separately identifiable components, revenue is allocated to these components generally by reference to their fair values. Revenue is recognised for each component separately by applying the recognition criteria below. For example, where a product is sold with a subsequent service, revenue is allocated initially to the product component and the service component, and it is recognised separately thereafter when the criteria for revenue recognition are met for each component.

Revenue – IAS 18

Revenue arising from the sale of goods is recognised when: an entity transfers the significant risks and rewards of ownership and gives up managerial involvement usually associated with ownership or control; it is probable that economic benefits will flow to the entity; and the amount of revenue and costs can be measured reliably.

Examples of transactions where the entity retains significant risks and rewards of ownership and revenue is not recognised are as follows:

- Where the entity retains an obligation for unsatisfactory performance not covered by normal warranty provisions;
- Where the buyer has the power to rescind the purchase for a reason specified in the sales contract, and the entity is uncertain about the probability of return; and
- Where the goods are shipped subject to installation, and that installation is a significant part of the contract.

Revenue from the rendering of services is recognised when the outcome of the transaction can be estimated reliably. This is done by reference to the stage of completion of the transaction at the balance sheet date, using requirements similar to those for construction contracts. The outcome of a transaction can be estimated reliably when: the amount of revenue can be measured reliably; it is probable that economic benefits will flow to the entity; the stage of completion can be measured reliably; and the costs incurred and costs to complete can be reliably measured.

Interest income is recognised using the effective interest rate method. Royalties are recognised on an accruals basis, in accordance with the substance of the relevant agreement. Dividends are recognised when the shareholder's right to receive payment is established.

IFRIC 13, 'Customer loyalty programmes', clarifies the accounting for award credits granted to customers when they purchase goods or services (for example, under frequent flyer or supermarket loyalty schemes). The fair value of the consideration received or receivable in respect of the initial sale is allocated between the award credits and the other components of the sale.

IFRIC 18, 'Transfers of assets from customers', clarifies the accounting for arrangements where an item of property, plant and equipment is transferred by a customer (or the entity might receive the cash from the customer for the acquisition or construction of those items of property, plant and equipment), in return for connection to a network and/or ongoing access to goods or services. IFRIC 18 will be most relevant to the utility industry, but it might also apply to other transactions (for example, where a customer transfers ownership of property, plant and equipment as part of an outsourcing agreement).

Revenue – IFRS 15

In May 2014, the IASB and FASB issued their converged standard on revenue recognition – IFRS 15 and ASC 606, Revenue from Contracts with Customers. The standard contains principles that an entity will apply to determine the measurement of revenue and the timing of when it is recognised. The underlying principle is that an entity will recognise revenue to depict the transfer of goods or services to customers at an amount that the entity expects to be entitled to in exchange for those goods or services. The standard could significantly change how many entities recognise revenue. The standard will also result in a significant increase in the volume of disclosures related to revenue recognition.

Under IFRS 15, revenue is recognised based on the satisfaction of performance obligations. In applying IFRS 15, entities would follow this five-step process:

1. Identify the contract with a customer.
2. Identify the separate performance obligations in the contract.
3. Determine the transaction price.
4. Allocate the transaction price to the separate performance obligations.
5. Recognise revenue when (or as) each performance obligation is satisfied.

1. Identify the contract with a customer

The model starts with identifying the contract with the customer, and whether an entity should combine, for accounting purposes, two or more contracts, to properly reflect the economics of the underlying transaction. An entity will need to conclude that it is 'probable', at the inception of the contract, that the entity will collect the consideration to which it will ultimately be entitled in exchange for the goods or services that are transferred to the customer in order for a contract to be within the scope of the revenue standard. The term 'probable' has a different meaning under IFRS (where it means 'more likely than not' – that is, greater than 50% likelihood) and US GAAP (where it is generally interpreted as 75–80% likelihood). This could result in a difference in the accounting for a contract if there is a likelihood of non-payment at inception. However, the Boards decided that there would not be a significant practical effect of the different meaning of the same term, because the population of transactions that would fail to meet the criterion in paragraph 9(e) of IFRS 15 would be small.

Two or more contracts (including contracts with related parties of the customers) should be combined if: the contracts are entered into at or near the same time and the contracts are negotiated with a single commercial objective; the amount of consideration in one contract depends on the other contract; or the goods or services in the contracts are interrelated. A contract modification is treated as a separate contract only if it results in the addition of a separate performance obligation and the price reflects the stand-alone selling price (that is, the price at which the good or service would be sold on a stand-alone basis) of the additional performance obligation. The modification is otherwise accounted for as an adjustment to the original contract, either through a cumulative catch-up adjustment to revenue or a prospective adjustment to revenue when future performance obligations are satisfied, depending on whether the remaining goods and services are distinct. While aspects of this model are similar to IAS 11/IAS 18, careful consideration will be needed to ensure that the model is applied to the appropriate unit of account.

2. Identify the separate performance obligations in the contract

An entity will be required to identify all performance obligations in a contract. Performance obligations are promises to transfer goods or services to a customer, and they are similar to what we know today as 'elements' or 'deliverables'. Performance obligations might be explicitly stated in the contract, but they might also arise in other ways. Legal or statutory requirements to deliver a good or perform a service might create performance obligations, even though such obligations are not explicit in the contract. A performance obligation could also be created through customary business practices, such as an entity's practice of providing customer support, or by published policies or specific company statements. This could result in an increased number of performance obligations within an arrangement, possibly changing the timing of revenue recognition.

An entity accounts for each promised good or service as a separate performance obligation if the good or service is distinct. Such a good or service is distinct if both of the following criteria are met:

1. The customer can benefit from the good or service, either on its own or together with other resources that are readily available to the customer (that is, the good or service is capable of being distinct); and
2. The entity's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract (that is, the promise to transfer the good or service is distinct within the context of the contract).

Sales-type incentives (such as free products or customer loyalty programmes) are currently recognised as marketing expense under US GAAP in some circumstances. These incentives might be performance obligations under IFRS 15; if so, revenue will be deferred until such obligations are satisfied, such as when a customer redeems loyalty points. Other potential changes in this area include accounting for return rights, licences and options.

3. Determine the transaction price

Once an entity identifies the performance obligations in a contract, the obligations will be measured by reference to the transaction price. The transaction price reflects the amount of consideration that an entity expects to be entitled to in exchange for goods or services transferred. The amount of expected consideration captures: (1) variable consideration if it is 'highly probable' (IFRS) or 'probable' (US GAAP) that the amount will not result in a significant revenue reversal if estimates change; (2) an assessment of time value of money (as a practical expedient, an entity need not make this assessment where the period between payment and the transfer of goods or services is less than one year); (3) non-cash consideration, generally at fair value; and (4) less any consideration paid to customers.

Variable consideration is measured using either a 'probability weighted' or 'most likely amount' approach, whichever is most predictive of the final outcome. Inclusion of variable consideration in the initial measurement of the transaction price might result in a significant change in the timing of revenue recognition. Such consideration is recognised as the entity satisfies its related performance obligations, provided that (1) the entity has relevant experience with similar performance obligations (or other valid evidence) that allows it to estimate the cumulative amount of revenue for a satisfied performance obligation, and (2) based on that experience, the entity does not expect a significant reversal in future periods in the cumulative amount of revenue recognised for that performance obligation. Revenue could, therefore, be recognised earlier than under IAS 11/IAS 18 if an entity meets the conditions to include variable consideration in the transaction price. Judgement will be needed to assess whether the entity has predictive experience about the outcome of a contract. The following indicators might suggest that the entity's experience is not predictive of the outcome of a contract: (1) the amount of consideration is highly susceptible to factors outside the influence of the entity; (2) the uncertainty about the amount of consideration is not expected to be resolved for a long period of time; (3) the entity's experience with similar types of contract is limited; and (4) the contract has a large number and broad range of possible consideration amounts.

4. Allocate the transaction price to the separate performance obligations

For contracts with multiple performance obligations (deliverables), the performance obligations should be separately accounted for, to the extent that the pattern of transfer of goods and services is different. Once an entity identifies and determines whether to separately account for all of the performance obligations in a contract, the transaction price is allocated to these separate performance obligations, based on relative stand-alone selling prices.

