Standard

Accounting and Reporting

FRC Financial Reporting Council

January 2022

FRS 102

The Financial Reporting Standard applicable in the UK and Republic of Ireland

The FRC's purpose is to serve the public interest by setting high standards of corporate governance, reporting and audit and by holding to account those responsible for delivering them. The FRC sets the UK Corporate Governance and Stewardship Codes and UK standards for accounting and actuarial work; monitors and takes action to promote the quality of corporate reporting; and operates independent enforcement arrangements for accountants and actuaries. As the Competent Authority for audit in the UK the FRC sets auditing and ethical standards and monitors and enforces audit quality.

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FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland* is an accounting standard. It is issued by the Financial Reporting Council, as a prescribed body, for application in the United Kingdom and the Republic of Ireland.

Contents

Appendices

Overview

(i) The FRC's overriding objective in setting accounting standards is to enable users of accounts to receive high-quality understandable financial reporting proportionate to the size and complexity of the entity and users' information needs.

(ii) This FRS is a single financial reporting standard that applies to the financial statements of entities that are not applying adopted IFRS, FRS 101 *Reduced Disclosure Framework* or FRS 105 *The Financial Reporting Standard applicable to the Micro-entities Regime*.[1]

FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland*

(iii) This FRS aims to provide entities with succinct financial reporting requirements. The requirements in this FRS are based on the International Accounting Standards Board's (IASB) International Financial Reporting Standard for Small and Medium-sized Entities (IFRS for SMEs) first issued in 2009. The IFRS for SMEs is intended to apply to the general purpose financial statements of, and other financial reporting by, entities that in many countries are referred to by a variety of terms including 'small and medium-sized', 'private' and 'non-publicly accountable'.

(iv) The FRC has modified the IFRS for SMEs substantially, both in terms of the scope of entities eligible to apply it and in terms of the accounting treatments provided. To reflect this wider scope the proposed name of the standard was revised to FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland*.

(v) FRS 102 is designed to apply to the general purpose financial statements and financial reporting of entities including those that are not constituted as companies and those that are not profit-oriented. General purpose financial statements are intended to focus on the common information needs of a wide range of users: shareholders, lenders, other creditors, employees and members of the public, for example.

Organisation of FRS 102

(vi) FRS 102 is organised by topic with each topic presented in a separate numbered section.

(vii) Terms defined in the Glossary are in **bold type** the first time they appear in each section, and sub-section within Section 34.

(viii) This edition of FRS 102 issued in January 2022 updates the edition of FRS 102 issued in March 2018 for the following:

(a) *Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Multi-employer defined benefit plans* issued in May 2019;

(b) *Amendments to FRS 101 Reduced Disclosure Framework – 2018/19 cycle* issued in July 2019;

(c) *Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Interest rate benchmark reform* issued in December 2019;

(d) *Amendments to FRS 101 Reduced Disclosure Framework – 2019/20 cycle* issued in May 2020;

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[1] This FRS does not, however, apply to the preparation of 'Companies Act financial statements' of certain entities under company law in the Republic of Ireland. Please refer to Appendix IV for further details.

(e) *Amendment to FRS 101 Reduced Disclosure Framework – Effective date of IFRS 17* issued in October 2020;

(f) *Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland and FRS 105 The Financial Reporting Standard applicable to the Micro-entities Regime – COVID-19-related rent concessions* issued in October 2020;

(g) *Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Interest rate benchmark reform (Phase 2)* issued in December 2020;

(h) *Amendments to UK and Republic of Ireland accounting standards – UK exit from the European Union* issued in December 2020;

(i) *Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland and FRS 105 The Financial Reporting Standard applicable to the Micro-entities Regime – COVID-19-related rent concessions beyond 30 June 2021* issued in June 2021;

(j) editorial amendments to paragraph A4.1 to reflect changes in legislation since the previous edition of FRS 102;

(k) amendments to the footnotes to paragraphs 1A.7, 3.1A and the definition of a small entity, Appendix D to Section 1A *Small Entities* and Appendix IV *Republic of Ireland legal references*, to reflect changes introduced by the *European Union (Qualifying Partnerships: Accounting and Auditing) Regulations 2019* applicable to qualifying partnerships for accounting periods beginning on or after 1 January 2020; and

(l) some minor typographical or presentational corrections.

FRS 102
The Financial Reporting Standard applicable in the UK and Republic of Ireland

Section 1
Scope

Scope of this Financial Reporting Standard

1.1 This FRS applies to **financial statements** that are intended to give a true and fair view of a reporting entity's **financial position** and **profit or loss** (or **income and expenditure**) for a period.

1.2 The requirements of this FRS are applicable to **public benefit entities** and other entities, not just to companies. However, those paragraph numbers prefixed with 'PBE' shall only be applied by public benefit entities, and shall not be applied directly, or by analogy, by entities that are not public benefit entities, other than, when specifically directed, entities within a **public benefit entity group**. A public benefit entity shall apply all paragraphs prefixed with 'PBE' to the extent that they are relevant and, for those public benefit entities within the scope of a **Statement of Recommended Practice (SORP)**, their use is permitted by the applicable SORP.

1.2A An entity applying this FRS must ensure it complies with any relevant legal requirements applicable to it. This FRS does not necessarily contain all legal disclosure requirements. In relation to small companies (see Section 1A *Small Entities*) most legal disclosure requirements are included, but, for example, those only relevant when the financial statements have been audited are not included.

Basis of preparation of financial statements

1.3 As stated in **FRS 100**, an entity that is required by the **Act** (or other legislation or regulation) to prepare **consolidated financial statements** in accordance with **adopted IFRS** must do so. The **individual financial statements** of such an entity, or the individual financial statements or consolidated financial statements of any other entity within the scope of FRS 100, must be prepared in accordance with the following requirements:

(a) If the financial statements are the individual financial statements of an entity that is eligible to apply **FRS 105**[2], they may be prepared in accordance with that standard.

(b) If the financial statements are those of an entity that is not eligible to apply FRS 105, or of an entity that is eligible to apply FRS 105 but chooses not to do so, they must[3] be prepared in accordance with this FRS, adopted IFRS or **FRS 101**.[4]

1.4 An entity whose **ordinary shares** or **potential ordinary shares** are **publicly traded**, or that files, or is in the process of filing, its financial statements with a securities commission or other regulatory organisation for the purpose of issuing ordinary shares

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[2] The eligibility criteria for applying FRS 105 are set out in legislation and FRS 105. In establishing whether the eligibility criteria have been met turnover and balance sheet total shall be measured in accordance with FRS 105; the measurement of turnover and balance sheet total in accordance with FRS 101 or FRS 102 need not be considered.

[3] Under company law in the Republic of Ireland, certain entities are permitted to prepare 'Companies Act financial statements' under a financial reporting framework based on accounting standards other than those issued by the FRC. Please refer to Appendix IV for further details.

[4] Individual financial statements that are prepared by a company in accordance with FRS 101 or FRS 102 are Companies Act individual accounts (in the UK, in accordance with section 395(1)(a) of the Act, and in Ireland, in accordance with sections 290(3)(a) and 290(4)(a) of the *Companies Act 2014*), whereas those prepared in accordance with adopted IFRS are IAS individual accounts (in the UK, in accordance with section 395(1)(b) of the Act, and in Ireland, in accordance with sections 290(3)(b) and 290(4)(b) of the *Companies Act 2014*).

in a public market, or an entity that chooses to disclose earnings per share, shall apply IAS 33 *Earnings per Share* (as adopted in the relevant jurisdiction).

1.5 An entity whose debt or equity instruments are publicly traded, or that files, or is in the process of filing, its financial statements with a securities commission or other regulatory organisation for the purpose of issuing any class of instruments in a public market, or an entity that chooses to provide information described as segment information, shall apply IFRS 8 *Operating Segments* (as adopted in the relevant jurisdiction). If an entity discloses disaggregated information, but the information does not comply with the requirements of IFRS 8, it shall not describe the information as segment information.

1.6 An entity shall apply **FRS 103** to:

(a) **insurance contracts** (including **reinsurance contracts**) that it issues and reinsurance contracts that it holds; and

(b) **financial instruments** with a **discretionary participation feature** that it issues.

1.7 When applying IAS 33, IFRS 8 and IFRS 6 *Exploration for and Evaluation of Mineral Resources* (see paragraphs 34.11 to 34.11C), references made to other IFRSs within those standards shall be taken to be references to the relevant section or paragraph in this FRS.

Application of Statements of Recommended Practice (SORPs)

1.7A Statements of Recommended Practice (SORPs) set out the circumstances in which they apply. When a SORP applies, an entity shall provide the disclosures required by paragraph 6 of FRS 100.

Reduced disclosures for subsidiaries (and ultimate parents)

1.8 A **qualifying entity** (for the purposes of this FRS) which is not a **financial institution** may take advantage in its individual financial statements of the disclosure exemptions set out in paragraph 1.12.

1.9 A qualifying entity (for the purposes of this FRS) which is a financial institution may take advantage in its individual financial statements of the disclosure exemptions set out in paragraph 1.12, except for the disclosure exemptions from Section 11 *Basic Financial Instruments* and Section 12 *Other Financial Instruments Issues*.

1.10 A qualifying entity (for the purposes of this FRS) which is required to prepare consolidated financial statements (for example, if the entity is required by section 399 of the Act to prepare consolidated financial statements, and is not entitled to any of the exemptions in sections 400 to 402 of the Act), or which voluntarily chooses to do so, may not take advantage of the disclosure exemptions set out in paragraph 1.12 in its consolidated financial statements.

1.11 A qualifying entity (for the purposes of this FRS) may take advantage of the disclosure exemptions in paragraph 1.12, in accordance with paragraphs 1.8 to 1.10, provided that:

(a) [Deleted]

(b) It otherwise applies the **recognition**, **measurement** and disclosure requirements of this FRS.

(c) It discloses in the **notes** to its financial statements:

(i) a brief narrative summary of the disclosure exemptions adopted; and

(ii) the name of the **parent**[5] of the **group** in whose consolidated financial statements its financial statements are consolidated, and from where those financial statements may be obtained.

1.12 A qualifying entity (for the purposes of this FRS) may take advantage of the following disclosure exemptions:

(a) [Deleted]

(b) The requirements of Section 7 *Statement of Cash Flows* and paragraph 3.17(d).

(c) The requirements of paragraphs 11.42, 11.44, 11.45, 11.47, 11.48(a)(iii), 11.48(a)(iv), 11.48(b), 11.48(c), 12.26 (in relation to those cross-referenced paragraphs from which a disclosure exemption is available), 12.27, 12.29(a), 12.29(b), 12.29A and 12.30 provided disclosures equivalent to those required by this FRS are included in the consolidated financial statements of the group in which the entity is consolidated.

(d) The requirements of paragraphs 26.18(b), 26.19 to 26.21 and 26.23, provided that for a qualifying entity that is:

(i) a **subsidiary**, the **share-based payment arrangement** concerns equity instruments of another group entity;

(ii) an ultimate parent, the share-based payment arrangement concerns its own equity instruments and its **separate financial statements** are presented alongside the consolidated financial statements of the group;

and, in both cases, provided that the equivalent disclosures required by this FRS are included in the consolidated financial statements of the group in which the entity is consolidated.

(e) The requirement of paragraph 33.7.

(f) The requirements of paragraph 24(b) of IFRS 6 to disclose the operating and investing cash flows arising from the exploration for and evaluation of mineral resources (when an entity applies IFRS 6 in accordance with paragraph 34.11).

1.13 Reference shall be made to the Application Guidance to FRS 100 in deciding whether the consolidated financial statements of the parent provide disclosures which are equivalent to the requirements of this FRS (ie the full requirements of this FRS when not applying the disclosure exemptions) from which relief is provided in paragraph 1.12.

Date from which effective and transitional arrangements

1.14 An entity shall apply this FRS for accounting periods beginning on or after 1 January 2015. Early application is permitted for accounting periods ending on or after 31 December 2012. For entities that are within the scope of a SORP, early application is permitted for accounting periods ending on or after 31 December 2012 providing it does not conflict with the requirements of a current SORP or legal requirements for the preparation of financial statements. If an entity applies this FRS before 1 January 2015 it shall disclose that fact.

[5] The parent identified in the definition of the term 'qualifying entity'.

Classification conditions for basic financial instruments

1.14A This FRS permits a financial instrument (provided it meets certain criteria) to be designated on initial recognition as a **financial asset** or **financial liability** at **fair value** through profit or loss. Entities that have applied this FRS in financial statements authorised for issue prior to 1 August 2014 are permitted in their first financial statements authorised for issue on or after 1 August 2014 to designate, as at the **date of transition** to this FRS, any financial asset or financial liability at fair value through profit or loss provided the **asset** or **liability** meets the criteria in paragraph 11.14(b) at that date. Entities that have applied this FRS in financial statements authorised for issue prior to 1 August 2014 are permitted in their first financial statements authorised for issue on or after 1 August 2014 to de-designate any financial asset or financial liability previously designated at fair value through profit or loss and classify and measure the financial instrument in accordance with Section 11.

Hedge accounting

1.14B This FRS permits entities to apply hedge accounting, provided certain qualifying conditions are met. Entities that have applied this FRS in financial statements authorised for issue prior to 1 August 2014 are permitted to apply hedge accounting to a hedging relationship existing on or before 31 July 2014 as set out in Section 12 of this FRS from a date no earlier than the conditions of paragraphs 12.18(a) to (c) are met, provided the conditions of paragraphs 12.18(d) and (e) are met no later than the date the first financial statements issued on or after 1 August 2014 are authorised for issue. This choice applies to each hedging relationship existing on or before 31 July 2014. This choice only applies in respect of the first financial statements that comply with this FRS that are authorised for issue on or after 1 August 2014.

In a fair value hedge the cumulative **hedging gain or loss** on the hedged item from the date hedge accounting commenced, shall be recognised in retained earnings (or if appropriate, another category of **equity**). In a cash flow hedge and net investment hedge, the lower of the following (in absolute amounts) shall be recognised in equity (in respect of cash flow hedges in the cash flow hedge reserve):

(a) the cumulative gain or loss on the hedging instrument from the date hedge accounting commenced to the **reporting date** of the last financial statements authorised for issue prior to 1 August 2014; and

(b) the cumulative change in fair value (ie the **present value** of the cumulative change of expected future **cash flows**) on the hedged item from the date hedge accounting commenced to the reporting date of the last financial statements authorised for issue prior to 1 August 2014.

Small entities and other minor amendments

1.15 In July 2015 amendments were made to this FRS to incorporate the new small entities regime and make other amendments necessary to maintain consistency with company law. An entity shall apply the amendments set out in *Amendments to FRS 102 – Small entities and other minor amendments* (the July 2015 amendments) other than the replacement of paragraph 26.15 with new paragraphs 26.15 to 26.15B for accounting periods beginning on or after 1 January 2016. Early application is:

(a) permitted for accounting periods beginning on or after 1 January 2015 provided that *The Companies, Partnerships and Groups (Accounts and Reports) Regulations 2015* (SI 2015/980) are applied from the same date; and

(b) required if an entity applies *The Companies, Partnerships and Groups (Accounts and Reports) Regulations 2015* (SI 2015/980) to a **reporting period** beginning before 1 January 2016.

For entities not subject to company law, early application is permitted from 1 January 2015.

If an entity applies the July 2015 amendments before 1 January 2016 it shall disclose that fact, unless it is a **small entity**, in which case it is encouraged to disclose that fact.

1.15A [Deleted]

Fair value hierarchy disclosures

1.16 In March 2016 amendments were made to paragraphs 34.22 and 34.42 of this FRS, revising the disclosure requirements for financial institutions and **retirement benefit plans**. An entity shall apply these amendments for accounting periods beginning on or after 1 January 2017. Early application is permitted. If an entity applies these amendments to an accounting period beginning before 1 January 2017 it shall disclose that fact.

Notification of shareholders

1.17 In December 2016 an amendment was made to this FRS to delete paragraph 1.11(a), and therefore remove the requirement for a qualifying entity to notify its shareholders about the proposed use of disclosure exemptions. A qualifying entity shall apply this amendment for accounting periods beginning on or after 1 January 2016.

Triennial review 2017

1.18 In December 2017 amendments were made to this FRS as a result of the triennial review 2017. An entity shall apply the amendments to this FRS as set out in the *Triennial review 2017 amendments*, other than the amendments for small entities in the Republic of Ireland, for accounting periods beginning on or after 1 January 2019. The amendments to Section 1A for small entities in the Republic of Ireland are effective for accounting periods beginning on or after 1 January 2017.

Early application is permitted provided that all the amendments to this FRS are applied at the same time, except that early application of each, or any, of the following amendments is permitted:

(a) paragraphs 11.13A(a), 11.13B, 11.13C and 11.14(a)(i);

(b) paragraphs 29.14A and 29.22A; and

(c) the amendments to Section 1A for small entities in the Republic of Ireland, provided the *Companies (Accounting) Act 2017* is applied from the same date.

If an entity applies the *Triennial review 2017 amendments*, other than the amendments for small entities in the Republic of Ireland, before 1 January 2019 it shall disclose that fact, unless it is a small entity applying Section 1A, in which case it is encouraged to disclose that fact.

If a small entity in the Republic of Ireland applies the amendments to Section 1A before 1 January 2017, in addition to the disclosure required by paragraph 1AD.3, it is encouraged to disclose that fact.

1.19 When an entity first applies the *Triennial review 2017 amendments*, as an exception to **retrospective application**, it:

(a) may elect to measure an **investment property** rented to another group entity, that is measured on an ongoing basis at cost less accumulated **depreciation** and accumulated **impairment losses**, at its fair value and use that fair value as its **deemed cost** at the date of transition for the *Triennial review 2017 amendments*; and

(b) shall only apply any change to an **accounting policy** arising from the *Triennial review 2017 amendments* to paragraph 18.8 **prospectively** (ie it shall not restate comparative information), and therefore shall not subsume **intangible assets** that previously have been separately recognised within **goodwill**.

Multi-employer defined benefit plans

1.20 In May 2019 an amendment was made to this FRS to insert paragraphs 28.11B to 28.11D, and make other minor consequential amendments. This amendment is effective for accounting periods beginning on or after 1 January 2020. Early application is permitted. If an entity applies this amendment to an accounting period beginning before 1 January 2020 it shall disclose that fact, unless it is a small entity, in which case it is encouraged to disclose that fact.

2018/19 cycle of amendments to FRS 101

1.21 In July 2019 an amendment was made to Appendix III *Note on legal requirements* of this FRS as a result of the 2018/19 cycle of amendments to FRS 101. This amendment is effective for accounting periods beginning on or after 1 January 2023.

If an entity applies the July 2019 amendments to FRS 101 early, this amendment to **FRS 102** shall be applied at the same time.

Interest rate benchmark reform (Phase 1)

1.22 In December 2019 amendments were made to this FRS to insert paragraphs 12.25B to 12.25H and 12.30, and make other minor consequential amendments. These amendments are effective for accounting periods beginning on or after 1 January 2020. Early application is permitted. If an entity applies these amendments to an accounting period beginning before 1 January 2020 it shall disclose that fact, unless it is a small entity, in which case it is encouraged to disclose that fact.

Entities shall apply paragraphs 12.25B to 12.25H to those hedging relationships that existed at the beginning of the reporting period in which an entity first applies these amendments, or were designated thereafter, and to the amount accumulated in the cash flow hedge reserve that existed at the beginning of the reporting period in which an entity first applies these amendments.

In the reporting period in which an entity first applies these amendments, in relation to these amendments only, an entity is not required to disclose the information required by paragraphs 10.13(b) to (d).

2019/20 cycle of amendments to FRS 101

1.23 In May 2020 an amendment was made to this FRS as a result of the 2019/20 cycle of amendments to FRS 101 to insert paragraph 1.12(f). The amendment provides a disclosure exemption for qualifying entities (for the purposes of this FRS) from part of paragraph 24(b) of IFRS 6. A qualifying entity may take advantage of this disclosure exemption from when IFRS 6 is applied (in accordance with paragraph 34.11).

COVID-19-related rent concessions

1.24 In October 2020 amendments were made to this FRS to insert or amend paragraphs 20.15C, 20.15D, 20.16 and 20.25B. These amendments are effective for accounting periods beginning on or after 1 January 2020. Early application is permitted. If an entity applies these amendments to an accounting period beginning before 1 January 2020 it shall disclose that fact, unless it is a small entity, in which case it is encouraged to disclose that fact.

Interest rate benchmark reform (Phase 2)

1.25 In December 2020 amendments were made to this FRS to insert or amend paragraphs 11.2, 11.2A, 11.2B, 11.20A to 11.20E, 11.49, 11.50, 12.2, 12.2A, 12.2B, 12.25B, 12.25H, 12.25I to 12.25V and 20.11. These amendments are effective for accounting periods beginning on or after 1 January 2021. Early application is permitted, if all amendments are applied at the same time. If an entity applies these amendments to an accounting period beginning before 1 January 2021 it shall disclose that fact, unless it is a small entity, in which case it is encouraged to disclose that fact.

1.26 On first-time application, an entity shall apply the amendments set out in paragraph 1.25 retrospectively, in accordance with paragraph 10.12, except as specified in paragraphs 1.27 to 1.29.

1.27 An entity shall commence new hedging relationships (including those described in paragraph 12.25V) only prospectively, ie an entity is prohibited from commencing a new hedge accounting relationship in prior periods. However, an entity shall reinstate a discontinued hedging relationship if, and only if, these conditions are met:

(a) the entity had discontinued that hedging relationship solely due to changes required by interest rate benchmark reform and the entity would not have been required to discontinue that hedging relationship if paragraphs 12.25J to 12.25U had been applied at that time; and

(b) at the beginning of the reporting period in which an entity first applies paragraphs 12.25J to 12.25U (the date of first-time application), that discontinued hedging relationship meets the qualifying criteria for hedge accounting in this FRS (after taking into account paragraphs 12.25J to 12.25U).

1.28 If, in applying paragraph 1.27, an entity reinstates a discontinued hedging relationship, the entity shall read references in paragraphs 12.25T and 12.25U to the date the alternative benchmark rate is identified as a non-contractually specified risk component for the first time, as referring to the date of first-time application of paragraphs 12.25T and 12.25U (ie the 24-month period for that alternative benchmark rate designated as a non-contractually specified risk component begins from the date of first-time application of these paragraphs).

1.29 An entity is not required to restate prior periods when applying the amendments in paragraph 1.25 retrospectively. If an entity does not restate prior periods, the entity shall apply those amendments in remeasuring the **carrying amounts** of assets and liabilities as at the beginning of the reporting period in which the amendments are first applied and shall make a corresponding adjustment to the opening balance of each affected component of equity.

1.30 On the first-time application of the requirements in paragraph 12.25J, and only then, instead of applying paragraph 12.25M, an entity shall amend the hedge documentation as required in paragraph 12.25J no later than the date the respective financial statements are authorised for issue.

1.31 In the reporting period in which an entity first applies these amendments, and in relation to these amendments only, an entity is not required to disclose the information required by paragraphs 10.13(b) to (d).

UK exit from the European Union

1.32 In December 2020 amendments were made to this FRS to reflect changes in UK company law following the UK exit from the European Union. An entity shall apply these amendments for accounting periods beginning on or after 1 January 2021. Early application, other than the amendments to paragraphs 1AC.26, 9.3, A3.4, A3.12, A3.12A and A3.33, is permitted by entities in the UK for:

(a) accounting periods beginning before, and ending on or after, 31 December 2020;

(b) accounting periods ending before 31 December 2020, when the period for filing the accounts (as set out in section 442 of the Act) ends after 31 December 2020.

For the purposes of early application, references to **UK-adopted international accounting standards** shall be interpreted as **IFRS** as adopted in the EU as at 31 December 2020, in addition to **IAS** that are adopted for use within the UK after this date.

If an entity applies these amendments to an accounting period beginning before 1 January 2021 it shall disclose that fact, unless it is a small entity, in which case it is encouraged to disclose that fact. The amendments to paragraphs 1AC.26, 9.3, A3.12, A3.12A and A3.33 are effective for accounting periods beginning on or after 1 January 2021.

COVID-19-related rent concessions beyond 30 June 2021

1.33 In June 2021 an amendment was made to paragraph 20.15D of this FRS. This amendment is effective for accounting periods beginning on or after 1 January 2021. Early application is permitted. If an entity applies this amendment to an accounting period beginning before 1 January 2021 it shall disclose that fact, unless it is a small entity, in which case it is encouraged to disclose that fact.

Section 1A
Small Entities

Scope of this section

1A.1 This section sets out the information that shall be presented and disclosed in the **financial statements** of a **small entity** that chooses to apply the small entities regime. Unless excluded below, all of the requirements of this FRS apply to a small entity, including the **recognition** and **measurement** requirements.

1A.2 Unless a small entity chooses to apply **adopted IFRS**, or if eligible, **FRS 101**, a small entity that chooses not to apply the small entities regime shall apply this FRS excluding Section 1A.

1A.3 References to a small entity in paragraphs 1A.4 to 1A.22 and the Appendices to Section 1A are to a small entity that chooses to apply the small entities regime.

1A.4 This section applies to all small entities applying the small entities regime, whether or not they report under the **Act**[6]. Small entities that do not report under the Act shall comply with the requirements of this section, and with the Act and **Small Companies Regulations**[7] (or, where applicable, the **Small LLP Regulations**) where referred to in this section, except to the extent that these requirements are not permitted by any statutory framework under which such entities report.

True and fair view

1A.5 The financial statements of a small entity shall give a true and fair view of the **assets**, **liabilities**, **financial position** and **profit or loss** of the small entity for the **reporting period** (section 393 of the Act)[8].

1A.6 A small entity may need to provide disclosures in addition to those set out in this section in order to comply with the requirement of paragraph 1A.5 (see also paragraphs 1A.16 and 1A.17).

Statement of compliance

1A.6A The financial statements of a small entity choosing to apply Section 1A of this FRS shall contain on the **statement of financial position**, in a prominent position above the signature, a statement that the financial statements are prepared in accordance with the provisions applicable to companies subject to the small companies regime.[9]

6 For Irish small entities reference to the Act shall be replaced with the *Companies Act 2014*.

7 For Irish small entities reference to the Small Companies Regulations shall be replaced with Schedule 3A to the *Companies Act 2014*.

8 Irish small entities shall refer to section 289 of the *Companies Act 2014*.

9 This is required by section 414(3) of the Act for small entities in the UK and by section 324(4A) of the *Companies Act 2014* for small entities in the Republic of Ireland. For small LLPs in the UK, section 414(3) of *The Limited Liability partnerships (Accounts and Audit) (Application of Companies Act 2006) Regulations 2008* (SI 2008/1911) requires a statement that the financial statements are prepared in accordance with the provisions applicable to LLPs subject to the small LLPs regime. Other entities may refer to the small entities regime.

Complete set of financial statements of a small entity

1A.7 A small entity is not required to comply with the requirements of paragraphs 3.3[10], PBE3.3A, 3.9[11], 3.12, 3.13, 3.17, 3.18, 3.19 and 3.24(b) which relate to presentation and disclosure requirements that are not required of small companies in company law, Section 4 *Statement of Financial Position*, Section 5 *Statement of Comprehensive Income and Income Statement*, Section 6 *Statement of Changes in Equity and Statement of Income and Retained Earnings* and Section 7 *Statement of Cash Flows*.

1A.8 Instead a complete set of financial statements of a small entity shall include all of the following:

(a) a statement of financial position as at the **reporting date** in accordance with paragraph 1A.12;

(b) an **income statement** for the reporting period in accordance with paragraph 1A.14; and

(c) **notes** in accordance with paragraphs 1A.16 to 1A.20.

1A.9 In addition to the statements required by company law and set out in paragraph 1A.8:

(a) when a small entity recognises **gains** or losses in **other comprehensive income** it is encouraged to present a statement of **total comprehensive income** (see Section 5); and

(b) when a small entity has transactions with equity holders it is encouraged to present a statement of changes in equity, or a **statement of income and retained earnings** (see Section 6), in order to meet the requirements of paragraph 1A.5.

1A.10 In accordance with paragraph 3.14 a small entity shall present comparative information in respect of the preceding period for all amounts presented in the current period's financial statements, except when this FRS permits or requires otherwise.

1A.11 In accordance with paragraph 3.22 a small entity may use titles for the financial statements other than those used in this FRS as long as they are not misleading.

Information to be presented in the statement of financial position

1A.12 A small entity shall present a statement of financial position in accordance with the requirements for a balance sheet set out in either Part 1 *General Rules and Formats* of Schedule 1 to the Small Companies Regulations[12] or Part 1 *General Rules and Formats* of Schedule 1 to the Small LLP Regulations.

1A.13 Guidance on applying these requirements is set out in Appendix A to this section, which shall be applied by a small entity.

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[10] Irish small entities, other than qualifying partnerships, are required to comply with the requirements of paragraph 3.3.

[11] If a small entity departs from the principle that it is presumed to be carrying on business as a going concern, it must provide the disclosure required by paragraph 1AC.10 or paragraph 1AD.11, as relevant.

[12] Irish small entities shall refer to Part II *General Rules and Formats* of Schedule 3A to the *Companies Act 2014*.

Information to be presented in the income statement

1A.14 A small entity shall present its profit or loss for a period in an income statement in accordance with the requirements for a profit and loss account set out in either Part 1 *General Rules and Formats* of Schedule 1 to the Small Companies Regulations[13] or Part 1 *General Rules and Formats* of Schedule 1 to the Small LLP Regulations.

1A.15 Guidance on applying these requirements is set out in Appendix B to this section, which shall be applied by a small entity.

Information to be presented in the notes to the financial statements

1A.16 A small entity shall present sufficient information in the notes to the financial statements to meet the requirement for the financial statements to give a true and fair view of the assets, liabilities, financial position and profit or loss of the small entity for the reporting period.

1A.17 A small entity is not required to comply with the disclosure requirements of Section 3 *Financial Statement Presentation* (to the extent set out in paragraph 1A.7) and Sections 8 to 35 of this FRS. However, because those disclosures are usually considered relevant to giving a true and fair view, a small entity is encouraged to consider and provide any of those disclosures that are relevant to **material** transactions, other events or conditions of the small entity in order to meet the requirement set out in paragraphs 1A.5 and 1A.16.

1A.17A In accordance with paragraph 3.16B a small entity need not provide a specific disclosure (including those set out in paragraph 1A.18 and Appendix C or Appendix D to this section, as relevant) if the information resulting from that disclosure is not material, except when required by the Act regardless of materiality.

1A.18 As a minimum, where relevant to its transactions, other events and conditions, a small entity reporting in the UK shall provide the disclosures set out in Appendix C to this section and a small entity reporting in the Republic of Ireland shall provide the disclosure set out in Appendix D to this section.

1A.19 The paragraphs of this FRS that are cross-referenced in Appendices C and D are also highlighted in those sections by including an * in the left-hand margin.

1A.20 In addition, a small entity is encouraged to make the disclosures set out in Appendix E to this section, which may nevertheless be necessary in order to give a true and fair view and meet the requirements of paragraph 1A.5.

Voluntary preparation of consolidated financial statements

1A.21 A small entity that is a **parent** entity is not required to prepare **consolidated financial statements**.

1A.22 If a small entity that is a parent voluntarily chooses to prepare consolidated financial statements it:

(a) shall apply the consolidation procedures set out in Section 9 *Consolidated and Separate Financial Statements*;

(b) is encouraged to provide the disclosures set out in paragraph 9.23;[14]

[13] Irish small entities shall refer to Part II *General Rules and Formats* of Schedule 3A to the *Companies Act 2014*.
[14] Irish small entities are required to provide certain of these disclosures.

(c) shall comply so far as practicable with the requirements of Section 1A as if it were a single entity (Schedule 6 of the Small Companies Regulations, paragraph 1(1))[15], subject to any restrictions or exemptions set out in legislation; and

(d) shall provide any disclosures required by Schedule 6 of the Small Companies Regulations[16].

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[15] Irish small entities shall refer to Schedule 4A to the *Companies Act 2014*, paragraph 2(1).

[16] Irish small entities shall refer to Schedule 4A to, and sections 294, 296, 307 to 309, 317, 320, 321 and 323 of, the *Companies Act 2014*.

Appendix A to Section 1A
Guidance on adapting the balance sheet formats

This appendix is an integral part of Section 1A

1AA.1 As set out in paragraph 1A.12 a **small entity** shall present a **statement of financial position** in accordance with the requirements for a balance sheet set out in either Part 1 *General Rules and Formats* of Schedule 1 to the **Small Companies Regulations**[17] or Part 1 *General Rules and Formats* of Schedule 1 to the **Small LLP Regulations**. This results in three alternatives:

(a) apply the required balance sheet formats as set out in legislation (subject to any permitted flexibility);

(b) draw up an abridged balance sheet (see paragraph 1AA.2);[18] or

(c) adapt one of the balance sheet formats (see paragraphs 1AA.3 to 1AA.6).

Abridged balance sheet

1AA.2 A small entity choosing to apply paragraph 1A(1) of Schedule 1 to the Small Companies Regulations and draw up an abridged balance sheet must still meet the requirement for the **financial statements** to give a true and fair view. A small entity shall therefore also consider the requirements of paragraph 1A.16, and provide any additional disclosure that is necessary in the **notes** to the financial statements, for example in relation to disaggregating the information in the balance sheet.

Adapted balance sheet

1AA.3 A small entity choosing to apply paragraph 1B(1) of Schedule 1 to the Small Companies Regulations[19] and adapt one of the balance sheet formats shall, as a minimum, include in its statement of financial position line items that present the following, distinguishing between those items that are **current** and those that are **non-current**:

(a) **property, plant and equipment**;

(b) **investment property** carried at **fair value** through **profit or loss**;

(c) **intangible assets**;

(d) **financial assets** (excluding amounts shown under (e), (f), (j) and (k));

(e) investments in **associates**;

(f) investments in **jointly controlled entities**;

(g) **biological assets** carried at cost less accumulated **depreciation** and impairment;

(h) biological assets carried at fair value through profit or loss;

(i) **inventories**;

(j) trade and other receivables;

(k) **cash** and **cash equivalents**;

[17] Irish small entities shall refer to Part II *General Rules and Formats* of Schedule 3A to the *Companies Act 2014*.
[18] Irish law does not provide for the preparation of abridged statutory financial statements. Consequently, this option to prepare an abridged balance sheet is not available to Irish small entities. This is not the same as abridgement for filing purposes.
[19] Irish small entities shall refer to paragraph 2(2) of Schedule 3A of the *Companies Act 2014*.

(l) trade and other payables;

(m) **provisions**;

(n) **financial liabilities** (excluding amounts shown under (l) and (m));

(o) **liabilities** and **assets** for **current tax**;

(p) **deferred tax liabilities** and **deferred tax assets** (classified as non-current);

(q) **non-controlling interest**, presented within **equity** separately from the equity attributable to the **owners** of the **parent**; and

(r) equity attributable to the owners of the parent.

1AA.4 A small entity choosing to apply paragraph 1B(1) of Schedule 1 to the Small Companies Regulations[20] and adapt one of the balance sheet formats shall also disclose, either in the statement of financial position or in the notes, the following sub-classifications of the line items presented:

(a) property, plant and equipment in classifications appropriate to the small entity;

(b) **goodwill** and other intangible assets;

(c) investments, showing separately shares and loans;

(d) trade and other receivables, showing separately amounts due from **related parties** and amounts due from other parties;

(e) trade and other payables, showing separately amounts payable to trade suppliers and amounts payable to related parties; and

(f) classes of equity, such as called up share capital, share premium, retained earnings, revaluation reserve, fair value reserve and other reserves.

1AA.5 The descriptions used in paragraphs 1AA.3 and 1AA.4, and the ordering of items or aggregation of similar items, may be amended according to the nature of the small entity and its transactions, to provide information that is relevant to an understanding of the small entity's **financial position**, providing the information given is at least equivalent to that required by the balance sheet format had it not been adapted.

1AA.6 In order to comply with the requirement to distinguish between those items that are current and those that are non-current a small entity shall present **current assets** and **non-current assets**, and **current liabilities** and **non-current liabilities**, as separate classifications in its statement of financial position.

[20] Irish small entities shall refer to paragraph 2(2) of Schedule 3A of the *Companies Act 2014*.

Appendix B to Section 1A
Guidance on adapting the profit and loss account formats

This appendix is an integral part of Section 1A

1AB.1 As set out in paragraph 1A.14 a **small entity** shall present its **profit or loss** for a period in an **income statement** in accordance with the requirements for a profit and loss account set out in either Part 1 *General Rules and Formats* of Schedule 1 to the **Small Companies Regulations**[21] or Part 1 *General Rules and Formats* of Schedule 1 to the **Small LLP Regulations**. This results in three alternatives:

(a) apply the required profit and loss account formats as set out in legislation (subject to any permitted flexibility);

(b) draw up an abridged profit and loss account (see paragraph 1AB.2);[22] or

(c) adapt one of the profit and loss account formats (see paragraphs 1AB.3 and 1AB.4).

Abridged profit and loss account

1AB.2 A small entity choosing to apply paragraph 1A(2) of Schedule 1 to the Small Companies Regulations and draw up an abridged profit and loss account must still meet the requirement for the **financial statements** to give a true and fair view. A small entity shall therefore also consider the requirements of paragraph 1A.16 and provide any additional disclosure that is necessary in the **notes** to the financial statements, for example in relation to disaggregating gross profit or loss and disclosing **turnover**.

Adapted profit and loss account

1AB.3 A small entity choosing to apply paragraph 1B(2) of Schedule 1 to the Small Companies Regulations[23] and adapt one of the profit and loss account formats shall, as a minimum, include in its income statement line items that present the following amounts for the period:

(a) **revenue**;

(b) finance costs;

(c) share of the profit or loss of investments in **associates** (see Section 14 *Investments in Associates*) and **jointly controlled entities** (see Section 15 *Investments in Joint Ventures*) accounted for using the equity method;

(d) profit or loss before taxation;

(e) **tax expense** excluding tax allocated to **other comprehensive income** or equity; and

(f) profit or loss.

1AB.4 A small entity may include additional line items in the income statement and it amends the descriptions used in paragraph 1AB.3, and the ordering of items, when this is necessary to explain the elements of financial **performance**, providing the information given is at least equivalent to that required by the profit and loss account format had it not been adapted.

[21] Irish small entities shall refer to Part II *General Rules and Formats* of Schedule 3A to the *Companies Act 2014*.

[22] Irish law does not provide for the preparation of abridged statutory financial statements. Consequently, this option to prepare an abridged profit and loss account is not available to Irish small entities. This is not the same as abridgement for filing purposes.

[23] Irish small entities shall refer to paragraph 2(3) of Schedule 3A to the *Companies Act 2014*.

Appendix C to Section 1A
Disclosure requirements for small entities in the UK

This appendix is an integral part of Section 1A.

This appendix sets out the disclosure requirements for small entities based on the requirements of company law in the UK. These are shown in italic font in the paragraphs below. Other than substituting company law terminology with the equivalent terminology used in FRS 102 (see Appendix II) the drafting is as close as possible to that set out in company law. References to Schedule 1 are to Schedule 1 of the Small Companies Regulations.

*When there is a similar disclosure requirement in FRS 102 this has been indicated and those paragraphs of FRS 102 that have been cross-referenced are also highlighted by including an * in the left-hand margin (the * against paragraph 6.3(c) refers to a legal requirement in the Republic of Ireland only). In many cases compliance with the similar requirement of FRS 102 will result in compliance with the requirements below, however a small entity must ensure it complies with all the disclosure requirements of this appendix.*

1AC.1 As a minimum, when relevant to its transactions, other events and conditions, a **small entity** in the UK shall provide the disclosures set out in this appendix.

1AC.2 *The notes must be presented in the order in which, where relevant, the items to which they relate are presented in the statement of financial position and in the income statement. (Schedule 1, paragraph 42(2))*

Paragraphs 8.3 and 8.4 address similar requirements.

Accounting policies

1AC.3 *The accounting policies adopted by the small entity in determining the amounts to be included in respect of items shown in the statement of financial position and in determining the profit or loss of the small entity must be stated (including such policies with respect to the depreciation and impairment of assets). (Schedule 1, paragraph 44)*

Paragraph 8.5 addresses similar requirements for disclosing significant **accounting policies**. Including information about the judgements made in applying the small entity's accounting policies, as set out in paragraph 8.6, may be useful to users of the small entity's **financial statements**.

1AC.4 *If any amount is included in a small entity's statement of financial position in respect of development costs, the note on accounting policies must include the following information:*

(a) the period over which the amount of those costs originally capitalised is being or is to be written off; and

(b) the reasons for capitalising the development costs in question. (Schedule 1, paragraph 21(2))

Paragraph 18.27(a) addresses similar requirements to paragraph 1AC.4(a).

1AC.5 *Where development costs are shown or included as an asset in the small entity's financial statements and the amount is not treated as a realised loss because there are special circumstances justifying this, a note to the financial statements must state the reasons for showing development costs as an asset and that it is not a realised loss. (Section 844 of the Act)*

1AC.6 *Where in exceptional cases the useful life of intangible assets cannot be reliably estimated, there must be disclosed in a note to the financial statements the period over which those intangible assets are being written off and the reasons for choosing that period. (Schedule 1, paragraph 22(4))*

Intangible assets include **goodwill**. Paragraphs 18.27(a) and 19.25(g) address similar requirements.

Changes in presentation and accounting policies and corrections of prior period errors

1AC.7 *Where there is a change in the presentation of a small entity's statement of financial position or income statement, particulars of any such change must be given in a note to the financial statements in which the new presentation is first used, and the reasons for the change must be explained. (Schedule 1, paragraph 2(2))*

Paragraphs 3.12 and 3.13 address similar requirements.

1AC.8 *Where the corresponding amount for the immediately preceding reporting period is not comparable with the amount to be shown for the item in question in respect of the reporting period, and the corresponding amount is adjusted, the particulars of the non-comparability and of any adjustment must be disclosed in a note to the financial statements. (Schedule 1, paragraph 7(2))*

This is likely to be relevant where there has either been a change in accounting policy or the correction of a **material** prior period **error**. Paragraphs 10.13, 10.14 and 10.23 address similar requirements.

1AC.9 *Where any amount relating to a preceding reporting period is included in any item in the income statement, the effect must be stated. (Schedule 1, paragraph 61(1))*

True and fair override

1AC.10 *If it appears to the small entity that there are special reasons for departing from any of the principles set out in company law in preparing the small entity's financial statements in respect of any reporting period, it may do so, in which case particulars of the departure, the reasons for it, and its effects must be given in the notes to the financial statements. (Schedule 1, paragraph 10(2))*

This is only expected to occur in special circumstances. Paragraphs 3.4 and 3.5 address similar requirements.

Notes supporting the statement of financial position

1AC.11 *Where an asset or liability relates to more than one item in the statement of financial position, the relationship of such asset or liability to the relevant items must be disclosed either under those items or in the notes to the financial statements. (Schedule 1, paragraph 9A)*

Fixed assets

1AC.12 *In respect of each item which is shown under the general item 'fixed assets' in the small entity's statement of financial position the following information must be given:*

(a) the aggregate amounts (on the basis of cost or revaluation) in respect of that item as at the date of the beginning of the reporting period and as at the reporting date respectively;

(b) *the effect on any amount shown in the statement of financial position in respect of that item of:*

(i) *any revision of the amount in respect of any assets included under that item made during the reporting period as a result of revaluation;*

(ii) *acquisitions during the reporting period of any assets;*

(iii) *disposals during the reporting period of any assets; and*

(iv) *any transfers of assets of the small entity to and from that item during the reporting period. (Schedule 1, paragraphs 48(1) and 48(2))*

1AC.13 *In respect of each item within paragraph 1AC.12 there must also be stated:*

(a) *the cumulative amount of provisions for depreciation and impairment of assets included under that item as at the date of the beginning of the reporting period and as at the reporting date respectively;*

(b) *the amount of any such provisions made in respect of the reporting period;*

(c) *the amount of any adjustments made in respect of any such provisions during the reporting period in consequence of the disposal of any assets; and*

(d) *the amount of any other adjustments made in respect of any such provisions during the reporting period. (Schedule 1, paragraph 48(3))*

These two paragraphs apply to all **fixed assets**, including **investment property**, **property, plant and equipment**, intangible assets (including goodwill), fixed asset investments, **biological assets** and **heritage assets** recognised in the **statement of financial position**.

Each item refers to a class of fixed assets shown separately either in the statement of financial position, or in the **notes to the financial statements**.

These reconciliations need not be presented for prior periods.

Paragraph 16.10(e) addresses similar requirements for investment property. Paragraphs 17.31(d) and (e) address similar requirements for property, plant and equipment. Paragraphs 18.27(c) and (e) address similar requirements for intangible assets other than goodwill. Paragraph 19.26 addresses similar requirements for goodwill. Paragraphs 34.7(c) and 34.10(e) address similar requirements for biological assets. Paragraphs 34.55(e) and (f) address similar requirements for heritage assets recognised in the statement of financial position.

Fixed assets measured at revalued amounts

1AC.14 *Where fixed assets are measured at revalued amounts the items affected and the basis of valuation adopted in determining the amounts of the assets in question in the case of each such item must be disclosed in the note on accounting policies. (Schedule 1, paragraph 34(2))*

These requirements apply when:

- investments in **subsidiaries**, **associates** and **joint ventures** are measured at **fair value** with changes in fair value recognised in **other comprehensive income**. Paragraph 9.27(b) addresses a similar disclosure requirement;
- property, plant and equipment are revalued using the revaluation model set out in paragraphs 17.15B to 17.15F. Paragraph 17.31(a) addresses a similar disclosure requirement; and

- intangible assets other than goodwill are revalued using the revaluation model set out in paragraphs 18.18B to 18.18H. Paragraph 18.29A(c) addresses a similar disclosure requirement;

These requirements do not apply to investment property and biological assets measured at fair value through **profit or loss**.

1AC.15 *Where any fixed assets of the small entity (other than listed investments) are included under any item shown in the small entity's statement of financial position at a revalued amount, the following information must be given:*

(a) the years (so far as they are known to the directors) in which the assets were severally valued and the several values;

(b) in the case of assets that have been valued during the reporting period, the names of the persons who valued them or particulars of their qualifications for doing so and (whichever is stated) the bases of valuation used by them. (Schedule 1, paragraph 49)

Paragraphs 17.32A(a) and (c), 18.29A(a) and (c) and 34.55(e)(ii) address similar requirements. These paragraphs do not require the names or qualifications of the persons who valued the fixed assets to be disclosed.

These requirements apply in the same circumstances as those set out in paragraph 1AC.14.

1AC.16 *In the case of each item in the statement of financial position measured at a revalued amount, the comparable amounts determined according to the historical cost accounting rules must be shown in a note to the financial statements. (Schedule 1, paragraph 34(3))*

The comparable amounts refers to the aggregate amount of cost and the aggregate of accumulated depreciation and accumulated impairment losses that would have been required according to the historical cost accounting rules (Schedule 1, paragraph 34(4)).

Paragraphs 17.32A(d) and 18.29A(d) address similar requirements.

These requirements apply in the same circumstances as those set out in paragraph 1AC.14.

1AC.17 *Where fixed assets are measured at revalued amounts the following information must be given in tabular form:*

(a) movements in the revaluation reserve in the reporting period, with an explanation of the tax treatment of items therein; and

(b) the carrying amount in the statement of financial position that would have been recognised had the fixed assets not been revalued. (Schedule 1, paragraph 54(2))

Paragraphs 6.3A, 17.32A(d), 18.29A(d) and 29.27(a) address similar requirements.

These requirements apply in the same circumstances as those set out in paragraph 1AC.14.

1AC.18 *The treatment for taxation purposes of amounts credited or debited to the revaluation reserve must be disclosed in a note to the financial statements. (Schedule 1, paragraph 35(6))*

Paragraph 29.27(a) addresses similar requirements.

These requirements apply in the same circumstances as those set out in paragraph 1AC.14.

Capitalisation of borrowing costs

1AC.19 *Where a small entity adopts a policy of capitalising borrowing costs, the inclusion of interest in determining the cost of the asset and the amount of the interest so included is disclosed in a note to the financial statements. (Schedule 1, paragraph 27(3))*

Paragraph 25.3A(a) addresses a similar requirement to the second part of this.

Impairment of assets

1AC.20 *Provisions for impairment of fixed assets (including fixed asset investments) must be disclosed separately in a note to the financial statements if not shown separately in the income statement. (Schedule 1, paragraph 19(3))*

Paragraph 27.32(a) addresses similar requirements.

1AC.21 *Any provisions for impairment of fixed assets that are reversed because the reasons for which they were made have ceased to apply must be disclosed (either separately or in aggregate) in a note to the financial statements if not shown separately in the income statement. (Schedule 1, paragraph 20(2))*

Paragraph 27.32(b) addresses similar requirements.

Fair value measurement

1AC.22 *Where financial instruments or other assets have been measured in accordance with the fair value accounting rules there must be stated:*

(a) the significant assumptions underlying the valuation models and techniques used to determine the fair values;

(b) for each category of financial instrument or other asset, the fair value of the assets in that category and the change in value:

  (i) included directly in the income statement; or

  (ii) credited to or (as the case may be) debited from the fair value reserve, in respect of those assets. (Schedule 1, paragraphs 51(2)(a) and (b))

This does not apply where **financial instruments** or other assets are measured at fair value only on initial recognition.

This applies where financial instruments, certain **inventories**, investment property and biological assets are subsequently measured at fair value through profit or loss, which is permitted or required by paragraphs 9.26(c), 11.14(b), 11.14(d)(iii), 11.14(d)(iv), 12.8, 13.4A, 14.4(d), 15.9(d), 16.7 and 34.4.

Paragraphs 11.41, 11.43, 11.48(a)(i), 11.48(a)(ii), 12.28, 12.29(c), and 12.29(e) address similar disclosure requirements for financial instruments. Paragraphs 16.10(a) and 16.10(e)(ii) address similar disclosure requirements for investment property. Paragraphs 34.7(b) and 34.7(c)(i) address similar disclosure requirements for biological assets.

1AC.23 *Where financial instruments or other assets have been measured in accordance with the fair value accounting rules there must be stated for each class of derivatives, the extent and nature of the instruments, including significant terms and conditions that may affect the amount, timing and certainty of future cash flows. (Schedule 1, paragraph 51(2)(c))*

1AC.24 *Where any amount is transferred to or from the fair value reserve during the reporting period, there must be stated in tabular form:*

(a) the amount of the reserve as at the beginning of the reporting period and as at the reporting date respectively; and

(b) the amount transferred to or from the reserve during that year. (Schedule 1, paragraph 51(3))

Paragraphs 6.3A, 12.29(c) and 12.29(d) address similar requirements.

