Grant Thornton

IFRS Top 20 Tracker

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Introduction

The IFRS Top 20 Tracker

With over 100 countries across the world now either requiring or allowing the use of IFRS for financial statements, a clear pattern has begun to emerge as to the areas that companies encounter difficulties with when preparing their financial statements.

To assist companies in dealing with these areas of difficulty, Grant Thornton International Ltd ("Grant Thornton International") has published The IFRS Top 20 Tracker. This publication takes management through twenty top disclosure and accounting issues identified by Grant Thornton International, based on the experience of member firms within Grant Thornton International who have assisted companies in transitioning to IFRS.

The IFRS Top 20 Tracker is not a comprehensive checklist for IFRS disclosures or accounting treatments; it is intended to highlight some of the key issues that companies are having to deal with in their IFRS financial statements and provide a heads-up for management to help them focus on key issues to address.

Completing the disclosures required by IFRS can take considerable time. The IFRS Top 20 Tracker draws on the experience of the member firms within Grant Thornton International, which shows that many companies under-estimate the extent and complexity of IFRS and hence put themselves under significant pressure in order to complete their financial statements within the required timescale.

Entities might wish to reduce the time pressure during the year-end process, by producing pro forma financial statements in advance, to enable management to deal with the more complex disclosures earlier in the reporting process. In addition, some key measurement processes can be addressed in advance. For example, impairment reviews for goodwill have to be done annually under IAS 36 *Impairment of Assets* but reviews do not need to be done at the year-end. Once the review has been completed there is no reason why companies cannot prepare the disclosure required by IAS 36. Where business combinations take place during a year, fair value and other adjustments and relevant disclosures can be addressed at the time and need not be left until after the year-end.

In Appendix A you will find a checklist which can be used to help management ensure that they have addressed the top 20 areas covered in this document in the year-end reporting process.

References to IAS 1 Presentation of Financial Statements (revised 2007)

All references in this guide to IAS 1 are based on the 2007 version of this standard. The revised version of IAS 1 introduced, amongst other amendments, various changes in the financial statement terminology. For example, IAS 1 uses the term “statement of financial position” instead of “balance sheet” and “statement of cash flows” instead of “cash flow statements”. This guide reflects these recent changes to the IFRS terminology.

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1 IAS 1 – Presentation issues: judgements and estimates

IAS 1.122. An entity shall disclose, in the summary of significant accounting policies or other notes, the judgements, apart from those involving estimations (see paragraph 125), that management has made in the process of applying the entity's accounting policies and that have the most significant effect on the amounts recognised in the financial statements.

IAS 1.125 An entity shall disclose information about the assumptions it makes about the future, and other major sources of estimation uncertainty at the end of the reporting period, that have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities within the next financial year. In respect of those assets and liabilities, the notes shall include details of:
(a) their nature, and
(b) their carrying amount as at the end of the reporting period.

1.1 Judgements and estimates

IFRS implementation may involve management having to make significant judgements about the application of accounting policies for the reporting entity. IAS 1 *Presentation of Financial Statements (revised 2007)* requires the disclosure of the judgements management has made in applying an entity's accounting policies that have the most significant effect on the assets and liabilities recognised in the financial statements (IAS 1.122). These requirements are wide-ranging as highlighted by the examples given in IAS 1.123 of judgements that may require disclosure:

- whether financial assets are held-to-maturity investments
- when substantially all the risks and rewards of ownership of financial assets and lease assets are transferred to other entities
- whether in substance sales of goods are financing arrangements and therefore do not give rise to revenue
- whether the substance of the relationship between the entity and a special purpose entity indicates that the special purpose entity is controlled by the entity.

Management are furthermore required to disclose assumptions they make about the future that have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities within the next financial year (IAS 1.125).

These assumptions regarding the effects of uncertain future events are likely to be the most subjective and complex estimates that management make in relation to the financial statements. Careful consideration needs to be given to ensure that the reader of the financial statements understands clearly the uncertainties described as well as the range of possible outcomes that might result from these uncertain future events.

IAS 1.129 gives some examples of areas that may be covered and the types of disclosures that can be made in order to help users to understand the judgements.

1.2 Disclosures should not be 'boilerplate'

Because the nature and extent of judgements and estimates made by management will vary significantly from company to company, there can be no 'model' or standard disclosure example. Management will need to assess carefully those areas of judgement and estimates that may need disclosure within the financial statements.

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2 IAS 1 – Presentation issues: primary statement formats

2.1 Primary statement formats

IAS 1 *Presentation of Financial Statements (Revised 2007)* does not mandate the order or format in which items are to be presented in the primary statements; it does however specify minimum requirements and also includes example disclosure regarding the function and nature of the expenses in the income statement. We often see primary statement formats being adopted which do not meet IAS 1's minimum disclosure requirements or the inclusion of additional line items and sub-totals in circumstances where this may not be justified under IAS 1.

2.2 Key areas to focus on

IAS 1.54(m) and (n) require current tax assets and liabilities and deferred tax assets and liabilities to be shown as separate line items on the face of the statement of financial position. This requirement is often overlooked in practice.

IAS 1.85 requires additional line items, headings and sub-totals to be presented in the statement of comprehensive income and the separate income statement (if presented), when such presentation is relevant to an understanding of the entity's financial performance. IAS 1.55 sets out a similar requirement in relation to the statement of financial position. Additional line items should be used only to explain elements of financial performance (or position).

IAS 1 does not mandate a line item in the income statement for operating profit, although the use of such a sub-total is not prohibited. Companies that present items below the operating profit line that appear to be operating in nature may be challenged to explain their presentation. Presentation of operating profit and exceptional items is discussed further in Section 17.

Although IFRS does not specify the nomenclature to be used in financial statements, use of local GAAP terms should be avoided where IFRS uses different terminology, especially where there are differences of meaning. For example, "fixed assets" in some local GAAPs may not correspond exactly with "non-current assets" as defined in IAS 1. Care also needs to be taken to avoid inconsistent terminology, such as using "property, plant and equipment" in the statement of financial position but referring to "tangible fixed assets" in notes.

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3 IAS 36 – Impairment disclosures

3.1 Impairments

IAS 36 *Impairment of Assets* prescribes the procedures to be applied by an entity to ensure that its assets are not carried above their recoverable amount.

Impairment requirements under IFRS are more stringent than many local GAAPs, with goodwill being tested annually for impairment. Any intangible assets with indefinite lives are also tested annually for impairment.

IAS 36 requires extensive disclosures in relation to the procedures applied by management, so that users of the financial statements understand the basis on which impairment decisions have been taken. The disclosures in relation to impairment are extensive due to the number and sensitivity of estimates and assumptions used by management as the basis for their review. Importantly, extensive IAS 36 disclosures apply in relation to goodwill and intangible assets with indefinite lives, even if no impairment is recognised (IAS 36.134 & IAS 36.135).

3.2 Disclosure

Summarised below are disclosure points from IAS 36 that companies often miss when they base their recoverable amount for impairment testing on value in use:

- key assumptions on which management bases its cash flow projections should be described (IAS 36.134(d)(i))
- the approach taken by management on how key assumptions were determined should be described (IAS 36.134(d)(ii))
- the period over which cash flows are projected by management should be disclosed with an explanation if a period of more that five years is used (IAS 36.134(d)(iii))
- the growth rate used to extrapolate cash flow projections beyond the period covered by the most recent budgets/forecasts should be disclosed and any growth rate that exceeds the relevant long term average growth rate should be justified (IAS 36.134(d)(iv))
- sensitivity disclosures are required if a reasonably possible change in a key assumption would cause the carrying amount to exceed its recoverable amount (IAS 36.134(f)).

Where recoverable amount is based on fair value less costs to sell, IAS 36.134(d) disclosures do not apply; these are replaced by equivalent disclosures in IAS 36.134(e).

3.3 Example disclosure

See Appendix D for example IAS 36 impairment disclosure. The example disclosure is based on a retail company.

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4 IFRS 3 – Goodwill justification disclosure

IFRS 3.67 To give effect to the principle in paragraph 66(a), the acquirer shall disclose the following information for each business combination that was effected during the period…

(h) a description of the factors that contributed to a cost that results in the recognition of goodwill – a description of each intangible asset that was not recognised separately from goodwill and an explanation of why the intangible asset's fair value could not be measured reliably – or a description of the nature of any excess recognised in profit or loss in accordance with paragraph 56.