The best evidence of stand-alone selling price is the observable price of a good or service where the entity sells that good or service separately. The selling price is estimated if a stand-alone selling price is not available. Some possible estimation methods include (1) cost plus a reasonable margin, and (2) evaluation of stand-alone sales prices of the same or similar products, if available. If the stand-alone selling price is highly variable or uncertain, entities could use a residual approach to aid in estimating the stand-alone selling price (that is, total transaction price less the stand-alone selling prices of other goods or services in the contract). An entity could also allocate discounts and variable amounts entirely to one (or more) performance obligations if certain conditions are met.

5. Recognise revenue when (or as) each performance obligation is satisfied

Revenue should be recognised when a promised good or service is transferred to the customer. This occurs when the customer obtains control of that good or service. Control can transfer at a point in time or continuously over time. Determining when control transfers will require significant judgement. An entity satisfies a performance obligation over time if: (1) the customer is receiving and consuming the benefits of the entity's performance as the entity performs (that is, another entity would not need to substantially re-perform the work completed to date); (2) the entity's performance creates or enhances an asset that the customer controls as the asset is created or enhanced; or (3) the entity's performance does not create an asset with an alternative use to the entity, the entity has a right to payment for performance completed to date that includes compensation for a reasonable profit margin, and it expects to fulfil the contract. A good or service not satisfied over time is satisfied at a point in time. Indicators to consider, in determining when the customer obtains control of a promised asset, include: (1) the customer has an unconditional obligation to pay; (2) the customer has legal title; (3) the customer has physical possession; (4) the customer has the risks and rewards of ownership of the good; and (5) the customer has accepted the asset. These indicators are not a checklist, nor are they all-inclusive. All relevant factors should be considered, to determine whether the customer has obtained control of a good.

If control is transferred continuously over time, an entity could use output methods (for example, units delivered) or input methods (for example, costs incurred or passage of time) to measure the amount of revenue to be recognised. The method that best depicts the transfer of goods or services to the customer should be applied consistently throughout the contract and to similar contracts with customers.

Contract cost guidance

IFRS 15 also includes guidance related to contract costs. Costs relating to satisfied performance obligations and costs related to inefficiencies should be expensed as incurred. Incremental costs of obtaining a contract (for example, a sales commission) should be recognised as an asset if they are expected to be recovered. An entity can expense the cost of obtaining a contract if the amortisation period would be less than one year. Entities should evaluate whether direct costs incurred in fulfilling a contract are within the scope of other standards (for example, inventory, intangibles, or property, plant and equipment). If so, the entity should account for such costs in accordance with those standards. If not, the entity should capitalise those costs only if the costs relate directly to a contract, relate to future performance, and are expected to be recovered under a contract. An example of such costs might be certain mobilisation, design or testing costs. These costs would then be amortised as control of the goods or services to which the asset relates is transferred to the customer. The amortisation period could extend beyond the length of the contract, where the economic benefit will be received over a longer period. An example might include set-up costs related to contracts likely to be renewed.

Licensing

IFRS 15 includes specific implementation guidance on accounting for licences of IP. The first step is to determine whether the licence is distinct or combined with other goods or services. The revenue recognition pattern for distinct licences is based on whether the licence is a right to access IP (revenue recognised over time) or a right to use IP (revenue recognised at a point in time). For licences that are bundled with other goods or services, management will apply judgement to assess the nature of the combined item and determine whether the combined performance obligation is satisfied at a point in time or over time. In addition, the revenue standard includes an exception to variable consideration guidance for the recognition of sales- or usage-based royalties promised in exchange for a licence of IP.

Principal versus agent considerations

Where an arrangement involves two or more unrelated parties that contribute to providing a specified good or service to a customer, management will need to determine whether the entity has promised to provide the specified good or service itself (as a principal) or to arrange for those specified goods or services to be provided by another party (as an agent). Determining whether an entity is the principal or an agent is not a policy choice. IFRS 15 includes indicators that an entity controls a specified good or service before it is transferred to the customer, to help entities to apply the concept of control to the principal versus agent assessment. The assessment should be made separately for each specified good or service. An entity could be the principal for some goods or services, and an agent for others, in contracts with multiple distinct goods or services.

Summary observations and anticipated timing

The above commentary is not all-inclusive. The effect of IFRS 15 is extensive, and all industries could be affected. Some will see pervasive changes, because the new model will replace all existing IFRS and US GAAP revenue recognition guidance, including industry-specific guidance with limited exceptions (for example, certain guidance on rate-regulated activities in US GAAP). Under US GAAP, the revenue standard will be effective (1) for public entities, for annual reporting periods, and interim periods therein, beginning after 15 December 2017, and (2) for non-public entities, for annual reporting periods beginning after 15 December 2018, and for interim periods within annual periods beginning after 15 December 2018. Under IFRS, the final standard will be effective for the first interim period within annual reporting periods beginning on or after 1 January 2018.

Entities should continue to evaluate how the model might affect current business activities, including contract negotiations, key metrics (including debt covenants and compensation arrangements), budgeting, controls and processes, information technology requirements, and accounting. IFRS 15 will permit an entity to apply it either retrospectively in accordance with IAS 8 or modified retrospectively (that is, including the cumulative effect at initial application date in opening retained earnings – or other equity components, as appropriate). IFRS 15 also provides certain practical expedients that an entity could elect to apply, to simplify transition.

Construction contracts – IAS 11

A construction contract (contract costs) is a contract specifically negotiated for the construction of an asset, or combination of assets, including contracts for the rendering of services directly related to the construction of the asset (such as project managers' and architects' services). Such contracts are typically fixed-price or cost-plus contracts.

Revenue and expenses on construction contracts are recognised using the percentage-of-completion method. This means that revenue, expenses and, therefore, profit are recognised gradually as contract activity occurs.

Where the outcome of the contract cannot be estimated reliably, revenue is recognised only to the extent of costs incurred that are recoverable; contract costs are recognised as an expense as incurred. Where it is probable that total contract costs will exceed total contract revenue, the expected loss is recognised immediately as an expense.

IFRIC 15, 'Agreements for the construction of real estate', clarifies which standard (IAS 18, 'Revenue', or IAS 11, 'Construction contracts') should be applied to particular transactions.

Government grants – IAS 20

Government grants are recognised when there is reasonable assurance that the entity will comply with the conditions related to them and that the grants will be received.

Grants related to income are recognised in profit or loss on a systematic basis over the periods necessary to match them with the related costs that they are intended to compensate. They are offset against the related expense or presented as income, either separately or under a general heading such as 'other income'. The timing of such recognition in profit or loss will also depend on the fulfilment of any conditions or obligations attaching to the grant.

Grants related to assets are either offset against the carrying amount of the relevant asset or presented as deferred income in the balance sheet. Profit or loss will be affected, either by a reduced depreciation charge or by deferred income being recognised as income systematically over the useful life of the related asset.

11. Segment reporting – IFRS 8

Segment guidance requires an entity to disclose information that enables users of the financial statements to evaluate the nature and financial effects of the business activities and the economic environments through the eyes of management ('management approach').

Although many entities manage their business using some level of 'segmented' data, the disclosure requirements are limited to (a) entities with listed or quoted equity or debt instruments, and (b) entities that are in the process of obtaining a listing or quotation of equity or debt instruments in a public market. To the extent that an entity not meeting either of these criteria chooses to disclose segmented data in financial statements, the information can only be referred to as 'segment information' if it complies with the segment guidance described below.

The identification of an entity's operating segments is the core determinant for the level of information included in the segment disclosures. Operating segments are components of an entity, identified based on the breakout of information contained in the internal reports that are regularly used by the entity's chief operating decision-maker (CODM) to allocate resources and to assess performance.

Reportable segments are individual operating segments or a group of operating segments for which segment information must be separately reported (that is, disclosed). Aggregation of one or more operating segments into a single reportable segment is permitted (but not required) where certain conditions are met, the principal condition being that the operating segments should have similar economic characteristics (for example, profit margin, spreads, sales growth rates, etc.). Whether multiple operating segments can be aggregated into a single reportable segment is a matter of significant judgement.

For each segment disclosed, entities are required to provide a measure of profit or loss in the format viewed by the CODM, as well as a measure of assets and liabilities if such amounts are regularly provided to the CODM. Other segment disclosures include the revenue from customers for each group of similar products and services, revenue by geography, and dependence on major customers. Additional detailed disclosures of performance and resources are required if the CODM reviews these amounts. A reconciliation of the total amount disclosed for all segments to the primary financial statements is required for revenue, profit and loss, and other material items reviewed by the CODM.