1AC.25 [Deleted]

Financial instruments measured at fair value

1AC.26 *Financial instruments which under UK-adopted international accounting standards may be included in accounts at fair value, may be so included, provided that the disclosures required by such accounting standards are made. (Schedule 1, paragraph 36(4))*

This only applies in certain circumstances; for example, it does not apply to **derivatives**. It applies where investments in subsidiaries, associates and joint ventures are measured at fair value through profit or loss. When it applies, the disclosures required by Section 11 *Basic Financial Instruments* that relate to **financial assets** and **financial liabilities** measured at fair value, including paragraph 11.48A, shall be given.

Indebtedness, guarantees and financial commitments

1AC.27 *For the aggregate of all items shown under 'creditors' in the small entity's statement of financial position there must be stated the aggregate of the following amounts:*

(a) the amount of any debts included under 'creditors' which are payable or repayable otherwise than by instalments and fall due for payment or repayment after the end of the period of five years beginning with the day next following the reporting date; and

(b) in the case of any debts so included which are payable or repayable by instalments, the amount of any instalments which fall due for payment after the end of that period. (Schedule 1, paragraph 55(1))

1AC.28 *In respect of each item shown under 'creditors' in the small entity's statement of financial position there must be stated the aggregate amount of any debts included under that item in respect of which any security has been given by the small entity with an indication of the nature and form of any such security. (Schedule 1, paragraph 55(2))*

Paragraphs 11.46, 13.22(e), 16.10(c), 17.32(a) and 18.28(c) address similar requirements.

1AC.29 *The total amount of any financial commitments, guarantees and contingencies that are not included in the balance sheet must be stated. (Schedule 1, paragraph 57(1))*

The total amount of any commitments concerning pensions must be separately disclosed. (Schedule 1, paragraph 57(3))

The total amount of any commitments which are undertaken on behalf of or for the benefit of:

(a) any parent, fellow subsidiary or any subsidiary of the small entity; or

(b) any undertaking in which the small entity has a participating interest,

must be separately stated and those within (a) must also be stated separately from those within (b). (Schedule 1, paragraph 57(4))

Such commitments can arise in a variety of situations, including in relation to **group** entities, investments, property, plant and equipment, leases and pension obligations. Paragraphs 15.19(d), 16.10(d), 17.32(b), 18.28(d), 20.16, 21.15, 28.40A(a), 28.40A(b), 28.41A(d), 33.9(b)(ii) and 34.62 address similar requirements.

1AC.30 *An indication of the nature and form of any valuable security given by the small entity in respect of commitments, guarantees and contingencies within paragraph 1AC.29 must be given. (Schedule 1, paragraph 57(2))*

Paragraphs 11.46, 13.22(e), 16.10(c), 17.32(a) and 18.28(c) address similar requirements.

1AC.31 *If in any reporting period a small entity is or has been party to arrangements that are not reflected in its statement of financial position and at the reporting date the risks or benefits arising from those arrangements are material the nature and business purpose of the arrangements must be given in the notes to the financial statements to the extent necessary for enabling the financial position of the small entity to be assessed. (Section 410A of the Act)*

Examples of off-balance sheet arrangements include risk and benefit-sharing arrangements or obligations arising from a contract such as debt factoring, combined sale and repurchase arrangements, consignment stock arrangements, take or pay arrangements, securitisation arranged through separate entities, pledged assets, operating lease arrangements, outsourcing and the like. In many cases the disclosures about financial commitments and contingencies required by paragraphs 1AC.29 and 1AC.30 will also address such arrangements.

Notes supporting the income statement

1AC.32 *The amount and nature of any individual items of income or expenses of exceptional size or incidence must be stated. (Schedule 1, paragraph 61(2))*

Paragraph 5.9A addresses a similar requirement in relation to material items.

Information about employee numbers

1AC.33 *The notes to a small entity's financial statements must disclose the average number of persons employed by the small entity in the reporting period. (Section 411 of the Act)*

Related party disclosures

1AC.34 *Where the small entity is a subsidiary, the following information must be given in respect of the parent of the smallest group for which consolidated financial statements are drawn up of which the small entity is a member:*

(a) the name of the parent which draws up the consolidated financial statements;

(b) the address of the parent's registered office (whether in or outside the UK); or

(c) if it is unincorporated, the address of its principal place of business. (Schedule 1, paragraph 65)

Paragraph 33.5 addresses a similar requirement to paragraph (a).

1AC.35 *Particulars must be given of material transactions the small entity has entered into that have not been concluded under normal market conditions with:*

(a) owners holding a participating interest in the small entity;

(b) companies in which the small entity itself has a participating interest; and

(c) the small entity's directors [or members of its governing body].

Particulars must include:

(a) the amount of such transactions;

(b) the nature of the related party relationship; and

(c) other information about the transactions necessary for an understanding of the financial position of the small entity.

Information about individual transactions may be aggregated according to their nature, except where separate information is necessary for an understanding of the effects of the related party transactions on the financial position of the small entity.

Particulars need not be given of transactions entered into between two or more members of a group, provided that any subsidiary which is a party to the transaction is wholly-owned by such a member. (Schedule 1, paragraph 66)

Although disclosure is only required of material transactions with the specified **related parties** that have not been concluded under normal market conditions, small entities disclosing all transactions with such related parties would still be compliant with company law.

Transactions with directors, or members of an entity's governing body, include directors' remuneration and dividends paid to directors.

Paragraphs 33.9 and 33.14 address similar requirements for all related parties.

1AC.36 *Details of advances and credits granted by the small entity to its directors and guarantees of any kind entered into by the small entity on behalf of its directors must be shown in the notes to the financial statements.*

The details required of an advance or credit are:

(a) its amount;

(b) an indication of the interest rate;

(c) its main conditions;

(d) any amounts repaid;

(e) any amounts written off; and

(f) any amounts waived.

There must also be stated in the notes to the financial statements the totals of amounts stated under (a), (d), (e) and (f).

The details required of a guarantee are:

(a) its main terms;

(b) the amount of the maximum liability that may be incurred by the small entity; and

(c) any amount paid and any liability incurred by the small entity for the purpose of fulfilling the guarantee (including any loss incurred by reason of enforcement of the guarantee).

There must also be stated in the notes to the financial statements the totals of amounts stated under (b) and (c). (Section 413 of the Act)

Paragraph 33.9 addresses similar requirements for all related parties.

A small entity that is not a company shall provide this disclosure in relation to members of its governing body.

Other

1AC.37 *The financial statements must state:*

(a) the part of the UK in which the small entity is registered;

(b) the small entity's registered number;

(c) whether the small entity is a public or a private company and whether the small entity is limited by shares or by guarantee;

(d) the address of the small entity's registered office; and

(e) where appropriate, the fact that the entity is being wound up. (Section 396 of the Act)

Paragraph 3.24(a) addresses similar requirements.

1AC.38 *Where items to which Arabic numbers are given in any of the formats have been combined, unless they are not material, the individual amounts of any items which have been combined must be disclosed in a note to the financial statements. (Schedule 1, paragraph 4(3))*

1AC.39 *The nature and financial effect of material events arising after the reporting date which are not reflected in the income statement or statement of financial position must be stated. (Schedule 1, paragraph 64)*

Paragraphs 32.10 and 32.11 address similar requirements.

Appendix D to Section 1A
Disclosure requirements for small entities in the Republic of Ireland

This appendix is an integral part of Section 1A.

This appendix sets out the disclosure requirements for small entities based on the requirements of company law in the Republic of Ireland. These are shown in italic font in the paragraphs below. The drafting is as close as possible to that set out in company law, other than, for example, substituting company law terminology with the equivalent terminology used in FRS 102 (see Appendix II). References in this appendix to sections of the Companies Act 2014 are to the sections of that Act as amended by the Companies (Accounting) Act 2017 and references to Schedule 3A are to Schedule 3A to the Companies Act 2014. Qualifying partnerships are required to apply the provisions of the Companies Act 2014 set out in this appendix in accordance with the European Union (Qualifying Partnerships: Accounting and Auditing) Regulations 2019 (SI No. 597 of 2019).

*When there is a similar disclosure requirement in FRS 102 this has been indicated and those paragraphs of FRS 102 that have been cross-referenced are also highlighted by including an * in the left-hand margin. In many cases compliance with the similar requirement of FRS 102 will result in compliance with the requirements below, however a small entity in the Republic of Ireland must ensure it complies with all the disclosure requirements of this appendix.*

1AD.1 As a minimum, when relevant to its transactions, other events and conditions, a **small entity** in the Republic of Ireland shall provide the disclosures set out in this appendix.

1AD.2 *These notes shall be presented in the order in which, where relevant, the items to which they relate are presented in the statement of financial position and in the income statement. (Schedule 3A, paragraph 43(2))*

Paragraphs 8.3 and 8.4 address similar requirements.

Basis of preparation

1AD.3 *A small entity shall ensure that its financial statements include a statement as to whether they have been prepared in accordance with Section 1A of FRS 102 and for any material departure from Section 1A of FRS 102, the effect of the departure and the reasons for it are noted in the financial statements.*[24] *(Section 291(7) of the Companies Act 2014)*

Accounting policies

1AD.4 *A small entity shall disclose in the notes to its financial statements the accounting policies adopted by the small entity in determining:*

(a) the items and amounts to be included in its statement of financial position; and

(b) the items and amounts to be included in its income statement. (Section 321(1) of the Companies Act 2014)

Paragraph 8.5 addresses similar requirements for disclosing significant **accounting policies**. Including information about the judgements made in applying the small

[24] Small entities that are qualifying partnerships are not required to comply with the disclosure requirements in paragraph 1AD.3 (Regulation 11 of the *European Union (Qualifying Partnerships: Accounting and Auditing) Regulations 2019* (SI No. 597 of 2019)). However, paragraph 9 of FRS 100 encourages a small entity applying the small entities regime to include a statement of compliance in the notes to the financial statements.

entity's accounting policies, as set out in paragraph 8.6, may be useful to users of the small entity's **financial statements**.

1AD.5 *If an amount is included in a small entity's statement of financial position in respect of development costs, the following information shall be given in a note to the financial statements:*

(a) the period over which the amount of those costs originally capitalised is being or is to be written off; and

(b) the reasons for capitalising the costs in question. (Schedule 3A, paragraph 24(2))

Paragraph 18.27(a) addresses similar requirements to paragraph 1AD.5(a).

1AD.6 *Where development costs are shown as an asset in the small entity's financial statements and the amount is not treated as a realised loss because there are special circumstances justifying this, a note to the financial statements shall state the circumstances and that it is not a realised loss.*[25] *(Section 120(3) of the Companies Act 2014)*

1AD.7 *In any case where any goodwill acquired by a small entity is shown or included as an asset in the entity's statement of financial position, the period chosen for writing off the consideration for that goodwill and the reasons for choosing that period shall be disclosed in a note to the financial statements. (Schedule 3A, paragraph 25(4))*

Paragraph 19.25(g) addresses similar requirements.

Changes in presentation and accounting policies and corrections of prior period errors

1AD.8 *Where any change is made in the format adopted in preparing a statement of financial position or income statement of a small entity, the reasons for the change, together with full particulars of the change, shall be given in a note to the financial statements in which the new format is first adopted. (Schedule 3A, paragraph 3(2))*

Paragraphs 3.12 and 3.13 address similar requirements.

1AD.9 *Where a small entity changes an accounting policy and has disclosed such change in the notes to the financial statements, the notes to those financial statements shall also disclose:*

(a) the reason for the change in accounting policy; and

(b) to the extent practicable, the impact of the change in accounting policy on the financial statements for the current reporting period and on the financial statements of preceding periods. (Section 321(3) of the Companies Act 2014)

Paragraphs 10.13 and 10.14 address similar requirements.

1AD.10 *Where the corresponding amount for the immediately preceding reporting period is not comparable with the amount to be shown for the item in question in respect of the reporting period to which the statement of financial position or income statement relates, the former amount may be adjusted, and particulars of the adjustment and the reasons therefor shall be given in a note to the financial statements. (Schedule 3A, paragraph 5(1))*

[25] The disclosure requirements in paragraph 1AD.6 do not apply to qualifying partnerships.

This is likely to be relevant when there has either been a change in accounting policy or the correction of a **material** prior period **error**. Paragraphs 10.13, 10.14 and 10.23 address similar requirements.

True and fair override

1AD.11 *If it appears to the small entity that there are special reasons for departing from any of the principles set out in company law in preparing the small entity's financial statements in respect of any reporting period, it may do so, in which case particulars of the departure, the reasons for it, and its effects on the statement of financial position and income statement shall be given in the notes to the financial statements. (Section 291(6) of the Companies Act 2014 and Schedule 3A, paragraph 19)*

This is only expected to occur in special circumstances. Paragraphs 3.4 and 3.5 address similar requirements.

Notes supporting the statement of financial position

1AD.12 *Where an asset or liability relates to more than one of the items listed in the statement of financial position, its relationship to other items shall be disclosed either under the item where it is shown or in the notes to the financial statements. (Schedule 3A, paragraph 4(7))*

Fixed assets

1AD.13 *In respect of each item which is shown under the general item 'fixed assets' in the small entity's statement of financial position the following information shall be given:*

(a) the aggregate amounts (on the basis of cost or revaluation, or under the fair value accounting rules) in respect of that item as at the date of the beginning of the reporting period and as at the reporting date respectively;

(b) the effect on any amount shown in the statement of financial position in respect of that item of:

(i) any revision of the amount in respect of any assets included under that item made during the reporting period as a result of revaluation or under the fair value accounting rules;

(ii) acquisitions during the reporting period of any assets;

(iii) disposals during the reporting period of any assets; and

(iv) any transfers of assets of the small entity to and from that item during the reporting period. (Schedule 3A, paragraphs 45(1) and 45(2))

1AD.14 *In respect of each item within paragraph 1AD.13 there shall also be stated:*

(a) the cumulative amount of value adjustments for depreciation and impairment of assets included under that item as at the date of the beginning of the reporting period and as at the reporting date respectively;

(b) the amount of any such value adjustments made in respect of the reporting period;

(c) the amount of any adjustments made in respect of any such value adjustments during the reporting period in consequence of the disposal of any assets; and

(d) the amount of any other adjustments made in respect of any such value adjustments during the reporting period. (Schedule 3A, paragraph 45(3))

Comparatives are not required for the movements in fixed assets during the reporting period noted in paragraphs 1AD.13 and 1AD.14 above. (Schedule 3A, paragraph 5(2))

These two paragraphs apply to all **fixed assets**, including **investment property**, **property, plant and equipmen**t, **intangible assets** (including **goodwill**), fixed asset investments, **biological assets** and **heritage assets** recognised in **the statement of financial position**.

Each item refers to a class of fixed assets shown separately either in the statement of financial position, or in the **notes to the financial statements**.

Paragraph 16.10(e) addresses similar requirements for investment property. Paragraphs 17.31(d) and (e) address similar requirements for property, plant and equipment. Paragraphs 18.27(c) and (e) address similar requirements for intangible assets other than goodwill. Paragraph 19.26 addresses similar requirements for goodwill. Paragraphs 34.7(c) and 34.10(e) address similar requirements for biological assets. Paragraphs 34.55(e) and (f) address similar requirements for heritage assets recognised in the statement of financial position.

Fixed assets measured at revalued amounts

1AD.15 *Where fixed assets are measured at revalued amounts, the items affected and the basis of valuation adopted in determining the amounts of the assets in question in the case of each such item shall be disclosed in the note on accounting policies. (Schedule 3A, paragraph 35(2))*

These requirements apply when:

- Investments in **subsidiaries**, **associates** and **joint ventures** are measured at **fair value** with changes in fair value recognised in **other comprehensive income**. Paragraph 9.27(b) addresses a similar disclosure requirement.
- Property, plant and equipment are revalued using the revaluation model set out in paragraphs 17.15B to 17.15F. Paragraph 17.31(a) addresses a similar disclosure requirement.
- Intangible assets other than goodwill are revalued using the revaluation model set out in paragraphs 18.18B to 18.18H. Paragraph 18.29A(c) addresses a similar disclosure requirement.

These requirements do not apply to investment property and biological assets measured at fair value through profit or loss.

1AD.16 *In the case of each item in the statement of financial position measured at a revalued amount, the comparable amounts determined according to the historical cost accounting rules shall be shown separately in the statement of financial position or in a note to the financial statements. (Schedule 3A, paragraph 35(3))*

The comparable amounts refers to the aggregate amount of cost and the aggregate of accumulated depreciation and accumulated impairment losses that would have been required according to the historical cost accounting rules. (Schedule 3A, paragraph 35(4))

Paragraphs 17.32A(d) and 18.29A(d) address similar requirements.

These requirements apply in the same circumstances as those set out in paragraph 1AD.15.

1AD.17 *Where any amount is transferred to or from any revaluation reserves and the revaluation reserves are shown as separate items in the small entity's statement of financial position, the following information shall be set out in tabular form:*

(a) the amount of the reserves as at the date of the beginning of the reporting period and as at the reporting date respectively;

(b) any amount transferred to or from the reserves during that period; and

(c) the source and application respectively of any amounts so transferred. (Schedule 3A, paragraph 49)

Paragraph 6.3A addresses similar requirements.

These requirements apply in the same circumstances as those set out in paragraph 1AD.15.

1AD.18 *The treatment for taxation purposes of amounts credited or debited to the revaluation reserve shall be disclosed in a note to the financial statements. (Schedule 3A, paragraph 36(6))*

Paragraph 29.27(a) addresses similar requirements.

These requirements apply in the same circumstances as those set out in paragraph 1AD.15.

Capitalisation of borrowing costs

1AD.19 *Where a small entity adopts a policy of capitalising borrowing costs, the inclusion of interest in determining the cost of the asset and the amount of the interest so included is disclosed in a note to the financial statements. (Schedule 3A, paragraph 29(3))*

Paragraph 25.3A(a) addresses a similar requirement to the second part of this.

Impairment of assets

1AD.20 *Value adjustments for impairment of fixed assets (including fixed asset investments) shall be disclosed (either separately or in aggregate) in a note to the financial statements if not shown separately in the income statement. (Schedule 3A, paragraphs 23(1) and (2))*

Paragraph 27.32(a) addresses similar requirements.

1AD.21 *Any value adjustments for impairment of fixed assets that are reversed because the reasons for which they were made have ceased to apply shall be disclosed (either separately or in aggregate) in a note to the financial statements if not shown separately in the income statement. (Schedule 3A, paragraph 23(3))*

Paragraph 27.32(b) addresses similar requirements.

Fair value measurement

1AD.22 *Where financial instruments or assets other than financial instruments have been measured in accordance with the fair value accounting rules there shall be stated:*

(a) the significant assumptions underlying the valuation models and techniques where fair values have been determined otherwise than by reference to market price in an active market;

(b) *for each category of financial instruments or assets other than financial instruments, the fair value of the financial instruments or assets other than financial instruments in that category and the change in value:*

  (i) *included in the income statement; or*

  (ii) *credited or debited to the fair value reserve,*

  in respect of those financial instruments or assets other than financial instruments. (Schedule 3A, paragraphs 46(2)(a) and (b))

This does not apply where **financial instruments** or assets other than financial instruments are measured at fair value only on initial recognition.

This applies where financial instruments, investment property and biological assets are subsequently measured at fair value through profit or loss, which is permitted or required by paragraphs 9.26(c), 11.14(b), 11.14(d)(i), 12.8, 14.4(d), 15.9(d), 16.7 and 34.4.

Paragraphs 11.41, 11.43, 11.48(a)(i), 11.48(a)(ii), 12.28, 12.29(c), and 12.29(e) address similar disclosure requirements for financial instruments. Paragraphs 16.10(a) and 16.10(e)(ii) address similar disclosure requirements for investment property. Paragraphs 34.7(b) and 34.7(c)(i) address similar disclosure requirements for biological assets.

1AD.23 *Where financial instruments or assets other than financial instruments have been measured in accordance with the fair value accounting rules there shall be stated for each class of derivatives, the extent and nature of the instruments, including significant terms and conditions that may affect the amount, timing and certainty of future cash flows. (Schedule 3A, paragraph 46(2)(c))*

1AD.24 *Where financial instruments or assets other than financial instruments have been measured in accordance with the fair value accounting rules there shall be stated in tabular form, the movements in the fair value reserve during the reporting period. (Schedule 3A, paragraph 46(2)(d))*

Paragraphs 6.3A, 12.29(c) and 12.29(d) address similar requirements.

Financial instruments measured at fair value

1AD.25 *Financial instruments that under international financial reporting standards (IFRS) may be accounted for in financial statements at fair value, may be so accounted for in financial statements to which the provisions of Schedule 3A apply, provided that the disclosures required by IFRS are made. (Schedule 3A, paragraph 38(1))*

This applies to all financial instruments measured in accordance with the fair value accounting rules. The disclosures required by Section 11 *Basic Financial Instruments* that relate to **financial assets** and **financial liabilities** measured at fair value, including paragraph 11.48A, shall be given.

Indebtedness, guarantees and financial commitments

1AD.26 *In respect of each item shown under 'creditors' in the small entity's statement of financial position there shall be stated the aggregate amount of any debts included under 'creditors' which fall due for payment or repayment after the end of the period of five years beginning with the day next following the reporting date. (Schedule 3A, paragraph 50(1))*

1AD.27 *In respect of each item shown under 'creditors' in the small entity's statement of financial position there shall be stated:*

(a) the aggregate amount of any debts included under that item in respect of which any security has been given; and

(b) an indication of the nature of the securities so given. (Schedule 3A, paragraph 50(2))

Paragraphs 11.46, 13.22(e), 16.10(c), 17.32(a) and 18.28(c) address similar requirements.

1AD.28 *Particulars shall be given of any charge on the assets of the small entity to secure the liabilities of any other person, including, where practicable, the amount secured. (Schedule 3A, paragraph 51(1))*

1AD.29 *Particulars and the total amount or estimated total amount shall be given with respect to any other financial commitment, guarantee or contingency not provided for in the statement of financial position. (Schedule 3A, paragraph 51(2))*

The aggregate amount of any such commitments, guarantees or contingencies which are undertaken on behalf of or for the benefit of:

(a) any parent or fellow subsidiary of the small entity;

(b) any subsidiary of the small entity; or

(c) any undertaking in which the small entity has a participating interest,

shall be separately stated and those within each of clause (a), (b) and (c) shall also be stated separately from those within any other of those clauses. (Schedule 3A, paragraph 51(7))

1AD.30 *An indication of the nature and form of any valuable security given by the small entity in respect of commitments, guarantees and contingencies not provided for in the statement of financial position shall be given. (Schedule 3A, paragraph 51(3))*

Paragraphs 11.46, 13.22(e), 16.10(c), 17.32(a) and 18.28(c) address similar requirements.

1AD.31 *The total amount of any commitments not provided for in the statement of financial position concerning retirement benefits shall be disclosed separately. (Schedule 3A, paragraph 51(4))*

1AD.32 *Particulars, including details of significant assumptions underlying the valuation models shall be given of retirement benefit commitments which are included in the statement of financial position. (Schedule 3A, paragraph 51(5))*

1AD.33 *Where any commitment referred to in paragraph 1AD.31 or 1AD.32 relates wholly or partly to retirement benefits payable to past directors of the company, separate particulars shall be given of that commitment. (Schedule 3A, paragraph 51(6))*

A small entity that is a qualifying partnership shall provide this disclosure in relation to past members of the qualifying partnership.

Such commitments as referred to in 1AD.29 to 1AD.33 can arise in a variety of situations, including in relation to group entities, investments, property, plant and equipment, leases and retirement benefit obligations. Paragraphs 15.19(d), 16.10(d), 17.32(b), 18.28(d), 20.16, 21.15, 28.40A(a), 28.40A(b), 28.41A(d), 33.9(b)(ii) and 34.62 address similar requirements.

Paragraph 28.41(k) addresses similar requirements for the assumptions underlying retirement benefit commitments recognised in the statement of financial position.

1AD.34 *The nature and business purpose of any arrangements of a small entity that are not included in its statement of financial position shall be provided in the notes to the financial statements if the risks or benefits arising from such arrangements are material and in so far as the disclosure of such risks or benefits is necessary for assessing the financial position of the small entity. (Sections 323(1) and 323(1A) of the Companies Act 2014)*

Examples of off-balance sheet arrangements include risk and benefit-sharing arrangements or obligations arising from a contract such as debt factoring, combined sale and repurchase arrangements, consignment stock arrangements, take or pay arrangements, securitisation arranged through separate entities, pledged assets, operating lease arrangements, outsourcing and the like. In many cases the disclosures about financial commitments and contingencies required by paragraphs 1AD.28 to 1AD.33 will also address such arrangements.

Appropriation of profit or loss

1AD.35 *The income statement, statement of financial position or notes to the financial statements of a small entity for a reporting period shall show:*

(a) the aggregate amount of dividends paid in the reporting period (other than dividends for which a liability existed at the immediately preceding reporting date);

(b) the aggregate amount of dividends the small entity is liable to pay at the reporting date (other than dividends for which a liability existed at the immediately preceding reporting date);

(c) separately, any transfer between retained earnings and other reserves;

(d) any other increase or reduction in the balance on retained earnings since the immediately preceding reporting date;

(e) the profit or loss brought forward at the beginning of the reporting period; and

(f) the profit or loss carried forward at the end of the reporting period. (Schedule 3A, paragraph 48)

Paragraph 6.3(c) addresses similar requirements.

Notes supporting the income statement

1AD.36 *The income statement or the notes to the financial statements shall disclose information on the nature, amount and effect of individual items of income and expenditure that are exceptional by virtue of size or incidence. (Schedule 3A, paragraph 53)*

Paragraph 5.9A addresses a similar requirement in relation to material items.

Information about employee numbers

1AD.37 *The notes to a small entity's financial statements shall disclose the average number of persons employed by the small entity in the reporting period. (Sections 317(1)(a) and 317(7A) of the Companies Act 2014)*

Directors' remuneration (Sections 305 and 306 of the Companies Act 2014)

1AD.38 *The notes to the financial statements of a small entity shall disclose both for the current and the preceding reporting period the following amounts in relation to persons who at any time during the financial year were directors of the small entity:*

(a) the aggregate amount of emoluments paid to or receivable by directors in respect of qualifying services;

(b) the aggregate amount of the gains by the directors on the exercise of share options during the reporting period;

(c) the aggregate amount of the money or value of other assets, including shares but excluding share options, paid to or receivable by the directors under long term incentive schemes in respect of qualifying services;

(d) the aggregate amount of any contributions paid, treated as paid, or payable during the reporting period to a retirement benefit scheme in respect of qualifying services of directors, identifying separately the amounts relating to:

(i) defined contribution schemes; and

(ii) defined benefit schemes;

and in each case showing the number of directors, if any, to whom retirement benefits are accruing under such schemes in respect of qualifying services,

(e) the aggregate amount of any compensation paid or payable to directors in respect of loss of office or other termination payments in the reporting period, distinguished between:

(i) amounts in respect of the office of director of the small entity; and

(ii) amounts in respect of other offices. (Sections 305(1) and 305(12)(b) of the Companies Act 2014)

The aggregate amounts in sub-paragraph (e) above should also be distinguished between amounts paid by or receivable from:

(i) the small entity;

(ii) the small entity's subsidiaries;

(iii) any parent of the small entity; and

(iv) any other person. (Section 305(13)(b) of the Companies Act 2014)

1AD.39 *The notes to the financial statements of a small entity shall disclose both for the current and the preceding reporting period the following amounts in relation to the one or more persons who are past directors of it or past directors of its parent:*

(a) the aggregate amount paid or payable for such directors' retirement benefits analysed between:

(i) retirement benefits for services as director of the small entity; and

(ii) other retirement benefits; (Sections 305(2) and 305(10) of the Companies Act 2014)

(b) the aggregate amount of any compensation paid or payable to such directors in respect of loss of office or other termination benefits distinguished between:

(i) amounts in respect of the office of director of the small entity; and

(ii) amounts in respect of other offices. (Sections 305(2) and 305(12)(b) of the Companies Act 2014)

The aggregate amounts in sub-paragraph (b) above should also be distinguished between amounts paid by or receivable from:

- *(i) the small entity;*
- *(ii) the small entity's subsidiaries;*
- *(iii) any parent of the small entity;*
- *(iv) and any other persons. (Section 305(13)(b) of the Companies Act 2014)*

The disclosures in paragraphs 1AD.38 and 1AD.39 shall include all amounts paid or payable to a person connected with a director (Section 306(1)) and shall include all relevant sums paid by or receivable from the small entity, its subsidiaries, any parent of the small entity, and any other person (Section 305(13)(a) of the Companies Act 2014).

Payments to third parties for services of directors (Sections 305A and 306 of the Companies Act 2014)[26]

1AD.40 *The notes to the financial statements of a small entity shall disclose, both for the current and the preceding reporting period, the aggregate amount of any consideration paid to, or receivable by, third parties for making available the services of any person:*

- *(a) as a director of the small entity;*
- *(b) as director of any of its subsidiaries; or*
- *(c) otherwise in connection with the management of the small entity's affairs or any of its subsidiaries.*

This disclosure shall include all relevant sums paid by or receivable from, and shall distinguish between the sums respectively paid by, or receivable from, the small entity, its subsidiaries, any parent of the small entity and any other persons. (Section 305A(1) and 305A(2) of the Companies Act 2014)

The nature of any consideration paid to, or receivable by, the third parties identified above, shall also be disclosed. (Section 305A(4)(a)(ii) of the Companies Act 2014)

Transactions with directors (Sections 307 to 309 of the Companies Act 2014)

1AD.41 *The financial statements of a small entity shall disclose, both for the current and the preceding reporting period, in the notes to the financial statements the particulars of the following arrangements (see paragraphs 1AD.42 to 1AD.45).*

Loans, quasi-loans and credit transactions[27] [28]

1AD.42 *The particulars required in respect of loans, quasi-loans and credit transactions entered into by the small entity with or for persons who at any time during the reporting*

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[26] Exemption: The disclosure requirements in paragraph 1AD.40 do not apply to qualifying partnerships. (Regulation 15 of the *European Union (Qualifying Partnerships: Accounting and Auditing) Regulations 2019* (SI No. 597 of 2019))

[27] Other arrangements: Similar disclosures must be given where a small entity has been assigned or has assumed any right or obligation or liability which, if it had itself undertaken that right or obligation or liability, would have fallen under these disclosures. (Sections 307(1)(e) and 307(7) of the *Companies Act 2014*)

[28] Exemption: The disclosure requirements in paragraphs 1AD.42 to 1AD.45 do not apply in relation to an individual director and persons connected with him/her if the aggregate value of all agreements, transactions and arrangements did not, at any time during the reporting period, exceed €7,500 for that director and those persons. Section 308(6) states that references to 'director' are also to be read as references to an 'officer who is not a director' as applicable. (Sections 308(3), 308(5) and 308(6) of the *Companies Act 2014*)

period, were directors of the company or of its parent or persons connected with such directors, separately for each director or other person, are:

(a) *the name of the person for whom the arrangements were made and where that person is or was connected with a director of the small entity or its parent, the name of the director;*

(b) *the value of the arrangements at the beginning and end of the reporting period;*

(c) *advances made under the arrangements during the reporting period;*

(d) *amounts repaid under the arrangements during the reporting period;*

(e) *the amounts of any allowance made during the reporting period in respect of any failure or anticipated failure by the borrower to repay the whole or part of the outstanding amount;*

(f) *amounts outstanding under the arrangements waived during the reporting period;*

(g) *an indication of the interest rate; and*

(h) *the arrangements' other main conditions. (Section 307(3) of the Companies Act 2014)*

Additionally, a separate total of the amounts stated for the purposes of each of paragraphs (b) to (f) above, and the amounts stated for the purposes of paragraph (b) expressed as a percentage of the net assets of the small entity at the beginning and end of the reporting period shall be disclosed. (Section 307(8)(a) and (c) of the Companies Act 2014) These additional requirements are extended to persons who are officers (but not directors) of the small entity or its parent, and separate disclosure in respect of these officers is required on an aggregate basis, as well as the number of officers for whom such arrangements were made. (Section 307(9) of the Companies Act 2014)

1AD.43 *The particulars required in respect of an agreement to enter into loans, quasi-loans or credit transactions by the small entity with or for persons who at any time during the reporting period, were directors of the small entity or directors of its parent or persons connected with such directors, are those of subparagraphs (a), (g) and (h) of paragraph 1AD.42, and additionally the value of the arrangements agreed to. (Section 307(4) of the Companies Act 2014)*

The disclosures shall be made separately for each director or other person.

Guarantees and security provided by the small entity[29] [30]

1AD.44 *The particulars required for guarantees entered into and security provided by the small entity on behalf of persons who at any time during the reporting period were directors of the small entity or of its parent or persons connected with such directors in*

[29] Other arrangements: Similar disclosures must be given where a small entity has been assigned or has assumed any right or obligation or liability which, if it had itself undertaken that right or obligation or liability, would have fallen under these disclosures. (Sections 307(1)(e) and 307(7) of the *Companies Act 2014*)

[30] Exemption: The disclosure requirements in paragraphs 1AD.42 to 1AD.45 do not apply in relation to an individual director and persons connected with him/her if the aggregate value of all agreements, transactions and arrangements did not, at any time during the reporting period, exceed €7,500 for that director and those persons. Section 308(6) states that references to 'director' are also to be read as references to an 'officer who is not a director' as applicable. (Sections 308(3), 308(5) and 308(6) of the *Companies Act 2014*)

connection with a loan, quasi-loan or credit transaction entered into with or for those directors or other persons, separately for each director or other person, are:

(a) the name of the person for whom the arrangements were made and where that person is or was connected with a director of the small entity or its parent, the name of the director;

(b) the amount of the maximum liability that may be incurred by the small entity;

(c) any amount paid and any liability incurred by the small entity for the purpose of fulfilling the guarantee or on foot of the provision of security (including any loss incurred by reason of enforcement of the guarantee or loss of the security); and

(d) the arrangements' main terms. (Section 307(5) of the Companies Act 2014)

Additionally, a separate total of the amounts stated for the purposes of each of paragraphs (b) and (c) above is required. (Section 307(8)(b) of the Companies Act 2014) This requirement is extended to persons who are officers (but not directors) of the small entity or its parent and separate disclosure in respect of these officers is required on an aggregate basis, as well as the number of officers for whom such arrangements were made. (Section 307(9) of the Companies Act 2014)

1AD.45 *The particulars required in respect of agreements by the small entity to enter into guarantees or provide security on behalf of persons who at any time during the reporting period were directors of the small entity or of its parent or persons connected with such directors in connection with a loan, quasi-loan or credit transaction entered into with or for those directors or other persons, are those of subparagraphs (a), (b) and (d) of paragraph 1AD.44. (Section 307(6) of the Companies Act 2014)*

The disclosures shall be made separately for each director or other person.

Additional requirements

1AD.46 *Where at any time during the reporting period the aggregate of the amounts of:*

(a) the amount outstanding under arrangements waived comprising loans, quasi-loans and credit transactions; and

(b) the amount of the maximum liability that may be incurred by the small entity in respect of arrangements comprising guarantees entered into or security provided in connection with a loan, quasi-loan or credit transaction

amount to more than 10 per cent of the net assets of the small entity, the aggregate amount shall be stated and the percentage of net assets that the total represents. (Section 307(10) of the Companies Act 2014)

1AD.47 *In the event that the small entity is a parent and is taking an exemption from the requirement to prepare group financial statements, it shall provide the information required by paragraphs 1AD.41 to 1AD.46 in its financial statements in relation to both the small entity and its subsidiaries. (Section 308(4) of the Companies Act 2014)*

1AD.48 *The financial statements of a small entity shall disclose, both for the current and the preceding reporting period, in the notes to the financial statements the following particulars of any other arrangement or transaction not dealt with in paragraphs 1AD.38 to 1AD.47, entered into by the small entity in which a person, who at any time during the reporting period was a director, a director of its parent or a person connected with such a director, had, directly or indirectly, a material interest:*

(a) particulars of the principal terms of the arrangement or transaction;

(b) the name of the director or other person with the material interest; and

(c) the nature of the interest. (Section 309 of the Companies Act 2014)

Disclosure is not required in relation to transactions or arrangements with a small entity in which a director of the small entity or of its parent, or a person connected with such a director, had directly or indirectly, a material interest if:

(a) they are excluded by virtue of section 309(5) of the Companies Act 2014; or

(b) (i) the value of each transaction or arrangement in which that director, or other person, had directly or indirectly a material interest and which was made after the commencement of the financial year with the small entity; and

(ii) the value of each such transaction or arrangement which was made before the commencement of the reporting period, less the amount, if any, by which the liabilities of the person for whom the transaction or arrangement was made have been reduced (that is, the value outstanding),

did not at any time in the reporting period exceed in aggregate €5,000 or, if more, did not exceed the lesser of €15,000 and 1% of the value of the small entity's net assets. (Section 309(6) of the Companies Act 2014)

In the event that the small entity is a parent and is taking an exemption from the requirement to prepare group financial statements, it shall provide the information required by this paragraph in its financial statements in relation to both the small entity and its subsidiaries. (Section 309(7) of the Companies Act 2014)

A small entity that is not a company shall provide the disclosures required by paragraphs 1AD.38 to 1AD.48 in relation to members of its governing body. For qualifying partnerships, the disclosures shall be provided in relation to its members.[31]

Other related party disclosures

1AD.49 *Where a small entity, or a nominee of the small entity or a person acting in that person's own name but on behalf of the small entity, holds shares in the small entity or an interest in such shares, the notes to the financial statements shall give separately:*

(a) the number and aggregate nominal value of those shares and, where shares of more than one class have been acquired, the number and aggregate nominal value of each class of such shares, at the beginning and end of the reporting period together with the consideration paid for such shares;

(b) a reconciliation of the number and nominal value of each class of such shares from the beginning of the reporting period to the end of the reporting period showing all changes during the reporting period, including further acquisitions, disposals and cancellations, in each case showing the value of the consideration paid or received, if any;

(c) the reasons for any acquisitions made during the reporting period;

(d) the proportion of called-up share capital held at the beginning and end of the reporting period; and

(e) particulars of any restriction on profits available for distribution by virtue of the application of section 320. (Section 320 of the Companies Act 2014)

A small entity that is a qualifying partnership shall provide these disclosures only to the extent that it holds shares in its parent or an interest in such shares.

[31] Where applicable, a partnership with capital shall read those references to shares as rights to share in the capital of the partnership. A partnership without capital shall read those references to shares as interests that: confer any rights to share in the profits or imposing liability to contribute to the losses of the partnership; or give rise to an obligation to contribute to the debts or expenses of the partnership in the event of a winding up. (Section 275(3) of the *Companies Act 2014*)

1AD.50 *Where a small entity is a parent and a subsidiary, the following information shall be stated with respect to the parent of the smallest group for which consolidated financial statements are drawn up and of which the small entity is a member:*

(a) the name of the parent; and

(b) if the parent is incorporated, the address of the parent's registered office whether in or outside of the Republic of Ireland; or

(c) if the parent is unincorporated, the address of its principal place of business. (Schedule 3A, paragraphs 57 and 58)

Paragraph 33.5 addresses a similar requirement to paragraph (a).

1AD.51 *Particulars shall be given in the notes to the financial statements of transactions which have been entered into with related parties by the small entity if such transactions are material and have not been concluded under normal market conditions. The particulars shall include the amount of such transactions, the nature of the related party relationship and other information about the transactions which is necessary for an understanding of the financial position of the small entity.*

The provision of particulars and other information about individual transactions may be aggregated according to their nature, except where separate information is necessary for an understanding of the effects of related party transactions on the financial position of the small entity.

Particulars need not be given of transactions which are entered into between two or more members of a group if any subsidiary which is party to the transaction is wholly owned by such a member.

These requirements apply only to related parties that are:

(a) the holders of participating interests in the small entity;

(b) entities in which the small entity holds a participating interest; and

(c) directors of the small entity or of a parent of the small entity. (Schedule 3A, paragraph 55)

A small entity that is not a company shall provide the disclosures required by this paragraph in relation to members of its governing body. For qualifying partnerships, the disclosures shall be provided in relation to its members.

Although disclosure is only required of material transactions with the specified **related parties** that have not been concluded under normal market conditions, small entities disclosing all transactions with such related parties would still be compliant with company law.

Transactions with directors, or members of a small entity's governing body, include dividends paid to directors.

Paragraphs 33.9 and 33.14 address similar requirements for all related parties.

Other

1AD.52 *The financial statements shall state the following:*

(a) the name and legal form of the small entity;

(b) the place of registration of the small entity and the number under which it is registered;[32]

(c) the address of its registered office;[33]

(d) if relevant, the fact that the small entity is being wound up, and where appropriate, whether a receiver or a provisional liquidator has been appointed and the former name as well as the existing name of the small entity if the winding up of the small entity commences within one year after the date on which it has changed its name. (Section 291(3A) of the Companies Act 2014)

Paragraph 3.24(a) addresses similar requirements to (a), (b) and (c).

1AD.53 *Where items to which Arabic numbers are given in any of the formats have been combined, unless they are not material, the individual amounts of any items which have been combined shall be disclosed in a note to the financial statements. (Schedule 3A, paragraph 4(5))*

1AD.54 *The particulars and financial impact of material events that have occurred after the end of the reporting period shall be given in the notes to the financial statements. (Schedule 3A, paragraph 56)*

Paragraphs 32.10 and 32.11 address similar requirements.

1AD.55 *Amounts in respect of items representing assets or income may be set off against amounts in respect of items representing liabilities or expenditure or vice versa in accordance with applicable accounting standards, provided that the gross amounts are disclosed in a note to the financial statements. (Schedule 3A, paragraph 7)*

[32] The disclosure requirements in sub-paragraph (b) do not apply to qualifying partnerships, except for those that are limited partnerships. (Regulation 11 of the *European Union (Qualifying Partnerships: Accounting and Auditing) Regulations 2019* (SI No. 597 of 2019))

[33] Qualifying partnerships shall state the address of their principal place of business. (Regulation 11 of the *European Union (Qualifying Partnerships: Accounting and Auditing) Regulations 2019* (SI No. 597 of 2019))

Appendix E to Section 1A
Additional disclosure encouraged for small entities

This appendix is an integral part of Section 1A.

1AE.1 When relevant to its transactions, other events and conditions, a **small entity** in the UK is encouraged to provide the following disclosures:

(a) a statement of compliance with this FRS as set out in paragraph 3.3, adapted to refer to Section 1A;

(b) a statement that it is a **public benefit entity** as set out in paragraph PBE3.3A;

(c) the disclosures relating to **material** uncertainties related to events or conditions that cast significant doubt upon the small entity's ability to continue as a **going concern** as set out in paragraph 3.9;

(d) dividends declared and paid or payable during the period (for example, as set out in paragraph 6.5(b)); and

(e) on first-time adoption of this FRS an explanation of how the transition has affected its **financial position** and financial performance as set out in paragraph 35.13.

1AE.2 When relevant to its transactions, other events and conditions, a small entity in the Republic of Ireland is encouraged to provide the disclosures in paragraph 1AE.1(b), (c) and (e).

Section 2
Concepts and Pervasive Principles

Scope of this section

2.1 This section sets out the **objective of financial statements** of entities within the scope of this FRS and the qualities that make the information in the **financial statements** of entities within the scope of this FRS useful. It also sets out the concepts and basic principles underlying the financial statements of entities within the scope of this FRS.

2.1A Although this section sets out the concepts and pervasive principles underlying financial statements, in some circumstances there may be inconsistencies between the concepts and principles in this section of the FRS and the specific requirements of another section. In these circumstances the specific requirements of the other section within the FRS take precedence over this section.

Objective of financial statements

2.2 The objective of financial statements is to provide information about the **financial position**, **performance** and **cash flows** of an entity that is useful for economic decision-making by a broad range of users who are not in a position to demand reports tailored to meet their particular information needs.

2.3 Financial statements also show the results of the stewardship of management – the accountability of management for the resources entrusted to it.

Qualitative characteristics of information in financial statements

Understandability

2.4 The information provided in financial statements should be presented in a way that makes it comprehensible by users who have a reasonable knowledge of **business** and economic activities and accounting and a willingness to study the information with reasonable diligence. However, the need for **understandability** does not allow relevant information to be omitted on the grounds that it may be too difficult for some users to understand.

Relevance

2.5 The information provided in financial statements must be relevant to the decision-making needs of users. Information has the quality of **relevance** when it is capable of influencing the economic decisions of users by helping them evaluate past, present or future events or confirming, or correcting, their past evaluations.

Materiality

2.6 Information is **material** – and therefore has relevance – if its omission or misstatement, individually or collectively, could influence the economic decisions of users taken on the basis of the financial statements. Materiality depends on the size and nature of the omission or misstatement judged in the surrounding circumstances. The size or nature of the item, or a combination of both, could be the determining factor. However, it is inappropriate to make, or leave uncorrected, immaterial departures from this FRS to achieve a particular presentation of an entity's financial position, financial performance or cash flows.

Reliability

2.7 The information provided in financial statements must be reliable. Information is reliable when it is free from material **error** and bias and represents faithfully that which it either purports to represent or could reasonably be expected to represent. Financial statements are not free from bias (ie not neutral) if, by the selection or presentation of information, they are intended to influence the making of a decision or judgement in order to achieve a predetermined result or outcome.

Substance over form

2.8 Transactions and other events and conditions should be accounted for and presented in accordance with their substance and not merely their legal form. This enhances the **reliability** of financial statements.

Prudence

2.9 The uncertainties that inevitably surround many events and circumstances are acknowledged 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 judgements 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 the deliberate understatement of assets or income, or the deliberate overstatement of liabilities or expenses. In short, prudence does not permit bias.

Completeness

2.10 To be reliable, the information in financial statements must be complete within the bounds of materiality and cost. An omission can cause information to be false or misleading and thus unreliable and deficient in terms of its relevance.

Comparability

2.11 Users must be able to compare the financial statements of an entity through time to identify trends in its financial position and performance. Users must also be able to compare the financial statements of different entities to evaluate their relative financial position, performance and cash flows. Hence, the **measurement** and display of the financial effects of like transactions and other events and conditions must be carried out in a consistent way throughout an entity and over time for that entity, and in a consistent way across entities. In addition, users must be informed of the **accounting policies** employed in the preparation of the financial statements, and of any changes in those policies and the effects of such changes.

Timeliness

2.12 To be relevant, financial information must be able to influence the economic decisions of users. **Timeliness** involves providing the information within the decision time frame. If there is undue delay in the reporting of information it may lose its relevance. Management may need to balance the relative merits of timely reporting and the provision of reliable information. In achieving a balance between relevance and reliability, the overriding consideration is how best to satisfy the needs of users in making economic decisions.

Balance between benefit and cost

2.13 The benefits derived from information should exceed the cost of providing it. The evaluation of benefits and costs is substantially a judgemental process. Furthermore, the costs are not necessarily borne by those users who enjoy the benefits, and often the benefits of the information are enjoyed by a broad range of external users.

2.14 Financial reporting information helps capital providers make better decisions, which results in more efficient functioning of capital markets and a lower cost of capital for the economy as a whole. Individual entities also enjoy benefits, including improved access to capital markets, favourable effect on public relations, and perhaps lower costs of capital. The benefits may also include better management decisions because financial information used internally is often based at least partly on information prepared for general purpose financial reporting purposes.

Financial position

2.15 The financial position of an entity is the relationship of its assets, liabilities and **equity** as of a specific date as presented in the **statement of financial position**. These are defined as follows:

(a) An asset is a resource controlled by the entity as a result of past events and from which future economic benefits are expected to flow to the entity.

(b) 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.

(c) Equity is the residual interest in the assets of the entity after deducting all its liabilities.

2.16 Some items that meet the definition of an asset or a liability may not be recognised as assets or liabilities in the statement of financial position because they do not satisfy the criteria for **recognition** in paragraphs 2.27 to 2.32. In particular, the expectation that future economic benefits will flow to or from an entity must be sufficiently certain to meet the probability criterion before an asset or liability is recognised.

Assets

2.17 The future economic benefit of an asset is its potential to contribute, directly or indirectly, to the flow of **cash** and **cash equivalents** to the entity. Those cash flows may come from using the asset or from disposing of it.

2.18 Many assets, for example **property, plant and equipment**, have a physical form. However, physical form is not essential to the existence of an asset. Some assets are intangible.

2.19 In determining the existence of an asset, the right of ownership is not essential. Thus, for example, property held on a **lease** is an asset if the entity controls the benefits that are expected to flow from the property.

Liabilities

2.20 An essential characteristic of a liability is that the entity has a present obligation to act or perform in a particular way. The obligation may be either a legal obligation or a **constructive obligation**. A legal obligation is legally enforceable as a consequence of a binding contract or statutory requirement. A constructive obligation is an obligation that derives from an entity's actions when:

(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.

2.21 The settlement of a present obligation usually involves the payment of cash, transfer of other assets, provision of services, the replacement of that obligation with another obligation, or conversion of the obligation to equity. An obligation may also be extinguished by other means, such as a creditor waiving or forfeiting its rights.

Equity

2.22 Equity is the residual interest in the assets of the entity after deducting all its liabilities. It may be sub-classified in the statement of financial position. For example, in a corporate entity, sub-classifications may include funds contributed by shareholders, retained earnings and **gains** or losses recognised in **other comprehensive income**.

Performance

2.23 Performance is the relationship of the income and expenses of an entity during a **reporting period**. This FRS permits entities to present performance in a single financial statement (a **statement of comprehensive income**) or in two financial statements (an **income statement** and a statement of comprehensive income). **Total comprehensive income** and **profit or loss** are frequently used as measures of performance or as the basis for other measures, such as return on investment or earnings per share. Income and expenses are defined as follows:

(a) Income is increases in economic benefits during the reporting period in the form of inflows or enhancements of assets or decreases of liabilities that result in increases in equity, other than those relating to contributions from equity investors.

(b) Expenses are decreases in economic benefits during the reporting period in the form of outflows or depletions of assets or incurrences of liabilities that result in decreases in equity, other than those relating to distributions to equity investors.

2.24 The recognition of income and expenses results directly from the recognition and measurement of assets and liabilities. Criteria for the recognition of income and expenses are discussed in paragraphs 2.27 to 2.32.

Income

2.25 The definition of income encompasses both **revenue** and gains.

(a) Revenue is income that arises in the course of the ordinary activities of an entity and is referred to by a variety of names including sales, fees, interest, dividends, royalties and rent.

(b) Gains are other items that meet the definition of income but are not revenue. When gains are recognised in the statement of comprehensive income, they are usually displayed separately because knowledge of them is useful for making economic decisions.

