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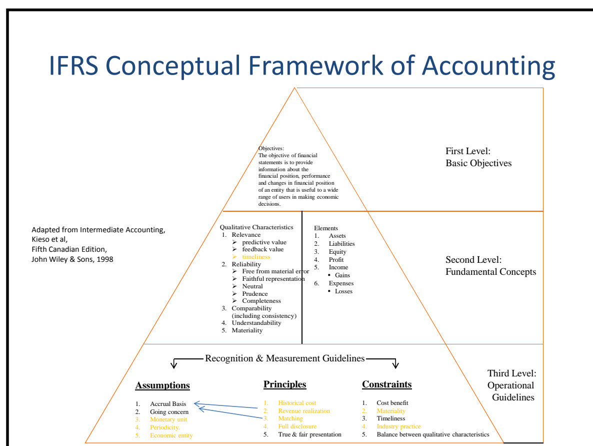
- **Disclaimer:**
- This material is designed to provide the student with a overview of changes brought about by the adoption of IFRS that may be tested on the CMA Entrance Examination. It has been provided with the understanding that the authors are not engaged in rendering legal, accounting or professional advice. If legal, accounting, professional or other expert assistance is required, the services of a competent professional should be sought.

IFRS

Synopsis' of Major Changes

IFRS

Conceptual Framework



IFRS Conceptual Framework of Accounting

- No one method of measurement embedded in the framework
- Capital maintenance
  - Financial
  - Physical
- Less a framework and more a collection of agreed upon principles

IFRS

Statement of Financial Position

IFRS

- Current/non-current distinction
  - Where a presentation based on liquidity provides information that is reliable and more relevant, an entity shall present all assets and liabilities in order of liquidity.

IFRS

- Current assets
  - An entity shall classify an asset as current when:
    a) It expects to realise the asset, or intends to sell or consume it, in its normal operating cycle;
    b) It holds the asset primarily for the purpose of trading;
    c) It expects to realise the asset within twelve months after the reporting period; or
    d) The asset is cash or a cash equivalent unless the asset is restricted from being exchanged or used to settle a liability for at least twelve months after the reporting period.
  - An entity shall classify all other assets as non-current

IFRS

- Current liabilities
  - An entity shall classify a liability as current when:
    a) It expects to settle the liability in its normal operating cycle;
    b) It holds the liability primarily for the purpose of trading;
    c) The liability is due to be settled within twelve months after the reporting period; or
    d) The entity does not have an unconditional right to defer settlement of the liability for at least twelve months after the reporting period.
  - IFRS requires current classification of breached long-term liabilities unless refinancing is complete by the balance sheet date.
  - An entity shall classify all other liabilities as non-current.

IFRS

Illustrative statement of financial position

XYZ GROUP— STATEMENT OF FINANCIAL POSITION AS AT 31 DECEMBER 2008

	2008	2007
ASSETS		
Non-current assets		
Property, plant and equipment	x	x
Goodwill	x	x
Other intangible assets	x	x
Investments in associates	x	x
Available-for-sale investments	x	x
	x	x
Current assets		
Inventories	x	x
Trade receivables	x	x
Other current assets	x	x
Cash and cash equivalents	x	x
	x	x
Total assets	x	x

IFRS

EQUITY AND LIABILITIES		
Equity attributable to owners of the parent		
Share capital	x	x
Other components of equity	x	x
Retained earnings	x	x
	x	x
Non-controlling interest	x	x
Total equity	x	x
Non-current liabilities		
Long-term borrowings	x	x
Deferred tax	x	x
Long-term provisions	x	x
Total non-current liabilities	x	x
Current liabilities		
Trade and other payables	x	x
Short-term borrowings	x	x
Current portion of long-term borrowings	x	x
Current tax payable	x	x
Short-term provisions	x	x
Total current liabilities	x	x
Total liabilities	x	x
Total equity and liabilities	x	x

IFRS

Illustrative Statement of Changes in Equity

	Share Capital	Retained earnings	Translation of foreign operations	Available-for-sale financial assets	Cash flow hedges	Revaluation surplus	Total	Non-controlling interests	Total equity
Balance at December 31, 2007	x	x	x	x	x	x	x	x	x
Changes in Equity for 2008									
Issue of share capital	x	-	-	-	-	-	x	-	x
Dividends	-	(x)					(x)	-	(x)
Total comprehensive income for the year	-	x	x	x	x	x	x	x	x
Transfer to retained earnings	-	x	-	-	-	x	x	-	x
Balance at December 31, 2008	x	x	x	x	x	x	x	x	x