12. Employee benefits – IAS 19

The accounting for employee benefits, and for pensions in particular, is complex. The liabilities in defined benefit pension plans are frequently material. They are long-term and difficult to measure, and this gives rise to difficulty in measuring the cost attributable to each year.

Employee benefits are all forms of consideration given or promised by an entity in exchange for services rendered by its employees. These benefits include salary-related benefits (such as wages, profit-sharing bonuses, and compensated absences, including paid holiday and long-service leave), termination benefits (such as severance and redundancy pay) and post-employment benefits (such as retirement benefit plans). IAS 19 is relevant for all employee benefits, except for those to which IFRS 2, 'Share-based payments', applies.

Post-employment benefits include pensions, post-employment life insurance and medical care. Pensions are provided to employees either through defined contribution plans or defined benefit plans.

Recognition and measurement for short-term benefits is relatively straightforward, because actuarial assumptions are not required and the obligations are not discounted. However, long-term benefits, particularly post-employment benefits, give rise to more complicated measurement issues.

Defined contribution plans

Accounting for defined contribution plans is straightforward: the cost of defined contribution plans is the contribution payable by the employer for that accounting period.

Defined benefit plans

Accounting for defined benefit plans is complex, because actuarial assumptions and valuation methods are required to measure the balance sheet obligation and the expense. The expense recognised generally differs from the contributions made in the period.

Subject to certain conditions, the net amount recognised on the balance sheet is the difference between the defined benefit obligation and the plan assets.

To calculate the defined benefit obligation, estimates (actuarial assumptions) regarding demographic variables (such as employee turnover and mortality) and financial variables (such as future increases in salaries and medical costs) are made and included in a valuation model. The resulting benefit obligation is then discounted to a present value. This normally requires the expertise of an actuary.

Where defined benefit plans are funded, the plan assets are measured at fair value. Where no market price is available, the fair value of plan assets is estimated (for example, by discounting expected future cash flows using a discount rate that reflects both the risk associated with the plan assets and the maturity of those assets). Plan assets are tightly defined, and only assets that meet a strict definition can be offset against the plan's defined benefit obligations, resulting in a net surplus or net deficit that is shown on the balance sheet.

At each balance sheet date, the plan assets and the defined benefit obligation are remeasured. The income statement reflects the change in the surplus or deficit, except for contributions to the plan and benefits paid by the plan, along with business combinations and remeasurement gains and losses. Remeasurement gains and losses comprise actuarial gains and losses, return on plan assets (excluding amounts included in net interest on the net defined benefit liability or asset) and any change in the effect of the asset ceiling (excluding amounts included in net interest on the net defined benefit liability or asset). Remeasurements are recognised in other comprehensive income.

The amount of pension expense (income) to be recognised in profit or loss comprises the following individual components, unless they are required or permitted to be included in the costs of an asset:

- Service costs (that is, the present value of the benefits earned by active employees); and
- Net interest costs (that is, the unwinding of the discount on the defined benefit obligation and a theoretical return on plan assets).

Service costs comprises the 'current service costs', which is the increase in the present value of the defined benefit obligation resulting from employee services in the current period, 'past-service costs' (as defined below and including any gain or loss on curtailment) and any gain or loss on settlement.

Net interest on the net defined benefit liability (asset) is defined as '*the change during the period in the net defined benefit liability (asset) that arises from the passage of time*'. [IAS 19 para 8]. The net interest cost can be viewed as comprising theoretical interest income on plan assets, interest cost on the defined benefit obligation (that is, representing the unwinding of the discount on the plan obligation) and interest on the effect of the asset ceiling. [IAS 19 para 124].

The net interest on the net defined benefit liability (asset) is calculated by multiplying the net defined benefit liability (asset) by the discount rate (both as determined at the start of the annual reporting period), taking account of any changes in the net defined benefit liability (asset) during the period as a result of contribution and benefit payments. [IAS 19 para 123]. The discount rate applicable to any financial year is an appropriate high-quality corporate bond rate (or government bond rate, if appropriate) in the currency in which the liabilities are denominated. Net interest on the net defined benefit liability (asset) can be viewed as effectively including theoretical interest income on plan assets.

Past-service costs are defined as a change in the present value of the defined benefit obligation for employee services in prior periods, resulting from a plan amendment (the introduction or withdrawal of, or changes to, a defined benefit plan) or a curtailment (a significant reduction by the entity in the number of employees covered by a plan). Past-service costs need to be recognised as an expense generally when a plan amendment or curtailment occurs. Settlement gains or losses are recognised in the income statement when the settlement occurs.

IFRIC 14, 'IAS 19 – The limit on a defined benefit asset, minimum funding requirements and their interaction', provides guidance on assessing the amount that can be recognised as an asset when plan assets exceed the defined benefit obligation creating a net surplus. It also explains how the pension asset or liability might be affected by a statutory or contractual minimum funding requirement.

13. Share-based payment – IFRS 2

IFRS 2 applies to all share-based payment transactions in which goods or services are received as part of a share-based payment arrangement. A share-based payment arrangement is defined as:

'An agreement between the entity (or another group entity or any shareholder of any group entity) and another party (including an employee) that entitles the other party to receive:

a. Cash or other assets of the entity for amounts that are based on the price (or value) of equity instruments (including shares or share options) of the entity or another group entity, or

b. Equity instruments (including shares or share options) of the entity or another group entity.'

The most common application is to employee share schemes, such as share option schemes. However, entities sometimes also pay for other expenses, such as professional fees and for the purchase of assets, by means of share-based payment.

The accounting treatment under IFRS 2 is based on the fair value of the instruments. Both the valuation of and the accounting for awards can be difficult, due to the complex models that need to be used to calculate the fair value of options and also due to the variety and complexity of schemes. In addition, the standard requires extensive disclosures. The result generally is to reduce reported profits, especially in entities that use share-based payment extensively as part of their remuneration strategy.

All transactions involving share-based payment are recognised as expenses or assets over any vesting period.

Equity-settled share-based payment transactions are measured at the grant date fair value for employee services; and, for non-employee transactions, they are measured at the fair value of the goods or services received at the date on which the entity recognises the goods or services. If the fair value of the goods or services cannot be estimated reliably (such as employee services and circumstances in which the goods or services cannot be specifically identified), the entity uses the fair value of the equity instruments granted. Additionally, management needs to consider if there are any unidentifiable goods or services received or to be received by the entity, as these also have to be recognised and measured in accordance with IFRS 2.

Equity-settled share-based payment transactions are not remeasured once the grant date fair value has been determined.

The treatment is different for cash-settled share-based payment transactions: cash-settled awards are measured at the fair value (as defined in IFRS 2, and not as defined in IFRS 13) of the liability. The liability is remeasured at each balance sheet date and at the date of settlement, with changes in fair value recognised in the income statement.

14. Taxation – IAS 12

IAS 12 deals with taxes on income, comprising current tax and deferred tax.

Current tax expense for a period is based on the taxable and deductible amounts that will be shown on the tax return for the current year. An entity recognises a liability in the balance sheet in respect of current tax expense for the current and prior periods to the extent that it is unpaid. It recognises an asset if current tax has been overpaid.

Current tax assets and liabilities for the current and prior periods are 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 balance sheet date.

Tax payable, based on taxable profit, seldom matches the tax expense that might be expected, based on pre-tax accounting profit. Tax laws and financial accounting standards recognise and measure income, expenditure, assets and liabilities in different ways.

Deferred tax accounting seeks to deal with this mismatch. It is based on the temporary differences between the tax base of an asset or liability and its carrying amount in the financial statements. For example, where an asset is revalued upwards but not sold, the revaluation creates a temporary difference (if the carrying amount of the asset in the financial statements is greater than the tax base of the asset), and the tax consequence is a deferred tax liability.

Deferred tax is provided in full for all temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements, except where the temporary difference arises from:

- Initial recognition of goodwill (for deferred tax liabilities only);
- Initial recognition of an asset or liability in a transaction that is not a business combination and that affects neither accounting profit nor taxable profit; and
- Investments in subsidiaries, branches, associates and joint ventures, but only where certain criteria apply.

Deferred tax assets and liabilities are 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 balance sheet date. The discounting of deferred tax assets and liabilities is not permitted.