Expenses

2.26 The definition of expenses encompasses losses as well as those expenses that arise in the course of the ordinary activities of the entity.

(a) Expenses that arise in the course of the ordinary activities of the entity include, for example, cost of sales, wages and **depreciation**. They usually take the form of an outflow or depletion of assets such as cash and cash equivalents, **inventory**, or property, plant and equipment.

(b) Losses are other items that meet the definition of expenses and may arise in the course of the ordinary activities of the entity. When losses are recognised in the statement of comprehensive income, they are usually presented separately because knowledge of them is useful for making economic decisions.

Recognition of assets, liabilities, income and expenses

2.27 Recognition is the process of incorporating in the statement of financial position or statement of comprehensive income an item that meets the definition of an asset, liability, equity, income or expense and satisfies the following criteria:

(a) it is **probable** that any future economic benefit associated with the item will flow to or from the entity; and

(b) the item has a cost or value that can be measured reliably.

2.28 The failure to recognise an item that satisfies those criteria is not rectified by disclosure of the accounting policies used or by **notes** or explanatory material.

The probability of future economic benefit

2.29 The concept of probability is used in the first recognition criterion to refer to the degree of uncertainty that the future economic benefits associated with the item will flow to or from the entity. Assessments of the degree of uncertainty attaching to the flow of future economic benefits are made on the basis of the evidence relating to conditions at the end of the reporting period available when the financial statements are prepared. Those assessments are made individually for individually significant items, and for a group for a large population of individually insignificant items.

Reliability of measurement

2.30 The second criterion for the recognition of an item is that it possesses a cost or value that can be measured with reliability. In many cases, the cost or value of an item is known. In other cases it must be estimated. The use of reasonable estimates is an essential part of the preparation of financial statements and does not undermine their reliability. When a reasonable estimate cannot be made, the item is not recognised in the financial statements.

2.31 An item that fails to meet the recognition criteria may qualify for recognition at a later date as a result of subsequent circumstances or events.

2.32 An item that fails to meet the criteria for recognition may nonetheless warrant disclosure in the notes or explanatory material or in supplementary schedules. This is appropriate when knowledge of the item is relevant to the evaluation of the financial position, performance and changes in financial position of an entity by the users of financial statements.

Measurement of assets, liabilities, income and expenses

2.33 Measurement is the process of determining the monetary amounts at which an entity measures assets, liabilities, income and expenses in its financial statements. Measurement involves the selection of a basis of measurement. This FRS specifies which measurement basis an entity shall use for many types of assets, liabilities, income and expenses.

2.34 Two common measurement bases are historical cost and **fair value**:

(a) For assets, historical cost is the amount of cash or cash equivalents paid or the fair value of the consideration given to acquire the asset at the time of its acquisition. For liabilities, historical cost is the amount of proceeds of cash or cash equivalents received or the fair value of non-cash assets received in exchange for the obligation at the time the obligation is incurred, or in some circumstances (for example, **income tax**) the amounts of cash or cash equivalents expected to be paid to settle the liability in the normal course of business. Amortised historical cost is the historical cost of an asset or liability plus or minus that portion of its historical cost previously recognised as an expense or income.

(b) Fair value is the amount for which an asset could be exchanged, a liability settled, or an equity instrument granted could be exchanged, between knowledgeable, willing parties in an arm's length transaction. In the absence of any specific guidance provided in the relevant section of this FRS, when fair value measurement is permitted or required the guidance in the appendix to this section shall be applied.

Pervasive recognition and measurement principles

2.35 The requirements for recognising and measuring assets, liabilities, income and expenses in this FRS are based on pervasive principles that are derived from the IASB *Framework for the Preparation and Presentation of Financial Statements*[34] and from **adopted IFRS**. In the absence of a requirement in this FRS that applies specifically to a transaction or other event or condition, paragraph 10.4 provides guidance for making a judgement and paragraph 10.5 establishes a hierarchy for an entity to follow in deciding on the appropriate accounting policy in the circumstances. The third level of that hierarchy requires an entity to look to the definitions, recognition criteria and measurement concepts for assets, liabilities, income and expenses and the pervasive principles set out in this section.

Accrual basis

2.36 An entity shall prepare its financial statements, except for cash flow information, using the **accrual basis** of accounting. On the accrual basis, items are recognised as assets, liabilities, equity, income or expenses when they satisfy the definitions and recognition criteria for those items.

[34] In 2010 the IASB issued the *Conceptual Framework for Financial Reporting*, which superseded the *Framework for the Preparation and Presentation of Financial Statements*.

Assets

2.37 An entity shall recognise an asset in the statement of financial position when it is probable that the future economic benefits will flow to the entity and the asset has a cost or value that can be measured reliably. An asset is not recognised in the statement of financial position when expenditure has been incurred for which it is considered not probable that economic benefits will flow to the entity beyond the current reporting period. Instead such a transaction results in the recognition of an expense in the statement of comprehensive income (or in the income statement, if presented).

2.38 An entity shall not recognise a **contingent asset** as an asset. However, when the flow of future economic benefits to the entity is virtually certain, then the related asset is not a contingent asset, and its recognition is appropriate.

Liabilities

2.39 An entity shall recognise a liability in the statement of financial position when:

(a) the entity has an obligation at the end of the reporting period as a result of a past event;

(b) it is probable that the entity will be required to transfer resources embodying economic benefits in settlement; and

(c) the settlement amount can be measured reliably.

2.40 A **contingent liability** is either a possible but uncertain obligation or a present obligation that is not recognised because it fails to meet one or both of the conditions (b) and (c) in paragraph 2.39. An entity shall not recognise a contingent liability as a liability, except for contingent liabilities of an acquiree in a **business combination** (see Section 19 *Business Combinations and Goodwill*).

Income

2.41 The recognition of income results directly from the recognition and measurement of assets and liabilities. An entity shall recognise income in the statement of comprehensive income (or in the income statement, if presented) when an increase in future economic benefits related to an increase in an asset or a decrease of a liability has arisen that can be measured reliably.

Expenses

2.42 The recognition of expenses results directly from the recognition and measurement of assets and liabilities. An entity shall recognise expenses in the statement of comprehensive income (or in the income statement, if presented) when a decrease in future economic benefits related to a decrease in an asset or an increase of a liability has arisen that can be measured reliably.

Total comprehensive income and profit or loss

2.43 Total comprehensive income is the arithmetical difference between income and expenses. It is not a separate element of financial statements, and a separate recognition principle is not needed for it.

2.44 Profit or loss is the arithmetical difference between income and expenses other than those items of income and expense that this FRS classifies as items of other comprehensive income. It is not a separate element of financial statements, and a separate recognition principle is not needed for it.

2.45 Generally this FRS does not allow the recognition of items in the statement of financial position that do not meet the definition of assets or of liabilities regardless of whether they result from applying the notion commonly referred to as the 'matching concept' for measuring profit or loss.

Measurement at initial recognition

2.46 At initial recognition, an entity shall measure assets and liabilities at historical cost unless this FRS requires initial measurement on another basis such as fair value.

Subsequent measurement

Financial assets and financial liabilities

2.47 An entity measures basic **financial assets** and basic **financial liabilities** at **amortised cost** less impairment except for:

(a) investments in non-derivative **financial instruments** that are equity of the issuer (eg most **ordinary shares** and certain preference shares) that are **publicly traded** or whose fair value can otherwise be measured reliably, which are measured at fair value with changes in fair value recognised in profit or loss; and

(b) any financial instruments that upon their initial recognition were designated by the entity as at fair value through profit or loss.

2.48 An entity generally measures all other financial assets and financial liabilities at fair value, with changes in fair value recognised in profit or loss, unless this FRS requires or permits measurement on another basis such as cost or amortised cost.

Non-financial assets

2.49 Most non-financial assets that an entity initially recognised at historical cost are subsequently measured on other measurement bases. For example:

(a) An entity measures property, plant and equipment using either the cost model or the revaluation model.

(b) An entity measures inventories at the lower of cost and selling price less costs to complete and sell.

Measurement of assets at amounts lower than initial historical cost is intended to ensure that an asset is not measured at an amount greater than the entity expects to recover from the sale or use of that asset.

2.50 For certain types of non-financial assets, this FRS permits or requires measurement at fair value. For example:

(a) Investments in **associates** and **joint ventures** that an entity measures at fair value (see paragraphs 14.4(c), 14.4(d) and 14.4B, and 15.9(c), 15.9(d) and 15.9B respectively).

(b) **Investment property** that an entity measures at fair value (see paragraph 16.7).

(c) **Biological assets** that an entity measures at fair value less estimated costs to sell in accordance with the fair value model (see paragraph 34.3A(a)) and **agricultural produce** that an entity measures, at the point of harvest, at fair value less estimated costs to sell in accordance with either the fair value model (see paragraph 34.3A(a)) or cost model (see paragraph 34.9).

(d) Property, plant and equipment that an entity measures in accordance with the revaluation model (see paragraph 17.15B).

(e) **Intangible assets** that an entity measures in accordance with the revaluation model (see paragraph 18.18B).

Liabilities other than financial liabilities

2.51 Most liabilities other than financial liabilities are measured at the best estimate of the amount that would be required to settle the obligation at the **reporting date**.

Offsetting

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

(a) Measuring assets net of valuation allowances (for example, allowances for inventory obsolescence and allowances for uncollectible receivables) is not offsetting.

(b) If an entity's normal **operating activities** do not include buying and selling **fixed assets**, including investments and operating assets, then the entity reports gains and losses on disposal of such assets by deducting from the proceeds on disposal the **carrying amount** of the asset and related selling expenses.

Appendix to Section 2
Fair value measurement

This appendix is an integral part of Section 2.

2A.1 Other sections of this FRS make reference to the **fair value** guidance in this appendix, including Section 9 *Consolidated and Separate Financial Statements*, Section 11 *Basic Financial Instruments*, Section 12 *Other Financial Instruments Issues*, Section 13 *Inventories*, Section 14 *Investments in Associates*, Section 15 *Investments in Joint Ventures*, Section 16 *Investment Property*, Section 17 *Property*, *Plant and Equipment*, Section 18 *Intangible Assets other than Goodwill*, Section 27 *Impairment of Assets,* Section 28 *Employee Benefits* (in relation to plan assets) and Section 34 *Specialised Activities*.

An entity shall use the following methodology to estimate the fair value of an **asset** (or a **liability**, in which case the references to an asset and current bid price in this appendix shall be read as references to a liability and current offer price respectively):

(a) The best evidence of fair value is a quoted price for an identical asset (or similar asset) in an **active market**. This is usually the current bid price.

(b) When quoted prices are unavailable, the price in a binding sale agreement or a recent transaction for an identical asset (or similar asset) in an arm's length transaction between knowledgeable, willing parties provides evidence of fair value. However, this price may not be a good estimate of fair value if there has been a significant change in economic circumstances or a significant period of time between the date of the binding sale agreement or the transaction, and the measurement date. If the entity can demonstrate that the last transaction price is not a good estimate of fair value (eg because it reflects the amount that an entity would receive or pay in a forced transaction, involuntary liquidation or distress sale), that price is adjusted.

(c) If the market for the asset is not active and any binding sale agreements or recent transactions for an identical asset (or similar asset) on their own are not a good estimate of fair value, an entity estimates the fair value by using another valuation technique. The objective of using another valuation technique is to estimate what the transaction price would have been on the measurement date in an arm's length exchange motivated by normal business considerations.

Valuation technique

2A.2 Valuation techniques include using the price in a binding sale agreement and recent arm's length market transactions for an identical asset between knowledgeable, willing parties, reference to the current fair value of another asset that is substantially the same as the asset being measured, discounted cash flow analysis and option pricing models. If there is a valuation technique commonly used by market participants to price the asset and that technique has been demonstrated to provide reliable estimates of prices obtained in actual market transactions, the entity uses that technique.

2A.3 The objective of using a valuation technique is to establish what the transaction price would have been on the measurement date in an arm's length exchange motivated by normal business considerations. Fair value is estimated on the basis of the results of a valuation technique that makes maximum use of market inputs, and relies as little as possible on entity-determined inputs. A valuation technique would be expected to arrive at a reliable estimate of the fair value if:

(a) it reasonably reflects how the market could be expected to price the asset; and

(b) the inputs to the valuation technique reasonably represent market expectations and measures of the risk return factors inherent in the asset.

No active market

2A.4 The fair value of an asset that does not have a quoted market price in an active market is reliably measurable if:

(a) the variability in the range of reasonable fair value estimates is not significant for that asset; or

(b) the probabilities of the various estimates within the range can be reasonably assessed and used in estimating fair value.

2A.5 There are many situations in which the variability in the range of reasonable fair value estimates of assets that do not have a quoted market price is likely not to be significant. Normally it is possible to estimate the fair value of an asset that an entity has acquired from an outside party. However, if the range of reasonable fair value estimates is significant and the probabilities of the various estimates cannot be reasonably assessed, an entity is precluded from measuring the asset at fair value.

2A.6 If a reliable measure of fair value is no longer available for an asset measured at fair value, its **carrying amount** at the last date the asset was reliably measurable becomes its new cost. The entity shall measure the asset at this cost amount less impairment, if any, until a reliable measure of fair value becomes available.

Section 3
Financial Statement Presentation

Scope of this section

3.1 This section sets out the requirement that the **financial statements** of an entity shall give a true and fair view, what compliance with this FRS requires, and what is a complete set of financial statements.

3.1A A **small entity** applying Section 1A *Small Entities* is not required to comply with:

(a) the disclosure requirements of paragraphs 3.3[35], PBE3.3A, 3.9[36], 3.12, 3.13 and 3.24(b); and

(b) paragraphs 3.17, 3.18 and 3.19.

3.1B A small entity (regardless of the regime it applies in the preparation of its financial statements) is not required to comply with paragraph 3.17(d) unless it is required to prepare a **statement of cash flows** by an applicable **Statement of Recommended Practice (SORP)** or law or other relevant regulation.

True and fair view

3.2 The financial statements shall give a true and fair view of the **assets**, **liabilities**, **financial position**, financial **performance** and, when required to be presented, **cash flows** of an entity.

(a) The application of this FRS, with additional disclosure when necessary, is presumed to result in financial statements that give a true and fair view of the financial position, financial performance and, when required to be presented, cash flows of entities within the scope of this FRS.

(b) [Deleted]

The additional disclosures referred to in (a) are necessary when compliance with the specific requirements in this FRS is insufficient to enable users to understand the effect of particular transactions, other events and conditions on the entity's financial position and financial performance.

Compliance with this FRS

3.3 An entity whose financial statements comply with this FRS shall make an explicit and unreserved statement of such compliance in the **notes**. Financial statements shall not be described as complying with this FRS unless they comply with all the requirements of this FRS.

PBE3.3A A **public benefit entity** that applies the 'PBE' prefixed paragraphs shall make an explicit and unreserved statement that it is a public benefit entity.

* 3.4 In special circumstances when management concludes that compliance with any requirement of this FRS or applicable legislation (only when it allows for a true and fair

[35] Irish small entities, other than qualifying partnerships, are required to comply with the requirements of paragraph 3.3.

[36] If a small entity departs from the principle that it is presumed to be a carrying on business as a going concern, it must provide the disclosure required by paragraph 1AC.10 or 1AD.11, as relevant.

override) is inconsistent with the requirement to give a true and fair view, the entity shall depart from that requirement in the manner set out in paragraph 3.5.

* 3.5 When an entity departs from a requirement of this FRS in accordance with paragraph 3.4, or from a requirement of applicable legislation, it shall disclose the following:

(a) that management has concluded that the financial statements give a true and fair view of the entity's financial position, financial performance and, when required to be presented, cash flows;

(b) that it has complied with this FRS or applicable legislation, except that it has departed from a particular requirement of this FRS or applicable legislation to the extent necessary to give a true and fair view; and

(c) the nature and effect of the departure, including the treatment that this FRS or applicable legislation would require, the reason why that treatment would be so misleading in the circumstances that it would conflict with the **objective of financial statements** set out in Section 2 *Concepts and Pervasive Principles*, and the treatment adopted.

3.6 When an entity has departed from a requirement of this FRS or applicable legislation in a prior period, and that departure affects the amounts recognised in the financial statements for the current period, it shall make the disclosures set out in paragraph 3.5(c).

3.7 [Deleted]

Going concern

3.8 When preparing financial statements, the management of an entity using this FRS shall make an assessment of the entity's ability to continue as a **going concern**. An entity is a going concern unless management either intends to liquidate the entity or to cease trading, or has no realistic alternative but to do so. In assessing whether the going concern assumption is appropriate, management takes into account all available information about the future, which is at least, but is not limited to, 12 months from the date when the financial statements are authorised for issue.

3.9 When management is aware, in making its assessment, of **material** uncertainties related to events or conditions that cast significant doubt upon the entity's ability to continue as a going concern, the entity shall disclose those uncertainties. When an entity does not prepare financial statements on a going concern basis, it shall disclose that fact, together with the basis on which it prepared the financial statements and the reason why the entity is not regarded as a going concern.

Frequency of reporting

3.10 An entity shall present a complete set of financial statements (including comparative information as set out in paragraph 3.14) at least annually. When the end of an entity's **reporting period** changes and the annual financial statements are presented for a period longer or shorter than one year, the entity shall disclose the following:

(a) that fact;

(b) the reason for using a longer or shorter period; and

(c) the fact that comparative amounts presented in the financial statements (including the related notes) are not entirely comparable.

Consistency of presentation

3.11 An entity shall retain the presentation and classification of items in the financial statements from one period to the next unless:

(a) it is apparent, following a significant change in the nature of the entity's operations or a review of its financial statements, that another presentation or classification would be more appropriate having regard to the criteria for the selection and application of **accounting policies** in Section 10 *Accounting Policies, Estimates and Errors*; or

(b) this FRS, or another applicable FRS, requires a change in presentation.

* 3.12 When the presentation or classification of items in the financial statements is changed, an entity shall reclassify comparative amounts unless the reclassification is **impracticable**. When comparative amounts are reclassified, an entity shall disclose the following:

(a) the nature of the reclassification;

(b) the amount of each item or class of items that is reclassified; and

(c) the reason for the reclassification.

* 3.13 If it is impracticable to reclassify comparative amounts, an entity shall disclose the reason why.

Comparative information

3.14 Except when this FRS permits or requires otherwise, an entity shall present comparative information in respect of the preceding period for all amounts presented 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.

3.14A An entity providing reconciliations of items of **fixed assets**, in accordance with paragraph 51 of Schedule 1 to the **Regulations**, need not present these reconciliations for prior periods.

Materiality and aggregation

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

3.16 Financial statements result from processing large numbers of transactions or other events that are aggregated into classes according to their nature or function. The final stage in the process of aggregation and classification is the presentation of condensed and classified data, which form line items in the financial statements. If a line item is not individually material, it is aggregated with other items either in those statements or in the notes. An item that may not warrant separate presentation in those statements may warrant separate presentation in the notes.

3.16A When applying this FRS an entity shall decide, taking into consideration all relevant facts and circumstances, how it aggregates information in the financial statements, which includes the notes. An entity shall not reduce the **understandability** of its financial statements by obscuring material information with immaterial information or by aggregating material items that have different natures or functions.

3.16B This FRS specifies information that is required to be included in the financial statements, which includes the notes. An entity need not provide a specific disclosure required by this FRS if the information resulting from that disclosure is not material. This is the case even if this FRS contains a list of specific requirements or describes them as minimum requirements.[37]

Complete set of financial statements

3.17 A complete set of financial statements of an entity shall include all of the following:

(a) a **statement of financial position** as at the **reporting date**;

(b) either:

(i) a single **statement of comprehensive income** for the reporting period displaying all items of **income** and **expense** recognised during the period including those items recognised in determining **profit or loss** (which is a subtotal in the statement of comprehensive income) and items of **other comprehensive income**; or

(ii) a separate **income statement** and a separate statement of comprehensive income. If an entity chooses to present both an income statement and a statement of comprehensive income, the statement of comprehensive income begins with profit or loss and then displays the items of other comprehensive income;

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

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

(e) notes, comprising significant accounting policies and other explanatory information.

3.18 If the only changes to **equity** during the periods for which financial statements are presented arise from profit or loss, payment of dividends, corrections of prior period **errors**, and changes in accounting policy, the entity may present a single **statement of income and retained earnings** in place of the statement of comprehensive income and statement of changes in equity (see paragraph 6.4).

3.19 If an entity has no items of other comprehensive income in any of the periods for which financial statements are presented, it may present only an income statement, or it may present a statement of comprehensive income in which the 'bottom line' is labelled 'profit or loss'.

3.20 Because paragraph 3.14 requires comparative amounts in respect of the previous period for all amounts presented in the financial statements, a complete set of financial statements means that an entity shall present, as a minimum, two of each of the required financial statements and related notes.

3.21 In a complete set of financial statements, an entity shall present each financial statement with equal prominence.

3.22 An entity may use titles for the financial statements other than those used in this FRS as long as they are not misleading.

[37] Certain disclosures required by the Act must be given regardless of materiality, such as information about subsidiary undertakings.

Identification of the financial statements

3.23 An entity shall clearly identify each of the financial statements and the notes and distinguish them from other information in the same document. In addition, an entity shall display the following information prominently, and repeat it when necessary for an understanding of the information presented:

(a) the name of the reporting entity and any change in its name since the end of the preceding reporting period;

(b) whether the financial statements cover the individual entity or a **group** of entities;

(c) the date of the end of the reporting period and the period covered by the financial statements;

(d) the **presentation currency**, as defined in Section 30 *Foreign Currency Translation*; and

(e) the level of rounding, if any, used in presenting amounts in the financial statements.

3.24 An entity shall disclose the following in the notes:

* (a) the legal form of the entity, its country of incorporation and the address of its registered office (or principal place of **business**, if different from the registered office); and

(b) a description of the nature of the entity's operations and its principal activities, unless this is disclosed in the business review (or similar statement) accompanying the financial statements.

Presentation of information not required by this FRS

3.25 This FRS does not address presentation of **interim financial reports**. An entity that prepares such reports shall describe the basis for preparing and presenting the information. **FRS 104** sets out a basis for the preparation and presentation of interim financial reports that an entity may apply.

Section 4
Statement of Financial Position

Scope of this section

4.1 An entity shall present its **financial position** at the end of the **reporting period**. This section sets out the information that shall be presented in a **statement of financial position** and how to present it. The statement of financial position (which is referred to as the balance sheet in the **Act**) presents an entity's **assets, liabilities** and **equity** at the end of the reporting period. This section applies to all entities, whether or not they report under the Act. Entities that do not report under the Act shall comply with the requirements of this section, and with the **Regulations** (or, where applicable, the **LLP Regulations**) where referred to in this section, except to the extent that these requirements are not permitted by any statutory framework under which such entities report.

4.1A A **small entity** applying Section 1A *Small Entities* is not required to comply with this section.

Information to be presented in the statement of financial position

4.2 An entity shall present a statement of financial position in accordance with one of the following requirements for a balance sheet:

(a) Part 1 *General Rules and Formats* of Schedule 1 to the Regulations.

(b) Part 1 *General Rules and Formats* of Schedule 2 to the Regulations.

(c) Part 1 *General Rules and Formats* of Schedule 3 to the Regulations.

(d) Part 1 *General Rules and Formats* of Schedule 1 to the LLP Regulations.

The consolidated statement of financial position of a **group** shall be presented in accordance with the requirements for a consolidated balance sheet in Schedule 6 to the Regulations or Schedule 3 to the LLP Regulations.

4.2A An entity choosing to apply paragraph 1A(1) of Schedule 1 to the Regulations and adapt one of the balance sheet formats shall, as a minimum, include in its statement of financial position line items that present the following, distinguishing between those items that are **current** and those that are **non-current**:

(a) **property, plant and equipment**;

(b) **investment property** carried at **fair value** through **profit or loss**;

(c) **intangible assets**;

(d) **financial assets** (excluding amounts shown under (e), (f), (j) and (k));

(e) investments in **associates**;

(f) investments in **jointly controlled entities**;

(g) **biological assets** carried at cost less accumulated **depreciation** and impairment;

(h) biological assets carried at fair value through profit or loss;

(i) **inventories**;

(j) trade and other receivables;

(k) **cash** and **cash equivalents**;

(l) trade and other payables;

(m) **provisions**;

(n) **financial liabilities** (excluding amounts shown under (l) and (m));

(o) liabilities and assets for **current tax**;

(p) **deferred tax liabilities** and **deferred tax assets** (classified as non-current);

(q) **non-controlling interest**, presented within equity separately from the equity attributable to the **owners** of the **parent**; and

(r) equity attributable to the owners of the parent.

4.2B An entity choosing to apply paragraph 1A(1) of Schedule 1 to the Regulations shall also disclose, either in the statement of financial position or in the **notes**, the following sub-classifications of the line items presented:

(a) property, plant and equipment in classifications appropriate to the entity;

(b) intangible assets and **goodwill** in classifications appropriate to the entity;

(c) investments, showing separately shares and loans;

(d) trade and other receivables showing separately amounts due from **related parties**, amounts due from other parties, prepayments and receivables arising from accrued income not yet billed;

(e) inventories, showing separately amounts of inventories:

  (i) held for sale in the ordinary course of **business**;

  (ii) in the process of production for such sale; and

  (iii) in the form of materials or supplies to be consumed in the production process or in the rendering of services.

(f) trade and other payables, showing separately amounts payable to trade suppliers, payable to related parties, deferred income and accruals; and

(g) classes of equity, such as share capital, share premium, retained earnings, revaluation reserve, fair value reserve and other reserves.

4.2C The descriptions used in paragraphs 4.2A and 4.2B, and the ordering of items or aggregation of similar items, may be amended according to the nature of the entity and its transactions, to provide information that is relevant to an understanding of the entity's financial position, providing the information given is at least equivalent to that required by the balance sheet format had it not been adapted.

4.2D In order to comply with the requirement to distinguish between those items that are current and those that are non-current an entity shall present current and **non-current assets**, and current and **non-current liabilities**, as separate classifications in its statement of financial position.

4.3 An entity shall present additional line items, headings and subtotals in the statement of financial position when such presentation is relevant to an understanding of the entity's financial position.

Debtors due after more than one year

4.4 [Deleted]

4.4A Unless an entity chooses to apply paragraph 1A(1) of Schedule 1 to the Regulations, in instances where the amount of debtors due after more than one year is so **material** in the context of the total net current assets that in the absence of disclosure of the debtors due after more than one year on the face of the statement of financial position readers may misinterpret the **financial statements**, the amount should be disclosed on the face of the statement of financial position within **current assets**. In most cases it will be satisfactory to disclose the amount due after more than one year in the notes to the financial statements.

4.5 [Deleted]

4.6 [Deleted]

Creditors: amounts falling due within one year

4.7 Unless an entity chooses to apply paragraph 1A(1) of Schedule 1 to the Regulations, an entity shall classify a creditor as due within one year when the entity does not have an unconditional right, at the end of the reporting period, to defer settlement of the creditor for at least 12 months after the **reporting date**. For example, this would be the case if the earliest date on which the lender, exercising all available options and rights, could require repayment or (as the case may be) payment was within 12 months after the reporting date.

4.8 [Deleted]

Information to be presented either in the statement of financial position or in the notes

4.9–4.11 [Deleted]

4.12 An entity with share capital shall disclose the following, either in the statement of financial position or in the notes:

(a) For each class of share capital:

(i) [Deleted]

(ii) The number of shares issued and fully paid, and issued but not fully paid.

(iii) Par value per share, or that the shares have no par value.

(iv) [Deleted]

(v) The rights, preferences and restrictions attaching to that class including restrictions on the distribution of dividends and the repayment of capital.

(vi) Shares in the entity held by the entity or by its **subsidiaries**, associates, or **joint ventures**.

(vii) Shares reserved for issue under options and contracts for the sale of shares, including the terms and amounts.

(b) A description of each reserve within equity.

4.13 An entity without share capital, such as a partnership or trust, shall disclose information equivalent to that required by paragraph 4.12(a), showing changes during the period in each category of equity, and the rights, preferences and restrictions attaching to each category of equity.

Information to be presented in the notes

4.14 If, at the reporting date, an entity has a binding sale agreement for a major disposal of assets, or a **disposal group**, the entity shall disclose the following information:

(a) a description of the asset(s) or the disposal group;

(b) a description of the facts and circumstances of the sale; and

(c) the **carrying amount** of the assets or, for a disposal group, the carrying amounts of the underlying assets and liabilities.

Section 5
Statement of Comprehensive Income and Income Statement

Scope of this section

5.1 An entity shall present its **total comprehensive income** for a **reporting period** – ie its financial **performance** for the reporting period – in one or two statements. This section sets out the information that shall be presented in those statements and how to present it. This section applies to all entities, whether or not they report under the **Act**. Entities that do not report under the Act should comply with the requirements of this section, and with the **Regulations** (or, where applicable, the **LLP Regulations**) where referred to in this section, except to the extent that these requirements are not permitted by any statutory framework under which such entities report. If an entity meets specified conditions and chooses to do so, it may present a **statement of income and retained earnings** as set out in Section 6 *Statement of Change in Equity and Statement of Income and Retained Earnings*.

5.1A A **small entity** applying Section 1A *Small Entities* is not required to comply with this section.

Presentation of total comprehensive income

5.2 An entity shall present its total comprehensive income for a period either:

(a) in a single **statement of comprehensive income**, in which case the statement of comprehensive income presents all items of **income** and **expense** recognised in the period; or

(b) in two statements – an **income statement** (which is referred to as the profit and loss account in the Act) and a statement of comprehensive income – in which case the income statement presents all items of income and expense recognised in the period except those that are recognised in total comprehensive income outside **profit or loss** as permitted or required by this FRS.

5.3 A change from the single-statement approach to the two-statement approach, or vice versa, is a change in **accounting policy** to which Section 10 *Accounting Policies, Estimates and Errors* applies.

Single-statement approach

5.4 [Deleted]

5.5 An entity shall present, in the statement of comprehensive income, the items to be included in a profit and loss account in accordance with one of the following requirements:

(a) Part 1 *General Rules and Formats* of Schedule 1 to the Regulations;

(b) Part 1 *General Rules and Formats* of Schedule 2 to the Regulations;

(c) Part 1 *General Rules and Formats* of Schedule 3 to the Regulations; or

(d) Part 1 *General Rules and Formats* of Schedule 1 to the LLP Regulations.

The consolidated statement of comprehensive income of a **group** shall be presented in accordance with the requirements for a consolidated profit and loss account of Schedule 6 to the Regulations or Schedule 3 to the LLP Regulations.

5.5A In addition an entity shall include, in the statement of comprehensive income, line items that present the following amounts for the period:

(a) Classified by nature (excluding amounts in (b)), the components of **other comprehensive income** recognised as part of total comprehensive income outside profit or loss as permitted or required by this FRS. An entity may present the components of other comprehensive income either:

(i) net of related tax effects; or

(ii) before the related tax effects with one amount shown for the aggregate amount of **income tax** relating to those components.

(b) Its share of the other comprehensive income of **associates** and **jointly controlled entities** accounted for by the equity method.

(c) Total comprehensive income.

5.5B An entity choosing to apply paragraph 1A(2) of Schedule 1 to the Regulations and adapt one of the profit and loss account formats shall, as a minimum, include in its statement of comprehensive income line items that present the following amounts for the period:

(a) **revenue**;

(b) finance costs;

(c) share of the profit or loss of investments in associates (see Section 14 *Investments in Associates*) and jointly controlled entities (see Section 15 *Investments in Joint Ventures*) accounted for using the equity method;

(d) profit or loss before taxation;

(e) **tax expense** excluding tax allocated to items (h) and (i) below or to **equity** (see paragraph 29.27);

(f) as set out in paragraph 5.7E (including a column identified as **discontinued operations**) a single amount comprising the total of:

(i) the post-tax profit or loss of a discontinued operation; and

(ii) the post-tax gain or loss attributable to the impairment or on the disposal of the **assets** or **disposal group(s)** constituting discontinued operations.

(g) profit or loss;

(h) each item of other comprehensive income classified by nature (excluding amounts in (i));

(i) share of other comprehensive income of associates and jointly controlled entities accounted for by the equity method; and

(j) total comprehensive income.

In addition, an analysis of expenses shall be presented, either in the income statement or in the **notes** to the **financial statements**, which is equivalent to what would have been presented if paragraph 5.5 had been applied.

5.5C An entity may include additional line items in the income statement and amend the descriptions used in paragraph 5.5B, and the ordering of items, when this is necessary to explain the elements of financial performance, providing the information given is at least equivalent to that required by the profit and loss account format had it not been adapted.

5.6 An entity shall present the following items as allocations of profit or loss and other comprehensive income in the statement of comprehensive income for the period:

(a) Profit or loss for the period attributable to:

(i) **non-controlling interest**; and

(ii) **owners** of the **parent**.

(b) Total comprehensive income for the period attributable to:

(i) non-controlling interest; and

(ii) owners of the parent.

Two-statement approach

5.7 Under the two-statement approach, an entity shall present in an income statement, the items to be included in a profit and loss account in accordance with one of the following requirements:

(a) Part 1 *General Rules and Formats* of Schedule 1 to the Regulations;

(b) Part 1 *General Rules and Formats* of Schedule 2 to the Regulations;

(c) Part 1 *General Rules and Formats* of Schedule 3 to the Regulations; or

(d) Part 1 *General Rules and Formats* of Schedule 1 to the LLP Regulations.

The consolidated income statement of a group shall be presented in accordance with the requirements for a consolidated profit and loss account of Schedule 6 to the Regulations or Schedule 3 to the LLP Regulations.

5.7A An entity choosing to apply paragraph 1A(2) of Schedule 1 to the Regulations and adapt one of the profit and loss account formats shall, as a minimum, include in its income statement line items that present the amounts in paragraphs 5.5B(a) to 5.5B(g), with profit or loss as the last line. The statement of comprehensive income shall begin with profit or loss as its first line and shall display, as a minimum, line items that present the amounts in paragraphs 5.5B(h) to 5.5B(j) and paragraph 5.6(b) for the period, with total comprehensive income as the last line.

5.7B If an entity presents profit or loss in an income statement, it shall present the information required in paragraph 5.6(a) in that statement.

5.7C The statement of comprehensive income shall begin with profit or loss as its first line and shall display, as a minimum, line items that present the amounts in paragraphs 5.5A and 5.6(b) for the period.

Requirements applicable to both approaches

5.7D In addition to the requirements of paragraphs 5.5 or 5.7, as a minimum, **turnover** must be presented on the face of the income statement (or statement of comprehensive income if presented).

5.7E An entity shall also disclose on the face of the income statement (or statement of comprehensive income if presented) an amount comprising the total of:

(a) the post-tax profit or loss of discontinued operations; and

(b) the post-tax gain or loss attributable to the impairment or on the disposal of the assets or disposal group(s) constituting discontinued operations.

A line-by-line analysis shall be presented in the income statement (or statement of comprehensive income if presented), in a column identified as relating to discontinued operations, ie separately from continuing operations; a total column shall also be presented.

5.7F An entity shall re-present the disclosures in paragraph 5.7E for prior periods presented in the financial statements so that the disclosures relate to all operations that have been discontinued by the end of the reporting period for the latest period presented.

5.8 An entity shall recognise all items of income or expense in a period in profit or loss unless an FRS requires or permits otherwise, or unless prohibited by the Act. For example, under this FRS, the effects of corrections of **material errors** and changes in accounting policies are presented as retrospective adjustments of prior periods rather than as part of profit or loss in the period in which they arise (see Section 10).

5.9 An entity shall present additional line items, headings and subtotals in the statement of comprehensive income (and in the income statement, if presented), when such presentation is relevant to an understanding of the entity's financial performance.

* 5.9A When items included in total comprehensive income are material, an entity shall disclose their nature and amount separately, in the statement of comprehensive income (and in the income statement, if presented) or in the notes.

5.9B This FRS does not require disclosure of 'operating profit'. However, if an entity elects to disclose operating profit the entity should ensure that the amount disclosed is representative of activities that would normally be regarded as 'operating'. For example, it would be inappropriate to exclude items clearly related to operations (such as **inventory** write-downs, profits or losses on the sale of **property, plant and equipment, investment property** and **intangible assets**, and **restructuring** and relocation expenses) because they occur irregularly or infrequently or are unusual in amount. Similarly, it would be inappropriate to exclude items on the grounds that they do not involve **cash flows**, such as **depreciation** and **amortisation** expenses. Profits or losses on the disposal of a discontinued operation shall be excluded from operating profit.

Ordinary activities and extraordinary items

5.10 An entity applying paragraph 5.5(a), 5.5(d), 5.7(a) or 5.7(d) shall not present or describe any items of income or expense as 'extraordinary items' in the statement of comprehensive income (or in the income statement, if presented) or in the notes.

Paragraphs 5.10A and 5.10B apply to entities applying paragraphs 5.5(b), 5.5(c), 5.7(b) or 5.7(c).

5.10A Ordinary activities are any activities which are undertaken by a reporting entity as part of its **business** and such related activities in which the reporting entity engages in furtherance of, incidental to, or arising from, these activities. Ordinary activities include any effects on the reporting entity of any event in the various environments in which it operates, including the political, regulatory, economic and geographical environments, irrespective of the frequency or unusual nature of the events.

5.10B Extraordinary items are material items possessing a high degree of abnormality which arise from events or transactions that fall outside the ordinary activities of the reporting entity and which are not expected to recur. The additional line items required to be presented by paragraph 5.9 and material items required to be disclosed by paragraph 5.9A, are not extraordinary items when they arise from the ordinary activities of the entity. Extraordinary items do not include prior period items merely because they relate to a prior period.

5.11 [Deleted]

Appendix to Section 5
Statement of Comprehensive Income and Income Statement

This appendix accompanies, but is not part of, Section 5. It provides guidance on applying the requirements of Section 5 paragraph 5.7E for presenting discontinued operations. The example illustrates the presentation of comprehensive income in a single statement and the classification of expenses within profit by function. A columnar format is used in order to present a single line item as required by paragraph 5.7E, while still complying with the requirements of the Act to show totals for items such as turnover, profit or loss before taxation and tax.

Statement of comprehensive income

for the year ended 31 December 20X1

	20X1			20X0		
	Continuing operations	**Discontinued operations**	**Total**	Continuing operations (as restated)	Discontinued operations (as restated)	Total
	CU	**CU**	**CU**	CU	CU	CU
Turnover	**4,200**	**1,232**	**5,432**	3,201	1,500	4,701
Cost of Sales	**(2,591)**	**(1,104)**	**(3,695)**	(2,281)	(1,430)	(3,711)
Gross profit	**1,609**	**128**	**1,737**	920	70	990
Administrative expenses	**(452)**	**(110)**	**(562)**	(418)	(120)	(538)
Other operating income	**212**	**–**	**212**	198	–	198
Operating profit	**1,369**	**18**	**1,387**	700	(50)	650
Profit on disposal of operations	**–**	**301**	**301**	–	–	–
Interest receivable and similar income	**14**	**–**	**14**	16	–	16
Interest payable and similar expenses	**(208)**	**–**	**(208)**	(208)	–	(208)
Profit before tax	**1,175**	**319**	**1,494**	508	(50)	458
Tax on profit or loss	**(390)**	**(4)**	**(394)**	(261)	3	(258)
Profit/(loss) after tax and profit/(loss) for the financial year	**785**	**315**	**1,100**	247	(47)	200
Other comprehensive income						
Actuarial losses on defined benefit pension plans			**(108)**			(68)
Deferred tax movement relating to actuarial losses			**28**			18
Total comprehensive income for the year			**1,020**			150

Section 6
Statement of Changes in Equity and Statement of Income and Retained Earnings

Scope of this section

6.1 An entity shall present its changes in **equity** for a **reporting period**. This section sets out the information that shall be presented in a statement of changes in equity or, if specified conditions are met and an entity chooses, in a **statement of income and retained earnings**.

6.1A A **small entity** applying Section 1A *Small Entities* is not required to comply with this section. However, paragraph 1A.9 encourages a small entity to present a statement of changes in equity or a statement of income and retained earnings.

Statement of changes in equity

Purpose

6.2 The statement of changes in equity presents an entity's **profit or loss** for a reporting period, **other comprehensive income** for the period, the effects of changes in **accounting policies** and corrections of **material errors** recognised in the period, and the amounts of investments by, and dividends and other distributions to, equity investors during the period.

Information to be presented in the statement of changes in equity

6.3 An entity shall present a statement of changes in equity showing in the statement:

(a) **total comprehensive income** for the period, showing separately the total amounts attributable to **owners** of the **parent** and to **non-controlling interests**;

(b) for each component of equity, the effects of **retrospective application** or retrospective restatement recognised in accordance with Section 10 *Accounting Policies, Estimates and Errors*; and

* (c) for each component of equity, a reconciliation between the **carrying amount** at the beginning and the end of the period, separately disclosing changes resulting from:

    (i) profit or loss;

    (ii) other comprehensive income; and

    (iii) the amounts of investments by, and dividends and other distributions to, owners, showing separately issues of shares, purchase of own share transactions, dividends and other distributions to owners, and changes in ownership interests in **subsidiaries** that do not result in a loss of **control**.

Information to be presented in the statement of changes in equity or in the notes

* 6.3A For each component of equity, an entity shall present, either in the statement of changes in equity or in the **notes**, an analysis of other comprehensive income by item (see paragraph 6.3(c)(ii)).

Statement of income and retained earnings

Purpose

6.4 The statement of income and retained earnings presents an entity's profit or loss and changes in retained earnings for a reporting period. Paragraph 3.18 permits an entity to present a statement of income and retained earnings in place of a **statement of comprehensive income** and a statement of changes in equity if the only changes to its equity during the periods for which **financial statements** are presented arise from profit or loss, payment of dividends, corrections of prior period material errors, and changes in accounting policy.

Information to be presented in the statement of income and retained earnings

6.5 An entity shall present, in the statement of income and retained earnings, the following items in addition to the information required by Section 5 *Statement of Comprehensive Income and Income Statement*:

(a) retained earnings at the beginning of the reporting period;

(b) dividends declared and paid or payable during the period;

(c) restatements of retained earnings for corrections of prior period material errors;

(d) restatements of retained earnings for changes in accounting policy; and

(e) retained earnings at the end of the reporting period.

Section 7
Statement of Cash Flows

Scope of this section

7.1 This section sets out the information that is to be presented in a **statement of cash flows** and how to present it. The statement of cash flows provides information about the changes in **cash** and **cash equivalents** of an entity for a **reporting period**, showing separately changes from **operating activities, investing activities** and **financing activities**.

7.1A This section and paragraph 3.17(d) do not apply to:

(a) mutual life assurance companies;

(b) **retirement benefit plans**; or

(c) investment funds that meet all the following conditions:

(i) substantially all of the entity's investments are highly liquid;

(ii) substantially all of the entity's investments are carried at market value; and

(iii) the entity provides a statement of changes in net assets.

7.1B A **small entity** is not required to comply with this section.

Cash equivalents

7.2 Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and that are subject to an insignificant risk of changes in value. Therefore, an investment normally qualifies as a cash equivalent only when it has a short maturity of, say, three months or less from the date of acquisition. Bank overdrafts are normally considered financing activities similar to borrowings. However, if they are repayable on demand and form an integral part of an entity's cash management, bank overdrafts are a component of cash and cash equivalents.

Information to be presented in the statement of cash flows

7.3 An entity shall present a statement of cash flows that presents **cash flows** for a reporting period classified by operating activities, investing activities and financing activities.

Operating activities

7.4 Operating activities are the principal revenue-producing activities of the entity. Therefore, cash flows from operating activities generally result from the transactions and other events and conditions that enter into the determination of **profit or loss**. Examples of cash flows from operating activities are:

(a) cash receipts from the sale of goods and the rendering of services;

(b) cash receipts from royalties, fees, commissions and other **revenue**;

(c) cash payments to suppliers for goods and services;

(d) cash payments to and on behalf of employees;

(e) cash payments or refunds of **income tax**, unless they can be specifically identified with financing and investing activities;

(f) cash receipts and payments from investments, loans and other contracts held for dealing or trading purposes, which are similar to **inventory** acquired specifically for resale; and

(g) cash advances and loans made to other parties by **financial institutions**.

Some transactions, such as the sale of an item of plant by a manufacturing entity, may give rise to a **gain** or loss that is included in profit or loss. However, the cash flows relating to such transactions are cash flows from investing activities.

Investing activities

7.5 Investing activities are the acquisition and disposal of long-term **assets** and other investments not included in cash equivalents. Examples of cash flows arising from investing activities are:

(a) cash payments to acquire **property, plant and equipment** (including self-constructed property, plant and equipment), **intangible assets** and other long-term assets. These payments include those relating to capitalised **development** costs and self-constructed property, plant and equipment;

(b) cash receipts from sales of property, plant and equipment, intangibles and other long-term assets;

(c) cash payments to acquire equity or debt instruments of other entities and interests in **joint ventures**, including the net cash flows arising from obtaining **control** of **subsidiaries** or other businesses (other than payments for those instruments classified as cash equivalents or held for dealing or trading);

(d) cash receipts from sales of equity or debt instruments of other entities and interests in joint ventures, including the net cash flows arising from losing control of subsidiaries or other businesses (other than receipts for those instruments classified as cash equivalents or held for dealing or trading);

(e) cash advances and loans made to other parties (except those made by financial institutions – see paragraph 7.4(g));

(f) cash receipts from the repayment of advances and loans made to other parties;

(g) cash payments for futures contracts, forward contracts, option contracts and swap contracts, except when the contracts are held for dealing or trading, or the payments are classified as financing activities; and

(h) cash receipts from futures contracts, forward contracts, option contracts and swap contracts, except when the contracts are held for dealing or trading, or the receipts are classified as financing activities.

When a contract is accounted for as a hedge (see Section 12 *Other Financial Instruments Issues*), an entity shall classify the cash flows of the contract in the same manner as the cash flows of the item being hedged.

Financing activities

7.6 Financing activities are activities that result in changes in the size and composition of the contributed **equity** and borrowings of an entity. Examples of cash flows arising from financing activities are:

(a) cash proceeds from issuing shares or other equity instruments;

(b) cash payments to **owners** to acquire or redeem the entity's shares;

(c) cash proceeds from issuing debentures, loans, notes, bonds, mortgages and other short-term or long-term borrowings;

(d) cash repayments of amounts borrowed; and

(e) cash payments by a lessee for the reduction of the outstanding **liability** relating to a **finance lease**.

Reporting cash flows from operating activities

7.7 An entity shall present cash flows from operating activities using either:

(a) the indirect method, whereby a measure of profit or loss disclosed in the **statement of comprehensive income** (or separate **income statement** if presented) is adjusted for the effects of non-cash transactions, any deferrals or accruals of past or future operating cash receipts or payments, and items of **income** or **expense** associated with investing or financing cash flows; or

(b) the direct method, whereby major classes of gross cash receipts and gross cash payments are disclosed.

Indirect method

7.8 Under the indirect method, an entity shall present a reconciliation determining the net cash flow from operating activities by adjusting a measure of profit or loss disclosed in the statement of comprehensive income (or separate income statement if presented) for the effects of:

(a) changes during the period in inventories and operating receivables and payables;

(b) non-cash items such as **depreciation**, **provisions**, **deferred tax**, accrued income (expenses) not yet received (paid) in cash, unrealised foreign currency **gains** and losses, undistributed profits of **associates**, and **non-controlling interests**; and

(c) all other items for which the cash effects relate to investing or financing.

Direct method

7.9 Under the direct method, net cash flow from operating activities is presented by disclosing information about major classes of gross cash receipts and gross cash payments. Such information may be obtained either:

(a) from the accounting records of the entity; or

(b) by adjusting sales, cost of sales and other items in the statement of comprehensive income (or the income statement, if presented) for:

  (i) changes during the period in inventories and operating receivables and payables;

  (ii) other non-cash items; and

  (iii) other items for which the cash effects are investing or financing cash flows.

Reporting cash flows from investing and financing activities

7.10 An entity shall present separately major classes of gross cash receipts and gross cash payments arising from investing and financing activities, except to the extent that net presentation is permitted by paragraphs 7.10A to 7.10E. The aggregate cash flows arising from acquisitions and from disposals of subsidiaries or other business units shall be presented separately and classified as investing activities.

Reporting cash flows on a net basis

7.10A Cash flows arising from the following operating, investing or financing activities may be reported on a net basis:

(a) cash receipts and payments on behalf of customers when the cash flows reflect the activities of the customer rather than those of the entity; and

(b) cash receipts and payments for items in which the turnover is quick, the amounts are large, and the maturities are short.

7.10B Examples of cash receipts and payments referred to in paragraph 7.10A(a) are:

(a) the acceptance and repayment of demand deposits of a bank;

(b) funds held for customers by an investment entity; and

(c) rents collected on behalf of, and paid over to, the owners of properties.

7.10C Examples of cash receipts and payments referred to in paragraph 7.10A(b) are advances made for, and the repayment of:

(a) principal amounts relating to credit card customers;

(b) the purchase and sale of investments; and

(c) other short-term borrowings, for example, those which have a maturity period of three months or less.

7.10D Financial institutions may report cash flows described in paragraph 34.33 on a net basis.

7.10E A financial institution that undertakes the business of effecting or carrying out **insurance contracts**, other than mutual life assurance companies scoped out of this section in paragraph 7.1A(a), should include the cash flows of their long-term business only to the extent of cash transferred and available to meet the obligations of the company or **group** as a whole.

Foreign currency cash flows

7.11 An entity shall record cash flows arising from transactions in a foreign currency in the entity's **functional currency** by applying to the foreign currency amount the exchange rate between the functional currency and the foreign currency at the date of the cash flow or an exchange rate that approximates the actual rate (for example, a weighted average exchange rate for the period).

7.12 An entity shall translate cash flows of a foreign subsidiary at the exchange rate between the group's **presentation currency** and the foreign currency of the subsidiary at the date of the cash flow or at an exchange rate that approximates the actual rate (for example, a weighted average exchange rate for the period).

7.13 Unrealised gains and losses arising from changes in foreign currency exchange rates are not cash flows. However, to reconcile cash and cash equivalents at the beginning and the end of the period, the effect of exchange rate changes on cash and cash equivalents held or due in a foreign currency must be presented in the statement of cash flows. Therefore, the entity shall remeasure cash and cash equivalents held during the reporting period (such as amounts of foreign currency held and foreign currency bank accounts) at period-end exchange rates. The entity shall present the resulting unrealised gain or loss separately from cash flows from operating, investing and financing activities.