(i) the amount of the acquiree's profit or loss since the acquisition date included in the acquirer's profit or loss for the period, unless disclosure would be impracticable. If such disclosure would be impracticable, that fact shall be disclosed, together with an explanation of why this is the case.

4.1 Goodwill

IFRS 3 *Business Combinations* includes extensive disclosure requirements (IFRS 3.66-77). IFRS 3 requires entities to recognise many more intangible assets separately from goodwill on a business combination compared to many local GAAPs. These disclosures have come under intense scrutiny, and entities have been challenged by regulators where they have recorded large goodwill balances on business combinations and have not provided adequate explanation as to why goodwill has been recognised, rather than identifiable intangible assets.

It is important to identify intangibles separately as, in most cases, their lives will be finite and hence amortisation under IAS 38 *Intangible Assets* will be required. This is particularly relevant for items such as customer relationships and technology-based intangibles.

For each business combination that was effected during a period (or in aggregate for business combinations that are individually immaterial), an acquirer should provide a description of the factors that contributed to a cost that results in recognising goodwill (IFRS 3.67(h)). This disclosure should include a description of each intangible asset that was not recognised separately from goodwill and an explanation of why the intangible asset's fair value could not be measured. In order to meet this requirement, an acquirer's management will need to have knowledge of the component parts of goodwill. This should be considered when management carries out an exercise to allocate goodwill to the group's cash generating units. This allocation is based on the synergies and other benefits expected to be derived from the combination. Typical examples of factors contributing to goodwill include:

- an acquired entity's workforce
- synergies resulting from cost savings and increase in market share, and
- non-contractual customer relationships that have not met the criteria for recognition as an intangible asset.

4.2 Example disclosure

Goodwill related to acquisitions amounted to CU3.7million. The amount of goodwill paid related to expected synergies to be achieved. Synergies to be achieved are a result of a stronger presence in the market and synergies in purchasing, sourcing and selling due to the integration of our activities and those of the acquired companies.

4.3 IFRS 3 Revised

References in section 4 are to the original version of IFRS 3. On 10 January 2008 the IASB published IFRS 3 Business Combinations (revised 2008). The revised Standard will introduce major changes to the accounting requirements for business combinations; careful study of the transition requirements is necessary.

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5 IFRS 3 – Other business combination issues and disclosures

IFRS 3 Appendix A - Definition of a business:

An integrated set of activities and assets conducted and managed for the purpose of providing:

(a) a return to investors; or

(b) lower costs or other economic benefits directly and proportionately to policyholders or participants.

A business generally consists of inputs, processes applied to those inputs, and resulting outputs that are, or will be, used to generate revenues. If **goodwill** is present in a transferred set of activities and assets, the transferred set shall be presumed to be a business.

5.1 Introduction

Accounting for business combinations under IFRS can pose significant accounting treatment challenges. There are three key issues that directors need to consider in relation to business combinations:

- Is the acquired entity actually a business?
- Is the acquisition in the scope of IFRS 3?
- Identifying the acquirer.

Set out below are some common areas where accounting issues arise and may take time to address fully.

5.2 Is the acquired entity actually a business?

IFRS 3 *Business Combinations* is applied to all business combinations that are in its scope. The first issue to consider is whether the entity acquired meets the definition of a business. This can often be subjective, for example if an entity simply contains a single asset, such as an investment property, it may not meet the definition of a business unless there are substantive business processes or services present.

5.3 Is the acquisition in the scope of IFRS 3?

One of the most common areas where we have seen issues arise in practice is group reconstructions where the entities concerned are under common control.

Business combinations involving entities under common control are outside the scope of IFRS 3 (IFRS 3.3(b)). Accordingly, management should use its judgement to develop an accounting policy that is relevant and reliable, in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* (IAS 8.10-12). There are two main approaches: the first is to look to local GAAPs which use merger accounting methodology; the second is to look back into IFRS 3 and use the purchase method.

5.4 Identifying the acquirer

Under IFRS 3 all combinations within the standard's scope are acquisitions or reverse acquisitions and therefore an entity will always need to identify an acquirer. The key to identifying the acquirer is who in substance has control over the other entity. IFRS 3 provides some indicators as to who is the acquirer; these include obtaining more than 50% of the voting rights in the other entity; which entity has the higher fair value; who is paying cash and who is issuing shares; and which entity's management is dominant following the business combination. This is a subjective area and judgement will be based on the collective weight of a number of factors.

Reverse acquisition

Reverse acquisitions may often be more common under IFRS than local GAAP. If a reverse acquisition is identified then in substance the legal subsidiary is identified as the acquirer. There

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is detailed guidance on reverse acquisitions accounting in IFRS 3 Appendix B.

Newly formed entity

If a business combination has been effected through a newly formed entity that issues shares, then under IFRS 3.22 this new company cannot be the acquirer. Therefore if this situation exists one of the existing entities that are combining must be identified as the acquirer. The combination of the new entity and the acquirer will be accounted for as a reverse acquisition.

5.5 Share-based payment

Issues also arise where share options are granted by the acquirer in a business combination to employees of the acquiree who were also shareholders or option holders. Judgement is required to determine whether an equity instrument issued in a business combination is in return for control of the acquiree (and thus within the scope of IFRS 3) or is for post-combination service of the acquiree's employees (and thus a share-based payment under IFRS 2 *Share-based Payment*). All the facts and circumstances of a transaction will need to be considered when deciding whether the options need to be accounted for under IFRS 2 or IFRS 3.

5.6 Cost of acquisition

Once the acquirer has been determined, the cost of the combination needs to be calculated. The cost of the combination is equivalent to the fair value of the consideration given and any directly attributable costs associated with the business combination. The acquiree's identifiable assets, liabilities and contingent liabilities are recognised at the fair value at the acquisition date.

Provisional fair values

When accounting for a business combination initially, in many cases fair value information can only be determined provisionally by the end of the period in which the combination was effected. If this is the case these figures must be disclosed clearly as provisional under IFRS 3. These provisional fair values should be adjusted (if necessary) as a result of completing the initial accounting within 12 months of the acquisition date.

5.7 IFRS 3 Revised

References in section 5 are to the original version of IFRS 3. On 10 January 2008 the IASB published IFRS 3 Business Combinations (revised 2008). The revised Standard will introduce major changes to the accounting requirements for business combinations; careful study of the transition requirements is necessary.

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6 IFRS 7 – Financial instruments: disclosures

6.1 IFRS 7 key issues

IFRS 7 *Financial Instruments: Disclosures* is effective for accounting periods beginning on or after 1 January 2007. IFRS 7 is having a significant impact on all IFRS financial statements.

Some of IFRS 7's new disclosure requirements may require disclosure of potentially commercially sensitive information. Companies that are adopting IFRS 7 should plan this in advance as systems may need refinements in order to extract the relevant disclosure information.

Two examples where companies may be required to disclose commercially sensitive information are:

- disclosures of financial assets that are either past due or impaired. "Past due" means a financial asset where the counterparty has failed to make payment when contractually due. This would include slow-paying trade receivables. Entities are required to disclose an ageing of financial assets past due (at the reporting date) but not impaired. Analysis is also required of financial assets determined to be impaired (eg trade receivables which have been written off or provided for)
- sensitivity analysis in relation to market risk. Market risk includes currency risk, interest rate risk and other price risk. This analysis will be required to show how the profit and loss account would be impacted by changes in the underlying variable, for example, disclosure of the impact of a change in interest rates or of the impact of changes in foreign exchange rates.

6.2 Regulator scrutiny

As IFRS 7 is mandatory only for accounting periods commencing on or after 1 January 2007, it is currently being addressed by regulators for the first time. Given the current credit crisis, it is likely that regulators will pay close attention to compliance with its extensive disclosure requirements.