Generally, the measurement of deferred tax liabilities and deferred tax assets reflects the tax consequences that would follow from the manner in which the entity expects, at the balance sheet date, to recover or settle the carrying amount of its assets and liabilities. The carrying amount of a non-depreciable asset (such as land) can only be recovered through sale. For other assets, the manner in which management expects to recover the asset (that is, through use or through sale, or through a combination of both) is considered at each balance sheet date. An exception has been introduced for investment property measured using the fair value model in IAS 40, with a rebuttable presumption that such investment property is recovered entirely through sale.

Management only recognises a deferred tax asset for deductible temporary differences to the extent that it is probable that taxable profit will be available against which the deductible temporary difference can be utilised. This also applies to deferred tax assets for unused tax losses carried forward.

Current and deferred tax is recognised in profit or loss for the period, unless the tax arises from a business combination or a transaction or event that is recognised outside profit or loss, either in other comprehensive income or directly in equity, in the same or different period. The tax consequences that accompany, for example, a change in tax rates or tax laws, a reassessment of the recoverability of deferred tax assets or a change in the expected manner of recovery of an asset are recognised in profit or loss, except to the extent that they relate to items previously charged or credited outside profit or loss.

15. Earnings per share – IAS 33

Earnings per share (EPS) is a ratio that is widely used by financial analysts, investors and others to gauge an entity's profitability and to value its shares. EPS is normally calculated in the context of ordinary shares of the entity. Earnings attributable to ordinary shareholders are therefore determined by deducting from net income the earnings attributable to holders of more senior equity instruments.

An entity whose ordinary shares are listed on a recognised stock exchange, or is otherwise publicly traded, is required to disclose both basic and diluted EPS with equal prominence in its separate or individual financial statements, or in its consolidated financial statements if it is a parent. Furthermore, entities that file, or are in the process of filing, financial statements with a securities commission or other regulatory body for the purposes of issuing ordinary shares (that is, not a private placement) are also required to comply with the standard.

Basic EPS is calculated by dividing the profit or loss for the period attributable to the equity holders of the parent by the weighted average number of ordinary shares outstanding (including adjustments for bonus and rights issues).

Diluted EPS is calculated by adjusting the profit or loss and the weighted average number of ordinary shares by taking into account the conversion of any dilutive potential ordinary shares. Potential ordinary shares are those financial instruments and contracts that might result in issuing ordinary shares, such as convertible bonds and options (including employee share options).

Basic and diluted EPS, for both continuing and total operations, are presented with equal prominence in the statement of comprehensive income (or in the separate income statement, where one is presented) for each class of ordinary shares. Separate EPS figures for discontinued operations are disclosed in the same statements or in the notes.

Balance sheet and related notes

16. Intangible assets – IAS 38

An intangible asset is an identifiable non-monetary asset without physical substance. The identifiable criterion is met when the intangible asset is separable (that is, when it can be sold, transferred or licensed), or where it arises from contractual or other legal rights.

Separately acquired intangible assets

Separately acquired intangible assets are recognised initially at cost. Cost comprises the purchase price, including import duties and non-refundable purchase taxes and any directly attributable costs of preparing the asset for its intended use. The purchase price of a separately acquired intangible asset incorporates assumptions about the probable economic future benefits that might be generated by the asset.

Internally generated intangible assets

The process of generating an intangible asset is divided into a research phase and a development phase. No intangible assets arising from the research phase can be recognised. Intangible assets arising from the development phase are recognised when the entity can demonstrate:

- Its technical feasibility;
- Its intention to complete the developments;
- Its ability to use or sell the intangible asset;
- How the intangible asset will generate probable future economic benefits (for example, the existence of a market for the output of the intangible asset or for the intangible asset itself);
- The availability of resources to complete the development; and
- Its ability to measure the attributable expenditure reliably.

Any expenditure written off during the research or development phase cannot subsequently be capitalised if the project meets the criteria for recognition at a later date.

The costs relating to many internally generated intangible items cannot be capitalised, and they are expensed as incurred. This includes research, start-up and advertising costs. Expenditure on internally generated brands, mastheads, customer lists, publishing titles and goodwill are not recognised as intangible assets.

Intangible assets acquired in a business combination

If an intangible asset is acquired in a business combination, both the probability and measurement criterion are always considered to be met. An intangible asset will therefore always be recognised, regardless of whether it has been previously recognised in the acquiree's financial statements.

Subsequent measurement

Intangible assets are amortised, unless they have an indefinite useful life. Amortisation is carried out on a systematic basis over the useful life of the intangible asset. An intangible asset has 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.

Intangible assets with finite useful lives are considered for impairment when there is an indication that the asset has been impaired. Intangible assets with indefinite useful lives, and intangible assets not yet in use, are tested annually for impairment and whenever there is an indication of impairment.

17. Property, plant and equipment – IAS 16

Property, plant and equipment (PPE) is recognised when the cost of an asset can be reliably measured and it is probable that the entity will obtain future economic benefits from the asset.

PPE is measured initially at cost. Cost includes the fair value of the consideration given to acquire the asset (net of discounts and rebates) and any directly attributable cost of bringing the asset to working condition for its intended use (inclusive of import duties and non-refundable purchase taxes).

Directly attributable costs include the cost of site preparation, delivery, installation costs, relevant professional fees and the estimated cost of dismantling and removing the asset and restoring the site (to the extent that such a cost is recognised as a provision). Classes of PPE are carried either at historical cost less accumulated depreciation and any accumulated impairment losses (the cost model), or at a revalued amount less any accumulated depreciation and subsequent accumulated impairment losses (the revaluation model). The depreciable amount of PPE (being the gross carrying value less the estimated residual value) is depreciated on a systematic basis over its useful life.

Subsequent expenditure relating to an item of PPE is capitalised if it meets the recognition criteria.

PPE might comprise parts with different useful lives. Depreciation is calculated based on each individual part's life. In case of replacement of one part, the new part is capitalised to the extent that it meets the recognition criteria of an asset, and the carrying amount of the part replaced is derecognised.

The cost of a major inspection or overhaul of an item, occurring at regular intervals over the useful life of the item, is capitalised to the extent that it meets the recognition criteria of an asset. The carrying amounts of the parts replaced are derecognised.

Borrowing costs

Under IAS 23, 'Borrowing costs', entities are required to capitalise borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset to be capitalised.

18. Investment property – IAS 40

Certain properties are classified as investment properties for financial reporting purposes in accordance with IAS 40, 'Investment property'. The characteristics of these properties differ significantly from owner-occupied properties. It is the current value of such properties and changes to those values that are relevant to users of financial statements.

Investment property is property (land or a building, or part of a building, or both) held by an entity to earn rentals and/or for capital appreciation (for example, property in the course of construction or development). Any other properties are accounted for as property, plant and equipment (PPE) or inventory in accordance with:

- IAS 16, 'Property, plant and equipment', if they are held for use in the production or supply of goods or services; or
- IAS 2, 'Inventories', as inventory, if they are held for sale in the ordinary course of business.

Investment property is initially measured at cost. Management could subsequently measure investment properties at fair value or at cost. This is an accounting policy choice. The policy chosen is applied consistently to all of the investment properties that the entity owns.

Investment properties in the course of construction or development are measured at fair value if this can be reliably measured, where the fair value option is chosen. Otherwise, they are measured at cost.

Fair value is '*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*'. Guidance on fair value measurement is given in IFRS 13. Changes in fair value are recognised in profit or loss in the period in which they arise.

The cost model requires investment properties to be carried at cost less accumulated depreciation and any accumulated impairment losses; the fair value of these properties is disclosed in the notes.

19. Impairment of assets – IAS 36

Nearly all current and non-current financial assets are subject to an impairment test, to ensure that they are not overstated on balance sheets.

The basic principle of impairment is that an asset cannot be carried on the balance sheet above its recoverable amount. Recoverable amount is the higher of the asset's fair value less costs of disposal and its value in use:

- Fair value less costs of disposal is '*the price that would be received to sell an asset in an orderly transaction between market participants at the measurement date*' less costs of disposal. Guidance on fair value is given in IFRS 13.
- Value in use requires management to estimate the present value of the future cash flows that are expected to be derived from the asset in its current condition.

The carrying value of an asset is compared to the recoverable amount. An asset or CGU is impaired when its carrying amount exceeds its recoverable amount. Any impairment is allocated to the asset or assets of the CGU, with the impairment loss recognised in profit or loss.