Interest and dividends

7.14 An entity shall present separately cash flows from interest and dividends received and paid. The entity shall classify these cash flows consistently from period to period as operating, investing or financing activities.

7.15 An entity may classify interest paid and interest and dividends received as operating cash flows because they are included in profit or loss. Alternatively, the entity may classify interest paid and interest and dividends received as financing cash flows and investing cash flows respectively, because they are costs of obtaining financial resources or returns on investments.

7.16 An entity may classify dividends paid as a financing cash flow because they are a cost of obtaining financial resources. Alternatively, the entity may classify dividends paid as a component of cash flows from operating activities because they are paid out of operating cash flows.

Income tax

7.17 An entity shall present separately cash flows arising from income tax and shall classify them as cash flows from operating activities unless they can be specifically identified with financing and investing activities. When tax cash flows are allocated over more than one class of activity, the entity shall disclose the total amount of taxes paid.

Non-cash transactions

7.18 An entity shall exclude from the statement of cash flows investing and financing transactions that do not require the use of cash or cash equivalents. An entity shall disclose such transactions elsewhere in the **financial statements** in a way that provides all the relevant information about those investing and financing activities.

7.19 Many investing and financing activities do not have a direct impact on current cash flows even though they affect the capital and asset structure of an entity. The exclusion of non-cash transactions from the statement of cash flows is consistent with the objective of a statement of cash flows because these items do not involve cash flows in the current period. Examples of non-cash transactions are:

(a) the acquisition of assets either by assuming directly related liabilities or by means of a finance lease;

(b) the acquisition of an entity by means of an equity issue; and

(c) the conversion of debt to equity.

Components of cash and cash equivalents

7.20 An entity shall present the components of cash and cash equivalents and shall present a reconciliation of the amounts presented in the statement of cash flows to the equivalent items presented in the **statement of financial position**. However, an entity is not required to present this reconciliation if the amount of cash and cash equivalents presented in the statement of cash flows is identical to the amount similarly described in the statement of financial position.

7.20A Entities applying Part 1 *General Rules and Formats* of Schedule 2 to the **Regulations** should include as cash, only cash and balances at central banks and loans and advances to banks repayable on demand.

Other disclosures

7.21 An entity shall disclose, together with a commentary by management, the amount of significant cash and cash equivalent balances held by the entity that are not available for use by the entity. Cash and cash equivalents held by an entity may not be available for use by the entity because of, among other reasons, foreign exchange controls or legal restrictions.

7.22 An entity shall disclose an analysis of changes in **net debt** from the beginning to the end of the reporting period showing changes resulting from:

(a) the cash flows of the entity;

(b) the acquisition and disposal of subsidiaries;

(c) new finance leases entered into;

(d) other non-cash changes; and

(e) the recognition of changes in market value and exchange rate movements.

When several balances (or parts thereof) from the statement of financial position have been combined to form the components of opening and closing net debt, sufficient detail shall be shown to enable users to identify these balances.

This analysis need not be presented for prior periods.

Section 8
Notes to the Financial Statements

Scope of this section

8.1 An entity shall present **notes** to its **financial statements**. This section sets out the principles underlying the information that shall be presented in the notes and how to present it. Notes contain information in addition to that presented in the **statement of financial position**, **statement of comprehensive income** (if presented), **income statement** (if presented), combined **statement of income and retained earnings** (if presented), **statement of changes in equity** (if presented), and **statement of cash flows** (if presented). Notes provide narrative descriptions or disaggregations of items presented in those statements and information about items that do not qualify for **recognition** in those statements. In addition to the requirements of this section, nearly every other section of this FRS requires disclosures that are normally presented in the notes.

Structure of the notes

8.2 The notes shall:

(a) present information about the basis of preparation of the financial statements and the specific **accounting policies** used, in accordance with paragraphs 8.5 to 8.7;

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

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

* 8.3 An entity shall, as far as practicable, present the notes in a systematic manner. An entity shall cross-reference each item in the financial statements to any related information in the notes.

* 8.4 An entity normally[38] presents the notes in the following order:

(a) a statement that the financial statements have been prepared in compliance with this FRS (see paragraph 3.3);

(b) a summary of significant accounting policies applied (see paragraph 8.5);

(c) supporting information for items presented in the financial statements, in the sequence in which each statement and each line item is presented; and

(d) any other disclosures.

Disclosure of accounting policies

* 8.5 An entity shall disclose its significant accounting policies comprising:

(a) the **measurement** basis (or bases) used in preparing the financial statements; and

[38] Company law requires the notes to be presented in the order in which, where relevant, the items to which they relate are presented in the statement of financial position and in the income statement.

(b) the other accounting policies used that are relevant to an understanding of the financial statements.

Information about judgements

* 8.6 An entity shall disclose, along with its significant accounting policies or other notes, the judgements, apart from those involving estimations (see paragraph 8.7), 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.

Information about key sources of estimation uncertainty

8.7 An entity shall disclose in the notes information about the key assumptions concerning the future, and other key sources of estimation uncertainty at the **reporting date**, that have a significant risk of causing 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**.

Section 9
Consolidated and Separate Financial Statements

Scope of this section

9.1 This section applies to **parents** that present **consolidated financial statements** (which are referred to as group accounts in the **Act**) intended to give a true and fair view of the **financial position** and **profit or loss** (or **income and expenditure**) of their **group**, whether or not they report under the Act. Parents that do not report under the Act shall comply with the requirements of this section, and of the Act where referred to in this section, unless consolidated financial statements are not required and except to the extent that these requirements are not permitted by any statutory framework under which such entities report. This section also includes requirements for **individual financial statements** and **separate financial statements.**

Requirement to present consolidated financial statements

9.2 Except as permitted or required by paragraph 9.3, a parent entity shall present consolidated financial statements in which it consolidates all its investments in **subsidiaries** in accordance with this FRS. A parent entity need only prepare consolidated accounts under the Act if it is a parent at the year end.

9.3 A parent is exempt from the requirement to prepare consolidated financial statements on any one of the following grounds:

For an entity reporting under the Act, when its immediate parent is established under the law of any part of the UK[39] or for an entity reporting under the *Companies Act 2014*, when its immediate parent is established under the law of an EEA State[40]:

(a) The parent is a wholly-owned subsidiary. Exemption is conditional on compliance with certain further conditions set out in company law.

(b) The immediate parent holds 90% or more of the allotted shares in the entity and the remaining shareholders have approved the exemption. Exemption is conditional on compliance with certain further conditions set out in company law.

(bA) The immediate parent holds more than 50% (but less than 90%) of the allotted shares in the entity, and notice requesting the preparation of consolidated financial statements has not been served on the entity by shareholders holding in aggregate at least 5% of the allotted shares in the entity. Exemption is conditional on compliance with certain further conditions set out in company law.

For an entity reporting under the Act, when its parent is not established under the law of any part of the UK[41] or for an entity reporting under the *Companies Act 2014*, when its parent is not established under the law of an EEA State[42]:

(c) The parent is a wholly-owned subsidiary. Exemption is conditional on compliance with certain further conditions set out in company law.

(d) The parent holds 90% or more of the allotted shares in the entity and the remaining shareholders have approved the exemption. Exemption is conditional on compliance with certain further conditions set out in company law.

[39] Section 400 of the Act.
[40] Section 299 of the *Companies Act 2014.*
[41] Section 401 of the Act.
[42] Section 300 of the *Companies Act 2014.*

(dA) The parent holds more than 50% (but less than 90%) of the allotted shares in the entity, and notice requesting the preparation of consolidated financial statements has not been served on the entity by shareholders holding in aggregate at least 5% of the allotted shares in the entity. Exemption is conditional on compliance with certain further conditions set out in company law.

Other situations

(e) The parent, and the group headed by it, qualify as small[43] and the parent and the group are considered eligible for the exemption[44].

(f) All of the parent's subsidiaries are required to be excluded from consolidation by paragraph 9.9.[45]

(g) For a parent not reporting under the Act, if its statutory framework does not require the preparation of consolidated financial statements.

In sub-paragraphs (a) to (dA), for an entity reporting under the Act, the parent is not exempt if any of its transferable securities are admitted to trading on a UK regulated market and for an entity reporting under the *Companies Act 2014*, the parent is not exempt if any of its transferable securities are admitted to trading on a regulated market of any EEA State within the meaning of Directive 2004/39/EC.

9.4 A subsidiary is an entity that is controlled by the parent. **Control** is the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

9.5 Control is presumed to exist when the parent owns, directly or indirectly through subsidiaries, more than half of the voting power of an entity. That presumption may be overcome in exceptional circumstances if it can be clearly demonstrated that such ownership does not constitute control. Control also exists when the parent owns half or less of the voting power of an entity but it has:

(a) power over more than half of the voting rights by virtue of an agreement with other investors;

(b) power to govern the financial and operating policies of the entity under a statute or an agreement;

(c) power to appoint or remove the majority of the members of the board of directors or equivalent governing body and control of the entity is by that board or body; or

(d) power to cast the majority of votes at meetings of the board of directors or equivalent governing body and control of the entity is by that board or body.

9.6 Control can also be achieved by having options or convertible instruments that are currently exercisable or by having an agent with the ability to direct the activities for the benefit of the controlling entity.

9.6A Control can also exist when the parent has the power to exercise, or actually exercises, dominant influence or control over the undertaking or it and the undertaking are managed on a unified basis.

9.7 [Deleted]

[43] UK entities shall refer to section 383 of the Act. Irish entities shall refer to section 280B of the *Companies Act 2014*.

[44] UK entities shall refer to sections 384 and 399(2A) of the Act. Irish entities shall refer to sections 280B and 293(1A) of the *Companies Act 2014*.

[45] UK entities shall refer to section 402 of the Act. Irish entities shall refer to section 301 of the *Companies Act 2014*.

9.8 A subsidiary is not excluded from consolidation because its business activities are dissimilar to those of the other entities within the consolidation. Relevant information is provided by consolidating such subsidiaries and disclosing additional information in the consolidated financial statements about the different business activities of subsidiaries.

9.8A A subsidiary is not excluded from consolidation because the information necessary for the preparation of consolidated financial statements cannot be obtained without disproportionate expense or undue delay, unless its inclusion is not **material** (individually or collectively for more than one subsidiary) for the purposes of giving a true and fair view in the context of the group.

9.9 A subsidiary shall be excluded from consolidation where:

(a) severe long-term restrictions substantially hinder the exercise of the rights of the parent over the **assets** or management of the subsidiary; or

(b) the interest in the subsidiary is **held exclusively with a view to subsequent resale**; and the subsidiary has not previously been consolidated in the consolidated financial statements prepared in accordance with this FRS.

9.9A A subsidiary may be excluded from consolidation when its inclusion is not material for the purpose of giving a true and fair view (but two or more subsidiaries may be excluded only if they are not material taken together).

9.9B A subsidiary excluded from consolidation on the grounds set out in paragraph 9.9(a) shall be measured using an **accounting policy** selected by the parent in accordance with paragraph 9.26, except where the parent still exercises a **significant influence** over the subsidiary. If this is the case, the parent should treat the subsidiary as an **associate** using the equity method set out in paragraph 14.8.

9.9C A subsidiary excluded from consolidation on the grounds set out in paragraph 9.9(b) which is:

(a) **held as part of an investment portfolio** shall be measured at **fair value** with changes in fair value recognised in profit or loss;[46] or

(b) not held as part of an investment portfolio shall be measured using an accounting policy selected by the parent in accordance with paragraph 9.26.

Special purpose entities

9.10 An entity may be created to accomplish a narrow objective (eg to effect a **lease**, undertake **research** and **development** activities, securitise **financial assets** or facilitate employee shareholdings under remuneration schemes, such as Employee Share Ownership Plans (ESOPs)). Such a special purpose entity (SPE) may take the form of a corporation, trust, partnership or unincorporated entity. Often, SPEs are created with legal arrangements that impose strict requirements over the operations of the SPE.

9.11 Except as permitted or required by paragraph 9.3, a parent entity shall prepare consolidated financial statements that include the entity and any SPEs that are controlled by that entity. In addition to the circumstances described in paragraph 9.5, the following circumstances may indicate that an entity controls an SPE (this is not an exhaustive list):

(a) the activities of the SPE are being conducted on behalf of the entity according to its specific business needs;

[46] Additional disclosures may need to be provided in accordance with company law (see Appendix III, paragraph A3.17).

(b) the entity has the ultimate decision-making powers over the activities of the SPE even if the day-to-day decisions have been delegated;

(c) the entity has rights to obtain the majority of the benefits of the SPE and therefore may be exposed to risks incidental to the activities of the SPE; and

(d) the entity retains the majority of the residual or ownership risks related to the SPE or its assets.

9.12 Paragraphs 9.10 and 9.11 do not apply to **post-employment benefit plans** or other long-term employee benefit plans to which Section 28 *Employee Benefits* applies. A special purpose entity that is an intermediate payment arrangement shall be accounted for in accordance with paragraphs 9.33 to 9.38.

Consolidation procedures

9.13 The consolidated financial statements present financial information about the group as a single economic entity. In preparing consolidated financial statements, an entity shall:

(a) combine the **financial statements** of the parent and its subsidiaries line by line by adding together like items of assets, **liabilities**, **equity**, **income** and **expenses**;

(b) eliminate the **carrying amount** of the parent's investment in each subsidiary and the parent's portion of equity of each subsidiary;

(c) measure and present **non-controlling interest** in the profit or loss of consolidated subsidiaries for the **reporting period** separately from the interest of the **owners** of the parent; and

(d) measure and present non-controlling interest in the net assets of consolidated subsidiaries separately from the parent shareholders' equity in them. Non-controlling interest in the net assets consists of:

(i) the non-controlling interest's share in the identifiable net assets (consisting of the identifiable assets, liabilities and **contingent liabilities** as recognised and measured in accordance with Section 19 *Business Combinations and Goodwill*, if any) at the date of the original combination; and

(ii) the non-controlling interest's share of changes in equity since the date of the combination or other acquisition.

9.14 The proportions of profit or loss and changes in equity allocated to the owners of the parent and to the non-controlling interest are determined on the basis of existing ownership interests and do not reflect the possible exercise or conversion of options or convertible instruments.

Intragroup balances and transactions

9.15 Intragroup balances and transactions, including income, expenses and dividends, are eliminated in full. Profits and losses resulting from intragroup transactions that are recognised in assets, such as **inventory** and **property, plant and equipment**, are eliminated in full. Intragroup losses may indicate an impairment that requires **recognition** in the consolidated financial statements (see Section 27 *Impairment of Assets*). Section 29 *Income Tax* applies to **timing differences** that arise from the elimination of profits and losses resulting from intragroup transactions.

Uniform reporting date and reporting period

9.16 The financial statements of the parent and its subsidiaries used in the preparation of the consolidated financial statements shall be prepared as of the same **reporting date**, and for the same reporting period, unless it is **impracticable** to do so. Where the reporting date and reporting period of a subsidiary are not the same as the parent's reporting date and reporting period, the consolidated financial statements must be made up:

(a) from the financial statements of the subsidiary as of its last reporting date before the parent's reporting date, adjusted for the effects of significant transactions or events that occur between the date of those financial statements and the date of the consolidated financial statements, provided that reporting date is no more than three months before that of the parent; or

(b) from interim financial statements prepared by the subsidiary as at the parent's reporting date.

Uniform accounting policies

9.17 Consolidated financial statements shall be prepared using uniform accounting policies for like transactions and other events and conditions in similar circumstances. If a member of the group uses accounting policies other than those adopted in the consolidated financial statements for like transactions and events in similar circumstances, appropriate adjustments are made to its financial statements in preparing the consolidated financial statements.

Acquisition and disposal of subsidiaries

9.18 The income and expenses of a subsidiary are included in the consolidated financial statements from the **acquisition date**, except when a **business combination** is accounted for by using the merger accounting method under Section 19 or, for certain **public benefit entity** combinations, Section 34 *Specialised Activities*. The income and expenses of a subsidiary are included in the consolidated financial statements until the date on which the parent ceases to control the subsidiary. A parent may cease to control a subsidiary with or without a change in absolute or relative ownership levels. This could occur, for example, when a subsidiary becomes subject to the control of a government, court, administrator or regulator.

Disposal – where control is lost

9.18A Where a parent ceases to control a subsidiary, a **gain** or loss is recognised in the consolidated **statement of comprehensive income** (or in the **income statement**, if presented) calculated as the difference between:

(a) the proceeds from the disposal (or the event that resulted in the loss of control); and

(b) the proportion of the carrying amount of the subsidiary's net assets, including any related **goodwill**, disposed of (or lost) as at the date of disposal (or date control is lost).

The cumulative amount of any exchange differences that relate to a foreign subsidiary recognised in equity in accordance with Section 30 *Foreign Currency Translation* is not recognised in profit or loss as part of the gain or loss on disposal of the subsidiary and shall be transferred directly to retained earnings.

9.18B The gain or loss arising on the disposal shall also include those amounts that have been recognised in **other comprehensive income** in relation to that subsidiary, where those amounts are required to be reclassified to profit or loss upon disposal in accordance with other sections of this FRS. Amounts that are not required to be reclassified to profit or loss upon disposal of the related assets or liabilities in accordance with other sections of this FRS shall be transferred directly to retained earnings.

9.19 If an entity ceases to be a subsidiary but the investor (former parent) continues to hold:

(a) an investment that is not an associate (see paragraph 9.19(b)) or a **jointly controlled entity** (see paragraph 9.19(c)), that investment shall be accounted for as a financial asset in accordance with Section 11 *Basic Financial Instruments* or Section 12 *Other Financial Instruments Issues* from the date the entity ceases to be a subsidiary;

(b) an associate, that associate shall be accounted for in accordance with Section 14 *Investments in Associates*; or

(c) a jointly controlled entity, that jointly controlled entity shall be accounted for in accordance with Section 15 *Investments in Joint Ventures*.

The carrying amount of the net assets (and goodwill) attributable to the investment at the date that the entity ceases to be a subsidiary shall be regarded as the cost on initial **measurement** of the financial asset, investment in associate or jointly controlled entity, as appropriate. In applying the equity method to investments in associate or jointly controlled entities as required in sub-paragraphs (b) and (c) above, paragraph 14.8(c) shall not be applied.

Disposal – where control is retained

9.19A Where a parent reduces its holding in a subsidiary and control is retained, it shall be accounted for as a transaction between equity holders and the resulting change in non-controlling interest shall be accounted for in accordance with paragraph 22.19. No gain or loss shall be recognised at the date of disposal.

Acquisition – Control achieved in stages

9.19B Where a parent acquires control of a subsidiary in stages, the transaction shall be accounted for in accordance with paragraphs 19.11A and 19.14 applied at the date control is achieved.

Acquisition – Increasing a controlling interest in a subsidiary

9.19C Where a parent increases its controlling interest in a subsidiary, the identifiable assets and liabilities and a **provision** for contingent liabilities of the subsidiary shall not be revalued to fair value and no additional goodwill shall be recognised at the date the controlling interest is increased.

9.19D The transaction shall be accounted for as a transaction between equity holders and the resulting change in non-controlling interest shall be accounted for in accordance with paragraph 22.19.

Non-controlling interest in subsidiaries

9.20 An entity shall present non-controlling interest in the consolidated **statement of financial position** within equity, separately from the equity of the owners of the parent.

9.21 An entity shall disclose non-controlling interest in the profit or loss of the group separately in the statement of comprehensive income (or income statement, if presented).

9.22 Profit or loss and each component of other comprehensive income shall be attributed to the owners of the parent and to non-controlling interest. **Total comprehensive income** shall be attributed to the owners of the parent and to non-controlling interest even if this results in non-controlling interest having a deficit balance.

Disclosures in consolidated financial statements

9.23 The following disclosures shall be made in consolidated financial statements:

(a) the fact that the statements are consolidated financial statements;

(b) the basis for concluding that control exists when the parent does not own, directly or indirectly through subsidiaries, more than half of the voting power;

(c) any difference in the reporting date of the financial statements of the parent and its subsidiaries used in the preparation of the consolidated financial statements;

(d) the nature and extent of any significant restrictions (eg resulting from borrowing arrangements or regulatory requirements) on the ability of subsidiaries to transfer funds to the parent in the form of cash dividends or to repay loans;

(e) the name of any subsidiary excluded from consolidation and the reason for exclusion; and

(f) the nature and extent of its interest in unconsolidated special purpose entities, and the risks associated with those interests.

Individual and separate financial statements

Preparation of individual and separate financial statements

9.23A The requirements for the preparation of individual financial statements are set out in the Act or other statutory framework.

9.24 Separate financial statements are those prepared by a parent in which the investments in subsidiaries, associates or jointly controlled entities are accounted for either at cost or fair value rather than on the basis of the reported results and net assets of the investees. Separate financial statements are included within the meaning of individual financial statements.

9.25 An entity that is not a parent shall account for any investments in associates and any interests in jointly controlled entities in accordance with paragraph 14.4 or 15.9, as appropriate in its individual financial statements.

Accounting policy election in separate financial statements

9.26 When a parent prepares separate financial statements, it shall select and adopt a policy of accounting for its investments in subsidiaries, associates and jointly controlled entities in those separate financial statements either:

(a) at cost less impairment;

(b) at fair value with changes in fair value recognised in other comprehensive income (or profit or loss) in accordance with paragraphs 17.15E and 17.15F; or

(c) at fair value with changes in fair value recognised in profit or loss.

The Appendix to Section 2 *Concepts and Pervasive Principles* provides guidance on determining fair value.

An entity shall apply the same accounting policy for all investments in a single class (for example investments in subsidiaries that are held as part of an investment portfolio, those that are not so held, associates or jointly controlled entities), but it can elect different policies for different classes.

This also applies to entities preparing individual financial statements.

9.26A A parent that is exempt in accordance with paragraph 9.3 from the requirement to present consolidated financial statements, and presents separate financial statements as its only financial statements, shall account for its investments in subsidiaries, associates and jointly controlled entities in accordance with paragraph 9.26.

Disclosures in separate financial statements

9.27 When a parent prepares separate financial statements, those separate financial statements shall disclose:

(a) that the statements are separate financial statements; and

* (b) a description of the methods used to account for the investments in subsidiaries, jointly controlled entities and associates.

9.27A A parent that uses one of the exemptions from presenting consolidated financial statements (described in paragraph 9.3) shall disclose the grounds on which the parent is exempt.

9.27B When a parent adopts a policy of accounting for its investments in subsidiaries, associates or jointly controlled entities at fair value with changes in fair value recognised in profit or loss, it must comply with the requirements of paragraph 36(4) of Schedule 1 to the **Regulations** by applying the disclosure requirements of Section 11 to those investments.

9.28–9.30 [Deleted]

Exchanges of businesses or other non-monetary assets for an interest in a subsidiary, jointly controlled entity or associate

9.31 Where a reporting entity exchanges a **business**, or other non-monetary assets, for an interest in another entity, and that other entity thereby becomes a subsidiary, jointly controlled entity or associate of the reporting entity, the following accounting treatment shall apply in the consolidated financial statements of the reporting entity:

(a) To the extent that the reporting entity retains an ownership interest in the business, or other non-monetary assets, exchanged, even if that interest is then held through the other entity, that retained interest, including any related goodwill, is treated as having been owned by the reporting entity throughout the transaction and should be included at its pre-transaction carrying amount.

(b) Goodwill should be recognised as the difference between:

(i) the fair value of the consideration given; and

(ii) the fair value of the reporting entity's share of the pre-transaction identifiable net assets of the other entity.

The consideration given for the interest acquired in the other entity will include that part of the business, or other non-monetary assets, exchanged and no longer owned by the reporting entity. The consideration may also include **cash** or monetary assets to achieve equalisation of values. Where it is difficult to value the consideration given, the best estimate of its value may be given by valuing what is acquired.

(c) To the extent that the fair value of the consideration received by the reporting entity exceeds the carrying value of the part of the business, or other non-monetary assets exchanged and no longer owned by the reporting entity, and any related goodwill together with any cash given up, the reporting entity should recognise a gain. Any unrealised gain arising on the exchange shall be recognised in other comprehensive income.

(d) To the extent that the fair value of the consideration received by the reporting entity is less than the carrying value of the part of the business, or other non-monetary assets no longer owned by the reporting entity, and any related goodwill, together with any cash given up, the reporting entity should recognise a loss. This loss should be recognised either as an impairment in accordance with Section 27 or, for any loss remaining after an impairment review of the relevant assets, in profit or loss.

9.32 No gain or loss should be recognised in those rare cases where the artificiality or lack of substance of the transaction is such that a gain or loss on the exchange could not be justified. Where a gain or loss on the exchange is not taken into account because the transaction is artificial or has no substance, the circumstances should be explained.

Intermediate payment arrangements

9.33 Intermediate payment arrangements may take a variety of forms:

(a) The intermediary is usually established by a sponsoring entity and constituted as a trust, although other arrangements are possible.

(b) The relationship between the sponsoring entity and the intermediary may take different forms. For example, when the intermediary is constituted as a trust, the sponsoring entity will not have a right to direct the intermediary's activities. However, in these and other cases the sponsoring entity may give advice to the intermediary or may be relied on by the intermediary to provide the information it needs to carry out its activities. Sometimes, the way the intermediary has been set up gives it little discretion in the broad nature of its activities.

(c) The arrangements are most commonly used to pay employees, although they are sometimes used to compensate suppliers of goods and services other than employee services. Sometimes the sponsoring entity's employees and other suppliers are not the only beneficiaries of the arrangement. Other beneficiaries may include past employees and their dependants, and the intermediary may be entitled to make charitable donations.

(d) The precise identity of the persons or entities that will receive payments from the intermediary, and the amounts that they will receive, are not usually agreed at the outset.

(e) The sponsoring entity often has the right to appoint or veto the appointment of the intermediary's trustees (or its directors or the equivalent).

(f) The payments made to the intermediary and the payments made by the intermediary are often cash payments but may involve other transfers of value.

Examples of intermediate payment arrangements are employee share ownership plans (ESOPs) and employee benefit trusts that are used to facilitate employee shareholdings under remuneration schemes. In a typical employee benefit trust arrangement for **share-based payments**, an entity makes payments to a trust or guarantees borrowing by the trust, and the trust uses its funds to accumulate assets to pay the entity's employees for services the employees have rendered to the entity.

Although the trustees of an intermediary must act at all times in accordance with the interests of the beneficiaries of the intermediary, most intermediaries (particularly those established as a means of remunerating employees) are specifically designed so as to serve the purposes of the sponsoring entity, and to ensure that there will be minimal risk of any conflict arising between the duties of the trustees of the intermediary and the interest of the sponsoring entity, such that there is nothing to encumber implementation of the wishes of the sponsoring entity in practice. Where this is the case, the sponsoring entity has de facto control.

9.33A It is possible for an entity to be owned by a trust established for the benefit of employees without the entity controlling the trust. An example is when the entity is a co-operative, owned by its employees, and all of the shares are held in a trust for the benefit of the employees but the shares never **vest** in individual employees, with dividends from the company being distributed to employees solely in accordance with the provisions of the trust deed.

Accounting for intermediate payment arrangements

9.34 When a sponsoring entity makes payments (or transfers assets) to an intermediary, there is a rebuttable presumption that the entity has exchanged one asset for another and that the payment itself does not represent an immediate expense. To rebut this presumption at the time the payment is made to the intermediary, the entity must demonstrate:

(a) it will not obtain future economic benefit from the amounts transferred; or

(b) it does not have control of the right or other access to the future economic benefit it is expected to receive.

9.35 Where a payment to an intermediary is an exchange by the sponsoring entity of one asset for another, any assets that the intermediary acquires in a subsequent exchange transaction will also be under the control of the entity. Accordingly, assets and liabilities of the intermediary shall be accounted for by the sponsoring entity as an extension of its own business and recognised in its own individual financial statements. An asset will cease to be recognised as an asset of the sponsoring entity when, for example, the asset of the intermediary vests unconditionally with identified beneficiaries.

9.36 A sponsoring entity may distribute its own equity instruments, or other equity instruments, to an intermediary in order to facilitate employee shareholdings under a remuneration scheme. Where this is the case and the sponsoring entity has control, or de facto control, of the assets and liabilities of the intermediary, the commercial effect is that the sponsoring entity is, for all practical purposes, in the same position as if it had purchased the shares directly.

9.37 Where an intermediary holds the sponsoring entity's equity instruments, the sponsoring entity shall account for the equity instruments as if it had purchased them directly. The sponsoring entity shall account for the assets and liabilities of the intermediary in its individual financial statements as follows:

(a) The consideration paid for the equity instruments of the sponsoring entity shall be deducted from equity until such time that the equity instruments vest unconditionally with employees.

(b) Consideration paid or received for the purchase or sale of the sponsoring entity's own equity instruments shall be shown as separate amounts in the **statement of changes in equity**.

(c) Other assets and liabilities of the intermediary shall be recognised as assets and liabilities of the sponsoring entity.

(d) No gain or loss shall be recognised in profit or loss or other comprehensive income on the purchase, sale, issue or cancellation of the entity's own equity instruments.

(e) Finance costs and any administration expenses shall be recognised on an **accrual basis** rather than as funding payments are made to the intermediary.

(f) Any dividend income arising on the sponsoring entity's own equity instruments shall be excluded from profit or loss and deducted from the aggregate of dividends paid.

Disclosures in individual and separate financial statements

9.38 When a sponsoring entity recognises the assets and liabilities held by an intermediary, it should disclose sufficient information in the **notes** to its financial statements to enable users to understand the significance of the intermediary and the arrangement in the context of the sponsoring entity's financial statements. This should include:

(a) a description of the main features of the intermediary including the arrangements for making payments and for distributing equity instruments;

(b) any restrictions relating to the assets and liabilities of the intermediary;

(c) the amount and nature of the assets and liabilities held by the intermediary, which have not yet vested unconditionally with the beneficiaries of the arrangement;

(d) the amount that has been deducted from equity and the number of equity instruments held by the intermediary, which have not yet vested unconditionally with the beneficiaries of the arrangement;

(e) for entities that have their equity instruments listed or **publicly traded** on a stock exchange or market, the market value of the equity instruments held by the intermediary which have not yet vested unconditionally with employees;

(f) the extent to which the equity instruments are under option to employees, or have been conditionally gifted to them; and

(g) the amount that has been deducted from the aggregate dividends paid by the sponsoring entity.

Section 10
Accounting Policies, Estimates and Errors

Scope of this section

10.1 This section sets out the requirements for:

(a) selecting and applying the **accounting policies** used in preparing **financial statements**;

(b) accounting for **changes in accounting estimates**; and

(c) accounting for corrections of **errors** in prior period financial statements.

Selection and application of accounting policies

10.2 Accounting policies are the specific principles, bases, conventions, rules and practices applied by an entity in preparing and presenting financial statements.

10.3 If an FRS specifically addresses a transaction, other event or condition, an entity shall apply that FRS. However, the entity need not follow a requirement in an FRS if the effect of doing so would not be **material**.

10.4 If an FRS does not specifically address a transaction, other event or condition, an entity's management shall use its judgement in developing and applying an accounting policy that results in information that is:

(a) relevant to the economic decision-making needs of users; and

(b) reliable, in that the financial statements:

(i) represent faithfully the **financial position**, financial **performance** and **cash flows** of the entity;

(ii) reflect the economic substance of transactions, other events and conditions, and not merely the legal form;

(iii) are neutral, ie free from bias;

(iv) are prudent; and

(v) are complete in all material respects.

10.5 In making the judgement described in paragraph 10.4, management shall refer to and consider the applicability of the following sources in descending order:

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

(b) where an entity's financial statements are within the scope of a **Statement of Recommended Practice (SORP)** the requirements and guidance in that SORP dealing with similar and related issues; and

(c) the definitions, **recognition** criteria and **measurement** concepts for **assets**, **liabilities**, **income** and **expenses** and the pervasive principles in Section 2 *Concepts and Pervasive Principles*.

10.6 In making the judgement described in paragraph 10.4, management may also consider the requirements and guidance in **adopted IFRS** dealing with similar and related issues. Paragraphs 1.4 to 1.7 require certain entities to apply IAS 33 *Earnings per Share* (as adopted in the relevant jurisdiction), IFRS 8 *Operating Segments* (as adopted in the relevant jurisdiction) or IFRS 6 *Exploration for and Evaluation of Mineral Resources* (as adopted in the relevant jurisdiction).

Consistency of accounting policies

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

Changes in accounting policies

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

(a) is required by an FRS; or

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

10.9 The following are not changes in accounting policies:

(a) the application of an accounting policy for transactions, other events or conditions that differ in substance from those previously occurring;

(b) the application of a new accounting policy for transactions, other events or conditions that did not occur previously or were not material; and

(c) a change to the cost model when a reliable measure of **fair value** is no longer available (or vice versa) for an asset that an FRS would otherwise require or permit to be measured at fair value.

10.10 If an FRS allows a choice of accounting treatment (including the measurement basis) for a specified transaction or other event or condition and an entity changes its previous choice, that is a change in accounting policy.

10.10A The initial application of a policy to revalue assets in accordance with Section 17 *Property, Plant and Equipment* or Section 18 *Intangible Assets other than Goodwill* is a change in accounting policy to be dealt with as a revaluation in accordance with those sections, rather than in accordance with paragraphs 10.11 and 10.12.

Applying changes in accounting policies

10.11 An entity shall account for changes in accounting policy as follows:

(a) an entity shall account for a change in accounting policy resulting from a change in the requirements of an FRS in accordance with the transitional provisions, if any, specified in that amendment;

(b) when an entity has elected to follow IAS 39 *Financial Instruments: Recognition and Measurement* and/or IFRS 9 *Financial Instruments* instead of following Section 11 *Basic Financial Instruments* and Section 12 *Other Financial Instruments Issues* as permitted by paragraph 11.2, and the requirements of IAS 39 and/or IFRS 9 change, the entity shall account for that change in accounting policy in accordance with the transitional provisions, if any, specified in the revised IAS 39 and/or IFRS 9; and

(c) when an entity is required or has elected to follow IAS 33, IFRS 8 or IFRS 6 and the requirements of those standards change, the entity shall account for that change in accounting policy in accordance with the transitional provisions, if any, specified in those standards as amended; and

(d) an entity shall account for all other changes in accounting policy retrospectively (see paragraph 10.12).

Retrospective application

10.12 When a change in accounting policy is applied retrospectively in accordance with paragraph 10.11, the entity shall apply the new accounting policy to comparative information for prior periods to the earliest date for which it is practicable, as if the new accounting policy had always been applied. When it is **impracticable** to determine the individual-period effects of a change in accounting policy on comparative information for one or more prior periods presented, the entity shall apply the new accounting policy to the **carrying amounts** of assets and liabilities as at the beginning of the earliest period for which **retrospective application** is practicable, which may be the current period, and shall make a corresponding adjustment to the opening balance of each affected component of **equity** for that period.

Disclosure of a change in accounting policy

* 10.13 When an amendment to an FRS has an effect on the current period or any prior period, or might have an effect on future periods, an entity shall disclose the following:

(a) the nature of the change in accounting policy;

(b) for the current period and each prior period presented, to the extent practicable, the amount of the adjustment for each financial statement line item affected;

(c) the amount of the adjustment relating to periods before those presented, to the extent practicable; and

(d) an explanation if it is impracticable to determine the amounts to be disclosed in (b) or (c) above.

Financial statements of subsequent periods need not repeat these disclosures.

* 10.14 When a voluntary change in accounting policy has an effect on the current period or any prior period, an entity shall disclose the following:

(a) the nature of the change in accounting policy;

(b) the reasons why applying the new accounting policy provides reliable and more relevant information;

(c) to the extent practicable, the amount of the adjustment for each financial statement line item affected, shown separately:

(i) for the current period;

(ii) for each prior period presented; and

(iii) in the aggregate for periods before those presented; and

(d) an explanation if it is impracticable to determine the amounts to be disclosed in (c) above.

Financial statements of subsequent periods need not repeat these disclosures.

Changes in accounting estimates

10.15 A change in accounting estimate is an adjustment of the carrying amount of an asset or a liability, or the amount of the periodic consumption of an asset, that results from the assessment of the present status of, and expected future benefits and obligations associated with, assets and liabilities. Changes in accounting estimates result from new information or new developments and, accordingly, are not corrections of errors. When it is difficult to distinguish a change in an accounting policy from a change in an accounting estimate, the change is treated as a change in an accounting estimate.

10.16 An entity shall recognise the effect of a change in an accounting estimate, other than a change to which paragraph 10.17 applies, **prospectively** by including it in **profit or loss** in:

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

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

10.17 To the extent that a change in an accounting estimate gives rise to changes in assets and liabilities, or relates to an item of equity, the entity shall recognise it by adjusting the carrying amount of the related asset, liability or equity item in the period of the change.

Disclosure of a change in estimate

10.18 An entity shall disclose the nature of any change in an accounting estimate and the effect of the change on assets, liabilities, income and expense for the current period. If it is practicable for the entity to estimate the effect of the change in one or more future periods, the entity shall disclose those estimates.

Corrections of prior period errors

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

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

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

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

10.21 To the extent practicable, an entity shall correct a material prior period error retrospectively in the first financial statements authorised for issue after its discovery by:

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

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

10.22 When it is impracticable to determine the period-specific effects of a material error on comparative information for one or more prior periods presented, the entity shall restate the opening balances of assets, liabilities and equity for the earliest period for which retrospective restatement is practicable (which may be the current period).

Disclosure of prior period errors

* 10.23 An entity shall disclose the following about material prior period errors:

(a) the nature of the prior period error;

(b) for each prior period presented, to the extent practicable, the amount of the correction for each financial statement line item affected;

(c) to the extent practicable, the amount of the correction at the beginning of the earliest prior period presented; and

(d) an explanation if it is impracticable to determine the amounts to be disclosed in (b) or (c) above.

Financial statements of subsequent periods need not repeat these disclosures.

Section 11
Basic Financial Instruments

Scope of Sections 11 and 12

11.1 This section and Section 12 *Other Financial Instruments Issues* together set out the requirements for the **recognition**, **derecognition**, **measurement** and disclosure of **financial instruments** (**financial assets** and **financial liabilities**). This section applies to basic financial instruments and is relevant to all entities. Section 12 applies to other, more complex financial instruments and transactions. If an entity enters into only basic financial instrument transactions then Section 12 is not applicable. However, even entities with only basic financial instruments shall consider the scope of Section 12 to ensure that it does not apply.

PBE11.1A **Public benefit entities** and other members of a **public benefit entity group** that make or receive **public benefit entity concessionary loans** shall refer to the relevant paragraphs of Section 34 *Specialised Activities* for the accounting requirements for such loans.

Accounting policy choice

11.2 An entity shall choose to apply either:

(a) the provisions of both Section 11 and Section 12 in full; or

(b) the recognition and measurement provisions of IAS 39 *Financial Instruments: Recognition and Measurement* (as adopted in the relevant jurisdiction)[47], the disclosure requirements of Sections 11 and 12 and the presentation requirements of paragraphs 11.38A and 12.25W; or

(c) the recognition and measurement provisions of IFRS 9 *Financial Instruments* (as adopted in the relevant jurisdiction) and IAS 39 (as amended following the publication of IFRS 9), the disclosure requirements of Sections 11 and 12 and the presentation requirements of paragraphs 11.38A and 12.25W;

to account for all of its financial instruments. Where an entity chooses (b) or (c) it applies the scope of the relevant standard to its financial instruments. An entity's choice of (a), (b) or (c) is an **accounting policy** choice. Paragraphs 10.8 to 10.14 contain requirements for determining when a change in accounting policy is appropriate, how such a change should be accounted for and what information should be disclosed about the change.

11.2A An entity choosing to apply the recognition and measurement provisions of IAS 39, in accordance with paragraph 11.2(b), shall apply the requirements in paragraphs 5.4.6 to 5.4.9 of IFRS 9 to a financial asset and a financial liability if, and only if, the basis for determining the contractual cash flows of that financial asset or financial liability changes as a result of interest rate benchmark reform.

11.2B For the purposes of applying paragraphs 5.4.6 to 5.4.9 of IFRS 9, the references to paragraph B5.4.5 of IFRS 9 shall be read as referring to paragraph AG7 of IAS 39.

[47] Until IAS 39 *Financial Instruments: Recognition and Measurement* is fully superseded by IFRS 9 *Financial Instruments* (ie for all entities, including insurers), an entity shall apply the version of IAS 39 that is in effect at the entity's reporting date. When IAS 39 is fully superseded by IFRS 9, an entity shall apply the version of IAS 39 that applied immediately prior to IFRS 9 fully superseding IAS 39. A copy of that version will be retained for reference on the FRC website. Entities shall apply the so-called 'EU carve-out' of IAS 39', which amended paragraph 81A and related Application Guidance in IAS 39.

References to paragraphs 5.4.3 and B5.4.6 of IFRS 9 shall be read as referring to paragraph AG8 of IAS 39.

Introduction to Section 11

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

11.4 [Deleted]

11.5 Basic financial instruments within the scope of Section 11 are those that satisfy the conditions in paragraph 11.8. Examples of financial instruments that normally satisfy those conditions include:

(a) **cash**;

(b) demand and fixed-term deposits when the entity is the depositor, eg bank accounts;

(c) commercial paper and commercial bills held;

(d) accounts, notes and loans receivable and payable;

(e) bonds and similar debt instruments;

(f) investments in non-derivative financial instruments that are **equity** of the issuer (eg most **ordinary shares** and certain preference shares); and

(g) commitments to receive a loan and commitments to make a loan to another entity that meet the conditions of paragraph 11.8(c).

11.6 Examples of financial instruments that do not normally satisfy the conditions in paragraph 11.8, and are therefore within the scope of Section 12, include:

(a) asset-backed securities, such as collateralised mortgage obligations, repurchase agreements and securitised packages of receivables;

(b) **derivatives**, eg options, rights, warrants, futures contracts, forward contracts and interest rate swaps;

(c) financial instruments that qualify and are designated as hedging instruments in accordance with the requirements in Section 12; and

(d) commitments to make a loan to another entity and commitments to receive a loan, if the commitment can be settled net in cash.

(e) [Deleted]

11.6A The initial classification of a financial instrument shall take into account contractual terms including those relating to future variations. Once the classification of a financial instrument is determined at initial recognition, re-assessment is only required subsequently when there has been a modification of contractual terms that is relevant to an assessment of the classification.

Scope of Section 11

11.7 This section applies to all financial instruments meeting the conditions of paragraph 11.8 except for:

(a) Investments in **subsidiaries, associates** and **joint ventures** (see Sections 9 *Consolidated and Separate Financial Statements*, 14 *Investments in Associates* and 15 *Investments in Joint Ventures*).

(b) Financial instruments that meet the definition of an entity's own equity and the equity component of **compound financial instruments** issued by the reporting entity that contain both a **liability** and an equity component (see Section 22 *Liabilities and Equity)*.

(c) **Leases** (see Section 20 *Leases*). However, the derecognition requirements in paragraphs 11.33 to 11.35 and impairment accounting requirements in paragraphs 11.21 to 11.26 apply to derecognition and impairment of receivables recognised by a lessor and the derecognition requirements in paragraphs 11.36 to 11.38 apply to payables recognised by a lessee arising under a **finance lease**. Section 12 applies to leases with characteristics specified in paragraph 12.3(f).

(d) Employers' rights and obligations under employee benefit plans (see Section 28 *Employee Benefits*), although the Appendix to Section 2 *Concepts and Pervasive Principles* does apply in determining the **fair value** of **plan assets**.

(e) Financial instruments, contracts and obligations to which Section 26 *Share-based Payment* applies, and contracts within the scope of paragraph 12.5.

(f) **Insurance contracts** (including **reinsurance contracts**) that the entity issues and reinsurance contracts that the entity holds (see **FRS 103**).

(g) Financial instruments issued by an entity with a **discretionary participation feature** (see FRS 103).

(h) Reimbursement assets (see Section 21 *Provisions and Contingencies*).

(i) **Financial guarantee contracts** (see Section 21).

Basic financial instruments

11.8 An entity shall account for the following financial instruments as basic financial instruments in accordance with this section:

(a) cash;

(b) a debt instrument (such as an account, note, or loan receivable or payable) that meets the conditions in paragraph 11.9 and is not a derivative financial instrument;

(bA) a debt instrument that, whilst not meeting the conditions in paragraph 11.9, nevertheless is consistent with the description in paragraph 11.9A, and is not a derivative financial instrument;

(c) commitments to receive or make a loan to another entity that:

(i) cannot be settled net in cash; and

(ii) when the commitment is executed, are expected to meet the conditions in paragraph 11.9 or be consistent with the description in paragraph 11.9A; and

(d) an investment in a non-derivative financial instrument that is equity of the issuer (eg most ordinary shares and certain preference shares).

11.9 A debt instrument that satisfies the following conditions shall be considered a basic financial instrument:

(a) The contractual return to the holder (the lender), assessed in the currency in which the debt instrument is denominated, is:

(i) a fixed amount;

(ii) a positive fixed rate or a positive variable rate[48]; or

(iii) [Deleted]

(iv) a combination of a positive or a negative fixed rate and a positive variable rate (eg LIBOR plus 200 basis points or LIBOR less 50 basis points, but not 500 basis points less LIBOR).

(aA) The contract may provide for repayments of the principal or the return to the holder (but not both) to be linked to a single relevant observable index of general price inflation of the currency in which the debt instrument is denominated, provided such links are not leveraged.

(aB) The contract may provide for a determinable variation of the return to the holder during the life of the instrument, provided that:

(i) the new rate satisfies condition (a) and the variation is not contingent on future events other than:

(1) a change of a contractual variable rate;

(2) to protect the holder against credit deterioration of the issuer; or

(3) changes in levies applied by a central bank or arising from changes in relevant taxation or law; or

(ii) the new rate is a market rate of interest and satisfies condition (a).

Contractual terms that give the lender the unilateral option to change the terms of the contract are not determinable for this purpose.

(b) There is no contractual provision that could, by its terms, result in the holder losing the principal amount or any interest attributable to the current period or prior periods. The fact that a debt instrument is subordinated to other debt instruments is not an example of such a contractual provision.

(c) Contractual provisions that permit the issuer (the borrower) to prepay a debt instrument or permit the holder (the lender) to put it back to the issuer before maturity are not contingent on future events other than to protect:

(i) the holder against the credit deterioration of the issuer (eg defaults, credit downgrades or loan covenant violations), or a change in control of the issuer; or

(ii) the holder or issuer against changes in levies applied by a central bank or arising from changes in relevant taxation or law.

The inclusion of contractual terms that, as a result of the early termination, require reasonable compensation for the early termination to be paid by either the holder or the issuer does not, in itself, constitute a breach of the conditions in paragraph 11.9.

(d) [Deleted]

(e) Contractual provisions may permit the extension of the term of the debt instrument, provided that the return to the holder and any other contractual provisions applicable during the extended term satisfy the conditions of paragraphs (a) to (c).

11.9A A debt instrument not meeting the conditions in paragraph 11.9 shall, nevertheless, be considered a basic financial instrument if it gives rise to cash flows on specified dates that constitute repayment of the principal advanced, together with reasonable

[48] A variable rate for this purpose is a rate which varies over time and is linked to a single observable interest rate or to a single relevant observable index of general price inflation of the currency in which the instrument is denominated, provided such links are not leveraged.

compensation for the time value of money, **credit risk** and other basic lending risks and costs (eg **liquidity risk**, administrative costs associated with holding the instrument and lender's profit margin). Contractual terms that introduce exposure to unrelated risks or volatility (eg changes in equity prices or commodity prices) are inconsistent with this.

Examples – Debt instruments

1 **A zero-coupon loan**

For a zero-coupon loan, the holder's return is the difference between the nominal value of the loan and the issue price. The holder (lender) receives a fixed amount when the loan matures and the issuer (borrower) repays the loan. The return to the holder meets the condition in paragraph 11.9(a)(i).

2 **A fixed interest rate loan with an initial tie-in period which reverts to the bank's standard variable interest rate after the tie-in period**

The initial fixed rate is a return permitted by paragraph 11.9(a)(ii). A bank's standard variable interest rate is an observable interest rate and, in accordance with the definition of a variable rate, is a permissible link and so meets the condition in paragraph 11.9(a)(ii).

The variation of the interest rate after the tie-in period is non-contingent and, since the new rate (ie the bank's standard variable rate) meets the conditions in paragraph 11.9(a), the conditions in paragraph 11.9(aB)(i) are met.

3 **A loan with interest payable at the bank's standard variable rate plus 1 per cent throughout the life of the loan**

As discussed under Example 2 above, a bank's standard variable rate is a permitted variable rate in accordance with the definition of variable rate. The combination of a positive fixed rate (ie plus 1 per cent) and a positive variable rate is a permitted return under paragraph 11.9(a)(iv). The combination of a bank's standard variable rate plus a fixed interest rate of 1 per cent therefore meets the condition in paragraph 11.9(a)(iv).

3A **A loan with interest payable at the bank's standard variable rate plus 1 per cent throughout the life of the loan – the bank's standard variable rate is negative**

As discussed in Example 3, the combination of a positive bank's standard variable rate plus a fixed interest rate of 1 per cent meets the condition in paragraph 11.9(a)(iv). However, the conditions in paragraph 11.9(a) do not explicitly address the case when the bank's standard variable rate is negative and such a rate may not meet the conditions.

The interest rate is consistent with the description in paragraph 11.9A provided the bank's standard variable rate reflects prevailing economic conditions and monetary policies. In this case the negative interest rate represents reasonable compensation for basic lending risks.

4 **A loan with interest payable at the bank's standard variable rate less 1 per cent throughout the life of the loan, with the condition that the interest rate can never fall below 2 per cent**

Paragraph 11.9(aB)(i)(1) permits variation of a return to a holder (lender) that is contingent on a change of a contractual variable rate. In this example the contractual variable rate is the bank's standard variable rate. The variation of the return to the holder is between the bank's standard variable rate less 1 and 2 per cent, depending on the bank's standard variable rate. For example, if the bank's standard variable rate is less than 3 per cent, the return to the holder is fixed at 2 per cent; if the bank's standard variable rate is higher than 3 per cent, the return to the holder is the bank's standard variable rate less 1 per cent. The contractual variation meets the condition in paragraph 11.9(aB)(i)(1).

The holder is protected against the risk of losing the principal amount of the loan via the interest rate floor of 2 per cent. The condition in paragraph 11.9(b) is therefore also met.

4A **A loan with a condition that the interest rate is reset to a higher rate if a set number of payments is missed**

In this case the change in interest rate is contingent on a set number of payments being missed. The missed payments are an indicator of credit deterioration of the issuer. The interest rate reset condition therefore meets the condition in paragraph 11.9(aB)(i)(2) (provided the new rate meets the conditions in paragraph 11.9(a)), and the interest rate reset condition would not result in the loan being measured at fair value in accordance with Section 12.