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7 IAS 12 – Deferred tax accounting and disclosure

7.1 IAS 12 approach

Under some local GAAPs, the accounting for deferred tax focuses on timing differences where gains and losses are recognised in the financial statements in different periods. IAS 12 *Income Taxes* focuses on the tax implications of items recognised in the statement of financial position, specifically temporary differences between carrying amount and tax base. This has a fundamental effect on whether specific accounting entries give rise to a deferred tax consequence. Some common areas where we have seen issues arise in practice are set out below.

7.2 Business combinations

Where a business combination is accounted for as an acquisition, deferred tax adjustments may arise as a result of:

- fair value adjustments, where the carrying value in the consolidated financial statements is adjusted but the tax base is unaffected
- assets or liabilities recognised on acquisition, not recognised in the acquiree's financial statements, for example, some intangible assets
- deferred tax balances recognised on acquisition, not recognised by the acquiree because of the initial recognition exemption, for example, those related to properties
- deferred tax asset recognised on acquisition in respect of tax losses of the acquiree as recovery is now probable due to use of group relief.

However, IAS 12 does not require provision of deferred tax on the initial recognition of goodwill or its subsequent impairment.

7.3 Share-based payments

Under local tax law, the tax deduction in connection with employee share options is often available at the date of exercise, based on the difference between the share's market price at that date and the option exercise price.

Consequently, a deductible temporary difference arises between the tax base of the share based payment expense and the carrying value in the statement of financial position of CU nil. The amount of the deduction is estimated based on the company's share price at the end of the period.

Where the amount of the deduction recognised exceeds the amount that would be calculated based on the cumulative share-based payment expense, the excess is regarded as an equity item and recognised directly in equity.

Where share options are outside the scope of IFRS 2 *Share-based payment* based on their grant date or vesting date (ie the options were granted pre 7 November 2002 or were granted after

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7 November 2002 and vested by the date of transition to IFRS), deferred tax will still need to be recognised in accordance with IAS 12. As no share-based payment expense is recognised, the deferred tax on these share options is recognised directly in equity.

7.4 Compound financial instruments

The initial recognition exemption in IAS 12 does not cover the taxable temporary difference which arises on separation of a compound financial instrument into liability and equity components.

Local tax rules in relation to compound financial instruments are often complex. Management should therefore obtain appropriate tax advice from the company's tax advisers.

It is possible a deferred tax liability may need to be recognised with a corresponding tax charge to equity (as the equity component is recognised directly in equity). Subsequent changes to any deferred tax liability will be recognised through the income statement (as the discount associated with the liability component is recognised in the income statement).

The measurement of the deferred tax liability should reflect the expected manner of settlement. Accordingly, if a taxable temporary difference arises on redemption but not conversion, management will need to assess at the reporting date which option the holders or the issuer are most likely to take. Where conversion is at the option of the holders, conversion should be assumed only where there is strong evidence the holders will exercise this option.

7.5 Property revaluations

When a property is revalued, the carrying amount is adjusted but there is generally no effect on the tax base. Hence, deferred tax balances arise.

Deferred tax provisions are calculated based on the expected manner of recovery of the property. The carrying amount of non-depreciable assets such as land can only be recovered through sale. The carrying amount of depreciable assets such as buildings may be recovered through use or sale or a combination of the two (where the entity plans to use the asset for a period then sell it).

For assets recovered partly through use and partly through sale, measuring the resulting deferred taxes will require a *blended measurement approach* as different tax rates and tax bases will apply.

Deferred tax may need to be provided on previous local GAAP revaluations of property where the revalued amounts are treated as deemed cost for IFRS transition purposes.

7.6 Watch out for unclear or inconsistent tax disclosures

IAS 12 requires the disclosure of a significant amount of information on current and deferred tax. Care needs to be taken to ensure that this information is clearly described and is consistent with other information disclosed in the financial statements. The following are typical errors or omissions:

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- reconciliation of the relationship between tax charge and accounting profit is required for total tax charge rather than current tax (IAS 12.81(c))
- disclosures of unrecognised temporary differences including those associated with unused tax losses and tax credits (IAS 12.81(e)) and investments in subsidiaries, branches, associates and interests in joint ventures (IAS 12.81(f))
- where a loss-making entity has recognised a deferred tax asset, the nature of the evidence supporting its recognition should be disclosed (unless the asset can be recovered through the reversal of existing taxable temporary differences) (IAS 12.82).

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8 Accounting policies – general messages

8.1 Disclosure of accounting policies

IAS 1 *Presentation of Financial Statements (Revised 2007)* requires disclosure of the recognition and measurement basis used in preparing the financial statements and the other accounting policies used that are relevant to an understanding of the financial statements (IAS 1.117). The policies are determined in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* (IAS 8.7-12).

IAS 1 requires that the policies disclosed are those **used** that are **relevant** to an understanding of the financial statements. This means that irrelevant or unnecessary accounting policies should not be stated because to do so might obscure the messages conveyed by those policies that are applied. Where policies are relevant and have been applied to material items, they must be stated.

On transition to IFRS, companies will have reviewed their accounting policies and adjusted them to achieve compliance with IFRS where necessary. Whilst the areas of major difference are usually addressed, there are many more subtle differences between local GAAP and IFRS which could lead to the inclusion of inappropriate accounting policy wording if policies from the previous local GAAP financial statements are simply carried across to the first-year IFRS financial statements. In addition, there are likely to be some specific IFRS requirements to disclose individual policies or aspects of policies that have no direct equivalent under the relevant local GAAP.

Care needs to be taken to use consistent terminology and eliminate local GAAP terms where these have different meanings under IFRS.

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9 Accounting policies – specific problems: revenue

IAS 18.35(b) states that the amount of each significant category of revenue recognised during the period should be disclosed including separate disclosure of the revenue arising from the sale of goods and the rendering of services.

9.1 Revenue policies

A frequent criticism of IFRS financial statements relates to the inadequacy of the revenue recognition policy in describing how revenue is recognised in respect of significant income streams. For example, an accounting policy note might refer to the sale of goods and supply of services but give no detail in respect of the way in which revenue from services is recognised.

Where a company refers to several income streams in its narrative reporting (such as a business review) or in segmental disclosures, it is essential that the accounting policies set out for revenue address each of the income streams identified.

All revenue recognition policies need to be tailored specifically to reflect the company's revenue recognition methods and address both timing and measurement of recognition. A frequent criticism by regulators is of companies using generic "boiler plate" accounting policies, in particular for revenue.

9.2 Example disclosure

The accounting policy shown here is tailored for a manufacturing and retailing group.

Revenue

Revenue is measured at the fair value of the consideration received or receivable and represents the amounts receivable for goods provided in the normal course of business, net of all related discounts and sales tax.

Sale of goods – retail

Retail sales are recognised at the date when the significant risks and rewards of ownership have been transferred to the customer. Revenue from the sale of gift vouchers is recognised when the vouchers have been redeemed or have expired.

Where the Group operates a customer loyalty scheme, the fair value of the award credits is recognised as a separately identifiable component of revenue and credited to deferred income. Fair value represents the retail value of free goods expected to be provided to customers. Revenue is recognised when the award credits are redeemed and the Group fulfils its supply obligations.

Past experience is used to estimate and provide for expected returns at the time of sale.

Sale of goods – wholesale

Wholesale sales are recognised when goods are dispatched to customers. Past experience is used to estimate and provide for expected returns at the time of sale.

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10 Accounting policies – specific problems: financial instruments

10.1 Financial instruments

All companies have financial instruments and therefore all companies should have accounting policies on financial instruments. However, the detail required within the accounting policy depends on the nature and type of financial instruments that a company has.

The accounting policies must be relevant and specific. For example, if a company has included a policy on hedge accounting but there is no evidence in the financial statements that hedge accounting has been applied, this would be an irrelevant policy to disclose.

The key point is whether the disclosure of a policy is needed by users of the financial statements to understand how transactions and events have been reflected in the financial statements. In relation to financial instruments, the policies an entity discloses should be specific to the types of instruments that they have. If a company only has straightforward instruments such as trade payables and receivables, it will not need to, and should not, include policies in other areas such as financial assets at fair value through profit or loss or held-to-maturity investments.

10.2 Financial instrument policies

In short, the financial instruments policy needs to cover the following (for each type of financial instrument a company has):

- initial recognition and measurement
- subsequent accounting treatment and measurement
- impairment
- derecognition.