All assets subject to the impairment guidance are tested for impairment when there is an indication that the asset might be impaired. Assets that are not amortised (such as goodwill, indefinite-lived intangible assets and intangible assets that are not yet available for use) are also tested for impairment annually, even if there is no impairment indicator.

Both external indicators (for example, significant adverse changes in the technological, market, economic or legal environment, or increases in market interest rates) and internal indicators (for example, evidence of obsolescence or physical damage of an asset, or evidence from internal reporting that the economic performance of an asset is, or will be, worse than expected) are considered, when considering whether an asset is impaired.

An asset seldom generates cash flows independently of other assets. Most assets are tested for impairment in groups of assets described as cash-generating units (CGUs). A CGU is the smallest identifiable group of assets that generates inflows that are largely independent from the cash flows from other CGUs.

Impairment should be identified at the individual asset level, where possible. The recoverable amount should be calculated for the CGU to which the asset belongs only where the recoverable amount for the individual asset cannot be identified. An impairment review of a CGU should cover all of its tangible assets, intangible assets and attributable goodwill. The carrying value of each CGU containing the assets and goodwill being reviewed should be compared with the higher of its value in use and fair value less costs of disposal.

Goodwill acquired in a business combination is allocated to the acquirer's CGUs or groups of CGUs that are expected to benefit from the synergies of the business combination. However, the largest group of CGUs permitted for goodwill impairment testing is an operating segment before aggregation.

20. Lease accounting – IAS 17, IFRS 16

IAS 17

A lease gives one party (the lessee) the right to use an asset over an agreed period of time in return for payment to the lessor. Leasing is an important source of medium- and long-term financing; accounting for leases can have a significant impact on lessees' and lessors' financial statements.

Leases are classified as finance or operating leases at inception, depending on whether substantially all of the risks and rewards of ownership transfer to the lessee. Under a finance lease, the lessee has substantially all of the risks and rewards of ownership. All other leases are operating leases. Leases of land and buildings are considered separately under IFRS.

Under a finance lease, the lessee recognises an asset held under a finance lease and a corresponding obligation to pay rentals. The lessee depreciates the asset.

The lessor recognises the leased asset as a receivable. The receivable is measured at the 'net investment' in the lease – that is, the minimum lease payments receivable, discounted at the internal rate of return of the lease, plus the unguaranteed residual that accrues to the lessor.

Under an operating lease, the lessee does not recognise an asset and lease obligation. The lessor continues to recognise the leased asset and depreciates it. The rentals paid are normally charged to the income statement of the lessee and credited to that of the lessor on a straight-line basis.

Linked transactions with the legal form of a lease are accounted for on the basis of their substance – for example, a sale and leaseback where the seller is committed to repurchase the asset might not be a lease, in substance, if the 'seller' retains the risks and rewards of ownership and substantially the same rights of use as before the transaction.

Equally, some transactions that do not have the legal form of a lease are, in substance, leases if they are dependent on a particular asset that the purchaser can control physically or economically.

IFRS 16

IFRS 16, 'Leases', was published in January 2016 and is mandatory from 1 January 2019. It will replace the current guidance in IAS 17. IFRS 16 defines a lease as a contract, or part of a contract, that conveys the right to use an asset (the underlying asset) for a period of time in exchange for consideration.

Under IFRS 16, lessees have to recognise a lease liability reflecting future lease payments and a 'right-of-use asset' for almost all lease contracts. This is a significant change compared to IAS 17, under which lessees were required to make a distinction between a finance lease (on balance sheet) and an operating lease (off balance sheet). IFRS 16 gives lessees optional exemptions for certain short-term leases and leases of low-value assets. In the income statement, lessees will have to present interest expense on the lease liability and depreciation on the right-of-use asset. In the cash flow statement, the part of the lease payments that reflects interest on the lease liability can be presented as an operating cash flow (if it is the entity's policy to present interest payments as operating cash flows). Cash payments for the principal portion of the lease liability are classified within financing activities. Payments for short-term leases, for leases of low-value assets and variable lease payments not included in the measurement of the lease liability are presented within operating activities.

As under IAS 17, the lessor has to classify leases as either finance or operating, depending on whether substantially all of the risks and rewards incidental to ownership of the underlying asset have been transferred.

For a finance lease, the lessor recognises a receivable; and, for an operating lease, the lessor continues to recognise the underlying asset.

IFRS 16 adds significant new, enhanced disclosure requirements for both lessors and lessees.

IFRS 16 is effective for annual reporting periods beginning on or after 1 January 2019. Earlier application is permitted, but only in conjunction with IFRS 15, 'Revenue from contracts with customers'. On transition, lessees can choose between full retrospective application and a 'simplified approach' that includes certain reliefs and does not require a restatement of comparatives. In addition, as a practical expedient, entities are not required to reassess whether a contract is, or contains, a lease at the date of initial application (that is, such contracts are 'grandfathered').

21. Inventories – IAS 2

Inventories are initially recognised at the lower of cost and net realisable value (NRV). Cost of inventories includes import duties, non-refundable taxes, transport and handling costs, and any other directly attributable costs less trade discounts, rebates and similar items. NRV is the estimated selling price in the ordinary course of business, less the estimated costs of completion and estimated selling expenses.

IAS 2, 'Inventories', requires the cost for items that are not interchangeable or that have been segregated for specific contracts to be determined on an individual-item basis. The cost of other items of inventory used is assigned by using either the first-in, first-out (FIFO) or weighted average cost formula. Last-in, first-out (LIFO) is not permitted. An entity uses the same cost formula for all inventories that have a similar nature and use to the entity. A different cost formula could be justified where inventories have a different nature or use. The cost formula used is applied on a consistent basis from period to period.

22. Provisions and contingencies – IAS 37

A liability is a '*present obligation of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits'. A provision is 'a liability of uncertain timing or amount'.*

Recognition and initial measurement

A provision is recognised when: the entity has a present obligation as a result of past events; it is probable (that is, more likely than not) that a transfer of economic benefits will be required to settle the obligation; and a reliable estimate of the amount of the obligation can be made.

The amount recognised as a provision is the best estimate of the expenditure required to settle the present obligation at the balance sheet date, measured at the present value of the expected cash outflows where the effect of the time value of money is material. Provisions are not recognised for future operating losses.

A present obligation arises from an obligating event, and it could take the form of either a legal obligation or a constructive obligation. An obligating event leaves the entity no realistic alternative to settling the obligation. If the entity can avoid the future expenditure by its future actions, it has no present obligation, and no provision is required. For example, an entity cannot recognise a provision based solely on the intent to incur expenditure at some future date or the expectation of future operating losses.

An obligation does not have to be a 'legal' obligation before a provision is recognised. An entity might have an established pattern of past practice, published policies or a sufficient specific current statement that indicates to other parties that it will accept certain responsibilities and, as a result, it has created a valid expectation on the part of those other parties that it will discharge those responsibilities (that is, the entity has a constructive obligation).

If an entity has an onerous contract (that is, the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it), the present obligation under the contract is recognised as a provision. Impairments of any assets dedicated to the contract are recognised before making a provision.

Restructuring provisions

A restructuring provision is recognised only when the general recognition criteria for a provision are met. The obligation for a restructuring is often constructive. A constructive restructuring obligation arises only when there is: (a) a detailed formal plan identifying the main features of the restructuring; and (b) a valid expectation in those affected that the entity will carry out the restructuring by starting to implement the plan or announcing its main features to those affected.

A restructuring plan does not create a present obligation at the balance sheet date if it is announced after that date, even if it is announced before the financial statements are approved. A sale or termination of a business might fall under the definition of a restructuring. No obligation arises in respect of restructuring costs associated with the sale of an operation until the entity is committed to the sale (that is, there is a binding sale agreement).

A restructuring provision includes only the direct expenditures arising from the restructuring, which are necessarily entailed by the restructuring, and not those associated with the entity's ongoing activities. Any expected gains on the sale of assets are not considered in measuring a restructuring provision.

Reimbursements

Where some or all of the expenditure required to settle a provision is expected to be reimbursed by another party, the reimbursement should be recognised only when it is virtually certain that reimbursement will be received if the entity settles the obligation. The entity typically remains liable for the entire obligation, and reimbursements are therefore presented separately as assets. The amount recognised should not exceed the amount of the related provision. Expenses relating to a provision can be presented net of the amount recognised for a reimbursement in the income statement.