IFRS

Statement of Income

IFRS

- No concept of EOI outside of profit for the year
  - DO is only item to be presented on an after tax basis

IFRS

- As a minimum, the statement of comprehensive income shall include line items that present the following amounts for the period:
  a) revenue;
  b) finance costs;
  c) share of the profit or loss of associates and joint ventures accounted for using the equity method;
  d) tax expense;
  e) a single amount comprising the total of:
     i. the post-tax profit or loss of discontinued operations and
     ii. 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;
  f) profit or loss;
  g) each component of other comprehensive income classified by nature (excluding amounts in (h));
  h) share of the other comprehensive income of associates and joint ventures accounted for using the equity method; and
  i) total comprehensive income.

IFRS

- When items of income or expense are material, an entity shall disclose their nature and amount separately.
- Circumstances that would give rise to the separate disclosure of items of income and expense include:
  a) write-downs of inventories to net realisable value or of property, plant and equipment to recoverable amount, as well as reversals of such write-downs;
  b) restructurings of the activities of an entity and reversals of any provisions for the costs of restructuring;
  c) disposals of items of property, plant and equipment;
  d) disposals of investments;
  e) discontinued operations;
  f) litigation settlements; and
  g) other reversals of provisions.
- An entity shall present an analysis of expenses recognised in profit or loss using a classification based on either their nature or their function within the entity, whichever provides information that is reliable and more relevant.
- An entity classifying expenses by function shall disclose additional information on the nature of expenses, including depreciation and amortisation expense and employee benefits expense.

IFRS

Presentation by Nature of Expense

Revenue		X
Other income		X
Changes in inventories of finished goods and work in progress	X	
Raw materials and consumables used	X	
Employee benefits expense	X	
Depreciation and amortisation expense	X	
Other expenses	X	
Total expenses		(X)
Profit before tax		X

IFRS

Presentation by Function of Expense

Revenue	X
Cost of sales	(X)
Gross profit	X
Other income	X
Distribution costs	(X)
Administrative expenses	(X)
Other expenses	(X)
Profit before tax	X

IFRS

- Long lived assets held for sale - non-current assets (disposal groups) classified as held for sale are to be classified separately on the balance sheet.
  - An entity shall classify a non-current asset (or disposal group) as held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use.
    - For this to be the case, the asset (or disposal group) must be available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such assets (or disposal groups) and its sale must be highly probable.
    - For the sale to be highly probable, the appropriate level of management must be committed to a plan to sell the asset (or disposal group), and an active programme to locate a buyer and complete the plan must have been initiated.

IFRS

Capital Maintenance

IFRS

- Concepts of capital
  - A financial concept of capital is adopted by most entities in preparing their financial statements.
  - Under a financial concept of capital, such as invested money or invested purchasing power, capital is synonymous with the net assets or equity of the entity.
  - Under a physical concept of capital, such as operating capability, capital is regarded as the productive capacity of the entity based on, for example, units of output per day.

IFRS

- The selection of the appropriate concept of capital by an entity should be based on the needs of the users of its financial statements.
- A financial concept of capital should be adopted if the users of financial statements are primarily concerned with the maintenance of nominal invested capital or the purchasing power of invested capital.
- A physical concept of maintenance should be used when the main concern of users is with the operating capability of the entity
- The concept chosen indicates the goal to be attained in determining profit, even though there may be some measurement difficulties in making the concept operational

IFRS

- Financial capital maintenance.
  - Under this concept a profit is earned only if the financial (or money) amount of the net assets at the end of the period exceeds the financial (or money) amount of net assets at the beginning of the period, after excluding any distributions to, and contributions from, owners during the period.
  - Financial capital maintenance can be measured in either nominal monetary units or units of constant purchasing power.

IFRS

- Physical capital maintenance.
  - Under this concept a profit is earned only if the physical productive capacity (or operating capability) of the entity (or the resources or funds needed to achieve that capacity) at the end of the period exceeds the physical productive capacity at the beginning of the period, after excluding any distributions to, and contributions from, owners during the period

IFRS

Cash Flow Statements

IFRS

- An entity has an accounting policy choice of classifying interest and dividends received as operating or investing activities.
- An entity has an accounting policy choice of classifying interest and dividends paid as operating or financing activities.
- Once the entity makes the choice of this accounting policy, it must be applied consistently to all similar transactions.