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11 IFRS 1 – Explanation of transition to IFRS

11.1 Accounting polices

IFRS 1 *First-time Adoption of International Financial Reporting Standards* generally requires an entity to comply with each IFRS effective at the reporting date of its first IFRS financial statements. The standard grants limited optional exemptions to this requirement. The most commonly applied include:

- business combinations prior to the transition date need not be accounted for under IFRS 3 *Business Combinations* (IFRS 1 Appendix B)
- previous local GAAP revaluations of property, plant and equipment may be treated as deemed cost at revaluation date. The entity may also remeasure an item of property, plant and equipment at fair value at the transition date and use that fair value as its deemed cost (IFRS 1.16-19)
- retrospective application of the "corridor approach" to recognising actuarial gains and losses on defined benefit pension liabilities is not required (IFRS 1.20)
- cumulative translation differences on foreign operations may be deemed to be zero at the transition date and need not be recognised as a separate component of equity (IFRS 1.21-22)
- an entity need not apply IAS 21 *The Effects of Changes in Foreign Exchange Rates* retrospectively to goodwill and fair value adjustments arising on those business combinations involving foreign operations which occurred prior to the transition date. These items are not then retranslated at the closing rate at each subsequent reporting date but are stated using the exchange rate applied under local GAAP (IFRS 1 Appendix B, B1A).

However, where optional exemptions to full retrospective application of IFRS are taken, this fact must be disclosed.

11.2 Clarity of transition disclosures

A frequent criticism of first-year IFRS financial statements is that the IFRS 1 reconciliations do not include sufficient detail to **explain** the effect of the transition to IFRS. Sufficient explanation of the IFRS adjustments is critical if the reader of the financial statements is to understand how the transition to IFRS has affected the company's results and financial position. In addition, material adjustments to the cash flow statement prepared under local GAAP are often overlooked (IFRS 1.40).

The correction of errors under local GAAP must be distinguished clearly from the effect of IFRS adjustments in the IFRS 1 reconciliations (IFRS 1.41).

11.3 Presentation and disclosure

IFRS 1 states that there are no exemptions for first-time adopters from the presentation and disclosure requirements of other IFRSs (IFRS 1.35) except in a limited number of cases (IFRS 1.36A-37). For a first time adopter of IFRS the comparatives must be presented in accordance with the policies in place for its first IFRS financial statements.

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12 IFRS 5 – Non-current assets held for sale and discontinued operations

IFRS 5.32 A discontinued operation is a component of an entity that either has been disposed of, or is classified as held for sale, and

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

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

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

12.1 IFRS 5 requirements

IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations* specifies the requirements relating to the classification, measurement and presentation of non-current assets held for sale and discontinued operations.

The criteria in IFRS 5 to meet the definition of discontinued are very strict and regulators have been known to question companies regarding whether the classification of discontinued operations actually met these criteria.

12.2 Non-current assets (and disposal groups) held for resale

Definition

A disposal group is a group of assets and related liabilities to be disposed of. Under IFRS 5 a non-current asset (or disposal group) is classified as held for sale if its carrying amount is expected to be recovered principally through sale rather than continuing use. The asset must be available for immediate sale subject to normal terms and conditions at a reasonable price, and the sale must be expected to be completed within one year of the asset (or disposal group) being classified as held for sale (IFRS 5.6-8).

Measurement

A non-current asset (or disposal group) classified as held for sale does not have depreciation or amortisation charged on it.

Items held for sale are remeasured to the lower of their carrying amount, under applicable IFRS, and their fair value less costs to sell. Where the fair value is greater than the carrying amount of the item this will have no effect on the reported value. However, where a fair value is less than the current carrying amount, the remeasurement will result in a loss to the entity.

Presentation

Where a non-current asset or disposal group is held for sale, the assets and liabilities should be reported separately from other assets and liabilities on the face of the statement of financial position. The assets and liabilities of a disposal group should not be netted off. The comparatives are not adjusted.

Common issues

Where entities have disclosed non-current assets held for sale on the statement of financial position, they have often failed to disclose the major classes of assets and liabilities classified as held for sale either on the face of the statement of financial position or within the notes to the financial statements as required by IFRS 5.38.

12.3 Discontinued operations

Definition

IFRS 5.32 sets out the definition of a discontinued operation. An operation is classed as discontinued under IFRS 5 if it is sold

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in the period or meets the conditions to be classified as held for sale at the reporting date.

Presentation and disclosure

Discontinued operations are disclosed on the face of the income statement as a single amount comprising the total of:

- 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.

IFRS 5 requires further analysis of the single amount into:

- revenue, expenses and pre-tax profit or loss of discontinued operations
- related income tax expense
- the 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.

This analysis may be presented in the notes or on the face of the income statement. If it is presented on the face of the income statement, it must be presented in a section identified clearly as relating to discontinued operations.

Common issues

In some cases, companies have failed to disclose on the face of the income statement the single amount required by IFRS 5 and have followed local GAAP disclosures rather than IFRS 5.

Companies that have disclosed discontinued operations often have not included basic and diluted earnings per share (EPS) relating to discontinued operations within the notes to the financial statements as required by IAS 33 *Earnings per Share* (IAS 33.68). Furthermore, companies have not always disclosed both basic and diluted EPS in relation to both continuing operations and profit or loss for the period on the face of the income statement (IAS 33.66).

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13 IAS 14 – Segment information

13.1 IAS 14 Requirements

IAS 14 *Segment Reporting* is more prescriptive than many local GAAPs in terms of how a segment is identified and the extent of the information required to be disclosed on a segmental basis. The objective of IAS 14 is to provide users with information on risks and returns attributable to different products and services or different geographical areas.

For example, there is no exemption from disclosure under IAS 14 where a company's directors consider that disclosure would have been seriously prejudicial to the company's interests.

13.2 Common issues

Some of the common issues that have been identified are as follows:

- segment assets and liabilities under IAS 14 do not include interest-bearing assets and liabilities or income tax assets and liabilities
- reconciliations between segment information and overall amounts in the financial statements need to be complete and accurate
- companies sometimes identify areas of the business as unallocated to segments which would benefit from further analysis to allow an understanding of the nature of the items
- where companies' other disclosures and narrative reporting appear to suggest that there are additional reportable segments in respect of which disclosure under IAS 14 might be expected, this may provoke questions from the regulators.

13.3 Disclosures

See Appendix B for example IAS 14 disclosure.

13.4 IFRS 8

IFRS 8 *Operating Segments* will replace IAS 14 for accounting periods beginning on or after 1 January 2009 and may be adopted early. However, for this document we have focused on IAS 14 issues, because we anticipate that a number of companies will continue to use IAS 14 for the moment.

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14 IAS 37 – Provisions disclosure

14.1 IAS 37 Key issues

Current and non-current liabilities

It should be noted that there is no separate statement of financial position category for provisions in IFRS; they are current or non-current liabilities like any other. Therefore, balances need to be allocated to the current liabilities or non-current liabilities sections as appropriate, applying the normal IAS 1.69 definitions.

Provisions and accruals

Under IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*, Provisions and accruals are different things (see IAS 37.11). Provisions are liabilities of uncertain timing or amount. Accruals are liabilities to pay for goods and services that have been received or supplied but not paid, invoiced or formally agreed. Though some degree of estimation may be required regarding the timing or amount of accruals, this is generally much less than for provisions. The distinction between provisions and accruals matters because provisions are covered by IAS 37's disclosure requirements whereas accruals are not. It is not acceptable to circumvent the disclosure requirements of IAS 37 by characterising something as an accrual where it is clearly a provision within the scope of IAS 37.

14.2 Key disclosures

Disclosure requirements for provisions, contingent liabilities and contingent assets are set out in IAS 37.84-92.

The experience of the member firms within Grant Thornton International is that some disclosures are easily missed, for example the requirement to show the movement in each class of provisions during the year (IAS 37.84). The disclosure of movements in the period should show separately unused amounts that have been reversed as at the year end. Where provisions are for different purposes, they should be presented separately in the disclosures and not aggregated. The unwinding of any discounts on provisions must also be shown (IAS 37.84(e)).