5 **Interest on a loan is referenced to 2 times the bank's standard variable rate**

In accordance with the definition of a variable rate, the contractual interest rate payable can be linked to a single observable interest rate. A bank's standard variable rate is an observable rate and meets the definition of a variable rate, but the rate in this example is 2 times the bank's standard variable rate and therefore the link to the observable interest rate is leveraged. As a result of the leverage, the rate in this example is not a variable rate as described in paragraph 11.9(a).

A leveraged link to an observable interest rate is also inconsistent with the description in paragraph 11.9A because it increases the variability of cash flows so that they do not represent reasonable compensation for the time value of money, credit risk or other basic lending risks and costs. The instrument is measured at fair value in accordance with Section 12.

6 **Interest on a loan is charged at 10 per cent less 6-month LIBOR over the life of the loan**

The effect of deducting a variable rate from a positive fixed rate is that the interest on the loan increases as and when the variable rate decreases and vice versa (so called inverse floating interest).

In accordance with paragraph 11.9(a)(iv) the combination of positive or negative fixed rate and positive variable rate is a permitted return. The variable rate (6-month LIBOR) meets the definition of a variable rate, as the rate is a quoted interest rate. However, since the variable rate is negative (minus 6-month LIBOR), the rate is in breach of the condition in paragraph 11.9(a)(iv).

The inverse floating interest rate is also inconsistent with the description in paragraph 11.9A because the interest charged increases when reasonable compensation for the time value of money, credit risk or other basic lending risks and costs would decrease, and vice versa. The instrument is measured at fair value in accordance with Section 12.

7 **Interest on a GBP denominated mortgage is linked to the UK Land Registry House Price Index (HPI) plus 3 per cent**

In accordance with paragraph 11.9(aA) the holder's return may be linked to an index of general price inflation of the currency of the debt instrument. The mortgage is denominated in GBP and a permitted inflation index would be an index that measures general price inflation of goods and services denominated in GBP.

As the HPI measures inflation for residential properties in the UK and is not a measure of general price inflation, the return to the holder breaches the condition in paragraph 11.9(aA).

The mortgage is also inconsistent with the description in paragraph 11.9A because the linkage to the HPI introduces exposure to a risk that is not consistent with a basic lending arrangement. The instrument is measured at fair value in accordance with Section 12.

8 **Early repayment of a loan is not permitted during an initial two-year period, but is thereafter**

The terms of a ten-year loan include that it may not be repaid within the initial two-year period, but thereafter it may be repaid at the issuer's option, subject only to the payment of reasonable compensation for early termination.

The early repayment condition is not contingent on future events, but automatically comes into effect with the passage of time, and therefore it meets the condition in paragraph 11.9(c) and would not result in the loan being measured at fair value in accordance with Section 12.

9 **Early repayment on subordinated debt contingent on repayment of senior debt**

Bank A lends CU10 million to Entity S. Entity S has an option to repay this loan at any time. Entity S's parent, Entity P, also lends it CU10 million. The loans have the same maturity date but the loan from Bank A is senior to the loan from Entity P. Entity S has the right to repay the loan to Entity P at par plus accrued interest at any time after the loan from Bank A has been repaid.

Early repayment terms that are within the control of the issuer are not contingent on future events. Therefore if early repayment of both loans is within Entity S's control then the prepayment option in the loan from Entity P is not considered to be contingent, does not breach the condition in paragraph 11.9(c) and does not therefore cause the loan from Entity P to be measured at fair value in accordance with Section 12.

If the terms were such that early repayment of the loan from Bank A was not within the control of Entity S, then the prepayment option in the loan from Entity P would be contingent on a future event other than those listed in paragraph 11.9(c). The nature of the contingent event may be an indicator when assessing whether a debt instrument is consistent with the description in paragraph 11.9A, but is not in itself a determinative factor. The restriction on the prepayment feature in the loan from Entity P would be consistent with the description in paragraph 11.9A because it exists simply to enforce its subordination relative to another debt instrument. The restriction on Entity S's ability to exercise the prepayment option in the loan from Entity P would not therefore cause the loan from Entity P to be measured at fair value in accordance with Section 12 by Entity S.

10 **A loan with interest equal to a percentage of the profits of the issuer** The contractual return is neither a fixed rate or amount, nor a variable rate linked to a single observable interest rate or index of general price inflation. Therefore, the return breaches the conditions in paragraphs 11.9(a). In addition, the loan is inconsistent with the description in paragraph 11.9A because the linkage to the profits of the issuer introduces exposure to a risk that is not consistent with a basic lending arrangement. The instrument is within the scope of Section 12 and will be measured at fair value by the holder. However, the issuer will need to consider whether measurement at fair value is permitted by the Small Companies Regulations, the Regulations, the Small LLP Regulations or the LLP Regulations (see paragraph A3.12A). These regulations prohibit the measurement of financial liabilities at fair value, except for those held as part of a trading portfolio, those that are derivatives and when permitted by IFRS as adopted in the relevant jurisdiction. An example of the latter category is financial liabilities with embedded derivatives that meet certain conditions. However this would exclude instruments with 'a non-financial variable specific to a party to a contract'. Therefore, if the issuer concludes that the issuer's profits are 'a non-financial variable specific to a party to a contract' and that the instrument could not otherwise be measured at fair value under IFRS as adopted in the relevant jurisdiction, then it must measure the instrument at amortised cost, rather than at fair value, in accordance with paragraph 12.8(c).

11.10 Examples of financial instruments that would normally satisfy the conditions in paragraph 11.9 are:

(a) trade accounts and notes receivable and payable, and loans from banks or other third parties;

(b) accounts payable in a foreign currency. However, any change in the account payable because of a change in the exchange rate is recognised in **profit or loss** as required by paragraph 30.10;

(c) loans to or from subsidiaries or associates that are due on demand; and

(d) a debt instrument that would become immediately receivable if the issuer defaults on an interest or principal payment (such a provision does not violate the conditions in paragraph 11.9).

11.11 Examples of financial instruments that do not satisfy the conditions in paragraph 11.9 or the description in paragraph 11.9A (and are therefore within the scope of Section 12) include:

(a) an investment in another entity's equity instruments other than a non-derivative financial instrument that is equity of the issuer (eg most ordinary shares and certain preference shares) (see paragraph 11.8(d)); and

(b) [Deleted]

(c) [Deleted]

(d) investments in convertible debt, because the return to the holder can vary with the price of the issuer's equity shares rather than just with market interest rates.

(e) [Deleted]

Initial recognition of financial assets and liabilities

11.12 An entity shall recognise a financial asset or a financial liability only when the entity becomes a party to the contractual provisions of the instrument.

Initial measurement

11.13 When a financial asset or financial liability is recognised initially, an entity shall measure it at the transaction price (adjusted for **transaction costs** except in the initial measurement of financial assets and liabilities that are subsequently measured at fair value through profit or loss) unless the arrangement constitutes, in effect, a financing transaction. An arrangement constitutes a financing transaction if payment is deferred beyond normal business terms or is financed at a rate of interest that is not a market rate, for example, providing interest-free credit to a buyer for the sale of goods or an interest-free or below market interest rate loan made to an employee. Except as set out in paragraph 11.13A, if the arrangement constitutes a financing transaction, the entity shall measure the financial asset or financial liability at the **present value** of the future payments discounted at a market rate of interest for a similar debt instrument as determined at initial recognition adjusted for transaction costs.

Examples – Financial assets

1 For a long-term loan at a market rate of interest made to another entity, a receivable is recognised at the amount of the cash advanced to that entity plus transaction costs incurred by the entity (see the example following paragraph 11.20).

2 For goods sold to a customer on short-term credit, a receivable is recognised at the undiscounted amount of cash receivable from that entity, which is normally the invoice price.

3 For an item sold to a customer on two-years interest-free credit, a receivable is recognised at the present value of the cash receivable discounted using the prevailing market rate of interest for a similar receivable. In transactions conducted on an arm’s length basis the cash sales price for immediate settlement would normally approximate to the present value.

4 For a cash purchase of another entity’s ordinary shares, the investment is recognised at the amount of cash paid to acquire the shares.

Examples – Financial liabilities

1 For a loan received from a bank at a market rate of interest, a payable is recognised initially at the amount of the cash received from the bank less separately incurred transaction costs.

2 For goods purchased from a supplier on short-term credit, a payable is recognised at the undiscounted amount owed to the supplier, which is normally the invoice price.

11.13A As an exception to paragraph 11.13, the following financing transactions may be measured initially at transaction price:

(a) a basic financial liability of a **small entity** that is a loan from a person who is within a director's group of close family members[49], when that group contains at least one shareholder[50] in the entity; and

(b) a public benefit entity concessionary loan (see paragraph PBE11.1A).

11.13B An entity taking advantage of the exemption in paragraph 11.13A(a) that subsequently ceases to be a small entity may, when remeasuring the financial liability to present value **prospectively** from the first **reporting date** after it ceases to be a small entity, determine the present value on the basis of the facts and circumstances existing at that time or at the date the financing arrangement was entered into.

11.13C An entity that subsequently becomes eligible to take advantage of the exemption in paragraph 11.13A(a) and chooses to do so shall apply the exemption retrospectively.

Subsequent measurement

11.14 At the end of each **reporting period**, an entity shall measure financial instruments as follows, without any deduction for transaction costs the entity may incur on sale or other disposal:

(a) Debt instruments that meet the conditions in paragraph 11.8(b) or paragraph 11.8(bA) shall be measured at **amortised cost** using the **effective interest method**. Paragraphs 11.15 to 11.20 provide guidance on determining amortised cost using the effective interest method.

(i) For a financing transaction measured initially at transaction price in accordance with paragraph 11.13A, the **effective interest rate** is the interest rate implicit in the contract, which may be zero.

(ii) For a non-interest bearing debt instrument that is payable or receivable within one year on normal business terms, amortised cost shall be measured at the undiscounted amount of the cash or other consideration expected to be paid or received (ie net of impairment – see paragraphs 11.21 to 11.26).

(iii) For a financing transaction (see paragraph 11.13) that is not accounted for in accordance with paragraph 11.13A the effective interest rate is the market rate of interest for a similar debt instrument used to determine initial measurement adjusted to amortise directly attributable transaction costs.

(b) Debt instruments that meet the conditions in paragraph 11.8(b) and commitments to receive a loan and to make a loan to another entity that meet the conditions in paragraph 11.8(c) may upon their initial recognition be designated by the entity as at fair value through profit or loss (the Appendix to Section 2 provides guidance on determining fair value) provided doing so results in more relevant information, because either:

(i) it eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as 'an accounting mismatch') that

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49 In this context, a director's group of close family members shall be the director and the close members of the family of that director (see glossary definition of **close members of the family of a person**). This includes a person who is the sole director-shareholder of an entity.

50 For small LLPs this shall be read as a member who is a person.

would otherwise arise from measuring **assets** or debt instruments or recognising the **gains** and losses on them on different bases; or

(ii) a group of debt instruments or financial assets and debt instruments is managed and its performance is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy, and information about the group is provided internally on that basis to the entity's **key management personnel** (as defined in Section 33 *Related Party Disclosures*, paragraph 33.6), for example members of the entity's board of directors and its chief executive officer.

(c) Commitments to receive a loan and to make a loan to another entity that meet the conditions in paragraph 11.8(c) shall be measured at cost (which sometimes is nil) less impairment.

(d) Investments in non-derivative financial instruments that are equity of the issuer shall be measured as follows (the Appendix to Section 2 provides guidance on determining fair value):

For investments in another **group** entity that are within the scope of this section, the following accounting policy choice shall apply to all investments in a single class, either:

(i) at cost less impairment;

(ii) at fair value with changes in fair value recognised in **other comprehensive income** (or profit or loss) in accordance with paragraphs 17.5E and 17.15F; or

(iii) at fair value with changes in fair value recognised in profit or loss.

For all other investments:

(iv) if the instruments are **publicly traded** or their fair value can otherwise be measured reliably (see paragraph 2A.4), the investment shall be measured at fair value with changes in fair value recognised in profit or loss; and

(v) all other such investments shall be measured at cost less impairment.

Impairment or uncollectability must be assessed for financial assets in (a), (c), (d)(i) and (d)(v) above. Paragraphs 11.21 to 11.26 provide guidance.

Amortised cost and effective interest method

11.15 The amortised cost of a financial asset or financial liability at each reporting date is the net of the following amounts:

(a) the amount at which the financial asset or financial liability is measured at initial recognition;

(b) minus any repayments of the principal;

(c) plus or minus the cumulative **amortisation** using the effective interest method of any difference between the amount at initial recognition and the maturity amount;

(d) minus, in the case of a financial asset, any reduction (directly or through the use of an allowance account) for impairment or uncollectability.

Financial assets and financial liabilities that have no stated interest rate (and do not constitute a financing transaction) and are classified as payable or receivable within one year are initially measured at an undiscounted amount in accordance with paragraph 11.14(a). Therefore, (c) above does not apply to them.

11.16 The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability (or a group of financial assets or financial liabilities) and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period, to the **carrying amount** of the financial asset or financial liability. The effective interest rate is determined on the basis of the carrying amount of the financial asset or liability at initial recognition. Under the effective interest method:

(a) the amortised cost of a financial asset (liability) is the present value of future cash receipts (payments) discounted at the effective interest rate; and

(b) in the absence of capital repayments, the interest expense (income) in a period equals the carrying amount of the financial liability (asset) at the beginning of a period multiplied by the effective interest rate for the period.

11.17 When calculating the effective interest rate, an entity shall estimate **cash flows** considering all contractual terms of the financial instrument (eg prepayment, call and similar options) and known credit losses that have been incurred, but it shall not consider possible future credit losses not yet incurred. For variable rate financial assets and variable rate financial liabilities the current market rate of interest or index of general price inflation may be used when estimating the contractual cash flows.

11.18 When calculating the effective interest rate, an entity shall amortise any related fees, finance charges paid or received (such as ‘points’), transaction costs and other premiums or discounts over the expected life of the instrument, except as follows. The entity shall use a shorter period if that is the period to which the fees, finance charges paid or received, transaction costs, premiums or discounts relate. This will be the case when the variable to which the fees, finance charges paid or received, transaction costs, premiums or discounts relate is repriced to market rates before the expected maturity of the instrument. In such a case, the appropriate amortisation period is the period to the next such repricing date.

11.19 For variable rate financial assets and variable rate financial liabilities, periodic re-estimation of cash flows to reflect changes in market rates of interest or an index of general price inflation alters the effective interest rate. If a variable rate financial asset or variable rate financial liability is recognised initially at an amount equal to the principal receivable or payable at maturity, re-estimating the future interest payments normally has no significant effect on the carrying amount of the asset or liability.

11.20 If an entity revises its estimates of payments or receipts, the entity shall adjust the carrying amount of the financial asset or financial liability (or group of financial instruments) to reflect actual and revised estimated cash flows. The entity shall recalculate the carrying amount by computing the present value of estimated future cash flows at the financial instrument’s original effective interest rate. The entity shall recognise the adjustment as **income** or **expense** in profit or loss at the date of the revision.

Example of determining amortised cost for a five-year loan using the effective interest method

On 1 January 20X0, an entity acquires a bond for Currency Units (CU)900, incurring transaction costs of CU50. Interest of CU40 is receivable annually, in arrears, over the next five years (31 December 20X0 to 31 December 20X4). The bond has a mandatory redemption of CU1100 on 31 December 20X4.

Year	Carrying amount at beginning of period	Interest income at 6.9583%*	Cash inflow	Carrying amount at end of period
	CU	CU	CU	CU
20X0	950.00	66.11	(40.00)	976.11
20X1	976.11	67.92	(40.00)	1,004.03
20X2	1,004.03	69.86	(40.00)	1,033.89
20X3	1,033.89	71.94	(40.00)	1,065.83
20X4	1,065.83	74.16	(40.00)	1,100.00
			(1,100.00)	0

* The effective interest rate of 6.9583 per cent is the rate that discounts the expected cash flows on the bond to the initial carrying amount:

$40/(1.069583)^1 + 40/(1.069583)^2 + 40/(1.069583)^3 + 40/(1.069583)^4 + 1{,}140/(1.069583)^5 = 950$

Amendments specific to interest rate benchmark reform (Phase 2)

11.20A An entity shall apply paragraphs 11.20B to 11.20D to a financial asset or a financial liability if, and only if, the basis for determining the contractual cash flows of that financial asset or financial liability changes as a result of interest rate benchmark reform.

11.20B The basis for determining the contractual cash flows of a financial asset or a financial liability can change:

(a) by amending the contractual terms specified at the initial recognition of the financial instrument (for example, the contractual terms are amended to replace the referenced interest rate benchmark with an alternative benchmark rate);

(b) in a way that was not considered by – or contemplated in – the contractual terms at the initial recognition of the financial instrument, without amending the contractual terms (for example, the method for calculating the interest rate benchmark is altered without amending the contractual terms); and/or

(c) because of the activation of an existing contractual term (for example, an existing fallback clause is triggered).

11.20C As a practical expedient, an entity shall apply paragraph 11.19 to account for a change in the basis for determining the contractual cash flows of a financial asset or a financial liability that is required by interest rate benchmark reform. This practical expedient applies only to such changes and only to the extent the change is required by interest rate benchmark reform (see also paragraph 11.20D). For this purpose, a change in the basis for determining the contractual cash flows is required by interest rate benchmark reform if, and only if, both these conditions are met:

(a) the change is necessary as a direct consequence of interest rate benchmark reform; and

(b) the new basis for determining the contractual cash flows is economically equivalent to the basis immediately preceding the change.

11.20D Examples of changes that give rise to a new basis for determining the contractual cash flows that is economically equivalent to the basis immediately preceding the change are:

(a) the replacement of an existing interest rate benchmark used to determine the contractual cash flows of a financial asset or a financial liability with an alternative benchmark rate – or the implementation of such a reform of an interest rate benchmark by altering the method used to calculate the interest rate benchmark – with the addition of a fixed spread necessary to compensate for the basis difference between the existing interest rate benchmark and the alternative benchmark rate;

(b) changes to the reset period, reset dates or the number of days between coupon payment dates in order to implement the reform of an interest rate benchmark; and

(c) the addition of a fallback provision to the contractual terms of a financial asset or a financial liability to enable any change described in (a) and (b) above to be implemented.

11.20E If changes are made to a financial asset or a financial liability in addition to changes to the basis for determining the contractual cash flows required by interest rate benchmark reform, an entity shall first apply the practical expedient in paragraph 11.20C to the changes required by interest rate benchmark reform. The entity shall then apply the applicable requirements in this FRS to any additional changes to which the practical expedient does not apply.

Impairment of financial instruments measured at cost or amortised cost

Recognition

11.21 At the end of each reporting period, an entity shall assess whether there is objective evidence of impairment of any financial assets that are measured at cost or amortised cost. If there is objective evidence of impairment, the entity shall recognise an **impairment loss** in profit or loss immediately.

11.22 Objective evidence that a financial asset or group of assets is impaired includes observable data that come to the attention of the holder of the asset about the following loss events:

(a) significant financial difficulty of the issuer or obligor;

(b) a breach of contract, such as a default or delinquency in interest or principal payments;

(c) the creditor, for economic or legal reasons relating to the debtor’s financial difficulty, granting to the debtor a concession that the creditor would not otherwise consider;

(d) it has become **probable** that the debtor will enter bankruptcy or other financial reorganisation; and

(e) observable data indicating that there has been a measurable decrease in the estimated future cash flows from a group of financial assets since the initial recognition of those assets, even though the decrease cannot yet be identified with the individual financial assets in the group, such as adverse national or local economic conditions or adverse changes in industry conditions.

11.23 Other factors may also be evidence of impairment, including significant changes with an adverse effect that have taken place in the technological, market, economic or legal environment in which the issuer operates.

11.24 An entity shall assess the following financial assets individually for impairment:

(a) all equity instruments regardless of significance; and

(b) other financial assets that are individually significant.

An entity shall assess other financial assets for impairment either individually or grouped on the basis of similar credit risk characteristics.

Measurement

11.25 An entity shall measure an impairment loss on the following instruments measured at cost or amortised cost as follows:

(a) For an instrument measured at amortised cost in accordance with paragraph 11.14(a), the impairment loss is the difference between the asset's carrying amount and the present value of estimated cash flows discounted at the asset's original effective interest rate. If such a financial instrument has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract.

(b) For an instrument measured at cost less impairment in accordance with paragraph 11.14(c) and (d)(ii) the impairment loss is the difference between the asset's carrying amount and the best estimate (which will necessarily be an approximation) of the amount (which might be zero) that the entity would receive for the asset if it were to be sold at the reporting date.

Reversal

11.26 If, in a subsequent period, the amount of an impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the entity shall reverse the previously recognised impairment loss either directly or by adjusting an allowance account. The reversal shall not result in a carrying amount of the financial asset (net of any allowance account) that exceeds what the carrying amount would have been had the impairment not previously been recognised. The entity shall recognise the amount of the reversal in profit or loss immediately.

11.27–11.32 [Moved to paragraphs 2A.1 to 2A.6]

Derecognition of a financial asset

11.33 An entity shall derecognise a financial asset only when:

(a) the contractual rights to the cash flows from the financial asset expire or are settled; or

(b) the entity transfers to another party substantially all of the risks and rewards of ownership of the financial asset; or

(c) the entity, despite having retained some, but not substantially all, risks and rewards of ownership, has transferred control of the asset to another party and the other party has the practical ability to sell the asset in its entirety to an unrelated third party and is able to exercise that ability unilaterally and without needing to impose additional restrictions on the transfer. In this case, the entity shall:

(i) derecognise the asset; and

(ii) recognise separately any rights and obligations retained or created in the transfer.

The carrying amount of the transferred asset shall be allocated between the rights or obligations retained and those transferred on the basis of their relative fair values at the transfer date. Newly created rights and obligations shall be measured at their fair values at that date. Any difference between the consideration received and the amounts recognised and derecognised in accordance with this paragraph shall be recognised in profit or loss in the period of the transfer.

11.34 If a transfer does not result in derecognition because the entity has retained significant risks and rewards of ownership of the transferred asset, the entity shall continue to recognise the transferred asset in its entirety and shall recognise a financial liability for the consideration received. The asset and liability shall not be offset. In subsequent periods, the entity shall recognise any income on the transferred asset and any expense incurred on the financial liability.

11.35 If a transferor provides non-cash collateral (such as debt or equity instruments) to the transferee, the accounting for the collateral by the transferor and the transferee depends on whether the transferee has the right to sell or repledge the collateral and on whether the transferor has defaulted. The transferor and transferee shall account for the collateral as follows:

(a) If the transferee has the right by contract or custom to sell or repledge the collateral, the transferor shall reclassify that asset in its **statement of financial position** (eg as a loaned asset, pledged equity instruments or repurchase receivable) separately from other assets.

(b) If the transferee sells collateral pledged to it, it shall recognise the proceeds from the sale and a liability measured at fair value for its obligation to return the collateral.

(c) If the transferor defaults under the terms of the contract and is no longer entitled to redeem the collateral, it shall derecognise the collateral, and the transferee shall recognise the collateral as its asset initially measured at fair value or, if it has already sold the collateral, derecognise its obligation to return the collateral.

(d) Except as provided in (c), the transferor shall continue to carry the collateral as its asset, and the transferee shall not recognise the collateral as an asset.

Example: Transfer that qualifies for derecognition

An entity sells a group of its accounts receivable to a bank at less than their face amount. The entity continues to handle collections from the debtors on behalf of the bank, including sending monthly statements, and the bank pays the entity a market rate fee for servicing the receivables. The entity is obliged to remit promptly to the bank any and all amounts collected, but it has no obligation to the bank for slow payment or non-payment by the debtors. In this case, the entity has transferred to the bank substantially all of the risks and rewards of ownership of the receivables. Accordingly, it removes the receivables from its statement of financial position (ie derecognises them), and it shows no liability in respect of the proceeds received from the bank. The entity recognises a loss calculated as the difference between the carrying amount of the receivables at the time of sale and the proceeds received from the bank. The entity recognises a liability to the extent that it has collected funds from the debtors but has not yet remitted them to the bank.

Example: Transfer that does not qualify for derecognition

The facts are the same as the preceding example except that the entity has agreed to buy back from the bank any receivables for which the debtor is in arrears as to principal or interest for more than 120 days.

In this case, the entity has retained the risk of slow payment or non-payment by the debtors – a significant risk with respect to receivables. Accordingly, the entity does not treat the receivables as having been sold to the bank, and it does not derecognise them. Instead, it treats the proceeds from the bank as a loan secured by the receivables. The entity continues to recognise the receivables as an asset until they are collected or written off as uncollectible.

Derecognition of a financial liability

11.36 An entity shall derecognise a financial liability (or a part of a financial liability) only when it is extinguished – ie when the obligation specified in the contract is discharged, is cancelled or expires.

11.37 If an existing borrower and lender exchange financial instruments with substantially different terms, the entities shall account for the transaction as an extinguishment of the original financial liability and the recognition of a new financial liability. Similarly, an entity shall account for a substantial modification of the terms of an existing financial liability or a part of it (whether or not attributable to the financial difficulty of the debtor) as an extinguishment of the original financial liability and the recognition of a new financial liability.

11.38 The entity shall recognise in profit or loss any difference between the carrying amount of the financial liability (or part of a financial liability) extinguished or transferred to another party and the consideration paid, including any non-cash assets transferred or liabilities assumed.

Presentation

11.38A A financial asset and a financial liability shall be offset and the net amount presented in the statement of financial position when, and only when, an entity:

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

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

Disclosures

11.39 [Deleted]

Disclosure of accounting policies for financial instruments

11.40 In accordance with paragraph 8.5, an entity shall disclose in its significant accounting policies, the measurement basis (or bases) used for financial instruments and the other accounting policies used for financial instruments that are relevant to an understanding of the **financial statements**.

Statement of financial position – categories of financial assets and financial liabilities

* 11.41 An entity shall disclose separately the carrying amounts at the reporting date of financial assets and financial liabilities measured at fair value through profit or loss. This disclosure may be made separately by category of financial instrument. Financial liabilities that are not held as part of a trading portfolio and are not derivatives shall be shown separately.

11.42 An entity shall disclose information that enables users of its financial statements to evaluate the significance of financial instruments for its **financial position** and **performance**. For example, for long-term debt such information would normally include the terms and conditions of the debt instrument (such as interest rate, maturity, repayment schedule, and restrictions that the debt instrument imposes on the entity). When the risks arising from financial instruments are particularly significant to the **business** (for example because they are principal risks for the entity), additional disclosure may be required. Paragraphs 34.19 to 34.30, which set out disclosure requirements for **financial institutions**, include examples of disclosure requirements for risks arising from financial instruments that may be relevant in such cases.

* 11.43 For all financial assets and financial liabilities measured at fair value, the entity shall disclose the basis for determining fair value, eg quoted market price in an **active market** or a valuation technique. When a valuation technique is used, the entity shall disclose the assumptions applied in determining fair value for each class of financial assets or financial liabilities. For example, if applicable, an entity discloses information about the assumptions relating to prepayment rates, rates of estimated credit losses, and interest rates or discount rates.

11.44 If a reliable measure of fair value is no longer available for any financial instruments that would otherwise be required to be measured at fair value through profit or loss in accordance with this FRS, the entity shall disclose that fact and the carrying amount of those financial instruments.

Derecognition

11.45 If an entity has transferred financial assets to another party in a transaction that does not qualify for derecognition (see paragraphs 11.33 to 11.35), the entity shall disclose the following for each class of such financial assets:

(a) the nature of the assets;

(b) the nature of the risks and rewards of ownership to which the entity remains exposed; and

(c) the carrying amounts of the assets and of any associated liabilities that the entity continues to recognise.

Collateral

* 11.46 When an entity has pledged financial assets as collateral for liabilities or **contingent liabilities**, it shall disclose the following:

(a) the carrying amount of the financial assets pledged as collateral; and

(b) the terms and conditions relating to its pledge.

Defaults and breaches on loans payable

11.47 For **loans payable** recognised at the reporting date for which there is a breach of terms or default of principal, interest, sinking fund, or redemption terms that has not been remedied by the reporting date, an entity shall disclose the following:

(a) details of that breach or default;

(b) the carrying amount of the related loans payable at the reporting date; and

(c) whether the breach or default was remedied, or the terms of the loans payable were renegotiated, before the financial statements were authorised for issue.

Items of income, expense, gains or losses

11.48 An entity shall disclose the following items of income, expense, gains or losses:

(a) income, expense, net gains or net losses, including changes in fair value, recognised on:

* (i) financial assets measured at fair value through profit or loss;

* (ii) financial liabilities measured at fair value through profit or loss (with separate disclosure of movements on those which are not held as part of a trading portfolio and are not derivatives);

(iii) financial assets measured at amortised cost;

(iv) financial liabilities measured at amortised cost; and

(v) when an entity has made the accounting policy choice in paragraphs 11.2(c) and 12.2(c) to apply the recognition and measurement provisions of IFRS 9, financial instruments measured at fair value through other comprehensive income.

(b) total interest income and total interest expense (calculated using the effective interest method) for financial assets or financial liabilities that are not measured at fair value through profit or loss; and

(c) the amount of any impairment loss for each class of financial asset. A class of financial asset is a grouping that is appropriate to the nature of the information disclosed and that takes into account the characteristics of the financial assets. When an entity has made the accounting policy choice in paragraph 11.2(c) and 12.2(c) to apply the recognition and measurement provisions of IFRS 9, the groupings shall be based on whether the amount is equal to 12-month expected credit risk losses, equal to the lifetime expected credit losses or financial assets that are purchased or originated credit-impaired.

Financial instruments at fair value through profit or loss

* 11.48A An entity, including an entity that is not a company, shall provide the following disclosures only for financial instruments measured at fair value through profit or loss in accordance with paragraph 36(4) of Schedule 1 to the **Regulations**[51]. This does not include financial liabilities held as part of a trading portfolio nor derivatives. The required disclosures are:

(a) For a financial liability designated as at fair value through profit or loss, the amount of change, during the period and cumulatively, in the fair value of the financial instrument that is attributable to changes in the credit risk of that instrument, determined either:

[51] And the equivalent requirements of the Small Companies Regulations, the Small LLP Regulations and the LLP Regulations.

(i) as the amount of change in its fair value that is not attributable to changes in market conditions that give rise to **market risk**; or

(ii) using an alternative method the entity believes more faithfully represents the amount of change in its fair value that is attributable to changes in the credit risk of the instrument.

(b) The method used to establish the amount of change attributable to changes in own credit risk, or, if the change cannot be measured reliably or is not **material**, that fact.

(c) For a financial liability, the difference between the financial liability's carrying amount and the amount the entity would be contractually required to pay at maturity to the holder of the obligation.

(d) If an instrument contains both a liability and an equity feature, and the instrument has multiple features that substantially modify the cash flows and the values of those features are interdependent (such as a callable convertible debt instrument), the existence of those features.

(e) If there is a difference between the fair value of a financial instrument at initial recognition and the amount determined at that date using a valuation technique, the aggregate difference yet to be recognised in profit or loss at the beginning and end of the period and a reconciliation of the changes in the balance of this difference.

(f) Information that enables users of the entity's financial statements to evaluate the nature and extent of relevant risks arising from financial instruments to which the entity is exposed at the end of the reporting period. These risks typically include, but are not limited to, credit risk, liquidity risk and market risk. The disclosure should include both the entity's exposure to each type of risk and how it manages those risks.

Financial institutions and retirement benefit plans

11.48B A financial institution shall, in addition, apply the requirements of paragraph 34.17.

11.48C A **retirement benefit plan** shall, in addition, apply the requirements of paragraphs 34.39 to 34.48.

Interest rate benchmark reform

11.49 An entity shall disclose information on the nature and extent of risks arising from financial instruments subject to interest rate benchmark reform, how the entity manages those risks and the entity's progress in completing the transition from interest rate benchmarks to alternative benchmark rates.

11.50 An entity that has applied the practical expedient in paragraph 11.20C shall disclose that fact. It shall also consider whether any further disclosure is necessary, for example in accordance with paragraphs 8.6 and 8.7.

Section 12
Other Financial Instruments Issues

Scope of Sections 11 and 12

12.1 This section and Section 11 *Basic Financial Instruments* together set out the requirements for the **recognition**, **derecognition**, **measurement**, and disclosure of **financial instruments** (**financial assets** and **financial liabilities**). Section 11 applies to basic financial instruments and is relevant to all entities. This section applies to other, more complex financial instruments and transactions. If an entity enters into only basic financial instrument transactions then this section is not applicable. However, even entities with only basic financial instruments shall consider the scope of this section to ensure that this section does not apply.

PBE12.1A **Public benefit entities** or other members of a **public benefit entity group** that make or receive **public benefit entity concessionary loans** shall refer to the relevant paragraphs of Section 34 *Specialised Activities* for the accounting requirements for such loans.

Accounting policy choice

12.2 An entity shall choose to apply either:

(a) the provisions of both Section 11 and Section 12 in full; or

(b) the recognition and measurement provisions of IAS 39 *Financial Instruments: Recognition and Measurement* (as adopted in the relevant jurisdiction)[52], the disclosure requirements of Sections 11 and 12 and the presentation requirements of paragraphs 11.38A and 12.25W; or

(c) the recognition and measurement provisions of IFRS 9 *Financial Instruments* (as adopted in the relevant jurisdiction) and IAS 39 (as amended following the publication of IFRS 9), the disclosure requirements of Sections 11 and 12 and the presentation requirements of paragraph 11.38A and 12.25W;

to account for all of its financial instruments. Where an entity chooses (b) or (c) it applies the scope of the relevant standard to its financial instruments. An entity's choice of (a), (b) or (c) is an **accounting policy** choice. Paragraphs 10.8 to 10.14 contain requirements for determining when a change in accounting policy is appropriate, how such a change should be accounted for and what information should be disclosed about the change in accounting policy.

12.2A An entity choosing to apply the recognition and measurement provisions of IAS 39, in accordance with paragraph 12.2(b), shall apply the requirements in paragraphs 5.4.6 to 5.4.9 of IFRS 9 to a financial asset and a financial liability if, and only if, the basis for determining the contractual cash flows of that financial asset or financial liability changes as a result of interest rate benchmark reform.

12.2B For the purposes of applying paragraphs 5.4.6 to 5.4.9 of IFRS 9, the references to paragraph B5.4.5 of IFRS 9 shall be read as referring to paragraph AG7 of IAS 39.

[52] Until IAS 39 *Financial Instruments: Recognition and Measurement* is fully superseded by IFRS 9 *Financial Instruments* (ie for all entities, including insurers), an entity shall apply the version of IAS 39 that is in effect at the entity's reporting date. When IAS 39 is fully superseded by IFRS 9, an entity shall apply the version of IAS 39 that applied immediately prior to IFRS 9 fully superseding IAS 39. A copy of that version will be retained for reference on the FRC website. Entities shall apply the so-called 'EU carve-out' of IAS 39', which amended paragraph 81A and related Application Guidance in IAS 39.

References to paragraphs 5.4.3 and B5.4.6 of IFRS 9 shall be read as referring to paragraph AG8 of IAS 39.

Scope of Section 12

12.3 This section applies to all financial instruments except for:

(a) Those covered by Section 11.

(b) Investments in **subsidiaries** (see Section 9 *Consolidated and Separate Financial Statements*), **associates** (see Section 14 *Investments in Associates*) and **joint ventures** (see Section 15 *Investments in Joint Ventures*).

(c) Employers' rights and obligations under employee benefit plans (see Section 28 *Employee Benefits*).

(d) **Insurance contracts** (including **reinsurance contracts**) that the entity issues and reinsurance contracts that the entity holds (see **FRS 103**).

(e) Financial instruments that meet the definition of an entity's own **equity** and the equity component of **compound financial instruments** issued by the reporting entity that contain both a **liability** and an equity component (see Section 22 *Liabilities and Equity)*.

(f) **Leases** (see Section 20 *Leases*) unless the lease could, as a result of non-typical contractual terms, result in a loss to the lessor or the lessee.

(g) Contracts for contingent consideration in a **business combination** (see Section 19 *Business Combinations and Goodwill*). This exemption applies only to the acquirer.

(h) Any forward contract between an acquirer and a selling shareholder to buy or sell an acquiree that will result in a business combination at a future **acquisition date**. The term of the forward contract should not exceed a reasonable period normally necessary to obtain any required approvals and to complete the transaction.

(i) Financial instruments, contracts and obligations to which Section 26 *Share-based Payment* applies, except for contracts within the scope of paragraph 12.5.

(j) Financial instruments issued by an entity with a **discretionary participation feature** (see FRS 103).

(k) Reimbursement assets (see Section 21 *Provisions and Contingencies*).

(l) **Financial guarantee contracts** (see Section 21).

12.4 Most contracts to buy or sell a non-financial item such as a commodity, **inventory**, or **property, plant and equipment** are excluded from this section because they are not financial instruments. However, this section applies to all contracts that impose risks on the buyer or seller that are not typical of contracts to buy or sell non-financial items. For example, this section applies to contracts that, as a result of its contractual terms, could result in a loss to the buyer or seller that is unrelated to changes in the price of the non-financial item, changes in foreign exchange rates, or a default by one of the counterparties.

12.5 In addition to the contracts described in paragraph 12.4, this section applies to contracts to buy or sell non-financial items if the contract can be settled net in **cash** or another financial instrument, or by exchanging financial instruments as if the contracts were financial instruments, with the following exception: contracts that were entered into and continue to be held for the purpose of the receipt or delivery of a non-financial item in accordance with the entity's expected purchase, sale or usage requirements are not financial instruments for the purposes of this section.

Initial recognition of financial assets and liabilities

12.6 An entity shall recognise a financial asset or a financial liability only when the entity becomes a party to the contractual provisions of the instrument.

Initial measurement

12.7 When a financial asset or financial liability is recognised initially, an entity shall measure it at its **fair value**, which is normally the transaction price (adjusted for **transaction costs** except in the initial measurement of financial assets and liabilities that are subsequently measured at fair value through **profit or loss**). If payment for an **asset** is deferred beyond normal business terms or is financed at a rate of interest that is not a market rate, the entity shall initially measure the asset at the **present value** of the future payments discounted at a market rate of interest for a similar debt instrument as determined at initial recognition and adjusted for transaction costs.

Subsequent measurement

12.8 At the end of each **reporting period**, an entity shall measure all financial instruments within the scope of Section 12 at fair value and recognise changes in fair value in profit or loss, except as follows:

(a) investments in non-derivative financial instruments that are equity of the issuer that are not **publicly traded** and whose fair value cannot otherwise be measured reliably and contracts linked to such instruments that, if exercised, will result in delivery of such instruments, shall be measured at cost less impairment;

(b) hedging instruments in a designated hedging relationship accounted for in accordance with paragraph 12.23 or 12.24; and

(c) financial instruments that are not permitted by the **Small Company Regulations**, the **Regulations**, the **Small LLP Regulations** or the **LLP Regulations** to be measured at fair value through profit or loss shall be measured at **amortised cost** in accordance with paragraphs 11.15 to 11.20.

12.9 If a reliable measure of fair value is no longer available for a financial asset or financial liability that is not publicly traded but is measured at fair value through profit or loss, its fair value at the last date the instrument was reliably measurable is treated as the cost of the instrument. The entity shall measure the instrument at this cost amount less impairment until a reliable measure of fair value becomes available.

Fair value

12.10 An entity shall apply the guidance on determining fair value in the Appendix to Section 2 *Concepts and Pervasive Principles* to fair value measurements in accordance with this section as well as for fair value measurements in accordance with Section 11.

12.11 The fair value of a financial liability that is due on demand is not less than the amount payable on demand, discounted from the first date that the amount could be required to be paid.

12.12 [Deleted]

Impairment of financial instruments measured at cost or amortised cost

12.13 An entity shall apply the guidance on impairment of a financial instrument measured at cost in paragraphs 11.21 to 11.26 to financial instruments measured at cost less impairment in accordance with this section.

Derecognition of a financial asset or financial liability

12.14 An entity shall apply the derecognition requirements in paragraphs 11.33 to 11.38 to financial assets and financial liabilities to which this section applies.

Hedge accounting

12.15 A hedging relationship consists of a hedging instrument and a hedged item. Provided the qualifying conditions in paragraph 12.18 are met, an entity may apply hedge accounting.

12.15A For a fair value hedge of interest rate exposure of a portfolio of financial assets or financial liabilities (and only for such a hedge), an entity may apply the hedge accounting requirements in IAS 39[53] instead of those in this FRS. In that case, the entity must also apply the specific requirements for the fair value hedge accounting for a portfolio hedge of interest rate risk and designate as the hedged item a portion that is a currency amount rather than the individual assets or liabilities (see paragraphs 81A, 89A and AG114 to AG132 of IAS 39).

Hedged items

12.16 A hedged item can be a recognised asset or liability, an unrecognised **firm commitment**, a **highly probable forecast transaction** or a **net investment in a foreign operation**, or a component of any such item, provided the item is reliably measurable.

12.16A For hedge accounting purposes, only assets, liabilities, firm commitments or a highly probable forecast transaction with a party external to the reporting entity can be a hedged item. Hedge accounting can be applied to transactions between entities in the same **group** only in the **individual financial statements** of those entities, except for:

(a) transactions with subsidiaries, where the subsidiaries are not consolidated in the **consolidated financial statements**;

(b) the foreign currency risk of intragroup **monetary items** that result in an exposure to foreign exchange **gains** or losses that are not fully eliminated on consolidation in accordance with Section 30 *Foreign Currency Translation*; and

(c) the foreign currency risk of highly probable forecast intragroup transactions, provided the transactions are denominated in a currency other than the **functional currency** of the entity entering into the transactions and the foreign currency risk affects consolidated profit or loss.

[53] Entities shall apply the so-called ‘EU carve-out of IAS 39’, which amended paragraph 81A and related Application Guidance in IAS 39.

12.16B A group of items, including components of items, can be an eligible hedged item provided that all of the following conditions are met:

(a) it consists of items that are individually eligible hedged items;

(b) the items in the group share the same risk;

(c) the items in the group are managed together on a group basis for risk management purposes; and

(d) it does not include items with offsetting risk positions.

12.16C A component of an item comprises less than the entire fair value change or **cash flow** variability of an item. The following components of an item (including combinations thereof) may be a hedged item:

(a) changes in the cash flows or fair value attributable to a separately identifiable and reliably measureable specific risk or risks, including cash flow and fair value changes above or below a specified price or other variable;

(b) one or more selected contractual cash flows; or

(c) a specified part of the nominal amount of an item.

Hedging instruments

12.17 An instrument may be a hedging instrument provided all of the following conditions are met:

(a) it is a financial instrument measured at fair value through profit or loss;

(b) it is a contract with a party external to the reporting entity (ie external to the group or individual entity that is being reported on); and

(c) it is not a written option, except as described in paragraph 12.17C.

12.17A An instrument (or a combination of such instruments) meeting the conditions of paragraph 12.17, may only be a hedging instrument:

(a) in its entirety;

(b) by designating a proportion of such an instrument or a proportion of a combination of such instruments, eg 50 per cent of the nominal amount of the instrument; or

(c) by separating the spot risk element of a foreign currency contract and excluding the forward element, or by separating the **intrinsic value** of an option and excluding the change in time value.

12.17B For a hedge of foreign currency risk, the foreign currency risk component of a financial instrument, provided that it is not a **derivative** financial instrument, may be a hedging instrument.

12.17C A written option is not a hedging instrument unless the written option is an offset to or is combined with a purchased option and the effect of the offset or combination is not a net written option. An example of a combination of a written and a purchased option that is not a net written option is a zero cost interest rate collar.

Conditions for hedge accounting

12.18 An entity may apply hedge accounting to a hedging relationship from the date all of the following conditions are met:

(a) the hedging relationship consists only of a hedging instrument and a hedged item as described in paragraphs 12.16 to 12.17C;

(b) the hedging relationship is consistent with the entity's risk management objectives for undertaking hedges;

(c) there is an economic relationship between the hedged item and the hedging instrument;

(d) the entity has documented the hedging relationship so that the risk being hedged, the hedged item and the hedging instrument are clearly identified; and

(e) the entity has determined and documented causes of hedge ineffectiveness.

12.18A An economic relationship between a hedged item and hedging instrument exists when the entity expects that the values of the hedged item and hedging instrument will typically move in opposite directions in response to movements in the same risk, which is the hedged risk.

Accounting for qualifying hedging relationships

12.19 There are three types of hedging relationships:

(a) fair value hedge: a hedge of the exposure to changes in fair value of a recognised asset or liability or an unrecognised firm commitment, or a component of any such item, that are attributable to a particular risk and could affect profit or loss;

(b) cash flow hedge: a hedge of the exposure to variability in cash flows that is attributable to a particular risk associated with all, or a component of, a recognised asset or liability (such as all or some future interest payments on variable rate debt) or a highly probable forecast transaction, and could affect profit or loss; and

(c) hedge of a net investment in a foreign operation.

12.19A A hedge of the foreign currency risk of an unrecognised firm commitment may be accounted for as a fair value hedge or as a cash flow hedge.

Fair value hedges

12.20 A fair value hedge shall be accounted for as follows from the date the conditions in paragraph 12.18 are met:

(a) the gain or loss on the hedging instrument shall be recognised in profit or loss; and

(b) the **hedging gain or loss** on the hedged item shall adjust the **carrying amount** of the hedged item (if applicable) and be recognised in profit or loss. When a hedged item is an unrecognised firm commitment, the cumulative hedging gain or loss on the hedged item is recognised as an asset or liability with a corresponding gain or loss recognised in profit or loss.

12.21 When an unrecognised firm commitment to acquire an asset or assume a liability is the hedged item, the initial carrying amount of the asset or liability that results from the entity meeting the firm commitment is adjusted to include the cumulative hedging gain or loss of the hedged item that was recognised in the **statement of financial position**.

12.22 Any adjustment arising from paragraph 12.20(b) shall be amortised to profit or loss if the hedged item is a financial instrument measured at amortised cost. **Amortisation** may begin as soon as an adjustment exists and shall begin no later than when the hedged item ceases to be adjusted for hedging gains and losses. The amortisation is based on a recalculated **effective interest rate** at the date amortisation begins.

Cash flow hedges

12.23 A cash flow hedge shall be accounted for as follows from the date the conditions in paragraph 12.18 are met:

(a) the separate component of equity associated with the hedged item (cash flow hedge reserve) is adjusted to the lower of the following (in absolute amounts):

(i) the cumulative gain or loss on the hedging instrument from the date the conditions of paragraph 12.18 are met; and

(ii) the cumulative change in fair value on the hedged item (ie the present value of the cumulative change of expected future cash flows) from the date the conditions of paragraph 12.18 are met;

(b) the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge (ie the portion that is offset by the change in the cash flow hedge reserve calculated in accordance with (a)) shall be recognised in **other comprehensive income**;

(c) any remaining gain or loss on the hedging instrument (or any gain or loss required to balance the change in the cash flow hedge reserve calculated in accordance with (a)), is hedge ineffectiveness that shall be recognised in profit or loss; and

(d) the amount that has been accumulated in the cash flow hedge reserve in accordance with (a) shall be accounted for as follows:

(i) if a hedged forecast transaction subsequently results in the recognition of a non-financial asset or non-financial liability, or a hedged forecast transaction for a non-financial asset or non-financial liability becomes a firm commitment for which fair value hedge accounting is applied, the entity shall remove that amount from the cash flow hedge reserve and include it directly in the initial cost or other carrying amount of the asset or liability;

(ii) for cash flow hedges other than those covered by (i), that amount shall be reclassified from the cash flow hedge reserve to profit or loss in the same period or periods during which the hedged expected future cash flows affect profit or loss (for example, in the periods that interest income or interest expense is recognised or when a forecast sale occurs); and

(iii) if the amount is a loss, and all or part of that loss is not expected to be recovered, the amount of the loss not expected to be recovered shall be reclassified to profit or loss immediately.

Hedges of a net investment in a foreign operation

12.24 Hedges of a net investment in a foreign operation, including a hedge of a monetary item that is accounted for as part of the net investment (see Section 30), shall be accounted for similarly to cash flow hedges from the date the conditions of paragraph 12.18 are met:

(a) the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge shall be recognised in other comprehensive income (see paragraphs 12.23(a) and (b)); and

(b) the ineffective portion shall be recognised in profit or loss.

The cumulative gain or loss on the hedging instrument relating to the effective portion of the hedge that has been accumulated in equity shall not be reclassified from equity to profit or loss on disposal or partial disposal of the **foreign operation**.

Discontinuing hedge accounting

12.25 The entity may discontinue hedge accounting provided the entity has documented its election.

The entity shall discontinue hedge accounting when:

(a) the hedging instrument has expired, is sold, terminated or exercised; or

(b) the conditions for hedge accounting in paragraph 12.18 are no longer met.

In all cases, hedge accounting shall be discontinued **prospectively**.

12.25A In a fair value hedge, any adjustment arising from paragraph 12.20(b) is dealt with in accordance with paragraph 12.22.

In a cash flow hedge, if the hedged future cash flows are no longer expected to occur, the amount that has been accumulated in the cash flow hedge reserve in accordance with paragraph 12.23(a) shall be reclassified from the cash flow hedge reserve to profit or loss immediately. If the hedged future cash flows are still expected to occur (for example a future cash flow that is no longer highly probable may still be expected to occur), the cumulative gain or loss in the cash flow hedge reserve is dealt with in accordance with paragraph 12.23(d).

In a net investment hedge, in accordance with paragraph 12.24, the amount that has been accumulated in equity is not reclassified to profit or loss.

Temporary amendments specific to interest rate benchmark reform (Phase 1)

12.25B Paragraphs 12.25C to 12.25F only apply to hedging relationships directly affected by interest rate benchmark reform. A hedging relationship is directly affected by interest rate benchmark reform only if the reform gives rise to uncertainties about:

(a) the interest rate benchmark designated as a hedge risk; and/or

(b) the timing and/or the amount of the interest rate benchmark-based cash flows of the hedged item and/or the hedging instrument.

12.25C In determining whether a forecast transaction (or a component thereof) is highly probable, an entity shall assume that the interest rate benchmark on which the hedged cash flows are based is not altered as a result of interest rate benchmark reform.

12.25D In applying the requirement in paragraph 12.25A, in order to determine whether the hedged future cash flows are expected to occur, an entity shall assume that the interest rate benchmark on which the hedged cash flows are based is not altered as a result of interest rate benchmark reform.