IFRS

- There is no restriction against the disclosure of cash flows per share.

IFRS

Revenue Recognition

IFRS

- Income = Revenue + gains
- Revenue is the gross inflow of economic benefits during the period arising in the course of the ordinary activities of an entity when those inflows result in increases in equity, other than increases relating to contributions from equity participants.
- Revenue shall be measured at the fair value of the consideration received or receivable.
  - Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

IFRS

- Revenue from the sale of goods or services shall be recognised when all the following conditions have been satisfied:
  a) the entity has transferred to the buyer the significant risks and rewards of ownership of the goods or services;
  b) the entity retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold or services provided;
  c) the amount of revenue can be measured reliably;
  d) it is probable that the economic benefits associated with the transaction will flow to the entity; and
  e) the costs incurred or to be incurred in respect of the transaction can be measured reliably.

IFRS

- Long term construction contracts
  - When the outcome of a construction contract can be estimated reliably, contract revenue and contract costs associated with the construction contract shall be recognised as revenue and expenses respectively by reference to the stage of completion of the contract activity at the end of the reporting period.
- An expected loss on the construction contract shall be recognised as an expense immediately.

IFRS

- Long term construction contracts
  - When the outcome of a construction contract cannot be estimated reliably:
    - revenue shall be recognised only to the extent of contract costs incurred that it is probable will be recoverable; and
    - contract costs shall be recognised as an expense in the period in which they are incurred.

IFRS

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

IFRS

Capital Assets

Property Plant & Equipment & Intangible Assets

IFRS

- IAS 16 permits the revaluation of property, plant and equipment to fair value;
- IAS 16 requires the depreciable amount to be the asset cost less its residual value, rather than using the greater of the asset cost less its residual value or asset cost less its salvage value;
- IAS 36 requires discounting in determining the net recoverable amount of property, plant and equipment;
- IAS 40 allows investment property to be accounted for using a fair value or a cost-based model; and
- IFRS 6 provides limited guidance on the financial reporting for exploration for, and evaluation of, mineral resources

IFRS

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

IFRS

- Revaluation model
  - After recognition as an asset, an item of property, plant and equipment whose fair value can be measured reliably shall be carried at a re-valued amount, being its fair value at the date of the revaluation less any subsequent accumulated depreciation and subsequent accumulated impairment losses.
  - Revaluations shall be made with sufficient regularity to ensure that the carrying amount does not differ materially from that which would be determined using fair value at the end of the reporting period

IFRS

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

IFRS

- Revaluation Model
  - If an asset's carrying amount is decreased as a result of a revaluation, the decrease shall be recognised in profit or loss. However, the decrease shall be recognised in other comprehensive income to the extent of any credit balance existing in the revaluation surplus in respect of that asset.
  - Wow and this increases transparency and understanding how??

IFRS

Adjusting Accumulated Depreciation for Re-Valued Assets

An entity bought a machine for $30,000 on January 1, 2004. The machine's useful life is 10 years with zero residual value. The revalued amount of the machine is $36,000 on December 31, 2004.

The two methods of adjusting accumulated depreciation are as follows:

Method 1: The accumulated depreciation is restated proportionately with the change in the asset's gross carrying amount.

	Before adjustment	Adjustment for revaluation surplus	After adjustment
Cost			
As at December 31	$30,000	$10,000	$40,000 ($30K x ($36K/$27K))
Accumulated depreciation			
As at December 31	($3,000) ($30K / 10 years) for 1 year	($1,000)	($4,000) ($3K x ($36K/$27K))
Net carrying amount	$27,000	$9,000 (to bring from $27K to $36K)	$36,000

IFRS

Adjusting Accumulated Depreciation for Re-Valued Assets

Method 2: The accumulated depreciation is eliminated against the asset's gross carrying amount.