Subsequent measurement

Provisions should be re-assessed at the end of each reporting period and adjusted to reflect current best estimates. This re-assessment should include the estimated cash flows and the discount rate. The unwinding of the discount due to the passage of time should be included as an element of borrowing costs in arriving at profit or loss for the year.

Contingent liabilities

Contingent liabilities are possible obligations that arise from past events and whose existence will be confirmed only on the occurrence or non-occurrence of uncertain future events outside the entity's control, or present obligations that arise from past events but are not recognised because: (a) it is not probable that an outflow of economic benefits will be required to settle the obligation; or (b) the amount cannot be measured reliably.

Contingent liabilities are not recognised, but are disclosed, unless the possibility of an outflow is remote.

Contingent assets

Contingent assets are possible assets that arise from past events and whose existence will be confirmed only on the occurrence or non-occurrence of uncertain future events outside the entity's control. Contingent assets are not recognised.

Contingent assets are disclosed if the inflow of economic benefits is probable.

Levies

A public authority could impose a levy on entities, based on measures such as gross revenues for a specified period or on assets or liabilities at a specified date. IFRIC 21 addresses the accounting for such levies. The obligating event that gives rise to a liability to pay a levy is the activity that triggers the payment of the levy, as identified by the legislation.

23. Events after the reporting period and financial commitments – IAS 10

It is not generally practicable for preparers to finalise financial statements without a period of time elapsing between the balance sheet date and the date on which the financial statements are authorised for issue. The question therefore arises as to the extent to which events occurring between the balance sheet date and the date of approval (that is, 'events after the reporting period') should be reflected in the financial statements.

Events after the reporting period are either adjusting events or non-adjusting events. Adjusting events provide further evidence of conditions that existed at the balance sheet date (for example, determining after the year end the consideration for assets sold before the year end). Non-adjusting events relate to conditions that arose after the balance sheet date (for example, announcing a plan to discontinue an operation after the year end or where there is a decline in market value of investments after the year end).

The carrying amounts of assets and liabilities at the balance sheet date are adjusted only for adjusting events or events that indicate that the going-concern assumption in relation to the whole entity is not appropriate. Significant non-adjusting events (such as the issue of shares, major business combinations or abnormally large changes after the reporting period in asset prices or foreign exchange rates) are disclosed.

Dividends proposed or declared after the balance sheet date, but before the financial statements have been authorised for issue, are not recognised as a liability at the balance sheet date. Details of these dividends are, however, disclosed.

An entity discloses the date on which the financial statements were authorised for issue, the persons authorising the issue and, where necessary, the fact that the owners or other persons have the ability to amend the financial statements after issue.

24. Share capital and reserves

Equity, along with assets and liabilities, is one of the three elements used to portray an entity's financial position. Equity is defined in the IASB's Framework as the residual interest in the entity's assets after deducting all of its liabilities. The term 'equity' is often used to encompass an entity's equity instruments and reserves. Equity is given various descriptions in the financial statements. Corporate entities might refer to it as owners' equity, shareholders' equity, capital and reserves, shareholders' funds and proprietorship. Equity includes various components with different characteristics.

Determining what constitutes an equity instrument for the purpose of IFRS, and how it should be accounted for, falls within the scope of IAS 32, 'Financial instruments: presentation'.

Equity instruments (for example, issued, non-redeemable ordinary shares) are generally recorded as the residual after recording the recognition or derecognition of assets or liabilities arising on the equity issue (the proceeds of issue) and after deducting directly attributable transaction costs. Equity instruments are not remeasured after initial recognition.

Reserves include retained earnings, together with reserves such as fair value reserves, hedging reserves, asset revaluation reserves and foreign currency translation reserves and other statutory reserves.

Treasury shares

Treasury shares are deducted from equity. No gain or loss is recognised in profit or loss on the purchase, sale, issue or cancellation of an entity's own equity instruments.

Non-controlling interests

Non-controlling interests (previously termed 'minority interests') in consolidated financial statements are presented as a component of equity, separately from the parent shareholders' equity.

Disclosures

IAS 1, 'Presentation of financial statements', requires various disclosures. These include the total issued share capital and reserves, presentation of a statement of changes in equity, capital management policies and dividend information.

Consolidated and separate financial statements

25. Consolidated financial statements – IFRS 10, IAS 27 and SIC 12

The principles concerning consolidated financial statements under IFRS are set out in IFRS 10, 'Consolidated financial statements'. IFRS 10 has a single definition of control.

IFRS 10's objective is to establish principles for presenting and preparing consolidated financial statements when an entity controls one or more entities. IFRS 10 sets out the requirements for when an entity should prepare consolidated financial statements, defines the principles of control, explains how to apply the principles of control, and explains the accounting requirements for preparing consolidated financial statements. [IFRS 10 para 2].

The key principle in the standard is that control exists, and consolidation is required, only if the investor possesses power over the investee, has exposure to variable returns from its involvement with the investee, and has the ability to use its power over the investee to affect its returns.

IFRS 10 provides guidance on the following issues when determining who has control:

- Assessment of the purpose and design of an investee.
- Relevant activities and power to direct those.
- Nature of rights – whether substantive or merely protective in nature.
- Assessment of voting rights and potential voting rights.
- Whether an investor is a principal or an agent when exercising its controlling power.
- Relationships between investors and how they affect control.
- Existence of power over specified assets only.

In difficult situations, the precise facts and circumstances will affect the analysis under IFRS 10. IFRS 10 does not provide 'bright lines', and it requires consideration of many factors, such as the existence of contractual arrangements and rights held by other parties, in order to assess control.

IFRS 10 does not contain any disclosure requirements; these are included within IFRS 12. Reporting entities should plan for, and implement, the processes and controls that will be required to gather the required information. This might involve a preliminary consideration of IFRS 12 issues, such as the level of disaggregation required.

The IASB amended IFRS 10 in October 2012 (effective 1 January 2014, as endorsed by the EU) to incorporate changes to how investment entities account for entities that they control. Entities that meet the definition of an investment entity are exempt from consolidating underlying investees that they control; instead, they are required to account for these subsidiaries at fair value through profit or loss under IFRS 9 (IAS 39). Some further amendments to clarify accounting for investment entities were made in December 2014 (effective 1 January 2016, as endorsed by the EU).

26. Separate financial statements – IAS 27

IAS 27 deals with the accounting for investments in subsidiaries, joint ventures and associates when an entity elects, or is required by local regulations, to present separate financial statements. Each category of investments should be accounted for either at cost, in accordance with IAS 39 and IFRS 9, or using the equity method in the separate financial statements.

27. Business combinations – IFRS 3

A business combination is a transaction or event in which an entity ('acquirer') obtains control of one or more businesses ('acquirees'). Under IFRS 10, 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. A number of factors might influence which entity has control, including: equity shareholding, control of the board and control agreements. There is a presumption of control if an entity owns more than 50% of the equity shareholding in another entity.

Business combinations occur in a variety of structures. IFRS 3, 'Business combinations', focuses on the substance of the transaction, rather than the legal form. The overall result of a series of transactions is considered if there are a number of transactions among the parties involved. For example, any transaction contingent on the completion of another transaction might be considered to be linked. Judgement is required to determine when transactions should be linked.

All business combinations within IFRS 3's scope are accounted for using the acquisition method. The acquisition method views a business combination from the perspective of the acquirer, and it can be summarised in the following steps:

- Identify the acquirer.
- Determine the acquisition date.
- Recognise and measure the identifiable assets acquired, liabilities assumed and any non-controlling interest in the acquiree.
- Recognise and measure the consideration transferred for the acquiree.
- Recognise and measure goodwill or a gain from a bargain purchase.

The acquiree's identifiable assets (including intangible assets not previously recognised), liabilities and contingent liabilities are generally recognised at their fair value. Fair value is measured in accordance with IFRS 13. If the acquisition is for less than 100% of the acquiree, there is a non-controlling interest. The non-controlling interest represents the equity in a subsidiary that is not attributable, directly or indirectly, to the parent. The acquirer can elect to measure the non-controlling interest at its fair value, or at its proportionate share of the identifiable net assets, on an acquisition-by-acquisition basis.