The narrative disclosures (IAS 37.85) are often missed. For **each class** of provision, the following needs to be disclosed:

- a brief description of the nature of the obligation and the expected timing of any resulting outflows of economic benefits
- an indication of the uncertainties about the amounts or timings of outflows (including, where necessary to provide adequate information, disclosure of the major assumptions made concerning future events). Here, the requirements of IAS 1.122 and 1.125 also need to be considered (see Section 1)
- the amount of any expected reimbursement, stating the amount of any related asset recognised.

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14.3 Example disclosure

Note to the accounts: Provisions

Group	Onerous leases CU000	Dilapidations CU000	Total CU000
1 January 2007	535	440	975
On acquisition (note 36)	342	-	342
Charged to income statement	17	10	27
Unwinding of discount	23	15	38
Utilised	(90)	(32)	(122)
31 December 2007	827	433	1,260

Company	Onerous leases CU000	Dilapidations CU000	Total CU000
1 January 2007	502	400	902
Charged to income statement	17	10	27
Unwinding of discount	21	14	35
Utilised	(19)	(32)	(51)
31 December 2007	521	392	913

Provisions are analysed between current and non-current as follows:

	Group		**Company**	
	2007 CU000	2006 CU000	2007 CU000	2006 CU000
Current	250	90	159	90
Non-current	1,010	885	754	812
	1,260	975	913	902

The provision for onerous leases is in respect of leasehold properties from which the Group no longer trades, but is liable to fulfil rent and other property commitments up to the lease expiry date. If a property is sub-let below the head rent, or for a period shorter than the remaining lease term, provision is made for the onerous element of the lease. Obligations are payable within a range of 1 to 9 years (2006: 2 to 10 years), the weighted average being 5 years (2006: 6 years). Amounts have been provided on current rentals which, following a rent review, could require additional provision.

The Group provides for the estimated cost of property dilapidations, where appropriate, during the period of the tenancy. The provisions are expected to be utilised over the next 5 to 6 years.

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15 IAS 39 – Financial instruments: recognition and measurement

15.1 IAS 39 Approach

IAS 39 *Financial Instruments: Recognition and Measurement* is a complex and rules-based standard that presents many companies with major challenges on transition to IFRS. The standard establishes the principles for recognising and measuring financial instruments. IAS 39's rules-based approach means that its results are not always intuitive. IAS 32 *Financial Instruments: Presentation* deals with the definition of financial assets, financial liabilities and equity, which has a consequential impact on measurement under IAS 39.

15.2 Wide-ranging scope

IAS 39 includes all financial instruments other than those specifically excluded from its scope. As a result, IAS 39 applies to a wide range of financial instruments including for example accounts receivable (trade debtors), accounts payable (trade creditors), loans, equity investments, derivatives and in some cases even sales or purchase orders. Whilst sales or purchase orders are normally excluded from the IAS 39 scope by virtue of the "own use exemption", this might not always be the case. For instance, industries involved in the exchanging of commodities, such as metal traders, mining companies or energy supply companies need to be mindful of the own use exemption. Financial guarantee contracts, for example guaranteeing a third party's borrowings, are also within the scope of IAS 39 unless previously specifically deemed to be insurance contracts.

15.3 Extensive use of fair values – profit volatility

At the date of inception, all financial instruments are required to be included at fair value. In most cases this will be the same as transaction price, but this is not always the case, for instance, below-market-rate loans with related parties who might provide loans on terms which do not equate to those which a bank would provide. In the context of a loan instrument, a market comparison should ensure a similar collateral, credit risk, maturity, currency and interest payment profile. For instance if a related party loan is provided on an unsecured basis for three years at an interest rate of 6%, this is unlikely to be comparable to a loan that a bank would provide. If the transaction price is not equal to fair value, an initial recognition gain or loss could arise on inception (with the difference also resulting in a different finance charge compared to the interest rate for cash purposes). This may also be important from a tax perspective.

After the date of inception, the measurement basis depends on the financial instrument's classification, with some being measured at amortised cost and others at fair value. Derivatives are measured at fair value with movements recognised in profit or loss, which may result in profit volatility.

15.4 Embedded derivatives

Embedded derivatives are items meeting the definition of a derivative but contained within a larger hybrid contract. Common examples are early repayment options (eg issuer has

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option to repay loans early) or foreign currency sales orders or purchase orders. Embedded derivatives are required to be separated from their host contract and carried at fair value through profit and loss (ie the same treatment as derivatives) unless they are deemed "closely related". There are detailed rules as to what is deemed closely related.

Throughout IAS 39, it is crucial to look at each financial instrument based on a clear understanding of its contractual terms. An example of this is interest collars. If an interest collar is a separate instrument in its own right then it is accounted for as a derivative (even if its economic purpose was clearly to hedge the interest cash flows – although as discussed below hedge accounting might also be possible). Conversely, if the collar arrangement is written directly into a loan agreement, such that it is an embedded derivative, it is possible that the collar would be deemed closely related to the host loan and would not require separation. Therefore, there is a significant distinction between an interest collar which is a financial instrument in its own right compared to an embedded collar.

15.5 Convertible bonds and warrants: conversion rights might not be equity

Companies often issue convertible bonds assuming they are compound instruments and issue warrants over own shares assuming they are equity. However this is not always the case because of the "fixed-for-fixed rule" (see IAS 32.16(b)(ii) and IAS 32.21-24). This needs careful examination. A convertible bond where the conversion terms fail the fixed-for-fixed test is a host debt with a separable embedded derivative. A warrant which fails the fixed-for-fixed test is a derivative within the scope of IAS 39.

15.6 Hedge accounting

Hedge accounting is purely optional under IFRS, but entities may choose to use it to counteract the profit volatility of a derivative which hedges a hedged item. However, hedge accounting is far from a free choice. It cannot simply be decided upon during the year-end reporting process, as detailed prescriptive documentation is required at the hedge inception. Furthermore, many economic hedges are precluded from hedge accounting because of the detailed IAS 39 rules. In addition, there are complex effectiveness tests to negotiate.

15.7 Common issues

Some companies' financial statements have been unclear on initial measurement of financial assets and liabilities, in particular regarding how transaction costs had been accounted for, how deferred consideration was determined or whether financial assets or financial liabilities were carried at fair value. It has not always been clear how companies had concluded that embedded derivatives were separable from the host contract. Some companies have classified financial assets in such a way that it is not possible to tell if they had applied IAS 39, as no analysis of financial instruments was disclosed.

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16 Standards in issue not yet effective

IAS 8.30 When an entity has not applied a new Standard or Interpretation that has been issued but is not yet effective, the entity shall disclose:

(a) this fact; and

(b) known or reasonably estimable information relevant to assessing the possible impact that application of the new Standard or Interpretation will have on the entity's financial statements in the period of initial application.

16.1 IAS 8 Requirements

IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* requires entities that have not applied a new standard or interpretation, which has been published but is not yet effective, to make certain disclosures. These disclosures include stating that the standard or interpretation has not yet been applied and the potential impact on the entity's financial statements in the period of initial application. These disclosures are often overlooked as there is frequently no direct equivalent under local GAAP.

When making the disclosure the entity should consider including the following information:

- the title of the new standard or interpretation
- the date by which the standard or interpretation must be applied
- the date from which the entity intends to apply the standard or interpretation
- the nature of the future changes in policy or policies
- a discussion of the impact that initial application is expected to have on the financial statements.

As the disclosures relate to Standards and Interpretations in issue when the financial statements are authorised for issue, it is important to monitor the IASB's and IFRIC's output to ensure that all relevant pronouncements are covered.

For European companies, as the legal requirement is to apply IFRS as adopted by the European Union, it is in addition helpful to indicate in the disclosures whether or not standards in issue not yet effective have been endorsed. The current endorsement status of IASB pronouncements may be found at: http://www.efrag.org/

16.2 Common issues

Experience to date shows that some companies fail to provide the relevant disclosures, whilst others fail to extend their disclosure to include relevant IFRIC Interpretations.

16.3 Example disclosure

Standards, amendments and Interpretations to existing Standards that are not yet effective and have not been early adopted by the group in the 30 September 2007 financial statements.