12.25E In applying the requirement in paragraph 12.18A, an entity shall assume that the interest rate benchmark on which the hedged cash flows and/or the hedged risk are based, or the interest rate benchmark on which the cash flows of the hedging instrument are based, are not altered as a result of interest rate benchmark reform.

12.25F For a hedge of a non-contractually specified benchmark component of interest rate risk, an entity shall apply the requirement in paragraph 12.16C(a) – that the changes, in the cash flows or fair value attributable, are a separately identifiable and reliably measurable specific risk or risks – only at the inception of the hedging relationship.

12.25G An entity shall cease applying paragraphs 12.25C to 12.25E at the earlier of:

(a) when the uncertainty arising from interest rate benchmark reform is no longer present with respect to the timing and the amount of the relevant interest rate benchmark-based cash flows; or

(b) when the entire amount accumulated in the cash flow hedge reserve with respect to that hedging relationship is reclassified to profit or loss.

If the hedging relationship is discontinued at an earlier date, an entity shall prospectively cease applying paragraph 12.25E to that hedging relationship at the date of discontinuation.

12.25H When designating a group of items as the hedged item, or a combination of financial instruments as the hedging instrument, an entity shall cease applying paragraphs 12.25C to 12.25E to an individual item or financial instrument as relevant in accordance with paragraph 12.25G, when the uncertainty arising from interest rate benchmark reform is no longer present with respect to that item or financial instrument.

12.25I An entity shall prospectively cease to apply paragraph 12.25F at the earlier of:

(a) when the uncertainty arising from interest rate benchmark reform is no longer present with respect to the non-contractually specified risk component; or

(b) when the hedging relationship in which the non-contractually specified risk component is the hedged item is discontinued.

Additional temporary amendments specific to interest rate benchmark reform (Phase 2)

12.25J As and when paragraphs 12.25C to 12.25F cease to apply to a hedging relationship because the uncertainties arising from interest rate benchmark reform described in paragraph 12.25B are no longer present (see also paragraphs 12.25G to 12.25I for Phase 1 cessation requirements), an entity shall apply paragraphs 12.25P to 12.25U as applicable and amend the documentation of that hedging relationship (see paragraph 12.18(d)) to reflect the changes required by interest rate benchmark reform, ie the changes are consistent with the requirements in paragraphs 11.20B to 11.20D. In this context, the hedge documentation shall be amended only to make one or more of these changes:

(a) specifying an alternative benchmark rate (contractually or non-contractually specified) as a hedged risk;

(b) amending the description of the hedged item, including the description of the portion of the cash flows or fair value being hedged; or

(c) amending the description of the hedging instrument (see also paragraph 12.25K).

12.25K An entity shall also apply the requirement in paragraph 12.25J(c) if these three conditions are met:

(a) the entity makes a change required by interest rate benchmark reform using an approach other than changing the basis for determining the contractual cash flows of the hedging instrument (as described in paragraph 11.20B);

(b) the original hedging instrument is not derecognised; and

(c) the chosen approach is economically equivalent to changing the basis for determining the contractual cash flows of the original hedging instrument (as described in paragraphs 11.20C and 11.20D).

12.25L Paragraphs 12.25C to 12.25F may cease to apply at different times. Therefore, in applying paragraph 12.25J, an entity may be required to amend the documentation of its hedging relationships at different times or may be required to amend the documentation of a hedging relationship more than once.

12.25M An entity shall amend the hedge documentation as required in paragraph 12.25J no later than the end of the reporting period during which a change is made to the hedged risk, hedged item or hedging instrument (see paragraph 1.30 for first-time application). For the avoidance of doubt, such an amendment to the documentation of a hedging relationship constitutes neither the discontinuation of the hedging relationship nor the commencement of a new hedging relationship.

12.25N If changes are made in addition to those changes required by interest rate benchmark reform (as described in paragraphs 11.20B to 11.20D) to the financial asset or the financial liability in a hedging relationship or to the documentation of the hedging relationship (as required by paragraph 12.25J), an entity shall first apply the applicable requirements in this FRS to determine whether those additional changes result in the discontinuation of hedge accounting. If the additional changes do not result in the discontinuation of hedge accounting, an entity shall apply paragraph 12.25J.

12.25O Paragraphs 12.25P to12.25V provide exceptions to the requirements specified in those paragraphs only. An entity shall apply all other hedge accounting requirements in this FRS, including the qualifying criteria in paragraph 12.18, to hedging relationships that were directly affected by interest rate benchmark reform. An entity shall also apply paragraph 12.20 (for a fair value hedge) or paragraph 12.23 (for a cash flow hedge) to account for any changes in the fair value of the hedged item or the hedging instrument.

Cash flow hedges

12.25P For the purposes of applying paragraph 12.23(d), at the point when an entity applies paragraph 12.25J to a hedged item in a cash flow hedge, the amount accumulated in the cash flow hedge reserve shall be deemed to be based on the alternative benchmark rate on which the hedged future cash flows are determined.

12.25Q For a discontinued hedging relationship, when the interest rate benchmark on which the hedged future cash flows had been based is changed as required by interest rate benchmark reform, for the purposes of applying paragraph 12.25A (as applicable to a cash flow hedge), in order to determine whether the hedged future cash flows are expected to occur, the amount accumulated in the cash flow hedge reserve for that hedging relationship shall be deemed to be based on the alternative benchmark rate on which the hedged future cash flows will be based.

Group of items

12.25R When an entity applies paragraph 12.25J to a hedged item that is a group of items (see paragraph 12.16B), the entity shall allocate the items in that group to subgroups based on the benchmark rate being hedged and document the benchmark rate as the hedged risk for each subgroup. For example, in a hedging relationship in which a group of items is hedged for changes in an interest rate benchmark subject to interest rate benchmark reform, the hedged cash flows or fair value of some items in the group could be changed to reference an alternative benchmark rate before other items in the group are changed. In this example, in applying paragraph 12.25J, the entity would document the alternative benchmark rate as the hedged risk for that relevant subgroup of hedged items. The entity would continue to document the existing interest rate benchmark as the hedged risk for the other subgroup of hedged items until the hedged cash flows or fair value of those items are changed to reference the alternative benchmark rate or the items expire and are replaced with hedged items that reference the alternative benchmark rate.

12.25S An entity applying paragraph 12.25R shall assess separately whether each subgroup meets the requirements in paragraph 12.16B. If any subgroup fails to meet the requirements in paragraph 12.16B, the entity shall discontinue hedge accounting prospectively for the hedging relationship in its entirety. An entity shall also apply the requirements in paragraphs 12.20 or 12.23 to account for ineffectiveness related to the hedging relationship in its entirety.

Components of an item

12.25T For the purposes of applying paragraph 12.16C(a), an alternative benchmark rate that is a non-contractually specified risk component, which is not separately identifiable, is deemed to be separately identifiable, if and only if, the entity reasonably expects that the alternative benchmark rate will be separately identifiable within the next 24 months. The 24-month period applies on a rate-by-rate basis, ie the period starts for each alternative benchmark rate when it is identified as a non-contractually specified risk component for the first time.

12.25U If an entity that applied paragraph 12.25T, subsequently reasonably expects that the alternative benchmark rate will not be separately identifiable within 24 months from the date it was identified as a non-contractually specified risk component for the first time, the entity shall cease to apply paragraph 12.25T to that alternative benchmark rate and discontinue hedge accounting prospectively from the date of that reassessment for all hedging relationships in which the alternative benchmark rate was identified as a non-contractually specified risk component.

12.25V An entity shall also apply paragraphs 12.25T and 12.25U to new hedging relationships in which an alternative benchmark rate is identified as a non-contractually specified risk component (see paragraph 12.16C(a)) when, because of interest rate benchmark reform, that risk component is not separately identifiable at the date it is documented as a hedged item.

Presentation

12.25W A financial asset and a financial liability shall be offset and the net amount presented in the statement of financial position when, and only when, an entity:

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

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

Disclosures

12.26 An entity applying this section shall make all of the disclosures required in Section 11 incorporating in those disclosures, financial instruments that are within the scope of this section as well as those within the scope of Section 11. For financial instruments in the scope of this section that are not held as part of a trading portfolio and are not derivative instruments, an entity shall provide additional disclosures as set out in paragraph 11.48A. In addition, if the entity uses hedge accounting, it shall make the additional disclosures in paragraphs 12.27 to 12.29A.

12.27 An entity shall disclose the following separately for each type of hedging relationship described in paragraph 12.19:

(a) a description of the hedge;

(b) a description of the financial instruments designated as hedging instruments and their fair values at the **reporting date**; and

(c) the nature of the risks being hedged, including a description of the hedged item.

* 12.28 If an entity uses hedge accounting for a fair value hedge it shall disclose the following:

(a) the amount of the change in fair value of the hedging instrument recognised in profit or loss for the period; and

(b) the amount of the change in fair value of the hedged item recognised in profit or loss for the period.

12.29 If an entity uses hedge accounting for a cash flow hedge it shall disclose the following:

(a) the periods when the cash flows are expected to occur and when they are expected to affect profit or loss;

(b) a description of any forecast transaction for which hedge accounting had previously been used, but which is no longer expected to occur;

* (c) the amount of the change in fair value of the hedging instrument that was recognised in other comprehensive income during the period;

* (d) the amount, if any, that was reclassified from equity to profit or loss for the period; and

* (e) the amount, if any, of any hedge ineffectiveness recognised in profit or loss for the period.

12.29A If an entity uses hedge accounting for a net investment in a foreign operation it shall disclose separately the amounts recognised in other comprehensive income in accordance with paragraph 12.24(a) and the amounts recognised in profit or loss in accordance with paragraph 12.24(b).

12.30 When an entity has taken advantage of the temporary amendments to specific hedge accounting requirements in paragraphs 12.25C to 12.25F, it shall disclose:

(a) that fact; and

(b) the significant interest rate benchmarks to which the entity's hedging relationships are exposed.

It shall also consider whether any further disclosure is necessary, for example in accordance with paragraphs 8.6 and 8.7.

Appendix to Section 12
Examples of hedge accounting

This appendix accompanies, but is not part of, Section 12. It provides guidance for applying the requirements of paragraphs 12.15 and 12.16 to 12.25A.

Example 1

Fair value hedge accounting – Hedge of forward foreign currency risk of an unrecognised firm commitment

In accordance with paragraph 12.19A, a hedge of the foreign currency risk of an unrecognised firm commitment may be accounted for as a cash flow or fair value hedge. This example illustrates fair value hedge accounting.

12A.1 On 9 June 20X5 an entity enters into a purchase agreement with a third party over a non-financial asset in a foreign currency (FC) for FC515,000. On the same day, the entity enters into a forward currency contract to buy FC500,000 for CU1,000,000. Under the purchase agreement, the non-financial asset will be delivered and paid for on 30 March 20X6, the same day the forward currency contract is required to be settled.

In this example the hedged item is the total of the commitment of FC515,000 and the hedging instrument is the forward contract to buy FC500,000. Since the nominal amounts of the two contracts do not match, hedge ineffectiveness arises. It should be noted that in practice an entity could avoid ineffectiveness arising for this reason by identifying an amount of FC500,000 of the total commitment as the hedged item in accordance with paragraph 12.16C.

For simplification, this example disregards other sources of ineffectiveness, eg counter party credit risk associated with the forward currency contract.

The entity's financial year ends on 31 December.

This example assumes that the qualifying conditions for hedge accounting in paragraph 12.18 are met from 9 June 20X5.

The table below sets out the applicable forward exchange rates, the fair value of the forward currency contract (the hedging instrument) and the hedging gains/losses on the purchase commitment (the hedged item) on the relevant dates. This example ignores the effects of discounting.

	9 Jun 20X5	31 Dec 20X5	30 Mar 20X6
Forward exchange rate (CU:FC)	2:1	2.2:1	2.16:1
Forward currency contract (hedging instrument)			
Fair value	nil	FC500,000 x CU0.2:FC = CU100,000	FC500,000 x CU0.16:FC = CU80,000†
Fair value change	nil	CU100,000 – 0 = CU100,000	CU80,000 – CU100,000 = (CU20,000)
Purchase commitment (hedged item)			
Cumulative hedging (loss)‡	nil	(FC515,000) x CU0.2:FC = (CU103,000)	(FC515,000) x CU0.16:FC = (CU82,400)
Hedging (loss)/ gain	nil	(CU103,000) – 0 = (CU103,000)	(CU82,400) – (CU103,000) = CU20,600

Key to table:

† This is the fair value of the contract prior to settlement.

‡ In accordance with paragraph 12.20(b), the commitment is fair valued only for the hedged risk, which in this example is the forward exchange rate risk.

12A.2 Hedge accounting:

Note that there are no hedge accounting entries on 9 June 20X5.

31 December 20X5

(1) In accordance with paragraph 12.20(a) the fair value gain of CU100,000 on the forward currency contract is recognised in profit or loss.

(2) In accordance with paragraph 12.20(b) the cumulative hedging loss of CU103,000 on the commitment is recognised as a liability with a corresponding loss recognised in profit or loss.

Accounting entries:

Ref		Debit	Credit
(1)	Forward currency contract	CU100,000	
	Profit or loss		CU100,000
(2)	Profit or loss	CU103,000	
	Hedged item (commitment)		CU103,000

30 March 20X6

(1) In accordance with paragraph 12.20(a) the fair value loss of CU20,000 on the forward currency contract is recognised in profit or loss.

(2) In accordance with paragraph 12.20(b) the hedging gain on the commitment of CU20,600 is recognised in profit or loss with a corresponding adjustment to the recognised liability from CU103,000 to CU82,400.

(3) In accordance with paragraph 12.21 the non-financial asset's carrying amount is adjusted to include the cumulative hedging loss on the hedged item of CU82,400.

Note A: For illustrative purposes the accounting entry in respect of the settlement of the forward currency contract in cash for CU80,000 is shown below.

Note B: For illustrative purposes the accounting entry for the purchase of the non-financial asset at the applicable spot rate of FC2.16:CU for CU1,112,400 (settled in cash) is shown below.

Accounting entries:

Ref		Debit	Credit
(1)	Profit or loss	CU20,000	
	Forward currency contract		CU20,000
(2)	Hedged item (commitment)	CU20,600	
	Profit or loss		CU20,600
(3)	Hedged item (commitment)	CU82,400	
	Property, plant and equipment		CU82,400
(A)	Cash	CU80,000	
	Forward currency contract		CU80,000
(B)	Property, plant and equipment	CU1,112,400	
	Cash		CU1,112,400

Example 2

Cash flow hedge accounting – Hedge of variability in cash flows in a floating rate loan due to interest rate risk

This example illustrates the accounting for a cash flow hedge of interest rate risk associated with a floating rate loan. The entity borrows money at a floating rate and enters into an interest rate swap with the effect of paying a fixed rate overall.

12A.3 On 1 January 20X5, an entity borrows CU10,000,000 from a bank at a floating rate of 3-month LIBOR plus 2.5 per cent. The interest is payable annually in arrears on 31 December. The loan is repayable on 31 December 20X7.

On 1 January 20X5 the entity also enters into an interest rate swap with a third party, under which it receives 6-month LIBOR and pays a fixed rate of interest of 4.5 per cent. The notional amount of the swap is CU10,000,000. The swap is settled annually in arrears on 31 December and expires on 31 December 20X7.

The LIBOR rates on the loan and the interest rate swap are reset and fixed annually in advance on 31 December based on the expected LIBOR rates applicable at that time. Note that in practice the loan and swap interest rates would be reset more frequently than assumed for the purpose of simplification in this example.

The entity hedges the variability of the interest rate payments on the bank loan based on 3-month LIBOR. It should be noted that because the entity receives interest based on 6-month LIBOR under the interest rate swap, ineffectiveness will arise because the expected cash flows of the hedged item and the hedging instrument differ. The fair value of the interest rate swap may be affected by other factors that cause ineffectiveness, for example counter party credit risk, but these have been disregarded in this example.

There are no transaction costs.

The entity's financial year ends on 31 December.

This example assumes that the qualifying conditions for hedge accounting in paragraph 12.18 are met from 1 January 20X5.

The table in paragraph 12A.5 summarises the impact of hedge accounting on the interest rate swap, profit or loss and other comprehensive income.

The table below sets out the applicable LIBOR rates, interest payments and swap settlements. The fair values of the interest rate swap and the hedged item shown in the table are shown for illustrative purposes only.

Note that in practice, when forecasted variable interest rate payments are the hedged item, the fair value of a hypothetical swap, that would be expected to perfectly offset the hedged cash flows, is used as a proxy of the fair value of the hedged item. The hypothetical derivative in this scenario is a fixed to floating interest rate swap with terms that match those of the loan and a fixed rate of 4.3 per cent, which for the purpose of this example, is the interest rate where the fair value of the hypothetical swap is nil at the inception of the hedging relationship.

	1 Jan 20X5	31 Dec 20X5	31 Dec 20X6	31 Dec 20X7
Actual 3-month LIBOR	4.3%	5%	3%	n/a
Actual 6-month LIBOR	4.5%	4.9%	3.2%	n/a
Interest payments based on 3-month LIBOR	n/a	CU10m × (4.3% + 2.5%) = CU680,000	CU10m × (5% + 2.5%) = CU750,000	CU10m × (3% + 2.5%) = CU550,000
Interest rate swap (hedging instrument)				
Fair value	nil	CU78,000	(CU89,000)[†]	(CU130,000)[‡]
Fair value change	nil	CU78,000 – 0 = CU78,000	(CU89,000) – CU78,000 = (CU167,000)	(CU130,000) – (CU40,000)[§] – (CU89,000) = (CU1,000)
Swap settlement receipts/ (payments) based on 6-month LIBOR	n/a	CU10m × (4.5% – 4.5%) = nil	CU10m × (4.9% – 4.5%) = CU40,000	CU10m × (3.2% – 4.5%) = (CU130,000)
Hedged item				
Fair value	nil	(CU137,000)	CU59,000	CU130,000

Key to table:

† This valuation is determined before the receipt of the cash settlement of CU40,000 due on 31 December 20X6.

‡ This valuation is determined before the payment of the cash settlement of CU130,000 due on 31 December 20X7.

§ CU40,000 is the settlement of the interest rate swap as at 31 December 20X6 which affects the fair value of the swap, but is not included in the fair value of the swap at 31 December 20X6 of CU89,000.

12A.4 Hedge accounting:

31 December 20X5

(1) In accordance with paragraph 12.23(a), the cash flow hedge reserve is adjusted to the lower of (in absolute amounts) the cumulative gain on the hedging instrument (ie the interest rate swap), which equals its fair value, of CU78,000 and the cumulative change in fair value of the hedged item, which equals its fair value of (CU137,000).

In accordance with paragraph 12.23(b), the gain of CU78,000 on the interest rate swap is recognised in other comprehensive income.

(2) The fixed interest element on the hypothetical swap is CU430,000, the same amount as the variable rate component. The variability of the 3-month LIBOR did therefore not affect profit or loss during the period. The reclassification adjustment in accordance with paragraph 12.23(d)(ii) is nil. (Note that no accounting entry is shown below.)

Note A: For illustrative purposes the accounting entry for interest payments is shown below. Note that in practice the accrual and payment of interest may be recorded in separate accounting entries.

Accounting entries:

Note that the accounting entries shown are only those relevant to demonstrate the effects of hedge accounting. In practice other accounting entries would be required, eg an entry to recognise the loan liability.

Ref		Debit	Credit
(1)	Interest rate swap	CU78,000	
	Other comprehensive income		CU78,000
(A)	Profit or loss	CU680,000	
	Cash		CU680,000

31 December 20X6

(1) In accordance with paragraph 12.23(a), the cash flow hedge reserve is adjusted to the lower of (in absolute amounts) the cumulative loss on the hedging instrument (ie the interest rate swap) which equals its fair value of (CU89,000) and the cumulative change in fair value of the hedged item, which equals its fair value of CU59,000. The cash flow hedge reserve moves from CU78,000 to (CU59,000), a change of (CU137,000).

In accordance with paragraph 12.23(b), a loss of CU137,000 on the interest rate swap is recognised in other comprehensive income, as this part of the loss is fully off-set by the change in the cash flow hedge reserve. The remainder of the loss on the interest rate swap of CU30,000 is recognised in profit or loss, as required by paragraph 12.23(c).

(2) The fixed interest element on the hypothetical swap is CU430,000, whilst the variable rate component is CU500,000. The variability of the 3-month LIBOR affects profit or loss during the period by CU70,000. Accordingly, the reclassification adjustment in accordance with paragraph 12.23(d)(ii) is CU70,000.

Note A: For illustrative purposes the accounting entry for interest payments is shown below. Note that in practice the accrual and payment of interest may be recorded in separate accounting entries.

Note B: For illustrative purposes the accounting entry for the settlement of the swap is shown below.

Accounting entries:

Ref		Debit	Credit
(1)	Other comprehensive income	CU137,000	
	Profit or loss	CU30,000	
	Interest rate swap		CU167,000
(2)	Other comprehensive income	CU70,000	
	Profit or loss		CU70,000
(A)	Profit or loss	CU750,000	
	Cash		CU750,000
(B)	Cash	CU40,000	
	Interest rate swap		CU40,000

31 December 20X7

(1) In accordance with paragraph 12.23(a), the cash flow hedge reserve is adjusted to the lower of (in absolute amounts) the cumulative loss on the hedging instrument (ie the interest rate swap) which equals the fair value of (CU130,000) and the cumulative change in fair value of the hedged item, which equals its fair value of CU130,000.

The cash flow hedge reserve moves from (CU129,000) to (CU130,000), a change of (CU1,000). In accordance with paragraph 12.23(b), the loss of CU1,000 on the interest rate swap is recognised in other comprehensive income.

(2) The fixed interest element on the hypothetical swap is CU430,000, whilst the variable rate component is CU300,000. The variability of the 3-month LIBOR affects profit or loss during the period by (CU130,000). Accordingly, the reclassification adjustment in accordance with paragraph 12.23(d)(ii) is (CU130,000).

Note A: For illustrative purposes the accounting entry for interest payments is shown below. Note that in practice the accrual and payment of interest may be recorded in separate accounting entries.

Note B: For illustrative purposes the accounting entry for the settlement of the swap is shown below.

Accounting entries:

Ref		Debit	Credit
(1)	Other comprehensive income	CU1,000	
	Interest rate swap		CU1,000
(2)	Profit or loss	CU130,000	
	Other comprehensive income		CU130,000
(A)	Profit or loss	CU550,000	
	Cash		CU550,000
(B)	Interest rate swap	CU130,000	
	Cash		CU130,000

12A.5 The table below summarises the effects of the accounting entries shown in paragraph 12A.4 on the interest rate swap, profit or loss and other comprehensive income.

Description	Interest rate swap	Other comprehensive income	Profit or loss
31 December 20X5			
Opening balance	**nil**	**nil**†	**–**
Interest on the loan			CU680,000
Interest rate swap fair value movement	CU78,000	(CU78,000)	–
Closing balance	**CU78,000**	**(CU78,000)**†	**–**
31 December 20X6			
Opening balance	**CU78,000**	**(CU78,000)**†	**–**
Interest on the loan			CU750,000
Interest rate swap fair value movement	(CU167,000)	CU137,000	CU30,000
Settlement receipt interest rate swap	(CU40,000)	–	–
Reclassification from cash flow hedge reserve	–	CU70,000	(CU70,000)
Closing balance	**(CU129,000)**	**CU129,000**†	**–**
31 December 20X7			
Opening balance	**(CU129,000)**	**CU129,000**†	**–**
Interest on the loan			CU550,000
Interest rate swap movement	(CU1,000)	CU1,000	–
Settlement payment interest rate swap	CU130,000	–	–
Reclassification from cash flow hedge reserve	–	(CU130,000)	CU130,000
Closing balance	**nil**	**nil**†	**–**

Key to table:

† This is the balance of the cash flow hedge reserve.

Example 3

Hedge accounting: Net investment in a foreign operation

This example illustrates the accounting for a net investment hedge in the consolidated financial statements. The entity has a foreign operation and hedges its exposure to foreign currency risk in the foreign operation by the use of a foreign currency loan.

12A.6 On 1 April 20X5 an entity with functional currency CU acquires an investment in an overseas subsidiary (with functional currency FC) at a cost of FC1,200,000. On the same day the entity takes out a loan with a third party of FC1,200,000 to finance the investment. This example disregards the effects of interest or other transaction costs associated with the loan.

This example assumes that the carrying amount of the investment denominated in FC is impaired below FC1,200,000 as presented in the table below, which causes ineffectiveness.

The entity’s financial year ends on 31 December.

This example assumes that the qualifying conditions for hedge accounting in paragraph 12.18 are met from 1 April 20X5.

The table below sets out the applicable exchange rates, the carrying amount of the loan and the foreign exchange gains and losses on the loan as determined in accordance with Section 30 *Foreign Currency Translation*, as well as the retranslation differences on the foreign investment recognised in other comprehensive income in accordance with Section 30.

	1 Apr 20X5	**31 Dec 20X5**	**31 Dec 20X6**
Spot exchange rate (CU:FC)	0.35:1	0.3:1	0.45:1
Loan (hedging instrument)			
Carrying amount under Section 30	(FC1,200,000) x CU0.35:FC = (CU420,000)	(FC1,200,000) x CU0.3:FC = (CU360,000)	(FC1,200,000) x CU0.45:FC = (CU540,000)
Cumulative gain/(loss)	nil	(CU360,000) – (CU420,000) = CU60,000	(CU540,000) – (CU420,000) = (CU120,000)
Gain/(loss)	nil	(CU360,000) – (CU420,000) = CU60,000	(CU540,000) – (CU360,000) = (CU180,000)

	1 Apr 20X5	31 Dec 20X5	31 Dec 20X6
Investment in foreign operation (hedged item)			
Retranslation difference in accordance with Section 30	nil	(CU55,000)†	CU157,500‡
Cumulative retranslation differences	nil	(CU55,000) – 0 = (CU55,000)	CU157,500 + (CU55,000) = CU102,500

Key to table:

† This is the exchange difference referred to in paragraph 30.20 which is recognised in other comprehensive income. The amount under paragraph 30.20(a) is CU5,000 and under paragraph 30.20(b) (CU60,000). The calculation is based on the translation of the FC200,000 loss at the average rate of 0.325CU:FC.

‡ This is the exchange difference referred to in paragraph 30.20 which is recognised in other comprehensive income. The amount under paragraph 30.20(a) is CU7,500 and under paragraph 30.20(b) CU150,000. The calculation is based on the translation of the FC100,000 profit at the average rate of 0.375CU:FC.

12A.7 Hedge accounting:

31 December 20X5

A component of equity is adjusted to the lower of (in absolute amounts) the cumulative exchange gain on the loan of CU60,000 and the cumulative retranslation difference on the net investment of (CU55,000).

In accordance with paragraph 12.24(a), a gain of CU55,000 on the loan is recognised in other comprehensive income. The remainder of the gain of CU5,000 is recognised in profit or loss, as required by paragraph 12.24(b).

Accounting entry:

Note that only the accounting entry in relation to hedge accounting as described in paragraph 12.24 is shown. Other accounting entries in relation to the loan and the investment in the foreign operation would be required in practice.

	Debit	Credit
Loan	CU60,000	
Other comprehensive income		CU55,000
Profit or loss		CU5,000

31 December 20X6

A component of equity is adjusted to the lower of (in absolute amounts) the cumulative exchange loss on the loan of CU120,000 and the cumulative exchange difference on the net investment of CU102,500.

The amount recognised in equity changes from CU55,000 to (CU102,500), a change of (CU157,500). In accordance with paragraph 12.24(a) a loss of CU157,500 on the loan is recognised in other comprehensive income. The remainder of the loss of CU22,500 is recognised in profit or loss, as required by paragraph 12.24(b).

Accounting entry:

	Debit	Credit
Other comprehensive income	CU157,500	
Profit or loss	CU22,500	
Loan		CU180,000

Section 13
Inventories

Scope of this section

13.1 [Deleted]

13.2 This section applies to **inventories**, except:

(a) work in progress arising under **construction contracts**, including directly related service contracts (see Section 23 *Revenue*);

(b) **financial instruments** (see Section 11 *Basic Financial Instruments* and Section 12 *Other Financial Instruments Issues*); and

(c) **biological assets** related to **agricultural activity** and **agricultural produce** at the point of harvest (see Section 34 *Specialised Activities*).

13.3 Other than the disclosure requirements in paragraph 13.22, this section does not apply to the **measurement** of inventories at **fair value less costs to sell** through **profit or loss** at each **reporting date**. Inventories shall not be measured at fair value less costs to sell unless it is a more relevant measure of the entity's **performance** because the entity operates in an **active market** where sale can be achieved at published prices, and inventory is a store of readily realisable value.

Measurement of inventories

13.4 An entity shall measure inventories at the lower of **cost** and estimated selling price less costs to complete and sell.

13.4A **Inventories held for distribution at no or nominal consideration** shall be measured at the lower of cost adjusted, when applicable, for any loss of **service potential** and replacement cost.

Cost of inventories

13.5 An entity shall include in the cost of inventories all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

13.5A Where inventories are acquired through a **non-exchange transaction**, their cost shall be measured at their **fair value** as at the date of acquisition. For **public benefit entities** and entities within a **public benefit entity group**, this requirement only applies to inventories that are recognised as a result of the requirements for incoming resources from non-exchange transactions as prescribed in Section 34 *Specialised Activities*.

Costs of purchase

13.6 The costs of purchase of inventories comprise the purchase price, import duties and other taxes (other than those subsequently recoverable by the entity from the taxing authorities), and transport, handling and other costs directly attributable to the acquisition of finished goods, materials and services. Trade discounts, rebates and other similar items are deducted in determining the costs of purchase.

13.7 An entity may purchase inventories on deferred settlement terms. In some cases, the arrangement effectively contains an unstated financing element, for example, a difference between the purchase price for normal credit terms and the deferred settlement amount. In these cases, the difference is recognised as interest expense over the period of the financing and is not added to the cost of the inventories unless the inventory is a **qualifying asset** (see Section 25 *Borrowing Costs)* and the entity adopts a policy of capitalisation of **borrowing costs**.

Costs of conversion

13.8 The costs of conversion of inventories include costs directly related to the units of production, such as direct labour. They also include a systematic allocation of fixed and variable production overheads that are incurred in converting materials into finished goods. Fixed production overheads are those indirect costs of production that remain relatively constant regardless of the volume of production, such as **depreciation** and maintenance of factory buildings and equipment, and the cost of factory management and administration. Variable production overheads are those indirect costs of production that vary directly, or nearly directly, with the volume of production, such as indirect materials and indirect labour.

13.8A Production overheads include the costs for obligations (recognised and measured in accordance with Section 21 *Provisions and Contingencies*) for dismantling, removing and restoring a site on which an item of **property, plant and equipment** is located that are incurred during the **reporting period** as a consequence of having used that item of property, plant and equipment to produce inventory during that period.

Allocation of production overheads

13.9 An entity shall allocate fixed production overheads to the costs of conversion on the basis of the normal capacity of the production facilities. Normal capacity is the production expected to be achieved on average over a number of periods or seasons under normal circumstances, taking into account the loss of capacity resulting from planned maintenance. The actual level of production may be used if it approximates normal capacity. The amount of fixed overhead allocated to each unit of production is not increased as a consequence of low production or idle plant. Unallocated overheads are recognised as an **expense** in the period in which they are incurred. In periods of abnormally high production, the amount of fixed overhead allocated to each unit of production is decreased so that inventories are not measured above cost. Variable production overheads are allocated to each unit of production on the basis of the actual use of the production facilities.

Joint products and by-products

13.10 A production process may result in more than one product being produced simultaneously. This is the case, for example, when joint products are produced or when there is a main product and a by-product. When the costs of raw materials or conversion of each product are not separately identifiable, an entity shall allocate them between the products on a rational and consistent basis. The allocation may be based, for example, on the relative sales value of each product either at the stage in the production process when the products become separately identifiable, or at the completion of production. Most by-products, by their nature, are immaterial. When this is the case, the entity shall measure them at selling price less costs to complete and sell and deduct this amount from the cost of the main product. As a result, the **carrying amount** of the main product is not materially different from its cost.

Other costs included in inventories

13.11 An entity shall include other costs in the cost of inventories only to the extent that they are incurred in bringing the inventories to their present location and condition.

13.12 [Deleted]

Costs excluded from inventories

13.13 Examples of costs excluded from the cost of inventories and recognised as expenses in the period in which they are incurred are:

(a) abnormal amounts of wasted materials, labour or other production costs;

(b) storage costs, unless those costs are necessary during the production process before a further production stage;

(c) administrative overheads that do not contribute to bringing inventories to their present location and condition; and

(d) selling costs.

Cost of inventories of a service provider

13.14 To the extent that service providers have inventories, they measure them at the costs of their production. These costs consist primarily of the labour and other costs of personnel directly engaged in providing the service, including supervisory personnel, and attributable overheads. Labour and other costs relating to sales and general administrative personnel are not included but are recognised as expenses in the period in which they are incurred. The cost of inventories of a service provider does not include profit margins or non-attributable overheads that are often factored into prices charged by service providers.

Cost of agricultural produce harvested from biological assets

13.15 Section 34 requires that inventories comprising agricultural produce that an entity has harvested from its biological assets should be measured on initial **recognition,** at the point of harvest, at either their fair value less estimated costs to sell or the lower of cost and estimated selling price less costs to complete and sell. This becomes the cost of the inventories at that date for application of this section.

Techniques for measuring cost, such as standard costing, retail method and most recent purchase price

13.16 An entity may use techniques such as the standard cost method, the retail method or most recent purchase price for measuring the cost of inventories if the result approximates cost. Standard costs take into account normal levels of materials and supplies, labour, efficiency and capacity utilisation. They are regularly reviewed and, if necessary, revised in the light of current conditions. The retail method measures cost by reducing the sales value of the inventory by the appropriate percentage gross margin.

Cost formulas

13.17 An entity shall measure the cost of inventories of items that are not ordinarily interchangeable and goods or services produced and segregated for specific projects by using specific identification of their individual costs.

13.18 An entity shall measure the cost of inventories, other than those dealt with in paragraph 13.17, by using the first-in, first-out (FIFO) or weighted average cost formula. An entity shall use the same cost formula for all inventories having a similar nature and use to the entity. For inventories with a different nature or use, different cost formulas may be justified. The last-in, first-out method (LIFO) is not permitted by this FRS.

Impairment of inventories

13.19 Paragraphs 27.2 to 27.4 require an entity to assess at the end of each reporting period whether any inventories are impaired, ie the carrying amount is not fully recoverable (eg because of damage, obsolescence or declining selling prices). If an item (or group of items) of inventory is impaired, those paragraphs require the entity to measure the inventory at its selling price less costs to complete and sell, and to recognise an **impairment loss**. Those paragraphs also require a reversal of a prior impairment in some circumstances.

Recognition as an expense

13.20 When inventories are sold, the entity shall recognise the carrying amount of those inventories as an expense in the period in which the related **revenue** is recognised.

13.20A When inventories held for distribution at no or nominal consideration are distributed, the carrying amount of those inventories shall be recognised as an expense.

13.21 Some inventories may be allocated to other asset accounts, for example, inventory used as a component of self-constructed property, plant or equipment. Inventories allocated to another **asset** in this way are accounted for subsequently in accordance with the section of this FRS relevant to that type of asset.

Disclosures

13.22 An entity shall disclose the following:

(a) the **accounting policies** adopted in measuring inventories, including the cost formula used;

(b) the total carrying amount of inventories and the carrying amount in classifications appropriate to the entity;

(c) [Deleted]

(d) impairment losses recognised or reversed in profit or loss in accordance with Section 27 *Impairment of Assets*; and

* (e) the total carrying amount of inventories pledged as security for **liabilities**.

Section 14
Investments in Associates

Scope of this section

14.1 This section applies to investments in **associates** in:

(a) **consolidated financial statements**; and

(b) the **individual financial statements** of an investor that is not a **parent**.

An entity that is a parent shall account for its investments in associates in its **separate financial statements** in accordance with paragraphs 9.26 and 9.26A, as appropriate.

Associates defined

14.2 An associate is an entity, including an unincorporated entity such as a partnership, over which the investor has **significant influence** and that is neither a **subsidiary** nor an interest in a **joint venture**.

14.3 Significant influence is the power to participate in the financial and operating policy decisions of the associate but is not **control** or **joint control** over those policies.

(a) If an investor holds, directly or indirectly (eg through subsidiaries), 20 per cent or more of the voting power of the associate, it is presumed that the investor has significant influence, unless it can be clearly demonstrated that this is not the case.

(b) Conversely, if the investor holds, directly or indirectly (eg through subsidiaries), less than 20 per cent of the voting power of the associate, it is presumed that the investor does not have significant influence, unless such influence can be clearly demonstrated.

(c) A substantial or majority ownership by another investor does not preclude an investor from having significant influence.

Measurement – accounting policy election

14.4 An investor that is not a parent but that has an investment in one or more associates shall, in its individual financial statements, account for all of its investments in associates using either:

(a) the cost model in accordance with paragraphs 14.5 to 14.6;

(b) [Deleted]

(c) at **fair value** in accordance with paragraphs 14.9 to 14.10A; or

(d) at fair value with changes in fair value recognised in **profit or loss**.

The Appendix to Section 2 *Concepts and Pervasive Principles* provides guidance on determining fair value.

14.4A An investor that is a parent shall, in its consolidated financial statements, account for all of its investments in associates using the equity method in accordance with paragraph 14.8, except as required by paragraph 14.4B.

14.4B Where an investor is a parent and has an associate that is **held as part of an investment portfolio**, the associate shall be measured at fair value with changes in fair value recognised in profit or loss in the consolidated financial statements.

Cost model

14.5 An investor that is not a parent, that chooses to adopt the cost model, shall measure its investments in associates at cost less any accumulated **impairment losses** recognised in accordance with Section 27 *Impairment of Assets*.

14.6 The investor shall recognise dividends and other distributions received from the investment as **income** without regard to whether the distributions are from accumulated profits of the associate arising before or after the date of acquisition.

14.7 [Deleted]

Equity method

14.8 Under the equity method of accounting, an equity investment is initially recognised at the transaction price (including **transaction costs**) and is subsequently adjusted to reflect the investor's share of the profit or loss, **other comprehensive income** and **equity** of the associate.

(a) *Distributions and other adjustments to carrying amount*. Distributions received from the associate reduce the **carrying amount** of the investment. Adjustments to the carrying amount may also be required as a consequence of changes in the associate's equity arising from items of other comprehensive income.

(b) *Potential voting rights*. Although potential voting rights are considered in deciding whether significant influence exists, an investor shall measure its share of profit or loss and other comprehensive income of the associate and its share of changes in the associate's equity on the basis of present ownership interests. Those measurements shall not reflect the possible exercise or conversion of potential voting rights.

(c) *Implicit goodwill and fair value adjustments*. On acquisition of the investment in an associate, an investor shall account for any difference (whether positive or negative) between the cost of acquisition and the investor's share of the fair values of the net identifiable assets of the associate in accordance with paragraphs 19.22 to 19.24. An investor shall adjust its share of the associate's profits or losses after acquisition to account for additional **depreciation** or **amortisation** of the associate's depreciable or amortisable assets (including **goodwill**) on the basis of the excess of their fair values over their carrying amounts at the time the investment was acquired.

(d) *Impairment*. If there is an indication that an investment in an associate may be impaired, an investor shall test the entire carrying amount of the investment for impairment in accordance with Section 27 as a single **asset**. Any goodwill included as part of the carrying amount of the investment in the associate is not tested separately for impairment but, rather, as part of the test for impairment of the investment as a whole.

(e) *Investor's transactions with associates*. The investor shall eliminate unrealised profits and losses resulting from upstream (associate to investor) and downstream (investor to associate) transactions to the extent of the investor's interest in the associate. Unrealised losses on such transactions may provide evidence of an impairment of the asset transferred.

(f) *Date of associate's financial statements*. In applying the equity method, the investor shall use the **financial statements** of the associate as of the same date as the financial statements of the investor unless it is **impracticable** to do so. If it is impracticable, the investor shall use the most recent available financial statements of the associate, with adjustments made for the effects of any significant transactions or events occurring between the accounting period ends.

(g) *Associate's accounting policies*. If the associate uses **accounting policies** that differ from those of the investor, the investor shall adjust the associate's financial statements to reflect the investor's accounting policies for the purpose of applying the equity method unless it is impracticable to do so.

(h) *Losses in excess of investment*. If an investor's share of losses of an associate equals or exceeds the carrying amount of its investment in the associate, the investor shall discontinue recognising its share of further losses. After the investor's interest is reduced to zero, the investor shall recognise additional losses by a **provision** (see Section 21 *Provisions and Contingencies*) only to the extent that the investor has incurred legal or **constructive obligations** or has made payments on behalf of the associate. If the associate subsequently reports profits, the investor shall resume recognising its share of those profits only after its share of the profits equals the share of losses not recognised.

(i) *Discontinuing the equity method*. An investor shall cease using the equity method from the date that significant influence ceases and, provided the associate does not become a subsidiary in accordance with Section 19 *Business Combinations and Goodwill* or a joint venture in accordance with Section 15 *Investments in Joint Ventures*, shall account for the investment as follows:

   (i) If the investor loses significant influence over an associate as a result of a full or partial disposal, it shall derecognise that associate and recognise in profit or loss the difference between the proceeds from the disposal and the carrying amount of the investment in the associate relating to the proportion disposed of or lost at the date significant influence is lost. The investor shall account for any retained interest using Section 11 *Basic Financial Instruments* or Section 12 *Other Financial Instruments Issues*, as appropriate. The carrying amount of the investment at the date that it ceases to be an associate shall be regarded as its cost on initial **measurement** as a **financial asset**; and

   (ii) If an investor loses significant influence for reasons other than a partial disposal of its investment, the investor shall regard the carrying amount of the investment at that date as a new cost basis and shall account for the investment using Sections 11 or 12, as appropriate.

   The gain or loss arising on the disposal shall also include those amounts that have been recognised in other comprehensive income in relation to that associate, where those amounts are required to be reclassified to profit or loss upon disposal in accordance with other sections of this FRS. Amounts that are not required to be reclassified to profit or loss upon disposal of the related assets or **liabilities** in accordance with other sections of this FRS shall be transferred directly to retained earnings.

Fair value in accordance with paragraph 14.4(c)

14.9 When an investment in an associate is recognised initially, an investor that is not a parent, that chooses to adopt the accounting policy set out in paragraph 14.4(c), shall measure it at the transaction price.

14.10 At each **reporting date**, investments in associates shall be measured at fair value using the fair value guidance in the Appendix to Section 2. Changes in fair value shall be recognised in other comprehensive income (or profit or loss) in accordance with paragraphs 17.15E and 17.15F.

14.10A The investor shall recognise dividends and other distributions received from the investment as income without regard to whether the distributions are from accumulated profits of the associate arising before or after the date of acquisition.

14.11 [Deleted]

Disclosures in individual and consolidated financial statements

14.12 The financial statements shall disclose:

(a) the accounting policy for investments in associates;

(b) the carrying amount of investments in associates; and

(c) the fair value of investments in associates accounted for using the equity method for which there are published price quotations.

14.13 For investments in associates accounted for in accordance with the cost model, an investor shall disclose the amount of dividends and other distributions recognised as income.

14.14 For investments in associates accounted for in accordance with the equity method, an investor shall disclose separately its share of the profit or loss of such associates and its share of any **discontinued operations** of such associates.

14.15 For investments in associates accounted for in accordance with paragraph 14.4(c), an investor shall make the disclosures required by paragraphs 11.43 and 11.44.

14.15A The individual financial statements of an investor that is not a parent shall disclose summarised financial information about the investments in the associates, along with the effect of including those investments as if they had been accounted for using the equity method. Investing entities that are exempt from preparing consolidated financial statements, or would be exempt if they had subsidiaries, are exempt from this requirement.

Section 15
Investments in Joint Ventures

Scope of this section

15.1 This section applies to:

(a) investments in **joint ventures** in:

(i) **consolidated financial statements**; and

(ii) the **individual financial statements** of a **venturer** that is not a **parent**; and

(b) investments in jointly controlled operations and jointly controlled assets in the **separate financial statements** of a venturer that is a parent.

A venturer that is a parent shall account for interests in **jointly controlled entities** in its separate financial statements in accordance with paragraphs 9.26 and 9.26A, as appropriate.

Joint ventures defined

15.2 **Joint control** is the contractually agreed sharing of **control** over an economic activity, and exists only when the strategic financial and operating decisions relating to the activity require the unanimous consent of the parties sharing control (the venturers).

15.3 A joint venture is a contractual arrangement whereby two or more parties undertake an economic activity that is subject to joint control. Joint ventures can take the form of jointly controlled operations, jointly controlled assets, or jointly controlled entities.

Jointly controlled operations

15.4 The operation of some joint ventures involves the use of the **assets** and other resources of the venturers rather than the establishment of a corporation, partnership or other entity, or a financial structure that is separate from the venturers themselves. Each venturer uses its own **property, plant and equipment** and carries its own **inventories**. It also incurs its own **expenses** and **liabilities** and raises its own finance, which represent its own obligations. The joint venture activities may be carried out by the venturer's employees alongside the venturer's similar activities. The joint venture agreement usually provides a means by which the **revenue** from the sale of the joint product and any expenses incurred in common are shared among the venturers.

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

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

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

Jointly controlled assets

15.6 Some joint ventures involve the joint control, and often the joint ownership, by the venturers of one or more assets contributed to, or acquired for the purpose of, the joint venture and dedicated to the purposes of the joint venture.

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

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

(b) any liabilities that it has incurred;

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

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

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

Jointly controlled entities

15.8 A jointly controlled entity is a joint venture that involves the establishment of a corporation, partnership or other entity in which each venturer has an interest. The entity operates in the same way as other entities, except that a contractual arrangement between the venturers establishes joint control over the economic activity of the entity.

Measurement – accounting policy election

15.9 A venturer that is not a parent but has one or more interests in jointly controlled entities shall, in its individual financial statements, account for all of its interests in jointly controlled entities using either:

(a) the cost model in accordance with paragraphs 15.10 to 15.11;

(b) [Deleted]

(c) at **fair value** in accordance with paragraphs 15.14 to 15.15A; or

(d) at fair value with changes in fair value recognised in **profit or loss**.

The Appendix to Section 2 *Concepts and Pervasive Principles* provides guidance on determining fair value.

15.9A A venturer that is a parent shall, in its consolidated financial statements, account for all of its investments in jointly controlled entities using the equity method in accordance with paragraph 15.13, except as required by paragraph 15.9B.

15.9B A venturer that is a parent, shall measure its investments in jointly controlled entities **held as part of an investment portfolio** at fair value with changes in fair value recognised in profit or loss in the consolidated financial statements.

Cost model

15.10 A venturer that is not a parent, that chooses to adopt the cost model, shall measure its investments in jointly controlled entities, at cost less any accumulated **impairment losses** recognised in accordance with Section 27 *Impairment of Assets*.

15.11 The venturer shall recognise distributions received from the investment as income without regard to whether the distributions are from accumulated profits of the jointly controlled entity arising before or after the date of acquisition.

15.12 [Deleted]

Equity method

15.13 A venturer shall measure its investments in jointly controlled entities by the equity method using the procedures in accordance with paragraph 14.8 (substituting 'joint control' where that paragraph refers to '**significant influence**', and 'jointly controlled entity' where that paragraph refers to '**associate**').

Fair value in accordance with paragraph 15.9(c)

15.14 When an investment in a jointly controlled entity is recognised initially, a venturer that is not a parent, that chooses to adopt the **accounting policy** set out in paragraph 15.9(c), shall measure it at the transaction price.

15.15 At each **reporting date**, investments in jointly controlled entities shall be measured at fair value using the fair value guidance in Appendix to Section 2. Changes in fair value shall be recognised in **other comprehensive income** (or profit or loss) in accordance with paragraphs 17.15E and 17.15F.

15.15A The venturer shall recognise dividends and other distributions received from the investment as income without regard to whether the distributions are from accumulated profits of the jointly controlled entity arising before or after the date of acquisition.

Transactions between a venturer and a joint venture

15.16 When a venturer contributes or sells assets to a joint venture, **recognition** of any portion of a **gain** or loss from the transaction shall reflect the substance of the transaction. While the assets are retained by the joint venture, and provided the venturer has transferred the significant risks and rewards of ownership, the venturer shall recognise only that portion of the gain or loss that is attributable to the interests of the other venturers in its consolidated financial statements. The venturer shall recognise the full amount of any loss when the contribution or sale provides evidence of an impairment loss.

15.17 When a venturer purchases an asset from a joint venture, the venturer shall not recognise its share of the profits of the joint venture from the transaction until it resells the assets to an independent party or otherwise realises its **carrying amount**. A venturer shall recognise its share of the losses resulting from these transactions in the same way as profits except that losses shall be recognised immediately when they represent an impairment loss.

If investor does not have joint control

15.18 An investor in a joint venture that does not have joint control shall account for that investment in accordance with Section 11 *Basic Financial Instruments* or Section 12 *Other Financial Instruments Issues* or, if it has significant influence in the joint venture, in accordance with Section 14 *Investments in Associates*.

Disclosures in individual and consolidated financial statements

15.19 The financial statements shall disclose the following:

(a) the accounting policy for recognising investments in jointly controlled entities;

(b) the carrying amount of investments in jointly controlled entities;

(c) the fair value of investments in jointly controlled entities accounted for using the equity method for which there are published price quotations; and

* (d) the aggregate amount of its commitments relating to joint ventures, including its share in the capital commitments that have been incurred jointly with other venturers, as well as its share of the capital commitments of the joint ventures themselves.

15.20 For jointly controlled entities accounted for in accordance with the equity method, the venturer shall disclose separately its share of the profit or loss of such investments and its share of any **discontinued operations** of such jointly controlled entities.

15.21 For jointly controlled entities accounted for in accordance with paragraph 15.9(c), the venturer shall make the disclosures required by paragraphs 11.43 and 11.44.

15.21A The individual financial statements of a venturer that is not a parent shall disclose summarised financial information about the investments in the jointly controlled entities, along with the effect of including those investments as if they had been accounted for using the equity method. Investing entities that are exempt from preparing consolidated financial statements, or would be exempt if they had **subsidiaries**, are exempt from this requirement.

Section 16
Investment Property

Scope of this section

16.1 This section applies to **investment property** and property interests held by a lessee under an **operating lease** that are classified as investment property (see paragraph 16.3).

16.1A This section does not apply to investment property rented to another **group** entity and transferred to **property, plant and equipment** (see paragraph 16.4A).