The consideration for the combination includes cash and cash equivalents, the fair value of any non-cash consideration given and liabilities assumed. Any equity instruments issued as part of the consideration are fair valued at the acquisition date. If any of the consideration is deferred, it is discounted to reflect its present value at the acquisition date, if the effect of discounting is material. Consideration includes only those amounts paid to the seller in exchange for control of the entity. Consideration excludes amounts paid to settle pre-existing relationships, payments that are contingent on future employee services and acquisition-related costs.

A portion of the consideration might be contingent on the outcome of future events or the acquired entity's performance ('contingent consideration'). Contingent consideration is also recognised at its fair value at the date of acquisition. The accounting for contingent consideration after the date of acquisition depends on whether it is classified as a liability (remeasured to fair value each reporting period through profit and loss) or as equity (no subsequent remeasurement). The classification as either a liability or equity is determined with reference to the guidance in IAS 32.

Goodwill is recognised for the future economic benefits arising from assets acquired that are not individually identified and separately recognised. Goodwill is the difference between the considerations transferred, the amount of any non-controlling interest in the acquiree, and the acquisition-date fair value of any previous equity interest in the acquiree over the fair value of the identifiable net assets acquired. If the non-controlling interest is measured at its fair value, goodwill includes amounts attributable to the non-controlling interest. If the non-controlling interest is measured at its proportionate share of identifiable net assets, goodwill includes only amounts attributable to the controlling interest (that is, the parent).

Goodwill is recognised as an asset and tested annually for impairment, or more frequently if there is an indication of impairment.

In rare situations (for example, a bargain purchase as a result of a distressed sale), it is possible that no goodwill will result from the transaction. Rather, a gain will be recognised.

Business combinations excluded from IFRS 3's scope (for example, those involving businesses under common control) have a policy choice of using either the acquisition accounting method outlined in IFRS 3 or predecessor accounting.

28. Disposal of subsidiaries, businesses and non-current assets – IFRS 5

IFRS 5, 'Non-current assets held for sale and discontinued operations', is relevant when any disposal occurs or is planned, including distribution of non-current assets to shareholders. The held-for-sale criteria in IFRS 5 apply to non-current assets (or disposal groups) whose value will be recovered principally through sale rather than through continuing use. The criteria do not apply to non-assets that are being scrapped, wound down or abandoned.

IFRS 5 defines a disposal group as 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.

The non-current asset (or disposal group) is classified as 'held for sale' if it is available for immediate sale in its present condition and its sale is highly probable. A sale is 'highly probable' where: there is evidence of management commitment; there is an active programme to locate a buyer and complete the plan; the asset is actively marketed for sale at a reasonable price compared to its fair value; the sale is expected to be completed within 12 months of the date of classification; and actions required to complete the plan indicate that it is unlikely that there will be significant changes to the plan or that it will be withdrawn.

A non-current asset (or disposal group) is classified as 'held for distribution to owners' where the entity is committed to such distribution (that is, the assets must be available for immediate distribution in their present condition and the distribution must be highly probable). For a distribution to be highly probable, actions to complete the distribution should have been initiated and should be expected to be completed within one year from the date of classification. Actions required to complete the distribution should indicate that it is unlikely that significant changes to the distribution will be made or that the distribution will be withdrawn. The probability of shareholders' approval (if required in the jurisdiction) should be considered in the assessment of 'highly probable'.

Non-current assets (or disposal groups) classified as held for sale or as held for distribution are:

- Measured at the lower of the carrying amount and fair value less costs to sell;
- Not depreciated or amortised; and
- Presented separately in the balance sheet (assets and liabilities should not be offset).

A discontinued operation is a component of an entity that can be distinguished operationally and financially for financial reporting purposes from the rest of the entity, and it:

- Represents a separate major line of business or geographical area of operation;
- Is part of a single co-ordinated plan to dispose of a separate major line of business or major geographical area of operation; or
- Is a subsidiary acquired exclusively with a view to resale?

An operation is classified as discontinued only at the date on which it meets the criteria to be classified as held for sale or when the entity has disposed of it. Although balance sheet information is neither restated nor remeasured for discontinued operations, the statement of comprehensive income information does have to be restated for the comparative period.

Discontinued operations are presented separately in the income statement and the cash flow statement. There are additional disclosure requirements in relation to discontinued operations.

The date of disposal of a subsidiary or disposal group is the date on which control passes. The consolidated income statement includes the results of a subsidiary or disposal group up to the date of disposal; the gain or loss on disposal is the difference between (a) the carrying amount of the net assets plus any attributable goodwill and amounts accumulated in other comprehensive income (for example, foreign translation adjustments and available-for-sale reserves), and (b) the proceeds of sale.

29. Equity accounting – IAS 28

IAS 28, 'Investments in associates and joint ventures', requires that interests in such entities are accounted for using the equity method of accounting. An associate is an entity in which the investor has significant influence, but which is neither a subsidiary nor a joint venture of the investor. Significant influence is the power to participate in the financial and operating policy decisions of the investee, but not to control those policies. It is presumed to exist where the investor holds at least 20% of the investee's voting power. It is presumed not to exist where less than 20% is held. These presumptions can be rebutted.

The equity method of accounting also applies to interests in joint ventures. A joint venture is a joint arrangement where the parties that have joint control have rights to the arrangement's net assets. Under the equity method, the investment in the associate or joint venture is initially carried at cost. It is increased or decreased to recognise the investor's share of the profit or loss of the associate or joint venture after the date of acquisition. Associates and joint ventures are accounted for using the equity method, unless they meet the criteria to be classified as 'held for sale' under IFRS 5.

Investments in associates or joint ventures are classified as non-current assets and presented as one line item in the balance sheet (inclusive of notional goodwill arising on acquisition). Investments in associates or joint ventures are tested for impairment in accordance with IAS 36, 'Impairment of assets', as single assets if there are impairment indicators under IAS 28 (as amended by IFRS 9).

An entity applies IFRS 9 to financial instruments in an associate or joint venture to which the equity method is not applied. These include long-term interests that, in substance, form part of the entity's net investment in an associate or joint venture. If an investor's share of its associate's or joint venture's losses exceeds the carrying amount of the investment (which, for this purpose, includes other long-term interests that, in substance, form part of the entity's investment in the associate or the joint venture), the carrying amount of the investment is reduced to nil. Recognition of further losses are discontinued, unless the investor has an obligation to fund the associate or joint venture, or the investor has guaranteed to support the associate or joint venture.

In the separate (non-consolidated) financial statements of the investor, the investments in associates or joint ventures are carried at cost, in accordance with IAS 39 and IFRS 9 or using the equity method.

30. Joint arrangements – IFRS 11

A joint arrangement is a contractual arrangement where at least two parties agree to share control over the activities of the arrangement. Unanimous consent towards decisions about relevant activities between the parties sharing control is a requirement in order to meet the definition of joint control.

Joint arrangements can be joint operations or joint ventures. The classification is principle-based, and it depends on the parties' rights and obligations in relation to the arrangement.

Where the parties' exposure to the arrangement only extends to the net assets of the arrangement, the arrangement is a joint venture.

Joint operators have rights to assets and obligations for liabilities. Joint operations are often not structured through separate vehicles.

Where a joint arrangement is included in a separate vehicle, it can be either a joint operation or a joint venture. In such cases, further analysis is required on the legal form of the separate vehicle, the terms and conditions included in the contractual agreement and, sometimes, other facts and circumstances. This is because, in practice, the latter two can override the principles derived from the legal form of the separate vehicle.

Joint operators account for their rights to assets and obligations for liabilities. Joint ventures account for their interest by using the equity method of accounting (see '29. Equity accounting – IAS 28' above).

Other subjects

31. Related-party disclosures – IAS 24

Under IAS 24, disclosures are required in respect of an entity's transactions with related parties. Related parties include:

- Parents;
- Subsidiaries;
- Fellow subsidiaries;
- Associates of the entity and other members of the group;
- Joint ventures of the entity and other members of the group;
- Members of key management personnel of the entity or of a parent of the entity (and close members of their families);
- Persons with control, joint control or significant influence over the entity (and close members of their families);
- Post-employment benefit plans; and
- Entities (or any of their group members) providing key management personnel services to the entity or its parent.

Finance providers are not related parties simply because of their normal dealings with the entity.

Management discloses the name of the entity's parent and, if different, the ultimate controlling party (which could be a person). Relationships between a parent and its subsidiaries are disclosed, irrespective of whether there have been transactions with them.