At the date of authorisation of these financial statements, certain new Standards, amendments and Interpretations to existing standards have been published but are not yet effective. The Group has not early adopted any of these pronouncements. The new Standards, amendments and Interpretations that are expected to be relevant to the Group's financial statements are as follows:

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Amendment to IAS 1 Presentation of Financial Statements (effective from 1 January 2009, ie for reporting periods beginning on or after this date)

This amendment affects the presentation of owner changes in equity and introduces a statement of comprehensive income. Preparers will have the option of presenting items of income and expense and components of other comprehensive income either in a single statement of comprehensive income with subtotals, or in two separate statements (a separate income statement followed by a statement of other comprehensive income). This amendment does not affect the financial position or results of the Group but will give rise to additional disclosures. Management is currently assessing the detailed impact of this amendment on the Group's financial statements.

Amendment to IAS 23 Borrowing Costs (effective from 1 January 2009)

This amendment requires the capitalisation of borrowing costs, to the extent they are directly attributable to the acquisition, production or construction of qualifying assets that need a period of time to get ready for their intended use or sale. The option of immediately expensing those borrowing costs, currently used by the Group, will be removed. In accordance with the transitional provisions of the amended Standard, no changes will be made for borrowing costs incurred to this date that have been expensed. This amendment will decrease the group's reported interest expense and increase the capitalised cost of qualifying assets under construction in future periods. Preliminary forecasts indicate that borrowing costs in the order of CU70,000 - CU120,000 are expected to be capitalised in the first year of application of this revised Standard.

IFRS 8 Operating segments (effective from 1 January 2009)

This IFRS specifies how an entity should report information about its operating segments in its financial statements. Generally, financial information is required to be reported on the same basis as is used internally for evaluating operating segment performance and deciding how to allocate resources to operating segments. Implementation of this Standard is expected to increase the number of reportable segments, as well as the manner in which the segments are reported, in a manner that is consistent with the internal reporting provided to the chief operating decision-maker. As goodwill is allocated to groups of cash-generating units based on segment level, the change will also require the reallocation of goodwill to the newly identified operating segments. Management does not anticipate that this will result in any material impairment of goodwill.

Revised IFRS 3 Business Combinations and revised IAS 27 Consolidated and Separate Financial Statements (effective from 1 July 2009)

These revisions require some significant changes to the application of the acquisition method to business combinations and the accounting for subsequent changes in ownership interests. The main changes likely to impact the Group's accounting policies for future business combinations and relevant ownership changes are: (a) transaction costs incurred in a business combination will be expensed instead of being included in the cost of investment; (b) an option is introduced to allow any non-controlling interest in the acquired entity to be measured at fair value, with a consequential impact on the calculation of goodwill; (c) once control is obtained, all other increases or decreases in ownership interest are reported in equity and will no longer result in goodwill adjustments or gains and losses. Management is currently

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assessing the detailed impact of these revisions on the Group's financial statements.

IFRIC 13 Customer loyalty programmes (effective from 1 July 2008).

This Interpretation clarifies that when goods or services are sold together with a customer loyalty incentive (for example, loyalty points or free products), the arrangement is a multiple-element arrangement and the consideration receivable from the customer is allocated between the components of the arrangement using fair values. The Group's current accounting policy is to recognise the consideration in full and to provide for the estimated cost of the future rewards. Consequently, the adoption of this Interpretation will delay the recognition of revenue and related profit allocated to the loyalty awards until the awards are redeemed or lapse. Management is currently assessing the expected financial effects on the Group's financial statements.

IFRIC 14 IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction (effective from 1 January 2008)

This Interpretation provides guidance on how to assess the limit on the amount of surplus in a defined benefit scheme that can be recognised as an asset under IAS 19 Employee Benefits. Management expects that this Interpretation will have no impact on the financial position or performance of the Group as all defined benefit schemes are currently in deficit but there may be an impact if the schemes return to a surplus position.

Management anticipate that all the above pronouncements will be adopted in the Group's financial statements for the period beginning 1 October 2008.

Other new Standards and Interpretations have been issued but are not expected to have a material impact on the Group's financial statements.

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17 Operating items and exceptional items

IAS 1.BC13 The Board recognises that an entity may elect to disclose the results of operating activities, or a similar line item, even though this term is not defined. In such cases, the Board notes that the entity should ensure the amount disclosed is representative of activities that would normally be considered to be 'operating'. In the Board's view, it would be misleading and would impair the comparability of financial statements if items of an operating nature were excluded from the results of operating activities, even if that had been industry practice.

17.1 Operating items

IAS 1 *Presentation of Financial Statements (Revised 2007)* has only minimum presentation requirements relating to the face of the income statement. Operating profit is not a required line under IFRS but, if such a line is included, it must include everything that is operating in nature (see IAS 1.BC13).

As can be seen from IAS 1.BC13, it is key that all items that are considered operating in nature are included above any operating profit line. Including this additional line and then not showing all items within the correct category would be misleading to the users of the financial statements.

17.2 Exceptional items

There is no definition of "exceptional items" in IFRS although IAS 1.86 states that "An entity includes additional line items in the statement of comprehensive income and in the separate income statement (if presented), and it amends the descriptions used and the ordering of items when this is necessary to explain the elements of financial performance" and "when items of income or expense are material, an entity shall disclose their nature and amount separately". The disclosure required by IAS 1.97 may be either on the face of the income statement or in the notes.

If an entity describes amounts as "exceptional items" an accounting policy should be provided in accordance with IAS 1.117 to explain the entity's policy for characterising such items as exceptional.

Typically, such items will be material items which individually or, if of a similar type, in aggregate, need to be disclosed by virtue of their size or incidence because of their relevance to understanding the entity's financial performance.

17.3 Example accounting policy

Exceptional items

Exceptional items are those which are separately identified by virtue of their size or incidence to allow a full understanding of the underlying performance of the Group.

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18 Comparative information

IAS 1.38 Except when IFRSs permit or require otherwise, an entity shall disclose comparative information in respect of the previous period for all amounts reported in the current period's financial statements. An entity shall include comparative information for narrative and descriptive information when it is relevant to an understanding of the current period's financial statements.

18.1 Comparative information and IAS 1

IAS 1 *Presentation of Financial Statements (Revised 2007)* requires comparative information to be disclosed in respect of all amounts reported in the financial statements (IAS 1.38).

Very limited exceptions to the general requirement to provide comparatives for all numerical information are given in IFRS. One such example is that IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* requires a reconciliation of the opening and closing provisions but does not require disclosure of a comparative reconciliation (IAS 37.84).

18.2 Common issues

Experience to date shows that comparative information is often omitted in situations where there is no direct equivalent requirement under local GAAP. For example, there are no exemptions from providing full comparatives in IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets.* Hence, a full comparative table of the movement from opening to closing position is required for property, plant and equipment and intangible assets.

18.3 Other key areas

The revised version of IAS 1 introduces a new requirement for comparatives in some situations. Under IAS 1.39, when an entity applies an accounting policy retrospectively or makes a retrospective restatement of items in its financial statements or when it reclassifies items in its financial statements, it shall present, as a minimum, three statements of financial position, two of each of the other statements, and related notes. An entity presents statements of financial position as at:

(a) the end of the current period,
(b) the end of the previous period (which is the same as the beginning of the current period), and
(c) the beginning of the earliest comparative period.

IAS 1 *Presentation of Financial Statements (Revised 2007)* is effective for annual periods beginning on or after 1 January 2009. Earlier adoption is permitted.

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19 IAS 19 – Employee Benefit Disclosures

19.1 Employee benefits

IAS 19 *Employee Benefits* requires extensive disclosures in respect of defined benefit plans, including the accounting policy for recognising actuarial gains and losses, a reconciliation of the various categories and the net totals in the statement of financial position and income statement, any investment by the plan in the entity, and the principal actuarial assumptions.

19.2 Common issues

The main points where the quality of pensions reporting under IFRS could be improved include:

- better disclosure of the uncertainties surrounding accounting estimates
- more consistent interpretation of what is meant by principal assumptions
- a focus on more accessible and less technical explanations
- more information about non-standard types of assets held
- avoiding detailed disclosure of immaterial amounts.

IAS 19.120A(n)(vi) requires disclosure of "any other material actuarial assumptions". Both inflation and mortality assumptions would normally be expected to qualify as such, thus requiring disclosure.