16.2 [Deleted]

Classification

16.3 A property interest that is held by a lessee under an operating lease may be classified and accounted for as investment property using this section if, and only if, the property would otherwise meet the definition of an investment property and the lessee can measure the **fair value** of the property interest on an on-going basis. The Appendix to Section 2 *Concepts and Pervasive Principles* provides guidance on determining fair value. This classification alternative is available on a property-by-property basis.

16.3A Property held primarily for the provision of social benefits, eg social housing held by a **public benefit entity**, shall not be classified as investment property and shall be accounted for as property, plant and equipment in accordance with Section 17 *Property, Plant and Equipment*.

16.4 Mixed use property shall be separated between investment property and property, plant and equipment if the resulting portions could be sold separately or leased out separately under a **finance lease**. However, if the fair value of the investment property component cannot be measured reliably, the entire property shall be accounted for as property, plant and equipment in accordance with Section 17. The Appendix to Section 2 provides guidance on determining fair value.

Investment property rented to another group entity

16.4A An entity that rents investment property to another group entity shall account for those properties either:

(a) at fair value with changes in fair value recognised in **profit or loss** in accordance with this section (the Appendix to Section 2 provides guidance on determining fair value); or

(b) by transferring them to property, plant and equipment and applying the cost model in accordance with Section 17.

An entity choosing to apply (b) above shall provide all the disclosures required by Section 17, other than those related to fair value measurement.

16.4B When only part of a property is rented to another group entity and the remainder is used for other purposes (such as being rented to an external third party or owner-occupied), paragraph 16.4A only applies to the component of that property that is rented to another group entity.

Initial measurement

16.5 An entity shall measure an investment property at its cost at initial **recognition**. The cost of a purchased investment property comprises its purchase price and any directly attributable expenditure such as legal and brokerage fees, property transfer taxes and other transaction costs. If payment is deferred beyond normal credit terms, the cost is the **present value** of all future payments. An entity shall determine the cost of a self-constructed investment property in accordance with paragraphs 17.10 to 17.14.

16.6 The initial cost of a property interest held under a **lease** and classified as an investment property shall be as prescribed for a finance lease by paragraphs 20.9 and 20.10, even if the lease would otherwise be classified as an operating lease if it was in the scope of Section 20 *Leases*. In other words, the **asset** is recognised at the lower of the fair value of the property and the present value of the **minimum lease payments**. An equivalent amount is recognised as a **liability** in accordance with paragraphs 20.9 and 20.10. Any premium paid for a lease is treated as part of the minimum lease payments for this purpose, and is therefore included in the cost of the asset, but is excluded from the liability.

Subsequent measurement

16.7 An investment property shall be measured at fair value at each **reporting date** with changes in fair value recognised in profit or loss. If a property interest held under a lease is classified as an investment property, the item accounted for at fair value is that interest and not the underlying property. The Appendix to Section 2 provides guidance on determining fair value.

Transfers

16.8 [Deleted]

16.9 Unless otherwise required by this FRS, an entity shall transfer a property to, or from, investment property only when the property first meets, or ceases to meet, the definition of investment property.

16.9A When a property ceases to meet the definition of an investment property (for example it becomes owner-occupied or **inventory**), the **deemed cost** for subsequent accounting as property, plant and equipment (in accordance with Section 17) or inventory (in accordance with Section 13 *Inventories*) shall be its fair value at the date of change in use.

16.9B If an owner-occupied property becomes an investment property, an entity shall apply Section 17 up to the date of change in use. The entity shall treat any difference at that date between the **carrying amount** of the property in accordance with Section 17 and its fair value in the same way as a revaluation in accordance with Section 17.

16.9C For a transfer from inventories to investment property that will be carried at fair value, any difference between the fair value of the property at that date and its previous carrying amount shall be recognised in profit or loss.

Disclosures

16.10 An entity shall disclose the following:

* (a) the methods and significant assumptions applied in determining the fair value of investment property;

(b) the extent to which the fair value of investment property (as measured or disclosed in the **financial statements**) is based on a valuation by an independent valuer who holds a recognised and relevant professional qualification and has recent experience in the location and class of the investment property being valued. If there has been no such valuation, that fact shall be disclosed;

* (c) the existence and amounts of restrictions on the realisability of investment property or the remittance of **income** and proceeds of disposal;

* (d) contractual obligations to purchase, construct or develop investment property or for repairs, maintenance or enhancements; and

* (e) a reconciliation between the carrying amounts of investment property at the beginning and end of the period, showing separately:

  (i) additions, disclosing separately those additions resulting from acquisitions through **business combinations**;

  * (ii) net **gains** or losses from fair value adjustments;

  (iii) transfers to and from property, plant and equipment (see paragraphs 16.9 to 16.9B);

  (iv) transfers to and from inventories (see paragraphs 16.9, 16.9A and 16.9C); and

  (v) other changes.

  This reconciliation need not be presented for prior periods.

16.11 In accordance with Section 20, an entity shall provide all relevant disclosures required in that section about leases into which it has entered.

Section 17
Property, Plant and Equipment

Scope

17.1 This section applies to:

(a) **property**, **plant and equipment**; and

(b) **investment property** rented to another **group** entity when the reporting entity chooses to use the cost model in this section as permitted by paragraph 16.4A.

17.2 [Deleted]

17.3 This section does not apply to:

(a) **biological assets** related to **agricultural activity** (see Section 34 *Specialised Activities*) or **heritage assets** (see Section 34); or

(b) mineral rights and mineral reserves, such as oil, natural gas and similar non-regenerative resources (see Section 34).

Recognition

17.4 An entity shall apply the **recognition** criteria in paragraph 2.27 in determining whether to recognise an item of property, plant or equipment. Therefore, the entity shall recognise the cost of an item of property, plant and equipment as an **asset** if, and only if:

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

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

17.5 Items such as spare parts, stand-by equipment and servicing equipment are recognised in accordance with this section when they meet the definition of property, plant and equipment. Otherwise, such items are classified as **inventory**.

17.6 Parts of some items of property, plant and equipment may require replacement at regular intervals (eg the roof of a building). An entity shall add to the **carrying amount** of an item of property, plant and equipment the cost of replacing part of such an item when that cost is incurred if the replacement part is expected to provide incremental future benefits to the entity. The carrying amount of those parts that are replaced is derecognised in accordance with paragraphs 17.27 to 17.30 regardless of whether the replaced parts had been depreciated separately. If it is **impracticable** for an entity to identify the carrying amount of the replaced part, it may be estimated using the current cost of the replacement part as a proxy for the original cost of the replaced part and adjusting it for **depreciation** and impairment. Paragraph 17.16 provides that if the major components of an item of property, plant and equipment have significantly different patterns of consumption of economic benefits, an entity shall allocate the initial cost of the asset to its major components and depreciate each such component separately over its **useful life**.

17.7 A condition of continuing to operate an item of property, plant and equipment (eg a bus) may be performing regular major inspections for faults regardless of whether parts of the item are replaced. When each major inspection is performed, its cost is recognised in the carrying amount of the item of property, plant and equipment as a replacement if the recognition criteria are satisfied. Any remaining carrying amount of the cost of the previous major inspection (as distinct from physical parts) is derecognised. This is done regardless of whether the cost of the previous major inspection was identified in the transaction in which the item was acquired or constructed. If necessary, the estimated cost of a future similar inspection may be used as an indication of what the cost of the existing inspection component was when the item was acquired or constructed.

17.8 Land and buildings are separable assets, and an entity shall account for them separately, even when they are acquired together.

Initial measurement

17.9 An entity shall measure an item of property, plant and equipment at initial recognition at its cost.

Elements of cost

17.10 The cost of an item of property, plant and equipment comprises all of the following:

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

(b) Any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management. These can include the costs of site preparation, initial delivery and handling, installation and assembly, and testing of functionality.

(c) The initial estimate of the costs, recognised and measured in accordance with Section 21 *Provisions and Contingencies,* of dismantling and removing the item and restoring the site on which it is located, the obligation for which an entity incurs either when the item is acquired or as a consequence of having used the item during a particular period for purposes other than to produce inventories during that period.

(d) Any **borrowing costs** capitalised in accordance with paragraph 25.2.

17.11 The following costs are not costs of an item of property, plant and equipment, and an entity shall recognise them as an **expense** when they are incurred:

(a) costs of opening a new facility;

(b) costs of introducing a new product or service (including costs of advertising and promotional activities);

(c) costs of conducting **business** in a new location or with a new class of customer (including costs of staff training); and

(d) administration and other general overhead costs.

17.12 The **income** and related expenses of incidental operations during construction or development of an item of property, plant and equipment are recognised in **profit or loss** if those operations are not necessary to bring the item to its intended location and operating condition.

Measurement of cost

17.13 The cost of an item of property, plant and equipment is the cash price equivalent at the recognition date. If payment is deferred beyond normal credit terms, the cost is the **present value** of all future payments.

Exchanges of assets

17.14 An item of property, plant or equipment may be acquired in exchange for a non-monetary asset or assets, or a combination of monetary and non-monetary assets. An entity shall measure the cost of the acquired asset at **fair value** unless:

(a) the exchange transaction lacks commercial substance; or

(b) the fair value of neither the asset received nor the asset given up is reliably measurable. In that case, the asset's cost is measured at the carrying amount of the asset given up.

Subsequent measurement

17.15 An entity shall measure all items of property, plant and equipment after initial recognition using the cost model (in accordance with paragraph 17.15A) or the revaluation model (in accordance with paragraphs 17.15B to 17.15F). Where the revaluation model is selected, this shall be applied to all items of property, plant and equipment in the same **class of asset** (ie having a similar nature, function or use in the business). An entity shall recognise the costs of day-to-day servicing of an item of property, plant and equipment in profit or loss in the period in which the costs are incurred.

Cost model

17.15A Under the cost model, an entity shall measure an item of property, plant and equipment at cost less any accumulated depreciation and any accumulated **impairment losses**.

Revaluation model

17.15B Under the revaluation model, an item of property, plant and equipment whose fair value can be measured reliably shall be carried at a revalued amount, being its fair value at the date of 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**.

17.15C The fair value of land and buildings is usually determined from market-based evidence by appraisal that is normally undertaken by professionally qualified valuers. The fair value of items of plant and equipment is usually their market value determined by appraisal. The Appendix to Section 2 *Concepts and Pervasive Principles* provides further guidance on determining fair value.

17.15D If there is no market-based evidence of fair value because of the specialised nature of the item of property, plant and equipment and the item is rarely sold, except as part of a continuing business, an entity may need to estimate fair value using an income or a **depreciated replacement cost** approach.

Reporting gains and losses on revaluations

17.15E 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**. 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.

17.15F The decrease of an asset's carrying amount as a result of a revaluation shall be recognised in other comprehensive income to the extent of any previously recognised revaluation increase accumulated in equity, in respect of that asset. If a revaluation decrease exceeds the accumulated revaluation **gains** accumulated in equity in respect of that asset, the excess shall be recognised in profit or loss.

Depreciation

17.16 If the major components of an item of property, plant and equipment have significantly different patterns of consumption of economic benefits, an entity shall allocate the initial cost of the asset to its major components and depreciate each such component separately over its useful life. Other assets shall be depreciated over their useful lives as a single asset. There are some exceptions, such as land which generally has an unlimited useful life and therefore is not usually depreciated.

17.17 The depreciation charge for each period shall be recognised in profit or loss unless another section of this FRS requires the cost to be recognised as part of the cost of an asset. For example, the depreciation of manufacturing property, plant and equipment is included in the costs of inventories (see Section 13 *Inventories*).

Depreciable amount and depreciation period

17.18 An entity shall allocate the **depreciable amount** of an asset on a systematic basis over its useful life.

17.19 Factors such as a change in how an asset is used, significant unexpected wear and tear, technological advancement, and changes in market prices may indicate that the **residual value** or useful life of an asset has changed since the most recent annual **reporting date**. If such indicators are present, an entity shall review its previous estimates and, if current expectations differ, amend the residual value, depreciation method or useful life. The entity shall account for the change in residual value, depreciation method or useful life as a change in an accounting estimate in accordance with paragraphs 10.15 to 10.18.

17.20 Depreciation of an asset begins when it is available for use, ie when it is in the location and condition necessary for it to be capable of operating in the manner intended by management. Depreciation of an asset ceases when the asset is derecognised. Depreciation does not cease when the asset becomes idle or is retired from active use unless the asset is fully depreciated. However, under usage methods of depreciation the depreciation charge can be zero while there is no production.

17.21 An entity shall consider all the following factors in determining the useful life of an asset:

(a) The expected usage of the asset. Usage is assessed by reference to the asset's expected capacity or physical output.

(b) Expected physical wear and tear, which depends on operational factors such as the number of shifts for which the asset is to be used and the repair and maintenance programme, and the care and maintenance of the asset while idle.

(c) Technical or commercial obsolescence arising from changes or improvements in production, or from a change in the market demand for the product or service output of the asset.

(d) Legal or similar limits on the use of the asset, such as the expiry dates of related **leases**.

Depreciation method

17.22 An entity shall select a depreciation method that reflects the pattern in which it expects to consume the asset's future economic benefits. The possible depreciation methods include the straight-line method, the diminishing balance method and a method based on usage such as the units of production method.

17.23 If there is an indication that there has been a significant change since the last annual reporting date in the pattern by which an entity expects to consume an asset's future economic benefits, the entity shall review its present depreciation method and, if current expectations differ, change the depreciation method to reflect the new pattern. The entity shall account for the change as a change in an accounting estimate in accordance with paragraphs 10.15 to 10.18.

Impairment

Recognition and measurement of impairment

17.24 At each reporting date, an entity shall apply Section 27 *Impairment of Assets* to determine whether an item or group of items of property, plant and equipment is impaired and, if so, how to recognise and measure the impairment loss. That section explains when and how an entity reviews the carrying amount of its assets, how it determines the **recoverable amount** of an asset, and when it recognises or reverses an impairment loss.

Compensation for impairment

17.25 An entity shall include in profit or loss, compensation from third parties for items of property, plant and equipment that were impaired, lost or given up only when the compensation is virtually certain.

Property, plant and equipment held for sale

17.26 Paragraph 27.9(f) states that a plan to dispose of an asset before the previously expected date is an indicator of impairment that triggers the calculation of the asset's recoverable amount for the purpose of determining whether the asset is impaired.

Derecognition

17.27 An entity shall derecognise an item of property, plant and equipment:

(a) on disposal; or

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

17.28 An entity shall recognise the **gain** or loss on the **derecognition** of an item of property, plant and equipment in profit or loss when the item is derecognised (unless Section 20 *Leases* requires otherwise on a sale and leaseback). The entity shall not classify such gains as **revenue**.

17.29 In determining the date of disposal of an item, an entity shall apply the criteria in Section 23 *Revenue* for recognising revenue from the sale of goods. Section 20 applies to disposal by a sale and leaseback.

17.30 An entity shall determine the gain or loss arising from the derecognition of an item of property, plant and equipment as the difference between the net disposal proceeds, if any, and the carrying amount of the item.

Disclosures

17.30A The following disclosures (other than those related to fair value measurement) are relevant to an entity that chooses to measure investment properties rented to another group entity under the cost model in this section, as permitted by paragraph 16.4A(b).

17.31 An entity shall disclose the following for each class of property, plant and equipment:

* (a) the **measurement** bases used for determining the gross carrying amount;

(b) the depreciation methods used;

(c) the useful lives or the depreciation rates used;

* (d) the gross carrying amount and the accumulated depreciation (aggregated with accumulated impairment losses) at the beginning and end of the reporting period; and

* (e) a reconciliation of the carrying amount at the beginning and end of the reporting period showing separately:

(i) additions;

(ii) disposals;

(iii) acquisitions through **business combinations**;

(iv) revaluations;

(v) transfers to or from investment property (see paragraphs 16.9 to 16.9C);

(vi) impairment losses recognised or reversed in profit or loss in accordance with Section 27;

(vii) depreciation; and

(viii) other changes.

This reconciliation need not be presented for prior periods.

17.31A An entity shall disclose the carrying amount at the end of the reporting period of investment property rented to another group entity, where the entity has chosen to account for such properties using the cost model in accordance with this section (see paragraph 16.4A).

17.32 An entity shall also disclose the following:

* (a) the existence and carrying amounts of property, plant and equipment to which the entity has restricted title or that is pledged as security for **liabilities**; and

* (b) the amount of contractual commitments for the acquisition of property, plant and equipment.

17.32A If items of property, plant and equipment are stated at revalued amounts, the following shall be disclosed:

* (a) the effective date of the revaluation;

(b) whether an independent valuer was involved;

* (c) the methods and significant assumptions applied in estimating the items' fair values; and

* (d) for each revalued class of property, plant and equipment, the carrying amount that would have been recognised had the assets been carried under the cost model.

Section 18
Intangible Assets other than Goodwill

Scope of this section

18.1 This section applies to **intangible assets** except for **goodwill** (see Section 19 *Business Combinations and Goodwill*) and intangible assets held by an entity for sale in the ordinary course of **business** (see Section 13 *Inventories* and Section 23 *Revenue*).

18.1A [Moved to paragraph 18.3(d)]

18.2 [Deleted]

18.3 This section does not apply to:

(a) **financial assets** (see Section 11 *Basic Financial Instruments* and Section 12 *Other Financial Instruments Issues*);

(b) **heritage assets** (see Section 34 *Specialised Activities*);

(c) exploration for and evaluation of mineral resources, such as oil, natural gas and similar non-regenerative resources (see Section 34) and expenditure on the development and extraction of such resources; or

(d) **deferred acquisition costs** and intangible assets arising from contracts in the scope of **FRS 103**, except for the disclosure requirements in this section which apply to intangible assets arising from contracts with in the scope of FRS 103.

Recognition

General principle for recognising intangible assets

18.4 An entity shall apply the **recognition** criteria in paragraph 2.27 in determining whether to recognise an intangible asset. Therefore, the entity shall recognise an intangible asset as an **asset** if, and only if:

(a) it is **probable** that the expected future economic benefits that are attributable to the asset will flow to the entity; and

(b) the cost or value of the asset can be measured reliably.

18.5 An entity shall assess the probability of expected future economic benefits using reasonable and supportable assumptions that represent management's best estimate of the economic conditions that will exist over the **useful life** of the asset.

18.6 An entity uses judgement to assess the degree of certainty attached to the flow of future economic benefits that are attributable to the use of the asset on the basis of the evidence available at the time of initial recognition, giving greater weight to external evidence.

18.7 The probability recognition criterion in paragraph 18.4(a) is always considered satisfied for intangible assets that are separately acquired.

Acquisition as part of a business combination

18.8 Intangible assets acquired in a **business combination** shall be recognised separately from goodwill when all the following three conditions are satisfied:

(a) the recognition criteria set out in paragraph 18.4 are met;

(b) the intangible asset arises from contractual or other legal rights; and

(c) the intangible asset is separable (ie capable of being separated or divided from the entity and sold, transferred, licensed, rented or exchanged either individually or together with a related contract, asset or **liability**).

An entity may additionally choose to recognise intangible assets separately from goodwill for which condition (a) and only one of (b) or (c) above is met. When an entity chooses to recognise such additional intangible assets, this policy shall be applied to all intangible assets in the same class (ie having a similar nature, function or use in the business), and must be applied consistently to all business combinations. Licences are an example of a category of intangible asset that may be treated as a separate class, however, further subdivision may be appropriate, for example, where different types of licences have different functions within the business.

Internally generated intangible assets

18.8A To assess whether an internally generated intangible asset meets the criteria for recognition, an entity classifies the generation of the asset into:

(a) a **research** phase; and

(b) a **development** phase.

18.8B If an entity cannot distinguish the research phase from the development phase of an internal project to create an intangible asset, the entity treats the expenditure on that project as if it were incurred in the research phase only.

18.8C An entity shall recognise expenditure on the following items as an **expense** and shall not recognise such expenditure as intangible assets:

(a) Internally generated brands, logos, publishing titles, customer lists and items similar in substance.

(b) Start-up activities (ie start-up costs), which include establishment costs such as legal and secretarial costs incurred in establishing a legal entity, expenditure to open a new facility or business (ie pre-opening costs) and expenditure for starting new operations or launching new products or processes (ie pre-operating costs).

(c) Training activities.

(d) Advertising and promotional activities (unless it meets the definition of **inventories held for distribution at no or nominal consideration** (see paragraph 13.4A)).

(e) Relocating or reorganising part or all of an entity.

(f) Internally generated goodwill.

18.8D Paragraph 18.8C does not preclude recognising a prepayment as an asset when payment for goods or services has been made in advance of the delivery of the goods or the rendering of the services.

Research phase

18.8E No intangible asset arising from research (or from the research phase of an internal project) shall be recognised. Expenditure on research (or on the research phase of an internal project) shall be recognised as an expense when it is incurred.

18.8F In the research phase of an internal project, an entity cannot demonstrate that an intangible asset exists that will generate probable future economic benefits.

18.8G Examples of research activities are:

(a) Activities aimed at obtaining new knowledge.

(b) The search for, evaluation and final selection of, applications of research findings and other knowledge.

(c) The search for alternatives for materials, devices, products, processes, systems or services.

(d) The formulation, design, evaluation and final selection of possible alternatives for new or improved material, devices, projects, processes, systems or services.

Development phase

18.8H An entity may recognise an intangible asset arising from development (or from the development phase of an internal project) if, and only if, an entity can demonstrate all of the following:

(a) The technical feasibility of completing the intangible asset so that it will be available for use or sale.

(b) Its intention to complete the intangible asset and use or sell it.

(c) Its ability to use or sell the intangible asset.

(d) How the intangible asset will generate probable future economic benefits. Among other things, the entity can demonstrate the existence of a market for the output of the intangible asset or the intangible asset itself or, if it is to be used internally, the usefulness of the intangible asset.

(e) The availability of adequate technical, financial and other resources to complete the development and to use or sell the intangible asset.

(f) Its ability to measure reliably the expenditure attributable to the intangible asset during its development.

18.8I In the development phase of an internal project, an entity can, in some instances, identify an intangible asset and demonstrate that the asset will generate probable future economic benefits. This is because the development phase of a project is further advanced than the research phase.

18.8J Examples of development activities are:

(a) The design, construction and testing of pre-production or pre-use prototypes and models.

(b) The design of tools, jigs, moulds and dies involving new technology.

(c) The design, construction and operation of a pilot plant that is not of a scale economically feasible for commercial production.

(d) The design, construction and testing of a chosen alternative for new or improved materials, devices, products, processes, systems or services.

18.8K Where an entity adopts a policy of capitalising expenditure in the development phase that meets the conditions of paragraph 18.8H, that policy shall be applied consistently to all expenditure that meets the requirements of paragraph 18.8H. Expenditure that does not meet the conditions of paragraph 18.8H is expensed as incurred.

Initial measurement

18.9 An entity shall measure an intangible asset initially at cost.

Separate acquisition

18.10 The cost of a separately acquired intangible asset comprises:

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

(b) any directly attributable cost of preparing the asset for its intended use.

Internally generated intangible assets

18.10A The cost of an internally generated intangible asset for the purpose of paragraph 18.9 is the sum of expenditure incurred from the date when the intangible asset first meets the recognition criteria in paragraphs 18.4 and 18.8H.

18.10B The cost of an internally generated intangible asset comprises all directly attributable costs necessary to create, produce and prepare the asset to be capable of operating in the manner intended by management. Examples of directly attributable costs are:

(a) costs of materials and services used or consumed in generating the intangible asset;

(b) costs of **employee benefits** (as defined in Section 28 *Employee Benefits*) arising from the generation of the intangible asset;

(c) fees to register a legal right; and

(d) **amortisation** of patents and licences that are used to generate the intangible asset.

Section 25 *Borrowing Costs* specifies criteria for the recognition of interest as an element of the cost of an internally generated intangible asset.

Acquisition as part of a business combination

18.11 If an intangible asset is acquired in a business combination, the cost of that intangible asset is its **fair value** at the **acquisition date**.

Acquisition by way of a grant

18.12 If an intangible asset is acquired by way of a grant, the cost of that intangible asset is its fair value at the date the grant is received or receivable in accordance with Section 24 *Government Grants* in respect of **government grants** or, for **public benefit entities**, Section 34 in respect of incoming resources from **non-exchange transactions** as appropriate.

Exchanges of assets

18.13 An intangible asset may be acquired in exchange for a non-monetary asset or assets, or a combination of monetary and non-monetary assets. An entity shall measure the cost of such an intangible asset at fair value unless:

(a) the exchange transaction lacks commercial substance; or

(b) the fair value of neither the asset received nor the asset given up is reliably measurable. In that case, the asset's cost is measured at the **carrying amount** of the asset given up.

18.14 [Replaced by paragraph 18.8A]

18.15 [Moved to paragraph 18.8C]

18.16 [Moved to paragraph 18.8D]

Past expenses not to be recognised as an asset

18.17 Expenditure on an intangible item that was initially recognised as an expense shall not be recognised at a later date as part of the cost of an asset.

Subsequent measurement

18.18 An entity shall measure intangible assets after initial recognition using the cost model (in accordance with paragraph 18.18A) or the revaluation model (in accordance with paragraphs 18.18B to 18.18H). Where the revaluation model is selected, this shall be applied to all intangible assets in the same **class of asset**. If an intangible asset in a class of revalued intangible assets cannot be revalued because there is no **active market** for this asset, the asset shall be carried at its cost less any accumulated amortisation and **impairment losses**.

Cost model

18.18A Under the cost model, an entity shall measure its assets at cost less any accumulated amortisation and any accumulated impairment losses. The requirements for amortisation are set out in paragraphs 18.19 to 18.24.

Revaluation model

18.18B Under the revaluation model, an intangible asset shall be carried at a revalued amount, being its fair value at the date of revaluation less any subsequent accumulated amortisation and subsequent accumulated impairment losses, provided that the fair value can be determined by reference to an active market. The requirements for amortisation are set out in paragraphs 18.19 to 18.24.

18.18C The revaluation model does not allow:

(a) the revaluation of intangible assets that have not previously been recognised as assets; or

(b) the initial recognition of intangible assets at amounts other than cost.

18.18D 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**.

18.18E If the fair value of a revalued intangible asset can no longer be determined by reference to an active market in accordance with the requirements of paragraph 18.18B, the carrying amount of the asset shall be its revalued amount at the date of the last revaluation by reference to the active market, less any subsequent accumulated amortisation and any subsequent accumulated impairment losses.

18.18F The revaluation model is applied after an asset has been initially recognised at cost. However, if only part of the cost of an intangible asset is recognised as an asset because the asset did not meet the criteria for recognition until part of the way through the process (see paragraph 18.10A), the revaluation model may be applied to the whole of that asset.

Reporting gains and losses on revaluations

18.18G 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**. 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.

18.18H The decrease of an asset's carrying amount as a result of a revaluation shall be recognised in other comprehensive income to the extent of any previously recognised revaluation increase accumulated in equity, in respect of that asset. If a revaluation decrease exceeds the accumulated revaluation **gains** recognised in equity in respect of that asset, the excess shall be recognised in profit or loss.

Amortisation over useful life

18.19 For the purpose of this FRS, all intangible assets shall be considered to have a finite useful life. The useful life of an intangible asset that arises from contractual or other legal rights shall not exceed the period of the contractual or other legal rights, but may be shorter depending on the period over which the entity expects to use the asset. If the contractual or other legal rights are conveyed for a limited term that can be renewed, the useful life of the intangible asset shall include the renewal period(s) only if there is evidence to support renewal by the entity without significant cost.

18.20 If, in exceptional cases, an entity is unable to make a reliable estimate of the useful life of an intangible asset, the life shall not exceed 10 years.

Amortisation period and amortisation method

18.21 An entity shall allocate the **depreciable amount** of an intangible asset on a systematic basis over its useful life. The amortisation charge for each period shall be recognised in profit or loss, unless another section of this FRS requires the cost to be recognised as part of the cost of an asset. For example, the amortisation of an intangible asset may be included in the costs of **inventories** or **property, plant and equipment**.

18.22 Amortisation begins when the intangible asset is available for use, ie when it is in the location and condition necessary for it to be usable in the manner intended by management. Amortisation ceases when the asset is derecognised. The entity shall choose an amortisation method that reflects the pattern in which it expects to consume the asset's future economic benefits. If the entity cannot determine that pattern reliably, it shall use the straight-line method.

Residual value

18.23 An entity shall assume that the **residual value** of an intangible asset is zero unless:

(a) there is a commitment by a third party to purchase the asset at the end of its useful life; or

(b) there is an active market for the asset and:

(i) residual value can be determined by reference to that market; and

(ii) it is probable that such a market will exist at the end of the asset's useful life.

Review of amortisation period and amortisation method

18.24 Factors such as a change in how an intangible asset is used, technological advancement, and changes in market prices may indicate that the residual value or useful life of an intangible asset has changed since the most recent annual **reporting date**. If such indicators are present, an entity shall review its previous estimates and, if current expectations differ, amend the residual value, amortisation method or useful life. The entity shall account for the change in residual value, amortisation method or useful life as a change in an accounting estimate in accordance with paragraphs 10.15 to 10.18.

Recoverability of the carrying amount – impairment losses

18.25 To determine whether an intangible asset is impaired, an entity shall apply Section 27 *Impairment of Assets*. That section explains when and how an entity reviews the carrying amount of its assets, how it determines the **recoverable amount** of an asset, and when it recognises or reverses an impairment loss.

Retirements and disposals

18.26 An entity shall derecognise an intangible asset, and shall recognise a **gain** or loss in profit or loss:

(a) on disposal; or

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

Disclosures

18.27 An entity shall disclose the following for each class of intangible assets:

* (a) the useful lives or the amortisation rates used and the reasons for choosing those periods;

(b) the amortisation methods used;

* (c) the gross carrying amount and any accumulated amortisation (aggregated with accumulated impairment losses) at the beginning and end of the reporting period;

(d) the line item(s) in the **statement of comprehensive income** (or in the **income statement**, if presented) in which any amortisation of intangible assets is included; and

* (e) a reconciliation of the carrying amount at the beginning and end of the reporting period showing separately:
  - (i) additions, indicating separately those from internal development and those acquired separately;
  - (ii) disposals;
  - (iii) acquisitions through business combinations;
  - (iv) revaluations;
  - (v) amortisation;
  - (vi) impairment losses; and
  - (vii) other changes.

  This reconciliation need not be presented for prior periods.

18.28 An entity shall also disclose:

(a) a description, the carrying amount and remaining amortisation period of any individual intangible asset that is **material** to the entity's **financial statements**;

(b) for intangible assets acquired by way of a grant and initially recognised at fair value (see paragraph 18.12):

- (i) the fair value initially recognised for these assets; and
- (ii) their carrying amounts.

* (c) the existence and carrying amounts of intangible assets to which the entity has restricted title or that are pledged as security for liabilities; and

* (d) the amount of contractual commitments for the acquisition of intangible assets.

18.28A When, as part of a business combination, an acquirer chooses to recognise intangible assets separately from goodwill that meet condition (a) and only one of (b) or (c) in paragraph 18.8, the acquirer shall disclose the nature of those intangible assets and the reason why they have been separated from goodwill.

18.29 An entity shall disclose the aggregate amount of research and development expenditure recognised as an expense during the period (ie the amount of expenditure incurred internally on research and development that has not been capitalised as an intangible asset or as part of the cost of another asset that meets the recognition criteria in this FRS).

18.29A If intangible assets are accounted for at revalued amounts, an entity shall disclose the following:

* (a) the effective date of the revaluation;

(b) whether an independent valuer was involved;

* (c) the methods and significant assumptions applied in estimating the assets' fair values; and

* (d) for each revalued class of intangible assets, the carrying amount that would have been recognised had the assets been carried under the cost model.

Section 19
Business Combinations and Goodwill

Scope of this section

19.1 This section applies to **business combinations**.

19.2 This section does not apply to:

(a) the formation of a **joint venture**; and

(b) the acquisition of a group of **assets** that does not constitute a **business**.

PBE19.2A In addition, **public benefit entities** shall consider the requirements of Section 34 *Specialised Activities* in accounting for **public benefit entity combinations**.

Business combinations defined

19.3 A business combination is the bringing together of separate entities or businesses into one reporting entity. The result of nearly all business combinations is that one entity, the acquirer, obtains **control** of one or more other businesses, the acquiree. The **acquisition date** is the date on which the acquirer obtains control of the acquiree.

19.4 A business combination may be structured in a variety of ways for legal, taxation or other reasons. It may involve the purchase by an entity of the **equity** of another entity, the purchase of all the net assets of another entity, the assumption of the **liabilities** of another entity, or the purchase of some of the net assets of another entity that together form one or more businesses.

19.5 A business combination may be effected by the issue of equity instruments, the transfer of **cash**, **cash equivalents** or other assets, or a mixture of these. The transaction may be between the shareholders of the combining entities or between one entity and the shareholders of another entity. It may involve the establishment of a new entity to control the combining entities or net assets transferred, or the **restructuring** of one or more of the combining entities.

Purchase method

19.6 All business combinations shall be accounted for by applying the purchase method, except for:

(a) **group reconstructions** which may be accounted for by using the merger accounting method (see paragraphs 19.27 to 19.33); and

(b) public benefit entity **combinations that are in substance a gift** or that are a **merger** which shall be accounted for in accordance with Section 34.

19.7 Applying the purchase method involves the following steps:

(a) identifying an acquirer;

(aA) determining the acquisition date;

(b) measuring the cost of the business combination;

(c) allocating, at the acquisition date, the cost of the business combination to the assets acquired and liabilities and **provisions** for **contingent liabilities** assumed and recognising and measuring any **non-controlling interest** in the acquiree; and

(d) recognising and measuring **goodwill**.

Identifying the acquirer

19.8 An acquirer shall be identified for all business combinations accounted for by applying the purchase method. The acquirer is the combining entity that obtains control of the other combining entities or businesses.

19.9 Control is the power to govern the financial and operating policies of an entity or business so as to obtain benefits from its activities. Control of one entity by another is described in Section 9 *Consolidated and Separate Financial Statements*.

19.10 Although it may sometimes be difficult to identify an acquirer, there are usually indications that one exists. For example:

(a) If the **fair value** of one of the combining entities is significantly greater than that of the other combining entity, the entity with the greater fair value is likely to be the acquirer.

(b) If the business combination is effected through an exchange of voting ordinary equity instruments for cash or other assets, the entity giving up cash or other assets is likely to be the acquirer.

(c) If the business combination results in the management of one of the combining entities being able to dominate the selection of the management team of the resulting combined entity, the entity whose management is able so to dominate is likely to be the acquirer.

Determining the acquisition date

19.10A Application of the purchase method starts from the acquisition date, which is the date on which the acquirer obtains control of the acquiree. Because control is the power to govern the financial and operating policies of an entity or business so as to obtain benefits from its activities, it is not necessary for a transaction to be closed or finalised at law before the acquirer obtains control. All pertinent facts and circumstances surrounding a business combination shall be considered in assessing when the acquirer has obtained control.

Cost of a business combination

19.11 The acquirer shall measure the cost of a business combination as the aggregate of:

(a) the fair values, at the acquisition date, of assets given, liabilities incurred or assumed, and equity instruments issued by the acquirer, in exchange for control of the acquiree; plus

(b) any costs directly attributable to the business combination.

19.11A Where control is achieved following a series of transactions, the cost of the business combination is the aggregate of the fair values of the assets given, liabilities assumed and equity instruments issued by the acquirer at the date of each transaction in the series.

Adjustments to the cost of a business combination contingent on future events

19.12 When a business combination agreement provides for an adjustment to the cost of the combination contingent on future events, the acquirer shall include the estimated amount of that adjustment (reflecting the time value of money, if **material**) in the cost of the combination at the acquisition date if the adjustment is **probable** and can be measured reliably.

19.13 However, if the potential adjustment is not recognised at the acquisition date but subsequently becomes probable and can be measured reliably, the additional consideration shall be treated as an adjustment (reflecting the time value of money, if material) to the cost of the combination.

19.13A If the future events that at the acquisition date were expected to occur do not occur, or the estimate needs to be revised, the cost of the business combination shall be adjusted accordingly.

19.13B The unwinding of any discounting shall be recognised as a finance cost in **profit or loss** in the period it arises.

Allocating the cost of a business combination to the assets acquired and liabilities and contingent liabilities assumed and recognising and measuring any non-controlling interest in the acquiree

19.14 The acquirer shall, at the acquisition date, allocate the cost of a business combination by recognising the acquiree's identifiable assets and liabilities and a provision for those contingent liabilities (that satisfy the **recognition** criteria in paragraph 19.20) at their fair values at that date, except for the items specified in paragraphs 19.15A to 19.15C. Any difference between the cost of the business combination and the acquirer's interest in the net amount of the identifiable assets, liabilities and provisions for contingent liabilities so recognised shall be accounted for in accordance with paragraphs 19.22 to 19.24.

19.14A At the acquisition date, any non-controlling interest in the acquiree is stated at the non-controlling interest's share of the net amount of the identifiable assets, liabilities and provisions for contingent liabilities so recognised.

19.15 Except for the items specified in paragraphs 19.15A to 19.15C, the acquirer shall recognise separately the acquiree's identifiable assets, liabilities and contingent liabilities at the acquisition date only if they satisfy the following criteria at that date:

(a) In the case of an asset, it is probable that any associated future economic benefits will flow to the acquirer, and its fair value can be measured reliably.

(b) In the case of a liability other than a contingent liability, it is probable that an outflow of resources will be required to settle the obligation, and its fair value can be measured reliably.

(c) In the case of a contingent liability, its fair value can be measured reliably.

19.15A The acquirer shall recognise and measure a **deferred tax asset** or **liability** arising from the assets acquired and liabilities assumed in accordance with Section 29 *Income Tax.*

19.15B The acquirer shall recognise and measure a liability (or asset, if any) related to the acquiree's employee benefit arrangements in accordance with Section 28 *Employee Benefits*.

19.15C The acquirer shall recognise and measure a **share-based payment** in accordance with Section 26 *Share-based Payment.*

19.16 The acquirer's **statement of comprehensive income** shall incorporate the acquiree's profits or losses after the acquisition date by including the acquiree's **income** and **expenses** based on the cost of the business combination to the acquirer. For example, **depreciation** expense included after the acquisition date in the acquirer's statement of comprehensive income that relates to the acquiree's depreciable assets shall be based on the fair values of those depreciable assets at the acquisition date, ie their cost to the acquirer.

19.17 [Moved to paragraph 19.10A]

19.18 In accordance with paragraph 19.14, the acquirer recognises separately only the identifiable assets, liabilities and contingent liabilities of the acquiree that existed at the acquisition date and satisfy the recognition criteria in paragraph 19.15 (except for the items specified in paragraphs 19.15A to 19.15C). Therefore:

(a) the acquirer shall recognise liabilities for terminating or reducing the activities of the acquiree as part of allocating the cost of the combination only to the extent that the acquiree has, at the acquisition date, an existing liability for restructuring recognised in accordance with Section 21 *Provisions and Contingencies*; and

(b) the acquirer, when allocating the cost of the combination, shall not recognise liabilities for future losses or other costs expected to be incurred as a result of the business combination.

19.19 If the initial accounting for a business combination is incomplete by the end of the **reporting period** in which the combination occurs, the acquirer shall recognise in its **financial statements** provisional amounts for the items for which the accounting is incomplete. Within 12 months after the acquisition date, the acquirer shall retrospectively adjust the provisional amounts recognised as assets and liabilities at the acquisition date (ie account for them as if they were made at the acquisition date) to reflect new information obtained. Beyond 12 months after the acquisition date, adjustments to the initial accounting for a business combination shall be recognised only to correct a material **error** in accordance with Section 10 *Accounting Policies, Estimates and Errors*.

Contingent liabilities

19.20 Paragraph 19.15(c) specifies that the acquirer recognises separately a provision for a contingent liability of the acquiree only if its fair value can be measured reliably. If its fair value cannot be measured reliably:

(a) there is a resulting effect on the amount recognised as goodwill or the amount accounted for in accordance with paragraph 19.24; and

(b) the acquirer shall disclose the information about that contingent liability as required by Section 21.

19.21 After their initial recognition, the acquirer shall measure contingent liabilities that are recognised separately in accordance with paragraph 19.15(c) at the higher of:

(a) the amount that would be recognised in accordance with Section 21; and

(b) the amount initially recognised less amounts previously recognised as **revenue** in accordance with Section 23 *Revenue*.

Recognising and measuring goodwill

19.22 The acquirer shall, at the acquisition date:

(a) recognise goodwill acquired in a business combination as an asset; and

(b) initially measure that goodwill at its cost, being the excess of the cost of the business combination over the acquirer's interest in the net amount of the identifiable assets, liabilities and contingent liabilities recognised and measured in accordance with paragraphs 19.15 to 19.15C.

19.23 After initial recognition, the acquirer shall measure goodwill acquired in a business combination at cost less accumulated **amortisation** and accumulated **impairment losses**:

(a) An entity shall follow the principles in paragraphs 18.19 to 18.24 for amortisation of goodwill. Goodwill shall be considered to have a finite **useful life**, and shall be amortised on a systematic basis over its life. If, in exceptional cases, an entity is unable to make a reliable estimate of the useful life of goodwill, the life shall not exceed 10 years.

(b) An entity shall follow Section 27 *Impairment of Assets* for recognising and measuring the impairment of goodwill.

Excess over cost of acquirer's interest in the net fair value of acquiree's identifiable assets, liabilities and contingent liabilities

19.24 If the acquirer's interest in the net amount of the identifiable assets, liabilities and provisions for contingent liabilities recognised in accordance with paragraph 19.14 exceeds the cost of the business combination (also referred to as 'negative goodwill'), the acquirer shall:

(a) Reassess the identification and **measurement** of the acquiree's assets, liabilities and provisions for contingent liabilities and the measurement of the cost of the combination.

(b) Recognise and separately disclose the resulting excess on the face of the **statement of financial position** on the acquisition date, immediately below goodwill, and followed by a subtotal of the net amount of goodwill and the excess.

(c) Recognise subsequently the excess up to the fair value of non-monetary assets acquired in profit or loss in the periods in which the non-monetary assets are recovered. Any excess exceeding the fair value of non-monetary assets acquired shall be recognised in profit or loss in the periods expected to be benefited.

Disclosures

For business combinations effected during the reporting period

19.25 For each business combination, excluding any group reconstructions, that was effected during the period, the acquirer shall disclose the following:

(a) the names and descriptions of the combining entities or businesses;

(b) the acquisition date;

(c) the percentage of voting equity instruments acquired;

(d) the cost of the combination and a description of the components of that cost (such as cash, equity instruments and debt instruments);

(e) the amounts recognised at the acquisition date for each class of the acquiree's assets, liabilities and contingent liabilities, including goodwill;

(f) [Deleted]

(fA) a qualitative description of the nature of **intangible assets** included in goodwill;

* (g) the useful life of goodwill, and if this cannot be reliably estimated, supporting reasons for the period chosen; and

(h) the periods in which the excess recognised in accordance with paragraph 19.24 will be recognised in profit or loss.

19.25A The acquirer shall disclose, separately for each material business combination that occurred during the reporting period, the amounts of revenue and profit or loss of the acquiree since the acquisition date included in the consolidated statement of comprehensive income for the reporting period. The disclosure may be provided in aggregate for business combinations that occurred during the reporting period which, individually, are not material.

For all business combinations

* 19.26 An acquirer shall disclose a reconciliation of the **carrying amount** of goodwill at the beginning and end of the reporting period, showing separately:

(a) changes arising from new business combinations;

(b) amortisation;

(c) impairment losses;

(d) disposals of previously acquired businesses; and

(e) other changes.

This reconciliation need not be presented for prior periods.

19.26A An acquirer shall disclose a reconciliation of the carrying amount of the excess recognised in accordance with paragraph 19.24 at the beginning and end of the reporting period, showing separately:

(a) changes arising from new business combinations;

(b) amounts recognised in profit or loss in accordance with paragraph 19.24(c);

(c) disposals of previously acquired businesses; and

(d) other changes.

This reconciliation need not be presented for prior periods.

Group reconstructions

19.27 Group reconstructions may be accounted for by using the merger accounting method provided:

(a) the use of the merger accounting method is not prohibited by company law or other relevant legislation;

(b) the ultimate equity holders remain the same, and the rights of each equity holder, relative to the others, are unchanged; and

(c) no non-controlling interest in the net assets of the **group** is altered by the transfer.

Applicability to various structures of business combinations

19.28 The provisions of paragraphs 19.29 to 19.33, which are explained by reference to an acquirer or issuing entity that issues shares as consideration for the transfer to it of shares in the other parties to the combination, should also be read so as to apply to other arrangements that achieve similar results.

Merger accounting method

19.29 With the merger accounting method the carrying values of the assets and liabilities of the parties to the combination are not required to be adjusted to fair value, although appropriate adjustments shall be made to achieve uniformity of **accounting policies** in the combining entities.

19.30 The results and **cash flows** of all the combining entities shall be brought into the financial statements of the combined entity from the beginning of the financial year in which the combination occurred, adjusted so as to achieve uniformity of accounting policies. The comparative information shall be restated by including the **total comprehensive income** for all the combining entities for the previous reporting period and their statement of financial position for the previous **reporting date**, adjusted as necessary to achieve uniformity of accounting policies.

19.31 The difference, if any, between the nominal value of the shares issued plus the fair value of any other consideration given, and the nominal value of the shares received in exchange shall be shown as a movement on other reserves in the **consolidated financial statements**. Any existing balances on the share premium account or capital redemption reserve of the new **subsidiary** shall be brought in by being shown as a movement on other reserves. These movements shall be shown in the **statement of changes in equity**.

19.32 Merger expenses are not to be included as part of this adjustment, but shall be charged to the statement of comprehensive income as part of profit or loss of the combined entity at the effective date of the group reconstruction.

Disclosures

19.33 For each group reconstruction, that was effected during the period, the combined entity shall disclose the following:

(a) the names of the combining entities (other than the reporting entity);

(b) whether the combination has been accounted for as an acquisition or a merger; and

(c) the date of the combination.

Section 20
Leases

Scope of this section

20.1 This section applies to **leases**, except for:

(a) leases to explore for or use minerals, oil, natural gas and similar non-regenerative resources;

(b) licensing agreements for such items as motion picture films, video recordings, plays, manuscripts, patents and copyrights (see Section 18 *Intangible Assets other than Goodwill*);

(c) **measurement** of property held by lessees that is accounted for as **investment property** and measurement of investment property provided by lessors under **operating leases** (see Section 16 *Investment Property*);

(d) measurement of **biological assets** held by lessees under **finance leases** and biological assets provided by lessors under operating leases (see Section 34 *Specialised Activities*); and

(e) leases that could lead to a loss to the lessor or the lessee as a result of non-typical contractual terms (see paragraph 12.3(f)).

(f) [Deleted]

20.2 This section applies to agreements that transfer the right to use **assets** even though substantial services by the lessor may be called for in connection with the operation or maintenance of such assets. This section does not apply to agreements that are contracts for services that do not transfer the right to use assets from one contracting party to the other.

20.3 Some arrangements do not take the legal form of a lease but convey rights to use assets in return for payments. Examples of arrangements in which one entity (the supplier) may convey a right to use an asset to another entity (the purchaser), often together with related services, may include outsourcing arrangements, telecommunication contracts that provide rights to capacity and take-or-pay contracts.

20.3A Determining whether an arrangement is, or contains, a lease shall be based on the substance of the arrangement and requires an assessment of whether:

(a) fulfilment of the arrangement is dependent on the use of a specific asset or assets. Although a specific asset may be explicitly identified in an arrangement, it is not the subject of a lease if fulfilment of the arrangement is not dependent on the use of the specified asset. An asset is implicitly specified if, for example, the supplier owns or leases only one asset with which to fulfil the obligation and it is not economically feasible or practicable for the supplier to perform its obligation through the use of alternative assets; and

(b) the arrangement conveys a right to use the asset. This will be the case where the arrangement conveys to the purchaser the right to control the use of the underlying asset.

Classification of leases

20.4 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.

20.5 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 specialised nature that only the lessee can use them without major modifications.

20.6 Indicators of situations that individually or in combination could also lead to a lease being classified as a finance lease are:

(a) if the lessee can cancel the lease, the lessor's losses associated with the cancellation are borne by the lessee;

(b) **gains** or losses from the fluctuation in the **residual value** of the leased asset accrue to the lessee (eg in the form of a rent rebate equalling most of the sales proceeds at the end of the lease); and

(c) the lessee has the ability to continue the lease for a secondary period at a rent that is substantially lower than market rent.

20.7 The examples and indicators in paragraphs 20.5 and 20.6 are not always conclusive. If it is clear from other features that the lease does not transfer substantially all risks and rewards incidental to ownership, the lease is classified as an operating lease. For example, this may be the case if ownership of the asset is transferred to the lessee at the end of the lease for a variable payment equal to the asset's then fair value, or if there are **contingent rents**, as a result of which the lessee does not have substantially all risks and rewards incidental to ownership.

20.8 Lease classification is made at the inception of the lease and is not changed during the term of the lease unless the lessee and the lessor agree to change the provisions of the lease (other than simply by renewing the lease), in which case the lease classification shall be re-evaluated.

Financial statements of lessees: finance leases

Initial recognition and measurement

20.9 At the **commencement of the lease term**, a lessee shall recognise its rights of use and obligations under finance leases as assets and **liabilities** in its **statement of financial position** at amounts equal to the fair value of the leased asset or, if lower, the present value of the minimum lease payments, determined at the inception of the lease. Any initial direct costs of the lessee (incremental costs that are directly attributable to negotiating and arranging a lease) are added to the amount recognised as an asset.

20.10 The present value of the minimum lease payments shall be calculated using the **interest rate implicit in the lease**. If this cannot be determined, the **lessee's incremental borrowing rate** shall be used.

Subsequent measurement

20.11 A lessee shall apportion minimum lease payments between the finance charge and the reduction of the outstanding liability using the **effective interest method** (see paragraphs 11.15 to 11.20D). The lessee shall allocate the finance charge to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability. A lessee shall charge contingent rents as **expenses** in the periods in which they are incurred.

20.12 A lessee shall depreciate an asset leased under a finance lease in accordance with Section 17 *Property, Plant and Equipment* or Section 18. 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**. A lessee shall also assess at each **reporting date** whether an asset leased under a finance lease is impaired (see Section 27 *Impairment of Assets*).

Disclosures

20.13 A lessee shall make the following disclosures for finance leases:

(a) for each **class of asset**, the net **carrying amount** at the end of the **reporting period**;

(b) the total of future minimum lease payments at the end of the reporting period, for each of the following periods:

(i) not later than one year;

(ii) later than one year and not later than five years; and

(iii) later than five years; and

(c) a general description of the lessee's significant leasing arrangements including, for example, information about contingent rent, renewal or purchase options and escalation clauses, subleases, and restrictions imposed by lease arrangements.