Where there have been related party transactions during the period, management discloses the nature of the relationship, as well as information about the transactions and outstanding balances, including commitments, necessary for users to understand the potential impact of the relationship on the financial statements. Disclosure is made by category of related party and by major type of transaction. Items of a similar nature can be disclosed in aggregate, except where separate disclosure is necessary for an understanding of the effects of related party transactions on the entity's financial statements.

Management only discloses that related party transactions were made on terms equivalent to those that prevail in arm's length transactions, if such terms can be substantiated.

An entity is exempt from the disclosure of transactions (and outstanding balances) with a related party that is either a government that has control, joint control or significant influence over the entity or is another entity that is under the control, joint control or significant influence of the same government as the entity. Where the entity applies the exemption, it discloses the name of the government and the nature of its relationship with the entity. It also discloses the nature and amount of each individually significant transaction and the qualitative or quantitative extent of any collectively significant transactions.

32. Cash flow statements – IAS 7

The statement of cash flows is one of the primary statements in financial reporting (along with the statement of comprehensive income, the balance sheet and the statement of changes in equity). It presents the generation and use of 'cash and cash equivalents' by category (operating, investing and financing) over a specific period of time. It provides users with a basis to assess the entity's ability to generate and utilise its cash.

Operating activities are the entity's revenue-producing activities. Investing activities are the acquisition and disposal of long-term assets (including business combinations) and investments that are not cash equivalents. Financing activities are changes in equity and borrowings.

Management can present operating cash flows by using either the direct method (gross cash receipts/payments) or the indirect method (adjusting net profit or loss for non-operating and non-cash transactions, and for changes in working capital).

Cash flows from investing and financing activities are reported separately gross (that is, gross cash receipts and gross cash payments), unless they meet certain specified criteria.

The cash flows arising from dividends and interest receipts and payments are classified on a consistent basis, and they are separately disclosed under the activity appropriate to their nature. Cash flows relating to taxation on income are classified and separately disclosed under operating activities, unless they can be specifically attributed to investing or financing activities.

The total that summarises the effect of the operating, investing and financing cash flows is the movement in the balance of cash and cash equivalents for the period.

Separate disclosure is made of significant non-cash transactions (such as the issue of equity for the acquisition of a subsidiary or the acquisition of an asset through a finance lease). Non-cash transactions include impairment losses/reversals, depreciation, amortisation, fair value gains/losses, and income statement charges for provisions.

33. Interim financial reporting – IAS 34

There is no IFRS requirement for an entity to publish interim financial statements. However, a number of countries either require or recommend their publication, in particular for public companies.

Entities can prepare either full IFRS financial statements (conforming to the requirements of IAS 1) or condensed financial statements. Condensed reporting is the most common approach. Condensed financial statements include: (i) a condensed statement of financial position (balance sheet), (ii) a condensed statement of comprehensive income or, if presented separately, an income statement and other comprehensive income statement, (iii) a condensed statement of cash flows, (iv) a condensed statement of changes in equity, and (v) selected explanatory notes.

An entity should apply accounting policies consistently, for recognising and measuring assets, liabilities, revenues, expenses and gains and losses at interim dates, as compared to those to be used in the current-year annual financial statements.

There are special measurement requirements for certain costs that can only be determined on an annual basis (for example, items such as tax that is calculated based on an estimated full-year effective tax rate). It is also acknowledged that the preparation of interim reports generally requires a greater use of estimates than for annual financial reports. 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, should not be reversed.

As a minimum, current-period and comparative figures (for condensed or full primary statements) are disclosed as follows:

- Statement of financial position (balance sheet): as of the end of the current interim period, with comparatives for the immediately preceding year end.
- Statement of comprehensive income (or, if presented separately, income statement and statement of other comprehensive income): for the current interim period and the current year-to-date information, with comparatives for the equivalent periods in the previous year.
- Cash flow statement and statement of changes in equity: for the current interim period on a year-to-date basis, with comparatives for the equivalent period in the previous year.

34. Service concession arrangements – SIC 29 and IFRIC 12

There is no specific IFRS that applies to public-to-private service concession arrangements for delivery of public services. IFRIC 12, 'Service concession arrangements', interprets various standards in setting out the accounting requirements for service concession arrangements, while SIC 29, 'Services concession arrangements: disclosures', contains disclosure requirements.

IFRIC 12 applies to public-to-private service concession arrangements in which the public sector body (the grantor) controls and/or regulates the services provided with the infrastructure by the private sector entity (the operator).

The concession arrangement also addresses to whom the operator should provide the services and at what price. The grantor controls any significant residual interest in the infrastructure.

As the infrastructure is controlled by the grantor, the operator does not recognise the infrastructure as its property, plant and equipment; nor does the operator recognise a finance lease receivable for leasing the public service infrastructure to the grantor, regardless of the extent to which the operator bears the risk and rewards incidental to ownership of the assets.

The operator recognises a financial asset to the extent that it has an unconditional contractual right to receive cash, irrespective of the usage of the infrastructure.

The operator recognises an intangible asset to the extent that it receives a right (a licence) to charge users of the public service.

The operator accounts for revenue and costs relating to construction or upgrade services and operation services in accordance with IFRS 15.

Industry-specific topics

35. Agriculture – IAS 41

Agricultural activity is defined as the management of biological transformation and harvest of biological assets (living animals and plants) for sale or for conversion into agricultural produce (harvested product of biological assets) or into additional biological assets.

Biological assets that meet the definition of 'bearer plants' are measured either at cost or revalued amounts, less accumulated depreciation and impairment losses under IAS 16.

All other biological assets, including produce growing on a bearer plant, are usually measured at fair value less costs to sell, with the change in the carrying amount reported as part of profit or loss from operating activities. Agricultural produce harvested from an entity's biological assets is measured at fair value less costs to sell at the point of harvest.

The fair value is measured in terms of IFRS 13.

IFRS 13 looks to the principal market for the asset and not entity-specific measures. The fair value measurement should represent the price in the principal market (whether that price is directly observable or estimated using another valuation technique), even if the price in a different market is potentially more advantageous at the measurement date. [IFRS 13 para 18]. In the absence of a principal market, the entity should use the price in the most advantageous market for the relevant asset.

36. Extractive industries – IFRS 6

IFRS 6, 'Exploration for and evaluation of mineral resources', addresses the financial reporting for the exploration for and evaluation of mineral resources. It does not address other aspects of accounting by entities engaged in the exploration for and evaluation of mineral reserves (such as activities before an entity has acquired the legal right to explore, or after the technical feasibility and commercial viability to extract resources have been demonstrated). Activities outside the scope of IFRS 6 are accounted for according to the applicable standards (such as IAS 16, 'Property, plant and equipment', IAS 37, 'Provisions, contingent liabilities and contingent assets', and IAS 38, 'Intangible assets').

The accounting policy adopted for the recognition of exploration and evaluation assets should result in information that is relevant and reliable. As a concession, certain further rules of IAS 8 need not be applied. This permits companies in the extractive sector to continue, for the time being, to apply policies that were followed under national GAAP that would not comply with the requirements of IFRS. The accounting policy can be changed only if the change makes the financial statements more relevant and no less reliable, or more reliable and no less relevant – in other words, if the new accounting policy takes it closer to the requirements in the IASB's Framework.

Exploration and evaluation assets are initially measured at cost. They are classified as tangible or intangible assets, according to the nature of the assets acquired. Management applies that classification consistently. After recognition, management applies either the cost model or the revaluation model to the exploration and evaluation assets, based on IAS 16 or IAS 38, according to the nature of the assets. As soon as technical feasibility and commercial viability are determined, the assets are no longer classified as exploration and evaluation assets.

The exploration and evaluation assets are tested for impairment when facts and circumstances suggest that the carrying amounts might not be recovered. The assets are also tested for impairment before reclassification out of exploration and evaluation. The impairment is measured, presented and disclosed according to IAS 36, except that exploration and evaluation assets are allocated to CGUs or groups of CGUs, either of which must be no larger than a segment. Management discloses the accounting policy adopted, as well as the amount of assets, liabilities, income and expense and investing cash flows arising from the exploration and evaluation of mineral resources.

IFRIC 20, 'Stripping costs in the production phase of a surface mine', applies to waste removal costs incurred in surface mining activity during the production phase.

Index by standard and interpretation

*Not covered in this overview

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