	Before adjustment	Adjustment for revaluation surplus	After adjustment
Cost			
As at December 31	$30,000	$6,000 ($9K – $3K)	$36,000
Accumulated depreciation			
As at December 31	$3,000 ($30K / 10 years) for 1 year	$3,000	$0 (wipes out any accumulated depreciation)
Net carrying amount	$27,000	$9,000 (to bring from $27K to $36K)	$36,000

IFRS

- Capitalization of interest is required on self constructed assets
  - Do not have to capitalize interest on borrowing costs directly attributable to the acquisition, construction or production of:
    - a qualifying asset measured at fair value, for example a biological asset; or
    - inventories that are manufactured, or otherwise produced, in large quantities on a repetitive basis.

IFRS

- Intangible assets
  - Standards are converged with respect to the initial recognition and measurement of intangible assets.
  - IFRS permits revaluation at fair value for intangible assets that have an active market.

IFRS

Amortization

IFRS

- Each part of an item of property, plant and equipment with a cost that is significant in relation to the total cost of the item shall be depreciated separately (componentization).

IFRS

Componentization

Component	Useful life (years)	Cost	Depreciation (per annum)
Fuselage	20	$10,000,000	$ 500,000
Wings	15	$ 6,000,000	$ 400,000
Avionics	10	$ 4,000,000	$ 400,000
Seats	8	$ 500,000	$ 62,500
Engines	2	$10,000,000	$ 5,000,000
		$30,500,000	$ 6,362,500

IFRS

- Property plant & equipment should be recorded at the lower of carrying value and net recoverable amount.
- An entity shall assess at the end of each reporting period whether there is any indication that an asset may be impaired. If any such indication exists, the entity shall estimate the recoverable amount of the asset.
- The recoverable amount of an asset or a cash-generating unit is the higher of its fair
- value less costs to sell and its value in use.

IFRS

- The following elements shall be reflected in the calculation of an asset's value in use:
  a) an estimate of the future cash flows the entity expects to derive from the asset;
  b) expectations about possible variations in the amount or timing of those future cash flows;
  c) the time value of money, represented by the current market risk-free rate of interest;
  d) the price for bearing the uncertainty inherent in the asset; and
  e) other factors, such as illiquidity, that market participants would reflect in pricing the future cash flows the entity expects to derive from the asset.

IFRS

- Estimating the value in use of an asset involves the following steps:
  - estimating the future cash inflows and outflows to be derived from continuing use of the asset and from its ultimate disposal; and
  - applying the appropriate discount rate to those future cash flows.

IFRS

Liabilities

IFRS

- Provision
  - A provision is a liability of uncertain timing or amount.
- Liability
  - 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.
- Obligating event
  - An obligating event is an event that creates a legal or constructive obligation that results in an entity having no realistic alternative to settling that obligation.

IFRS

- Legal obligation
  - A legal obligation is an obligation that derives from:
    - a) contract (through its explicit or implicit terms);
    - b) legislation; or
    - c) other operation of law.
- Constructive obligation
  - A constructive obligation is an obligation that derives from an entity's actions where:
    - a) by an established pattern of past practice, published policies or a sufficiently specific current statement, the entity has indicated to other parties that it will accept certain responsibilities; and
    - b) as a result, the entity has created a valid expectation on the part of those other parties that it will discharge those responsibilities.

IFRS

- Contingent liability
  - A contingent liability is:
    - a) a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity; or
    - b) a present obligation that arises from past events but is not recognized because:
      - i. it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation; or
      - ii. the amount of the obligation cannot be measured with sufficient reliability.

IFRS

- Contingent asset
  - A contingent asset is a possible asset that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity.
- Onerous contract
  - An onerous contract is a contract in which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it.

IFRS

- Restructuring
  - A restructuring is a program that is planned and controlled by management, and materially changes either:
    - the scope of a business undertaken by an entity; or
    - the manner in which that business is conducted

IFRS

- A provision shall be recognized when:
  - an entity has a present obligation (legal or constructive) as a result of a past event;
  - it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and
  - a reliable estimate can be made of the amount of the obligation.
- If these conditions are not met, no provision shall be recognized.

IFRS

- Present obligation
  - In rare cases it is not clear whether there is a present obligation. In these cases, a past event is deemed to give rise to a present obligation if, taking account of all available evidence, it is more likely than not that a present obligation exists at the end of the reporting period.