Disclosure (narrative or quantified) of the uncertainties surrounding estimates and the impact of changes to those estimates in relation to pension liabilities needs to be provided in accordance with IAS 1.125-133 (see also Section 1). Sensitivity disclosures often show that very small movements in major assumptions, such as discount rates or inflation, could have a very significant effect on the level of liability estimated, thus indicating the importance of providing adequate disclosures relating to sources of estimation uncertainty under IAS 1.

19.3 Example disclosures

See Appendix C for example IAS 19 disclosures.

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20 Detail counts – don't forget…

20.1 Introduction

This IFRS Top 20 Tracker is, by its nature, not a comprehensive checklist of IFRS requirements. The experience of the Grant Thornton member firms is that many companies that have already transitioned to IFRS have found it much more difficult than they had anticipated to achieve full compliance with all the detailed requirements. Though the major recognition, measurement and overall format issues may have been addressed, achieving compliance with the significant volume of detailed disclosure requirements under IFRS can take much more time and effort than anticipated. If such matters are not addressed sufficiently early, completion of the financial statements risks being delayed. A key message from this experience is that the detail counts. By way of example, this section highlights a selection of detailed areas where there is evidence that many companies encounter difficulties in achieving IFRS compliance.

20.2 IAS 1 Analysis of expenses

Under IAS 1 *Presentation of Financial Statements (Revised 2007)*, expenses may be analysed on the face of the statement of comprehensive income or in the notes, either by nature or function, depending on which presentation provides users with the more useful information (IAS 1.99). A number of companies have been criticised by regulators for providing a mixed presentation or not analysing expenses in full, making it difficult to appreciate how expenses vary with a change in the level of sales.

20.3 IAS 2 Inventories

IAS 2 *Inventories* sets out the accounting requirements for inventories, covering how cost and subsequent expense is to be determined, including any write down to net realisable value. Many companies fail to provide the disclosure in relation to the amount of inventory recognised as an expense in the period (IAS 2.36(d)) or the amount of any write-down to net realisable value or the reversal of such write-downs (IAS 2.36(e) and (f)).

20.4 IAS 7 Parent company cash flow statement

If a parent company has adopted IFRS for its individual company accounts, it must disclose a full cash flow statement with comparatives. This is different from many local GAAPs where an exemption often exists allowing the parent company not to present its individual cash flow statement.

20.5 IAS 24 Key management personnel compensation

IAS 24 *Related Party Disclosures* prescribes the accounting and disclosure in relation to related parties. IAS 24 requires entities to consider key management personnel as related parties of the entity. The extent to which senior management meet the definition of key management is a matter for the directors' judgement (and may encompass more individuals than simply

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the parent company Board of Directors). IAS 24.16 prescribes the disclosure required in relation to key management personnel compensation. This will not necessarily be the same as disclosure of directors' emoluments.

The most common omission from IAS 24 disclosures is the amount of compensation given by way of a share-based payment. Here, the disclosure under IAS 24 relates to the cost recognised by the company under IFRS 2 *Share-based Payment* for share-based payments to key management personnel. Furthermore if the parent company has transitioned to IFRS, full IAS 24 disclosures are required as there are no inter-company transaction disclosure exemptions.

20.6 IAS 33 EPS

IAS 33 *Earnings per Share* prescribes the requirements for determining earnings per share to ensure consistency across accounting periods and companies. Regulators noted a number of common disclosure issues, which were:

- if basic and diluted EPS are the same, that fact should be made clear from the disclosure provided in the income statement (IAS 33.67)
- if an adjusted EPS is disclosed, a diluted adjusted EPS should also be given (IAS 33.73)
- if a discontinued operation is reported, a basic and diluted EPS for that operation should be disclosed either on the face of the income statement or in a note (IAS 33.68).

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A IFRS Top 20 Checklist table

	Topic	Relevant	Addressed
1	IAS 1 – Presentation issues: judgements and estimates	Y/N	Y/N
2	IAS 1 – Presentation issues: primary statement formats	Y/N	Y/N
3	IAS 36 – Impairment disclosures	Y/N	Y/N
4	IFRS 3 – Goodwill justification disclosure	Y/N	Y/N
5	IFRS 3 – Other business combination issues and disclosures	Y/N	Y/N
6	IFRS 7 – Financial instruments: disclosures	Y/N	Y/N
7	IAS 12 – Deferred tax accounting and disclosure	Y/N	Y/N
8	Accounting policies – general messages	Y/N	Y/N
9	Accounting policies – specific problems: revenue	Y/N	Y/N
10	Accounting policies – specific problems: financial instruments	Y/N	Y/N
11	IFRS 1 – Explanation of transition to IFRS	Y/N	Y/N
12	IFRS 5 – Non-current assets held for sale and discontinued operations	Y/N	Y/N
13	IAS 14 – Segment information	Y/N	Y/N
14	IAS 37 – Provisions disclosure	Y/N	Y/N
15	IAS 39 – Financial instruments: recognition and measurement	Y/N	Y/N
16	Standards in issue not yet effective	Y/N	Y/N
17	Operating items and exceptional items	Y/N	Y/N
18	Comparative information	Y/N	Y/N
19	IAS 19 – Employee Benefit Disclosures	Y/N	Y/N
20	Detail counts – don't forget…	Y/N	Y/N

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B Example IAS 14 segmental disclosure

Business segments

The Group is managed according to three operating divisions: confectionery, coffee and wine. These divisions are the basis on which the Group reports its primary segment information. The principal activities of each division are as follows:

- the confectionery division manufactures, distributes and sells confectionary through its high street retail outlets and in the wholesale market;
- the coffee division sells coffee, patisserie, sandwiches and baked goods through a chain of high quality coffee bars; and
- the wine division sells wine direct to the public, through a chain of branded retail outlets.

The inter-segment sales are immaterial. Segment results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Unallocated assets and liabilities comprise items such as cash and cash equivalents, taxation, and borrowings. Segment capital expenditure is the total cost incurred during the year to acquire segment assets that are expected to be used for more than one period.

	Confectionery		Coffee		Wine		Unallocated		Total	
	2007	2006	2007	2006	2007	2006	2007	2006	2007	2006
Continuing Operations	CU000	CU000	CU000	CU000	CU000	CU000	CU000	CU000	CU000	CU000
Revenue	110,810	109,302	18,140	17,832	15,895	16,358	-	-	144,845	143,492
Segment result	12,943	13,980	1,350	1,423	345	639	(7,972)	(8,229)	6,666	7,813
Finance income									184	289
Finance costs									(1,902)	(1,997)
Profit before taxation									4,948	6,105
Taxation									(1,473)	(1,853)
Profit for the year from continuing operations									3,475	4,252
Discontinued Operations										
Revenue	-	-	-	-	6,331	7,752	-	-	6,331	7,752
Segment result	-	-	-	-	(228)	178	-	-	(228)	178

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The segment result from discontinued operations is equal to the (loss)/profit before tax from discontinued operations disclosed in note 10, which provides a reconciliation to the (loss)/profit for the year from discontinued operations.

	Confectionery		Coffee		Wine		Total	
	2007	**2006**	**2007**	**2006**	**2007**	**2006**	**2007**	**2006**
	CU000	CU000	CU000	CU000	CU000	CU000	CU000	CU000
Segment assets	65,608	61,018	12,835	12,614	10,576	11,473	89,019	85,105
Unallocated assets							5,059	2,873
Total assets							94,078	87,978
Segment liabilities	(17,659)	(21,154)	(7,006)	(8,235)	(3,496)	(4,611)	(28,161)	(34,000)
Unallocated liabilities							(30,774)	(27,898)
Total liabilities							(58,935)	(61,898)
Other segment items:								
Capital expenditure (including acquisitions)								
– Property, plant and equipment (note 17)	6,824	3,870	304	800	261	735	7,389	5,405
– Intangible assets (note 16)	1,585	2,217	-	458	-	422	1,585	3,097
Depreciation (note 17)	5,630	5,389	1,084	1,061	910	976	7,624	7,426
Amortisation of intangible assets (note 16)	1,347	1,150	233	238	197	219	1,777	1,607
Impairment loss recognised in income	58	75	-	-	325	108	383	183
Restructuring costs (note 6)	310	1,529	-	-	-	-	310	1,529

Geographical segments

The Group's business segments operate in both the UK and Europe. The Group's principal manufacturing, distribution and retail operations are located in the UK. Distribution of confectionery and wines to wholesale customers is also carried out in Europe.