IFRS

- An entity shall not recognize a contingent liability.
  - A contingent liability is disclosed, unless the possibility of an outflow of resources embodying economic benefits is remote.
- An entity shall not recognize a contingent asset.
  - A contingent asset is disclosed, where an inflow of economic benefits is probable

IFRS

- The amount recognized as a provision shall be the best estimate of the expenditure required to settle the present obligation at the end of the reporting period.
- Where the effect of the time value of money is material, the amount of a provision shall be the present value of the expenditures expected to be required to settle the obligation.
  - The discount rate (or rates) shall be a pre-tax rate (or rates) that reflect(s) current market assessments of the time value of money and the risks specific to the liability. The discount rate(s) shall not reflect risks for which future cash flow estimates have been adjusted.

IFRS

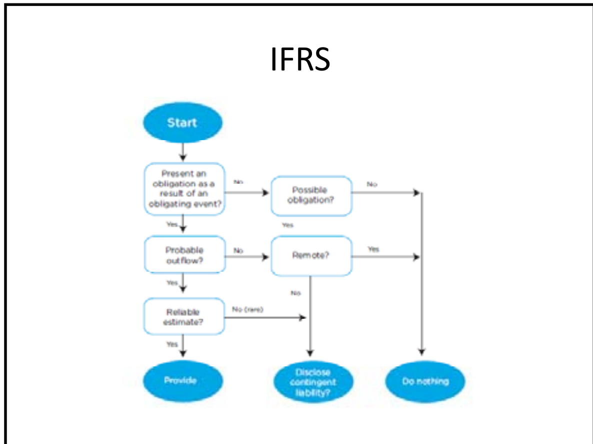
- Provisions shall not be recognized for future operating losses
- If an entity has a contract that is onerous, the present obligation under the contract shall be recognized and measured as a provision
- Provisions are to be classified and disclosed separately from trade payables and accruals

IFRS

	Obligation	probable that an outflow of resources will occur	Amount can be measured reliably
Trade payables	Present obligation	Yes	Yes
Accruals	Present obligation	Yes	Can be reasonably estimated
Provision	Present obligation	Likely (but there may be uncertainty in timing or amount)	Likely (but there may be uncertainty in timing or amount)
Contingency	Present or possible obligation	there is uncertainty in timing or amount	there is uncertainty in timing or amount

IFRS

- Prudence
  - The preparers of financial statements do, however, have to contend with the uncertainties that inevitably surround many events and circumstances, such as the collectability of doubtful receivables, the probable useful life of plant and equipment and the number of warranty claims that may occur. Such uncertainties are recognized by the disclosure of their nature and extent and by the exercise of prudence in the preparation of the financial statements. Prudence is the inclusion of a degree of caution in the exercise of the judgments needed in making the estimates required under conditions of uncertainty, such that assets or income are not overstated and liabilities or expenses are not understated.
- However, the exercise of prudence does not allow, for example, the creation of hidden reserves or excessive provisions, the deliberate understatement of assets or income, or the deliberate overstatement of liabilities or expenses, because the financial statements would not be neutral and, therefore, not have the quality of reliability.
- One of the issues of not having a strong conceptual framework is communicating to users the shift from conservatism to prudence



IFRS

Leases

IFRS

- Section 3065 and IAS 17 are converged, except that
  - Terminology and classification of leases differ:
    - Leases are classified as either
      - an operating lease or
      - finance lease, for both the lessee and the lessor.
    - The expression capital lease does not exist under IFRS.

IFRS

- Under IFRS, both parties (lessor and lessee) use the same criteria (but the lessor and lessee in a given transaction will not necessarily have symmetrical accounting);
- The main criteria used by the lessee are the same, but the quantitative thresholds (e.g., 75% and 90%) are absent to allow for professional judgment;
- One additional criterion is used under IFRS: if the leased asset is specialized for the lessee's needs, the lease is deemed to transfer the risks and rewards of ownership to the lessee.
- Some additional "secondary" criteria are present for situations when a lease is on the borderline of being classified as operating or finance using the primary criteria.

IFRS

- Accounting treatment – lessee
- The discount rate used in determining the present value of the minimum lease payments by the lessee is the interest rate implicit in the lease or, if this is not practicable to determine, the lessee's incremental borrowing rate.
- The reference to the smallest of the two rates is absent under IFRS.
- The definition of the interest rate implicit in the lease is slightly different: the initial direct costs borne by the lessor are to be added to the asset's fair value for the purpose of the calculation of the rate.
- Under IFRS, there are guidelines pertaining to the initial direct costs borne by the lessee: they are to be included in the carrying value of the leased asset for finance leases.

IFRS

- **A lease is classified as a finance lease if it transfers substantially all the risks and rewards incidental to ownership. A lease is classified as an operating lease if it does not transfer substantially all the risks and rewards incidental to ownership.**
- Whether a lease is a finance lease or an operating lease depends on the substance of the transaction rather than the form of the contract. Examples of situations that individually or in combination would normally lead to a lease being classified as a finance lease are:
  a) the lease transfers ownership of the asset to the lessee by the end of the lease term;
  b) the lessee has the option to purchase the asset at a price that is expected to be sufficiently lower than the fair value at the date the option becomes exercisable for it to be reasonably certain, at the inception of the lease, that the option will be exercised;
  c) the lease term is for the major part of the economic life of the asset even if title is not transferred;
  d) at the inception of the lease the present value of the minimum lease payments amounts to at least substantially all of the fair value of the leased asset; and
  e) the leased assets are of such a specialized nature that only the lessee can use them without major modifications.

IFRS

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

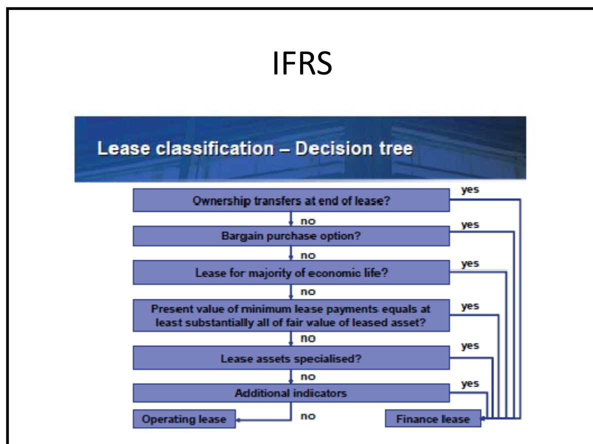
IFRS

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

IFRS

- A finance lease gives rise to depreciation expense for depreciable assets as well as finance expense for each accounting period. The depreciation policy for depreciable leased assets shall be consistent with that for depreciable assets that are owned, and the depreciation recognized shall be calculated in accordance with IRFS standards.
- If there is no reasonable certainty that the lessee will obtain ownership by the end of the lease term, the asset shall be fully depreciated over the shorter of the lease term and its useful life

IFRS



IFRS

- Lessor
  - All leases deemed to transfer the risks and rewards of ownership to the lessee are labeled “finance leases”. However, the accounting treatment is different between lessors that are financial institutions and lessors who are manufacturers/dealers.
  - When the lessor is a manufacturer/dealer, the amount to be recognized as sales is the lower of the fair value of the asset and the present value of the minimum lease payments.
  - However, the discount rate is not the interest rate implicit in the lease but rather a market interest rate.
  - Initial direct costs for an operating lease are to be added to the carrying value of the leased assets.

IFRS

- If a sale and leaseback transaction results in a finance lease, any excess of sales proceeds over the carrying amount shall not be immediately recognised as income by a seller-lessee. Instead, it shall be deferred and amortised over the lease term.
- If a sale and leaseback transaction results in an operating lease, and it is clear that the transaction is established at fair value, any profit or loss shall be recognised immediately. If the sale price is below fair value, any profit or loss shall be recognised immediately except that, if the loss is compensated for by future lease payments at below market price, it shall be deferred and amortised in proportion to the lease payments over the period for which the asset is expected to be used. If the sale price is above fair value, the excess over fair value shall be deferred and amortised over the period for which the asset is expected to be used.

IFRS

Pensions & Post Retirement Benefits

IFRS

- Section 3461 and IAS 19 are converged, except that IAS 19 requires
  - (i) plan assets to be measured at fair value for all purposes at all reporting dates;
  - (ii) requires past service costs to be recognized on a straight-line basis over the average period until the amended benefits become vested;
  - (iii) requires multi-employer plans with defined benefit characteristics to be accounted for as defined benefit plans; and
  - (iv) permits a choice of recognizing actuarial gains and losses directly in equity (OCI) in the period in which they occur, without subsequent recycling to net income.