In presenting information on the basis of geographical segments, segment revenue is based on the geographical location of customers and not on the legal entity in which the transaction occurred. Segment assets and capital expenditure are based on the geographical location of the assets.

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	Revenue		Segment Assets		Capital Expenditure	
	2007	**2006**	**2007**	**2006**	**2007**	**2006**
	CU000	CU000	CU000	CU000	CU000	CU000
United Kingdom	128,895	127,712	87,237	83,143	8,974	8,502
Europe	15,950	15,780	1,782	1,962	-	-
Unallocated assets	-	-	5,059	2,873	-	-
Total	144,845	143,492	94,078	87,978	8,974	8,502

Revenue from the Group's discontinued operations was derived wholly within the UK (2007: CU6,331,000 and 2006: CU7,752,000).

Analysis of revenue by category:

	2007	**2006**
	CU000	CU000
Continuing operations		
Sale of goods	144,845	143,492
Other operating income	378	385
Finance income	184	289
	145,407	144,166
Discontinued operations		
Sale of goods	6,331	7,752
	151,738	151,918

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C Example IAS 19 defined benefit pension scheme disclosure

These examples are included to illustrate the types of disclosures required by IAS 19 and also to show the significant amount of information which must be included within IAS 19 disclosures. The corridor method has not been used in this example.

Statement of Comprehensive Income (Extract)

	2007	2006
	CUm	CUm
Actuarial gain/(loss) on pension scheme	276	91
Deferred tax on actuarial gain/loss	XX	XX

Statement of financial position (Extract)

	2007	2006
	CUm	CUm
Non-current assets		
Retirement benefit asset	479	204

Note XX Pension scheme

The group has established a funded defined benefit pension scheme for eligible employees [give general description of type of plan. This should distinguish, for example, career average salary pension plans from final salary pension plans and from post-employment medical plans. The description must include informal practices that give rise to constructive obligations included in the measurement of the defined benefit obligation in accordance with IAS 19.52. Further detail is not required].

The most recent actuarial valuation was [give date and state whether actuaries are independent {this disclosure is not strictly required by IAS 19 but inclusion is good practice}].

The principal actuarial assumptions used by the actuaries were as follows:

	2007	2006
	%	%
Rate of future increase in pensionable salaries	4.0	5.5
Rate of future increase in pensions in payment	2.0	3.0
Discount rate at 31 December	4.5	7.0
Inflation assumption	2.5	4.0
Overall expected return on plan assets at 31 December	6.9	7.5

The expected return on plan assets is based on [give details of basis used to determine overall expected rate and the effect of major categories of plan assets].

Other material actuarial assumptions were: [give details of other material actuarial assumptions, which will typically include mortality assumptions.]

For example - Assumptions regarding future mortality experience are set based on the advice of actuaries and in accordance with published statistics. Life expectancies have been estimated as 84.5 years for men (2006: 84.5 years) and 87.5 years for women (2006: 87.5 years).

[Disclose uncertainties surrounding estimates and the impact of changes in these estimates in relation to pension liabilities, per IAS 1.125-133.]

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The amounts recognised in the consolidated statement of financial position are as follows:

	2007	2006
	CUm	CUm
Fair value of plan assets	1,488	962
Present value of funded retirement benefit obligations	(1,009)	(758)
Net asset	479	204

The major categories of plan asset, as a percentage of the total plan assets, are as follows:

	2007	2006
	%	%
Equities	75	75
Bonds	20	20
Property	5	5

{The above may be given as amounts or as percentages.}

[Give details of any amounts {must be amounts, not percentages} included in the fair value of plan assets for each category of the entity's own financial instruments and any property occupied by, or other assets used by, the entity.**]**

The actual return on plan assets was as follows:

	2007	2006
	CUm	CUm
Actual return on plan assets	553	206

The amounts charged or (credited) in profit or loss are as follows:

	2007	2006
	CUm	CUm
Current service cost	34	25
Past service cost	12	-
Expected return on plan assets	(73)	(68)
Interest cost	53	57
	26	14

The amounts charged or credited in profit or loss were included in **[**give details of line item or items to which amounts were charged/credited.**]**

{**Note:** IAS 19 does not specify line items to be used or whether current service cost, expected return on plan assets and interest cost should be presented as components of a single item of income or expense on the face of the income statement (IAS 19.119).}

Movements in the defined benefit obligation during the year were as follows:

	2007	2006
	CUm	CUm
At 1 January	758	668
Current service cost	34	25
Past service cost	12	-
Interest cost	53	57
Actuarial losses	204	47
[Show contributions by plan participants, if any**]**		
Benefits paid	(52)	(39)
At 31 December	1,009	758

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[The defined benefit obligation should be analysed into amounts arising from plans that are wholly unfunded and plans that are wholly or partly funded.]

Movements in the fair value of plan assets during the year were as follows:

	2007	2006
	CUm	CUm
At 1 January	962	760
Expected return on plan assets	73	68
Actuarial gain	480	138
Contributions by the group	25	35
[Show contributions by plan participants, if any]		
Benefits paid	(52)	(39)
At 31 December	1,488	962

The group expects to pay contributions of CUXX in 2008.

The cumulative actuarial gains and losses recognised in other comprehensive income at 31 December 2007 was CU367m (2006: CU91m).

{**Note:** under IAS 19.93D, actuarial gains and losses recognised in other comprehensive income are recognised immediately in retained earnings (not in a separate reserve) and are not recycled to profit or loss in a subsequent period.}

Movements in the statement of financial position retirement benefit asset during the year were as follows:

	2007	2006
	CUm	CUm
At 1 January	204	92
Net amount charged in profit or loss	(26)	(14)
Net actuarial gains	276	91
Contributions	25	35
At 31 December	479	204

Amounts for the current and previous four periods {See note below} are as follows:

	2007	2006	2005
	CUm	CUm	CUm
Fair value of plan assets at 31 December	1,488	962	{See note below}
Present value of defined benefit obligation at 31 December	(1,009)	(758)	
Surplus/(deficit) in the plan	479	204	
Experience adjustments arising on plan assets (see note below)	480	138	
Experience adjustments arising on plan liabilities (see note below)	(58)	(6)	

{**Note**: For first-time and recent adopters of IFRS, this information need be given only prospectively from the date of transition to IFRS, per IFRS 1.20A. It must eventually cover the current period and the four preceding periods.

The experience adjustments arising on plan liabilities and on plan assets may be expressed either as amounts or as a percentage of plan liabilities and of plan assets respectively at each reporting date.}

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D Example IAS 36 disclosure

Note 12 Goodwill

Group	CU'000
At 1 January	-
Additions (note XX)	4,849
At 31 December	**4,849**
Accumulated impairment losses	
At 1 January 2007 and 31 December 2007	**-**
Net book amount 31 December 2007	**4,849**
Net book amount 31 December 2006	-

Goodwill of CU4,849,000 arising on the business combination, detailed in note XX, has been allocated on the acquisition date to the confectionery division, as this segment is the group of cash-generating units expected to benefit from the synergies of the business combination.

Goodwill is tested at least annually for impairment and whenever there are indications that goodwill might be impaired.

The recoverable amount of a cash-generating unit is based on its value in use. Value in use is the present value of the projected cash flows of the cash generating unit. The key assumptions regarding the value in use calculations were budgeted growth in revenues, budgeted gross profit margins and the discount rate applied. Budgeted revenue growth and budgeted gross profit margins were estimated based on actual performance over the past two financial years and expected market changes. The discount rate used is a pre-tax rate and reflects the risks specific to the relevant business segment.

The Group prepares cash flow forecasts based on the most recent financial budgets approved by management, which cover a five year period. Cash flows beyond this period are extrapolated using a growth rate of 3%, which is consistent with the long-term average growth rate for the UK food retail sector in which the Group principally operates. The discount rate applied was 9.5%

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