20.14 In addition, the requirements for disclosure about assets in accordance with Sections 17, 18 and 27 apply to lessees for assets leased under finance leases.

Financial statements of lessees: operating leases

Recognition and measurement

20.15 A lessee shall recognise lease payments under operating leases (excluding costs for services such as insurance and maintenance) as an expense over the lease term on a straight-line basis unless either:

(a) another systematic basis is representative of the time pattern of the user's benefit, even if the payments are not on that basis; or

(b) the payments to the lessor are structured to increase in line with expected general inflation (based on published indexes or statistics) to compensate for the lessor's expected inflationary cost increases. If payments to the lessor vary because of factors other than general inflation, then this condition (b) is not met.

Example of applying paragraph 20.15(b):

X operates in a jurisdiction in which the consensus forecast by local banks is that the general price level index, as published by the government, will increase by an average of 10 per cent annually over the next five years. X leases some office space from Y for five years under an operating lease. The lease payments are structured to reflect the expected 10 per cent annual general inflation over the five-year term of the lease as follows:

Year 1	CU100,000
Year 2	CU110,000
Year 3	CU121,000
Year 4	CU133,000
Year 5	CU146,000

X recognises annual rent expense equal to the amounts owed to the lessor as shown above. If the escalating payments are not clearly structured to compensate the lessor for expected inflationary cost increases based on published indexes or statistics, then X recognises annual rent expense on a straight-line basis: CU122,000 each year (sum of the amounts payable under the lease divided by five years).

20.15A A lessee shall recognise the aggregate benefit of **lease incentives** as a reduction to the expense recognised in accordance with paragraph 20.15 over the lease term, on a straight-line basis unless another systematic basis is representative of the time pattern of the lessee's benefit from the use of the leased asset. Any costs incurred by the lessee (for example costs for termination of a pre-existing lease, relocation or leasehold improvements) shall be accounted for in accordance with the applicable section of this FRS.

20.15B Where an operating lease becomes an **onerous contract** an entity shall also apply Section 21 *Provisions and Contingencies.*

20.15C A lessee shall recognise any change in lease payments arising from rent concessions that meet the criteria in paragraph 20.15D on a systematic basis over the periods that the change in lease payments is intended to compensate.

20.15D An entity shall apply the requirements in paragraphs 20.15C and 20.25B to temporary rent concessions occurring as a direct consequence of the COVID-19 pandemic if, and only if, all of the following conditions are met:

(a) the change in lease payments results in revised consideration for the lease that is less than the consideration for the lease immediately preceding the change;

(b) any reduction in lease payments affects only payments originally due on or before 30 June 2022; and

(c) there is no significant change to other terms and conditions of the lease.

Disclosures

20.16 A lessee shall make the following disclosures for operating leases:

* (a) the total of future minimum lease payments under non-cancellable operating leases for each of the following periods:

(i) not later than one year;

(ii) later than one year and not later than five years; and

(iii) later than five years;

* (b) lease payments recognised as an expense; and

(c) the amount of the change in lease payments recognised in **profit or loss** in accordance with paragraph 20.15C.

Financial statements of lessors: finance leases

Initial recognition and measurement

20.17 A lessor shall recognise assets held under a finance lease in its statement of financial position and present them as a receivable at an amount equal to the net investment in the lease. The **net investment in a lease** is the lessor's **gross investment in the lease** discounted at the interest rate implicit in the lease. The gross investment in the lease is the aggregate of:

(a) the minimum lease payments receivable by the lessor under a finance lease; and

(b) any unguaranteed residual value accruing to the lessor.

20.18 For finance leases other than those involving manufacturer or dealer lessors, initial direct costs (costs that are incremental and directly attributable to negotiating and arranging a lease) are included in the initial measurement of the finance lease receivable and reduce the amount of **income** recognised over the lease term.

Subsequent measurement

20.19 The **recognition** of finance income shall be based on a pattern reflecting a constant periodic rate of return on the lessor's net investment in the finance lease. Lease payments relating to the period, excluding costs for services, are applied against the gross investment in the lease to reduce both the principal and the unearned finance income. If there is an indication that the estimated unguaranteed residual value used in computing the lessor's gross investment in the lease has changed significantly, the income allocation over the lease term is revised, and any reduction in respect of amounts accrued is recognised immediately in profit or loss.

Manufacturer or dealer lessors

20.20 Manufacturers or dealers often offer to customers the choice of either buying or leasing an asset. A finance lease of an asset by a manufacturer or dealer lessor gives rise to two types of income:

(a) profit or loss equivalent to the profit or loss resulting from an outright sale of the asset being leased, at normal selling prices, reflecting any applicable volume or trade discounts; and

(b) finance income over the lease term.

20.21 The sales **revenue** recognised at the commencement of the lease term by a manufacturer or dealer lessor is the fair value of the asset or, if lower, the present value of the minimum lease payments accruing to the lessor, computed at a market rate of interest. The cost of sale recognised at the commencement of the lease term is the cost, or carrying amount if different, of the leased asset less the present value of the unguaranteed residual value. The difference between the sales revenue and the cost of sale is the selling profit, which is recognised in accordance with the entity's policy for outright sales.

20.22 If artificially low rates of interest are quoted, selling profit shall be restricted to that which would apply if a market rate of interest were charged. Costs incurred by manufacturer or dealer lessors in connection with negotiating and arranging a lease shall be recognised as an expense when the selling profit is recognised.

Disclosures

20.23 A lessor shall make the following disclosures for finance leases:

(a) a reconciliation between the gross investment in the lease at the end of the reporting period, and the present value of minimum lease payments receivable at the end of the reporting period. In addition, a lessor shall disclose the gross investment in the lease and the present value of minimum lease payments receivable at the end of the reporting period, for each of the following periods:

  (i) not later than one year;

  (ii) later than one year and not later than five years; and

  (iii) later than five years;

(b) unearned finance income;

(c) the unguaranteed residual values accruing to the benefit of the lessor;

(d) the accumulated allowance for uncollectible minimum lease payments receivable;

(e) contingent rents recognised as income in the period; and

(f) a general description of the lessor's significant leasing arrangements, including, for example, information about contingent rent, renewal or purchase options and escalation clauses, subleases, and restrictions imposed by lease arrangements.

Financial statements of lessors: operating leases

Recognition and measurement

20.24 A lessor shall present assets subject to operating leases in its statement of financial position according to the nature of the asset.

20.25 A lessor shall recognise lease income from operating leases (excluding amounts for services such as insurance and maintenance) in profit or loss on a straight-line basis over the lease term, unless either:

(a) another systematic basis is representative of the time pattern of the lessee's benefit from the leased asset, even if the receipt of payments is not on that basis; or

(b) the payments to the lessor are structured to increase in line with expected general inflation (based on published indexes or statistics) to compensate for the lessor's expected inflationary cost increases. If payments to the lessor vary according to factors other than inflation, then condition (b) is not met.

20.25A A lessor shall recognise the aggregate cost of lease incentives as a reduction to the income recognised in accordance with paragraph 20.25 over the lease term on a straight-line basis, unless another systematic basis is representative of the time pattern over which the lessor's benefit from the leased asset is diminished.

20.25B A lessor shall recognise any change in lease income arising from rent concessions that meet the criteria in paragraph 20.15D on a systematic basis over the periods that the change in lease payments is intended to compensate.

20.26 A lessor shall recognise as an expense, costs, including **depreciation**, incurred in earning the lease income. The depreciation policy for depreciable leased assets shall be consistent with the lessor's normal depreciation policy for similar assets.

20.27 A lessor shall add to the carrying amount of the leased asset any initial direct costs it incurs in negotiating and arranging an operating lease and shall recognise such costs as an expense over the lease term on the same basis as the lease income.

20.28 To determine whether a leased asset has become impaired, a lessor shall apply Section 27.

20.29 A manufacturer or dealer lessor does not recognise any selling profit on entering into an operating lease because it is not the equivalent of a sale.

Disclosures

20.30 A lessor shall disclose the following for operating leases:

(a) the future minimum lease payments under non-cancellable operating leases for each of the following periods:

  (i) not later than one year;

  (ii) later than one year and not later than five years; and

  (iii) later than five years;

(b) total contingent rents recognised as income; and

(c) a general description of the lessor's significant leasing arrangements, including, for example, information about contingent rent, renewal or purchase options and escalation clauses, and restrictions imposed by lease arrangements.

20.31 In addition, the requirements for disclosure about assets in accordance with Sections 17, 18 and 27 apply to lessors for assets provided under operating leases.

Sale and leaseback transactions

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

Sale and leaseback transaction results in a finance lease

20.33 If a sale and leaseback transaction results in a finance lease, the seller-lessee shall not recognise immediately, as income, any excess of sales proceeds over the carrying amount. Instead, the seller-lessee shall defer such excess and amortise it over the lease term.

Sale and leaseback transaction results in an operating lease

20.34 If a sale and leaseback transaction results in an operating lease, and it is clear that the transaction is established at fair value, the seller-lessee shall recognise any profit or loss immediately. If the sale price is below fair value, the seller-lessee shall recognise any profit or loss immediately unless the loss is compensated for by future lease payments at below market price. In that case the seller-lessee shall defer and amortise such loss 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 seller-lessee shall defer the excess over fair value and amortise it over the period for which the asset is expected to be used.

Disclosures

20.35 Disclosure requirements for lessees and lessors apply equally to sale and leaseback transactions. The required description of significant leasing arrangements includes description of unique or unusual provisions of the agreement or terms of the sale and leaseback transactions.

Section 21
Provisions and Contingencies

Scope of this section

21.1 This section applies to **provisions** (ie **liabilities** of uncertain timing or amount), **contingent liabilities** and **contingent assets** except those provisions covered by other sections of this FRS. Where those other sections contain no specific requirements to deal with contracts that have become onerous, this section applies to those contracts.

21.1A This section applies to **financial guarantee contracts** unless:

(a) an entity has chosen to apply IAS 39 *Financial Instruments: Recognition and Measurement* and/or IFRS 9 *Financial Instruments* to its **financial instruments** (see paragraphs 11.2 and 12.2); or

(b) an entity has elected under **FRS 103** to continue the application of insurance contract accounting.

21.1B This section does not apply to:

(a) financial instruments (including loan commitments) that are within the scope of Section 11 *Basic Financial Instruments* or Section 12 *Other Financial Instruments Issues*;

(b) **insurance contracts** (including **reinsurance contracts**) that an entity issues and reinsurance contracts that the entity holds, or financial instruments issued by an entity with a **discretionary participation feature** that are within the scope of FRS 103; or

(c) executory contracts (ie contracts under which neither party has performed any obligations or both parties have partially performed their obligations to an equal extent) unless they are **onerous contracts**.

21.2 [Moved to paragraph 21.1B(c)]

21.3 The word 'provision' is sometimes used in the context of such items as **depreciation**, impairment of **assets**, and uncollectible receivables. Those are adjustments of the **carrying amounts** of assets, rather than **recognition** of liabilities, and therefore are not covered by this section.

Initial recognition

21.4 An entity shall recognise a provision only when:

(a) the entity has an obligation at the **reporting date** as a result of a past event;

(b) it is **probable** (ie more likely than not) that the entity will be required to transfer economic benefits in settlement; and

(c) the amount of the obligation can be estimated reliably.

21.5 The entity shall recognise the provision as a liability in the **statement of financial position** and shall recognise the amount of the provision as an **expense**, unless another section of this FRS requires the cost to be recognised as part of the cost of an asset such as **inventories** or **property, plant and equipment**.

21.6 The condition in paragraph 21.4(a) means that the entity has no realistic alternative to settling the obligation. This can happen when the entity has a legal obligation that can be enforced by law or when the entity has a **constructive obligation** because the past event (which may be an action of the entity) has created valid expectations in other parties that the entity will discharge the obligation. Obligations that will arise from the entity's future actions (ie the future conduct of its **business**) do not satisfy the condition in paragraph 21.4(a), no matter how likely they are to occur and even if they are contractual. To illustrate, because of commercial pressures or legal requirements, an entity may intend or need to carry out expenditure to operate in a particular way in the future (for example, by fitting smoke filters in a particular type of factory). Because the entity can avoid the future expenditure by its future actions, for example by changing its method of operation or selling the factory, it has no present obligation for that future expenditure and no provision is recognised.

Initial measurement

21.7 An entity shall measure a provision at the best estimate of the amount required to settle the obligation at the reporting date. The best estimate is the amount an entity would rationally pay to settle the obligation at the end of the **reporting period** or to transfer it to a third party at that time.

(a) When the provision involves a large population of items, the estimate of the amount reflects the weighting of all possible outcomes by their associated probabilities. Where there is a continuous range of possible outcomes, and each point in that range is as likely as any other, the mid-point of the range is used.

(b) When the provision arises from a single obligation, the individual most likely outcome may be the best estimate of the amount required to settle the obligation. However, even in such a case, the entity considers other possible outcomes. When other possible outcomes are either mostly higher or mostly lower than the most likely outcome, the best estimate will be a higher or lower amount.

When the effect of the time value of money is **material**, the amount of a provision shall be the **present value** of the amount 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 risks specific to the liability. The risks specific to the liability shall be reflected either in the discount rate or in the estimation of the amounts required to settle the obligation, but not both.

21.8 An entity shall exclude **gains** from the expected disposal of assets from the **measurement** of a provision.

21.9 When some or all of the amount required to settle a provision may be reimbursed by another party (eg through an insurance claim), the entity shall recognise the reimbursement as a separate asset only when it is virtually certain that the entity will receive the reimbursement on settlement of the obligation. The amount recognised for the reimbursement shall not exceed the amount of the provision. The reimbursement receivable shall be presented in the statement of financial position as an asset and shall not be offset against the provision. In the **statement of comprehensive income** (or in the **income statement**, if presented) the expense relating to a provision may be presented net of the amount recognised for a reimbursement.

Subsequent measurement

21.10 An entity shall charge against a provision only those expenditures for which the provision was originally recognised.

21.11 An entity shall review provisions at each reporting date and adjust them to reflect the current best estimate of the amount that would be required to settle the obligation at that reporting date. Any adjustments to the amounts previously recognised shall be recognised in **profit or loss** unless the provision was originally recognised as part of the cost of an asset (see paragraph 21.5). When a provision is measured at the present value of the amount expected to be required to settle the obligation, the unwinding of the discount shall be recognised as a finance cost in profit or loss in the period it arises.

Onerous contracts

21.11A If an entity has an onerous contract, the present obligation under the contract shall be recognised and measured as a provision (see Example 2 of the appendix to this section).

Future operating losses

21.11B Provisions shall not be recognised for future operating losses (see Example 1 of the appendix to this section).

Restructuring

21.11C A **restructuring** gives rise to a constructive obligation only when an entity:

(a) has a detailed formal plan for the restructuring identifying at least:

 (i) the business or part of a business concerned;

 (ii) the principal locations affected;

 (iii) the location, function, and approximate number of employees who will be compensated for terminating their services;

 (iv) the expenditures that will be undertaken; and

 (v) when the plan will be implemented; and

(b) has raised a valid expectation in those affected that it will carry out the restructuring by starting to implement that plan or announcing its main features to those affected by it.

21.11D An entity recognises a provision for restructuring costs only when it has a legal or constructive obligation at the reporting date to carry out the restructuring.

Contingent liabilities

21.12 A contingent liability is either a possible but uncertain obligation or a present obligation that is not recognised because it fails to meet one or both of the conditions (b) and (c) in paragraph 21.4. An entity shall not recognise a contingent liability as a liability, except for provisions for contingent liabilities of an acquiree in a **business combination** (see paragraphs 19.20 and 19.21). Disclosure of a contingent liability is required by paragraph 21.15 unless the possibility of an outflow of resources is remote. When an entity is jointly and severally liable for an obligation, the part of the obligation that is expected to be met by other parties is treated as a contingent liability.

Contingent assets

21.13 An entity shall not recognise a contingent asset as an asset. Disclosure of a contingent asset is required by paragraph 21.16 when an inflow of economic benefits is probable. However, when the flow of future economic benefits to the entity is virtually certain, then the related asset is not a contingent asset, and its recognition is appropriate.

Disclosures

Disclosures about provisions

21.14 For each class of provision, an entity shall disclose the following:

(a) a reconciliation showing:

   (i) the carrying amount at the beginning and end of the period;

   (ii) additions during the period, including adjustments that result from changes in measuring the discounted amount;

   (iii) amounts charged against the provision during the period; and

   (iv) unused amounts reversed during the period;

(b) a brief description of the nature of the obligation and the expected amount and timing of any resulting payments;

(c) an indication of the uncertainties about the amount or timing of those outflows; and

(d) the amount of any expected reimbursement, stating the amount of any asset that has been recognised for that expected reimbursement.

Comparative information for prior periods is not required.

Disclosures about contingent liabilities

* 21.15 Unless the possibility of any outflow of resources in settlement is remote, an entity shall disclose, for each class of contingent liability at the reporting date, a brief description of the nature of the contingent liability and, when practicable:

(a) an estimate of its financial effect, measured in accordance with paragraphs 21.7 to 21.11;

(b) an indication of the uncertainties relating to the amount or timing of any outflow; and

(c) the possibility of any reimbursement.

If it is **impracticable** to make one or more of these disclosures, that fact shall be stated.

Disclosures about contingent assets

21.16 If an inflow of economic benefits is probable (more likely than not) but not virtually certain, an entity shall disclose a description of the nature of the contingent assets at the end of the reporting period, and, when practicable, an estimate of their financial effect, measured using the principles set out in paragraphs 21.7 to 21.11. If it is impracticable to make this disclosure, that fact shall be stated.

Prejudicial disclosures

21.17 In extremely rare cases, disclosure of some or all of the information required by paragraphs 21.14 to 21.16 can be expected to prejudice seriously the position of the entity in a dispute with other parties on the subject matter of the provision, contingent liability or contingent asset. In such cases, an entity need not disclose all of the information required by those paragraphs insofar as it relates to the dispute, but shall disclose at least the following.

In relation to provisions, the following information shall be given:

(a) a table showing the reconciliation required by paragraph 21.14(a) in aggregate, including the source and application of any amounts transferred to or from provisions during the reporting period;

(b) particulars of each provision in any case where the amount of the provision is material; and

(c) the fact that, and reason why, the information required by paragraph 21.14 has not been disclosed.

In relation to contingent liabilities, the following information shall be given:

(a) particulars and the total amount of any contingent liabilities (excluding those which arise out of insurance contracts) that are not included in the statement of financial position;

(b) the total amount of contingent liabilities which are undertaken on behalf of or for the benefit of:

   (i) any **parent** or fellow **subsidiary** of the entity;

   (ii) any subsidiary of the entity; or

   (iii) any entity in which the reporting entity has a participating interest,

   shall each be stated separately; and

(c) the fact that, and reason why, the information required by paragraph 21.15 has not been disclosed.

In relation to contingent assets, the entity shall disclose the general nature of the dispute, together with the fact that, and reason why, the information required by paragraph 21.16 has not been disclosed.

Disclosure about financial guarantee contracts

21.17A An entity shall disclose the nature and business purpose of the financial guarantee contracts it has issued. If applicable, an entity shall also provide the disclosures required by paragraphs 21.14 and 21.15.

Appendix to Section 21
Examples of recognising and measuring provisions

This appendix accompanies, but is not part of, Section 21. It provides guidance for applying the requirements of Section 21 in recognising and measuring provisions.

All of the entities in the examples in this appendix have 31 December as their reporting date. In all cases, it is assumed that a reliable estimate can be made of any outflows expected. In some examples the circumstances described may have resulted in impairment of the assets; this aspect is not dealt with in the examples. References to 'best estimate' are to the present value amount, when the effect of the time value of money is material.

Example 1 Future operating losses

21A.1 An entity determines that it is probable that a segment of its operations will incur future operating losses for several years.

Present obligation as a result of a past obligating event: There is no past event that obliges the entity to pay out resources.

Conclusion: The entity does not recognise a provision for future operating losses. Expected future losses do not meet the definition of a liability. The expectation of future operating losses may be an indicator that one or more assets are impaired (see Section 27 *Impairment of Assets)*.

Example 2 Onerous contracts

21A.2 An onerous contract is one in which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it. The unavoidable costs under a contract reflect the least net cost of exiting from the contract, which is the lower of the cost of fulfilling it and any compensation or penalties arising from failure to fulfil it. For example, an entity may be contractually required under an operating lease to make payments to lease an asset for which it no longer has any use.

Present obligation as a result of a past obligating event: The entity is contractually required to pay out resources for which it will not receive commensurate benefits.

Conclusion: If an entity has a contract that is onerous, the entity recognises and measures the present obligation under the contract as a provision.

Example 3 Restructurings

21A.3 [Moved to paragraph 21.11C]

Example 4 Warranties

21A.4 A manufacturer gives warranties at the time of sale to purchasers of its product. Under the terms of the contract for sale, the manufacturer undertakes to make good, by repair or replacement, manufacturing defects that become apparent within three years from the date of sale. On the basis of experience, it is probable (ie more likely than not) that there will be some claims under the warranties.

Present obligation as a result of a past obligating event: The obligating event is the sale of the product with a warranty, which gives rise to a legal obligation.

An outflow of resources embodying economic benefits in settlement: Probable for the warranties as a whole.

Conclusion: The entity recognises a provision for the best estimate of the costs of making good under the warranty products sold before the reporting date.

Illustration of calculations:

In 20X0, goods are sold for CU1,000,000. Experience indicates that 90 per cent of products sold require no warranty repairs; 6 per cent of products sold require minor repairs costing 30 per cent of the sale price; and 4 per cent of products sold require major repairs or replacement costing 70 per cent of sale price. Therefore estimated warranty costs are:

CU1,000,000 × 90% × 0 =	CU0
CU1,000,000 × 6% × 30% =	CU18,000
CU1,000,000 × 4% × 70% =	CU28,000
Total	CU46,000

The expenditures for warranty repairs and replacements for products sold in 20X0 are expected to be made 60 per cent in 20X1, 30 per cent in 20X2, and 10 per cent in 20X3, in each case at the end of the period. Because the estimated cash flows already reflect the probabilities of the cash outflows, and assuming there are no other risks or uncertainties that must be reflected, to determine the present value of those cash flows the entity uses a 'risk-free' discount rate based on government bonds with the same term as the expected cash outflows (6 per cent for one-year bonds and 7 per cent for two-year and three-year bonds). Calculation of the present value, at the end of 20X0, of the estimated cash flows related to the warranties for products sold in 20X0 is as follows:

Year		**Expected cash payments (CU)**	**Discount rate**	**Discount factor**	**Present value (CU)**
1	60% × CU46,000	27,600	6%	0.9434 (at 6% for 1 year)	26,038
2	30% × CU46,000	13,800	7%	0.8734 (at 7% for 2 years)	12,053
3	10% × CU46,000	4,600	7%	0.8163 (at 7% for 3 years)	3,755
Total					41,846

The entity will recognise a warranty obligation of CU41,846 at the end of 20X0 for products sold in 20X0.

Example 5 Refunds policy

21A.5 A retail store has a policy of refunding purchases by dissatisfied customers, even though it is under no legal obligation to do so. Its policy of making refunds is generally known.

Present obligation as a result of a past obligating event: The obligating event is the sale of the product, which gives rise to a constructive obligation because the conduct of the store has created a valid expectation on the part of its customers that the store will refund purchases.

An outflow of resources embodying economic benefits in settlement: Probable that a proportion of goods will be returned for refund.

Conclusion: The entity recognises a provision for the best estimate of the amount required to settle the refunds.

Example 6 Closure of a division: no implementation before end of reporting period

21A.6 On 12 December 20X0 the board of an entity decided to close down a division. Before the end of the reporting period (31 December 20X0) the decision was not communicated to any of those affected and no other steps were taken to implement the decision.

Present obligation as a result of a past obligating event: There has been no obligating event, and so there is no obligation.

Conclusion: The entity does not recognise a provision.

Example 7 Closure of a division: communication and implementation before end of reporting period

21A.7 On 12 December 20X0 the board of an entity decided to close a division making a particular product. On 20 December 20X0 a detailed plan for closing the division was agreed by the board, letters were sent to customers warning them to seek an alternative source of supply, and redundancy notices were sent to the staff of the division.

Present obligation as a result of a past obligating event: The obligating event is the communication of the decision to the customers and employees, which gives rise to a constructive obligation from that date, because it creates a valid expectation that the division will be closed.

An outflow of resources embodying economic benefits in settlement: Probable.

Conclusion: The entity recognises a provision at 31 December 20X0 for the best estimate of the costs that would be incurred to close the division at the reporting date.

Example 8 Staff retraining as a result of changes in the income tax system

21A.8 The government introduces changes to the income tax system. As a result of those changes, an entity in the financial services sector will need to retrain a large proportion of its administrative and sales workforce in order to ensure continued compliance with tax regulations. At the end of the reporting period, no retraining of staff has taken place.

Present obligation as a result of a past obligating event: The tax law change does not impose an obligation on an entity to do any retraining. An obligating event for recognising a provision (the retraining itself) has not taken place.

Conclusion: The entity does not recognise a provision.

Example 9 A court case

21A.9 A customer has sued Entity X, seeking damages for injury the customer allegedly sustained from using a product sold by Entity X. Entity X disputes liability on grounds that the customer did not follow directions in using the product. Up to the date the board authorised the financial statements for the year to 31 December 20X1 for issue, the entity's lawyers advise that it is probable that the entity will not be found liable. However, when the entity prepares the financial statements for the year to 31 December 20X2, its lawyers advise that, owing to developments in the case, it is now probable that the entity will be found liable.

(a) At 31 December 20X1

Present obligation as a result of a past obligating event: On the basis of the evidence available when the financial statements were approved, there is no obligation as a result of past events.

Conclusion: No provision is recognised. The matter is disclosed as a contingent liability unless the probability of any outflow is regarded as remote.

(b) At 31 December 20X2

Present obligation as a result of a past obligating event: On the basis of the evidence available, there is a present obligation. The obligating event is the sale of the product to the customer.

An outflow of resources embodying economic benefits in settlement: Probable.

Conclusion: A provision is recognised at the best estimate of the amount to settle the obligation at 31 December 20X2, and the expense is recognised in profit or loss. It is not a correction of an error in 20X1 because, on the basis of the evidence available when the 20X1 financial statements were approved, a provision should not have been recognised at that time.

Section 22
Liabilities and Equity

Scope of this section

22.1 This section sets out the requirements for:

(a) classifying **financial instruments** as either **liabilities** or **equity** and the accounting for **compound financial instruments**;

(b) the issue of equity instruments, distributions to individuals or other parties acting in their capacity as investors in equity instruments (ie in their capacity as **owners**) and the accounting for purchases of own equity; and

(c) the accounting for **non-controlling interests** in **consolidated financial statements**.

Section 26 *Share-based Payment* sets out the requirements for a transaction in which the entity receives goods or services (including employee services) as consideration for its equity instruments (including shares or **share options**) from employees and other vendors acting in their capacity as vendors of goods and services.

22.2 This section applies to financial instruments except:

(a) Investments in **subsidiaries**, **associates** and **joint ventures** (see Section 9 *Consolidated and Separate Financial Statements*, Section 14 *Investments in Associates* and Section 15 *Investments in Joint Ventures*).

(b) Employers' rights and obligations under employee benefit plans (see Section 28 *Employee Benefits*).

(c) Contracts for contingent consideration in a **business combination** (see Section 19 *Business Combinations and Goodwill*). This exemption applies only to the acquirer.

(d) Financial instruments, contracts and obligations under **share-based payment transactions** (see Section 26), except that paragraphs 22.3 to 22.6 shall be applied to **treasury shares** issued, purchased, sold, transferred or cancelled in connection with employee share option plans, employee share purchase plans, and all other **share-based payment arrangements**.

(e) **Insurance contracts** (including **reinsurance contracts**) that an entity issues and reinsurance contracts that it holds (see **FRS 103**).

(f) Financial instruments with a **discretionary participation feature** that an entity issues (see FRS 103).

(g) **Financial guarantee contracts** (see Section 21 *Provisions and Contingencies*).

Classification of an instrument as liability or equity

22.3 Equity is the residual interest in the **assets** of an entity after deducting all its liabilities. Equity includes investments by the owners of the entity, plus additions to those investments earned through profitable operations and retained for use in the entity's operations, minus reductions to owners' investments as a result of unprofitable operations and distributions to owners.

A **financial liability** is any liability that is:

(a) a contractual obligation:

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

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

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

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

  (ii) a **derivative** that will or may be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the entity's own equity instruments. For this purpose the entity's own equity instruments do not include instruments that are themselves contracts for the future receipt or delivery of the entity's own equity instruments.

22.3A A financial instrument, where the issuer does not have the unconditional right to avoid settling in cash or by delivery of another financial asset (or otherwise to settle it in such a way that it would be a financial liability) and where settlement is dependent on the occurrence or non-occurrence of uncertain future events beyond the control of the issuer and the holder, is a financial liability of the issuer unless:

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

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

(c) the instrument has all the features and meets the conditions in paragraph 22.4.

22.4 Some financial instruments that meet the definition of a liability are classified as equity because they represent the residual interest in the net assets of the entity:

(a) A puttable instrument is a financial instrument that gives the holder the right to sell that instrument back to the issuer for cash or another financial asset or is automatically redeemed or repurchased by the issuer on the occurrence of an uncertain future event or the death or retirement of the instrument holder. A puttable instrument that has all of the following features is classified as an equity instrument:

  (i) It entitles the holder to a pro rata share of the entity's net assets in the event of the entity's liquidation. The entity's net assets are those assets that remain after deducting all other claims on its assets.

  (ii) The instrument is in the class of instruments that is subordinate to all other classes of instruments.

  (iii) All financial instruments in the class of instruments that is subordinate to all other classes of instruments have identical features.

  (iv) Apart from the contractual obligation for the issuer to repurchase or redeem the instrument for cash or another financial asset, the instrument does not include any contractual obligation to deliver cash or another financial asset to another entity, or to exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavourable to the entity, and it is not a contract that will or may be settled in the entity's own equity instruments as set out in paragraph 22.3(b) of the definition of a financial liability.

(v) The total expected **cash flows** attributable to the instrument over the life of the instrument are based substantially on the **profit or loss**, the change in the recognised net assets or the change in the **fair value** of the recognised and unrecognised net assets of the entity over the life of the instrument (excluding any effects of the instrument).

(b) Instruments, or components of instruments, that are subordinate to all other classes of instruments are classified as equity if they impose on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation.

22.5 The following are examples of instruments that are either classified as liabilities or equity:

(a) An instrument of the type described in paragraph 22.4(b) is classified as a liability if the distribution of net assets on liquidation is subject to a maximum amount (a ceiling). For example, if on liquidation the holders of the instrument receive a pro rata share of the net assets, but this amount is limited to a ceiling and the excess net assets are distributed to a charity organisation or the government, the instrument is not classified as equity.

(b) A puttable instrument is classified as equity if, when the put option is exercised, the holder receives a pro rata share of the net assets of the entity determined by:

(i) dividing the entity's net assets on liquidation into units of equal amounts; and

(ii) multiplying that amount by the number of the units held by the financial instrument holder.

However, if the holder is entitled to an amount measured on some other basis the instrument is classified as a liability.

(c) An instrument is classified as a liability if it obliges the entity to make payments to the holder before liquidation, such as a mandatory dividend.

(d) A puttable instrument that is classified as equity in a subsidiary's **financial statements** is classified as a liability in the consolidated financial statements.

(e) A preference share that provides for mandatory redemption by the issuer for a fixed or determinable amount at a fixed or determinable future date, or gives the holder the right to require the issuer to redeem the instrument at or after a particular date for a fixed or determinable amount, is a financial liability.

22.6 Members' shares in co-operative entities and similar instruments are equity if:

(a) the entity has an unconditional right to refuse redemption of the members' shares; or

(b) redemption is unconditionally prohibited by local law, regulation or the entity's governing charter.

Original issue of shares or other equity instruments

22.7 An entity shall recognise the issue of shares or other equity instruments as equity when it issues those instruments and another party is obliged to provide cash or other resources to the entity in exchange for the instruments.

(a) [Deleted]

(b) If the entity receives the cash or other resources before the equity instruments are issued, and the entity cannot be required to repay the cash or other resources received, the entity shall recognise the corresponding increase in equity to the extent of consideration received.

(c) To the extent that the equity instruments have been subscribed for but not issued (or called up), and the entity has not yet received the cash or other resources, the entity shall not recognise an increase in equity.

22.8 An entity shall measure equity instruments, other than when merger relief or group reconstruction relief under sections 611 to 615 of the **Act** are applied[54] or those accounted for in accordance with paragraphs 22.8A, at the fair value of the cash or other resources received or receivable, net of **transaction costs**. If payment is deferred and the time value of money is **material**, the initial **measurement** shall be on a **present value** basis.

22.8A An entity shall not apply paragraph 22.8 to transactions in which a financial liability is extinguished (partially or in full) by the issue of equity instruments if:

(a) the creditor is also a direct or indirect shareholder and is acting in its capacity as a direct or indirect existing shareholder;

(b) the creditor and the entity are controlled by the same party or parties before and after the transaction and the substance of the transaction includes an equity distribution by, or contribution to, the entity; or

(c) the extinguishment is in accordance with the original terms of the financial liability.

In these circumstances there is no **gain** or loss recognised in profit or loss as the result of such a transaction.

22.9 An entity shall account for the transaction costs of an equity transaction as a deduction from equity. **Income tax** relating to the transaction costs shall be accounted for in accordance with Section 29 *Income Tax*.

22.10 How the increase in equity arising on the issue of shares or other equity instruments is presented in the **statement of financial position** is determined by applicable laws. For example, the par value (or other nominal value) of shares and the amount paid in excess of par value may be presented separately.

Exercise of options, rights and warrants

22.11 An entity shall apply the principles in paragraphs 22.7 to 22.10 to equity issued by means of exercise of options, rights, warrants and similar equity instruments.

Capitalisation or bonus issues of shares and share splits

22.12 A capitalisation or bonus issue (sometimes referred to as a stock dividend) is the issue of new shares to shareholders in proportion to their existing holdings. For example, an entity may give its shareholders one dividend or bonus share for every five shares held. A share split (sometimes referred to as a stock split) is the dividing of an entity's existing shares into multiple shares. For example, in a share split, each shareholder may receive one additional share for each share held. In some cases, the previously outstanding shares are cancelled and replaced by new shares. Capitalisation and bonus issues and share splits do not change total equity. An entity shall reclassify amounts within equity as required by applicable laws.

[54] Paragraphs A3.24 and A3.24A provide more information.

Convertible debt or similar compound financial instruments

22.13 On issuing convertible debt or similar compound financial instruments that contain both a liability and an equity component, an entity shall allocate the proceeds between the liability component and the equity component. To make the allocation, the entity shall first determine the amount of the liability component as the fair value of a similar liability that does not have a conversion feature or similar associated equity component. The entity shall allocate the residual amount as the equity component. Transaction costs shall be allocated between the debt component and the equity component on the basis of their relative fair values.

22.14 The entity shall not revise the allocation in a subsequent period.

22.15 In periods after the instruments were issued, the entity shall account for the liability component as a financial instrument in accordance with Section 11 *Basic Financial Instruments* or Section 12 *Other Financial Instruments Issues* as appropriate. The appendix to this section illustrates the issuer's accounting for convertible debt where the liability component is a basic financial instrument.

Treasury shares

22.16 Treasury shares are the equity instruments of an entity that have been issued and subsequently reacquired by the entity. An entity shall deduct from equity the fair value of the consideration given for the treasury shares. The entity shall not recognise a gain or loss in profit or loss on the purchase, sale, transfer or cancellation of treasury shares.

Distributions to owners

22.17 An entity shall reduce equity for the amount of distributions to its owners (holders of its equity instruments).

22.18 An entity shall disclose the fair value of any non-cash assets that have been distributed to its owners during the **reporting period**, except when the non-cash assets are ultimately controlled by the same parties both before and after the distribution.

Non-controlling interest and transactions in shares of a consolidated subsidiary

22.19 In the consolidated financial statements, a non-controlling interest in the net assets of a subsidiary is included in equity. An entity shall treat changes in a **parent's** controlling interest in a subsidiary that do not result in a loss of **control** as transactions with equity holders in their capacity as equity holders. Accordingly, the **carrying amount** of the non-controlling interest shall be adjusted to reflect the change in the parent's interest in the subsidiary's net assets. Any difference between the amount by which the non-controlling interest is so adjusted and the fair value of the consideration paid or received, if any, shall be recognised directly in equity and attributed to equity holders of the parent. An entity shall not recognise a gain or loss on these changes. Also, an entity shall not recognise any change in the carrying amounts of assets (including **goodwill**) or liabilities as a result of such transactions.

Appendix to Section 22
Example of the issuer's accounting for convertible debt

This appendix accompanies, but is not part of, Section 22. It provides guidance for applying the requirements of paragraphs 22.13 to 22.15.

Example of the issuer's accounting for convertible debt

On 1 January 20X5 an entity issues 500 convertible bonds. The bonds are issued at par with a face value of CU100 per bond and are for a five-year term, with no transaction costs. The total proceeds from the issue are CU50,000. Interest is payable annually in arrears at an annual interest rate of 4 per cent. Each bond is convertible, at the holder's discretion, into 25 ordinary shares at any time up to maturity. At the time the bonds are issued, the market interest rate for similar debt that does not have the conversion option is 6 per cent.

When the instrument is issued, the liability component must be valued first, and the difference between the total proceeds on issue (which is the fair value of the instrument in its entirety) and the fair value of the liability component is assigned to the equity component. The fair value of the liability component is calculated by determining its present value using the discount rate of 6 per cent. The calculations and journal entries are illustrated below:

	CU
Proceeds from the bond issue (A)	50,000
Present value of principal at the end of five years (see calculations below)	37,363
Present value of interest payable annually in arrears for five years	8,425
Present value of liability, which is the fair value of liability component (B)	45,788
Residual, which is the fair value of the equity component (A) – (B)	4,212

The issuer of the bonds makes the following journal entry at issue on 1 January 20X5:

Dr Cash	CU50,000	
Cr Financial Liability – Convertible bond		CU45,788
Cr Equity		CU4,212

The CU4,212 represents a discount on issue of the bonds, so the entry could also be shown 'gross':

Dr Cash	CU50,000	
Dr Financial Liability – Convertible bond discount	CU4,212	
Cr Financial Liability – Convertible bond		CU50,000
Cr Equity		CU4,212

After issue, the issuer will amortise the bond discount according to the following table:

	(a) Interest payment	(b) Total interest expense = 6% × (e)	(c) Amortisation of bond discount = (b) – (a)	(d) Bond discount = (d) – (c)	(e) Net liability = 50,000 – (d)
	CU	CU	CU	CU	CU
01/01/20X5				4,212	45,788
31/12/20X5	2,000	2,747	747	3,465	46,535
31/12/20X6	2,000	2,792	792	2,673	47,327
31/12/20X7	2,000	2,840	840	1,833	48,167
31/12/20X8	2,000	2,890	890	943	49,057
31/12/20X9	2,000	2,943	943	0	50,000
Totals	10,000	14,212	4,212		

At the end of 20X5, the issuer would make the following journal entry:

Dr Interest expense	CU2,747	
Cr Bond discount		CU747
Cr Cash		CU2,000

Calculations

Present value of principal of CU50,000 at 6 per cent

CU50,000/$(1.06)^5$ = 37,363

Present value of the interest annuity of CU2,000 (= CU50,000 × 4 per cent) payable at the end of each of five years

The CU2,000 annual interest payments are an annuity: a cash flow stream with a limited number (n) of periodic payments (C), receivable at dates 1 to n. To calculate the present value of this annuity, future payments are discounted by the periodic rate of interest (i) using the following formula:

$PV = C/i \times [1 - 1/(1+i)^n]$

Therefore, the present value of the CU2,000 interest payments is $(2{,}000/.06) \times [1 - [(1/1.06)^5]$ = 8,425

This is equivalent to the sum of the present values of the five individual CU2,000 payments, as follows:

	CU
Present value of interest payment at 31 December 20X5 = 2,000/1.06	1,887
Present value of interest payment at 31 December 20X6 = $2,000/1.06^2$	1,780
Present value of interest payment at 31 December 20X7 = $2,000/1.06^3$	1,679
Present value of interest payment at 31 December 20X8 = $2,000/1.06^4$	1,584
Present value of interest payment at 31 December 20X9 = $2,000/1.06^5$	1,495
Total	8,425

Yet another way to calculate this is to use a table of present value of an ordinary annuity in arrears, five periods, interest rate of 6 per cent per period. (Such tables are easily found on the Internet.) The present value factor is 4.2124. Multiplying this by the annuity payment of CU2,000 determines the present value of CU8,425.

Section 23
Revenue

Scope of this section

23.1 This section applies to **revenue** arising from:

(a) the sale of goods (whether produced by the entity for the purpose of sale or purchased for resale);

(b) the rendering of services;

(c) **construction contracts** in which the entity is the contractor; and

(d) the use by others of entity assets yielding interest, royalties or dividends.

23.2 This section does not apply to revenue or other **income** arising from:

(a) **lease** agreements (see Section 20 *Leases*);

(b) dividends and other income arising from investments that are accounted for using the equity method (see Section 14 *Investments in Associates* and Section 15 *Investments in Joint Ventures*);

(c) changes in the **fair value** of **financial assets** and **financial liabilities** or their disposal (see Section 11 *Basic Financial Instruments* and Section 12 *Other Financial Instruments Issues*);

(d) changes in the fair value of **investment property** (see Section 16 *Investment Property*);

(e) initial **recognition** and changes in the fair value of **biological assets** related to **agricultural activity** (see Section 34 *Specialised Activities*);

(f) initial recognition of **agricultural produce** (see Section 34);

(g) incoming resources from **non-exchange transactions** for **public benefit entities** (see Section 34); and

(h) transactions and events dealt with in **FRS 103**.

23.2A [Moved to paragraph 23.2(h)]

Measurement of revenue

23.3 An entity shall measure revenue at the fair value of the consideration received or receivable. The fair value of the consideration received or receivable takes into account the amount of any trade discounts, prompt settlement discounts and volume rebates allowed by the entity.

23.4 An entity shall include in revenue only the gross inflows of economic benefits received and receivable by the entity on its own account. An entity shall exclude from revenue all amounts collected on behalf of third parties such as sales taxes, goods and services taxes and value added taxes. In an agency relationship, an entity (the **agent**) shall include in revenue only the amount of its commission. The amounts collected on behalf of the **principal** are not revenue of the entity.

Deferred payment

23.5 When the inflow of **cash** or **cash equivalents** is deferred, and the arrangement constitutes in effect a financing transaction, the fair value of the consideration is the

present value of all future receipts determined using an **imputed rate of interest**. A financing transaction arises when, for example, an entity provides interest-free credit to the buyer or accepts a note receivable bearing a below-market interest rate from the buyer as consideration for the sale of goods. The imputed rate of interest is the more clearly determinable of either:

(a) the prevailing rate for a similar instrument of an issuer with a similar credit rating; or

(b) a rate of interest that discounts the nominal amount of the instrument to the current cash sales price of the goods or services.

An entity shall recognise the difference between the present value of all future receipts and the nominal amount of the consideration as interest revenue in accordance with paragraphs 23.28 and 23.29 and Section 11.

Exchanges of goods or services

23.6 An entity shall not recognise revenue:

(a) when goods or services are exchanged for goods or services that are of a similar nature and value; or

(b) when goods or services are exchanged for dissimilar goods or services but the transaction lacks commercial substance.

23.7 An entity shall recognise revenue when goods are sold or services are exchanged for dissimilar goods or services in a transaction that has commercial substance. In that case, the entity shall measure the transaction:

(a) at the fair value of the goods or services received adjusted by the amount of any cash or cash equivalents transferred;

(b) if the amount under (a) cannot be measured reliably, then at the fair value of the goods or services given up adjusted by the amount of any cash or cash equivalents transferred; or

(c) if the fair value of neither the goods or services received nor the goods or services given up can be measured reliably, then at the **carrying amount** of the goods or services given up adjusted by the amount of any cash or cash equivalents transferred.

Identification of the revenue transaction

23.8 An entity usually applies the revenue recognition criteria in this section separately to each transaction. However, an entity applies the recognition criteria to the separately identifiable components of a single transaction when necessary to reflect the substance of the transaction. For example, an entity applies the recognition criteria to the separately identifiable components of a single transaction when the selling price of a product includes an identifiable amount for subsequent servicing. Conversely, an entity applies the recognition criteria to two or more transactions together when they are linked in such a way that the commercial effect cannot be understood without reference to the series of transactions as a whole. For example, an entity applies the recognition criteria to two or more transactions together when it sells goods and, at the same time, enters into a separate agreement to repurchase the goods at a later date, thus negating the substantive effect of the transaction.

23.9 Sometimes, as part of a sales transaction, an entity grants its customer a loyalty award that the customer may redeem in the future for free or discounted goods or services. In this case, in accordance with paragraph 23.8, the entity shall account for the award credits as a separately identifiable component of the initial sales transaction. The entity shall allocate the fair value of the consideration received or receivable in respect of the initial sale between the award credits and the other components of the sale. The consideration allocated to the award credits shall be measured by reference to their fair value, ie the amount for which the award credits could be sold separately.

Sale of goods

23.10 An entity shall recognise revenue from the sale of goods when all the following conditions are satisfied:

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

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

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

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

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

23.11 The assessment of when an entity has transferred the significant risks and rewards of ownership to the buyer requires an examination of the circumstances of the transaction. In most cases, the transfer of the risks and rewards of ownership coincides with the transfer of the legal title or the passing of possession to the buyer. This is the case for most retail sales. In other cases, the transfer of risks and rewards of ownership occurs at a time different from the transfer of legal title or the passing of possession.

23.12 An entity does not recognise revenue if it retains significant risks and rewards of ownership. Examples of situations in which the entity may retain the significant risks and rewards of ownership are:

(a) when the entity retains an obligation for unsatisfactory performance not covered by normal warranties;

(b) when the receipt of the revenue from a particular sale is contingent on the buyer selling the goods;

(c) when the goods are shipped subject to installation and the installation is a significant part of the contract that has not yet been completed; and

(d) when the buyer has the right to rescind the purchase for a reason specified in the sales contract, or at the buyer's sole discretion without any reason, and the entity is uncertain about the probability of return.

23.13 If an entity retains only an insignificant risk of ownership, the transaction is a sale and the entity recognises the revenue. For example, a seller recognises revenue when it retains the legal title to the goods solely to protect the collectability of the amount due. Similarly an entity recognises revenue when it offers a refund if the customer finds the goods faulty or is not satisfied for other reasons, and the entity can estimate the returns reliably. In such cases, the entity recognises a **provision** for returns in accordance with Section 21 *Provisions and Contingencies*.

Rendering of services

23.14 When the outcome of a transaction involving the rendering of services can be estimated reliably, an entity shall recognise revenue associated with the transaction by reference to the stage of completion of the transaction at the end of the **reporting period** (sometimes referred to as the percentage of completion method). The outcome of a transaction can be estimated reliably when all the following conditions are satisfied:

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

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

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

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

Paragraphs 23.21 to 23.27 provide guidance for applying the percentage of completion method.

23.15 When services are performed by an indeterminate number of acts over a specified period of time, an entity recognises revenue on a straight-line basis over the specified period unless there is evidence that some other method better represents the stage of completion. When a specific act is much more significant than any other act, the entity postpones recognition of revenue until the significant act is executed.

23.16 When the outcome of the transaction involving the rendering of services cannot be estimated reliably, an entity shall recognise revenue only to the extent of the **expenses** recognised that it is probable will be recovered.

Construction contracts

23.17 When the outcome of a construction contract can be estimated reliably, an entity shall recognise contract revenue and contract costs associated with the construction contract as revenue and expenses respectively by reference to the stage of completion of the contract activity at the end of the reporting period (often referred to as the percentage of completion method). Reliable estimation of the outcome requires reliable estimates of the stage of completion, future costs and collectability of billings. Paragraphs 23.21 to 23.27 provide guidance for applying the percentage of completion method.

23.17A Costs that relate directly to a contract and are incurred in securing the contract are also included as part of the contract costs if they can be separately identified and measured reliably and it is probable that the contract will be obtained. When costs incurred in securing a contract are recognised as an expense in the period in which they are incurred, they are not included in contract costs if the contract is obtained in a subsequent period.

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

23.19 When a contract covers a number of **assets**, the construction of each asset shall be treated as a separate construction contract when:

(a) separate proposals have been submitted for each asset;

(b) each asset has been subject to separate negotiation, and the contractor and customer are able to accept or reject that part of the contract relating to each asset; and

(c) the costs and revenues of each asset can be identified.

23.20 A group of contracts, whether with a single customer or with several customers, shall be treated as a single construction contract when:

(a) the group of contracts is negotiated as a single package;

(b) the contracts are so closely interrelated that they are, in effect, part of a single project with an overall profit margin; and

(c) the contracts are performed concurrently or in a continuous sequence.

Percentage of completion method

23.21 This method is used to recognise revenue from rendering services (see paragraphs 23.14 to 23.16) and from construction contracts (see paragraphs 23.17 to 23.20). An entity shall review and, when necessary, revise the estimates of revenue and costs as the service transaction or construction contract progresses.

23.22 An entity shall determine the stage of completion of a transaction or contract using the method that measures most reliably the work performed. Possible methods include:

(a) the proportion that costs incurred for work performed to date bear to the estimated total costs. Costs incurred for work performed to date do not include costs relating to future activity, such as for materials or prepayments;

(b) surveys of work performed; and

(c) completion of a physical proportion of the contract work or the completion of a proportion of the service contract.

Progress payments and advances received from customers often do not reflect the work performed.

23.23 An entity shall recognise costs that relate to future activity on the transaction or contract, such as for materials or prepayments, as an asset if it is probable that the costs will be recovered.

23.24 An entity shall recognise as an expense immediately any costs whose recovery is not probable.

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

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

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

23.26 When it is probable that total contract costs will exceed total contract revenue on a construction contract, the expected loss shall be recognised as an expense immediately, with a corresponding provision for an **onerous contract** (see Section 21).

23.27 If the collectability of an amount already recognised as contract revenue is no longer probable, the entity shall recognise the uncollectible amount as an expense rather than as an adjustment of the amount of contract revenue.

Interest, royalties and dividends

23.28 An entity shall recognise revenue arising from the use by others of entity assets yielding interest, royalties and dividends on the bases set out in paragraph 23.29 when:

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

(b) the amount of the revenue can be measured reliably.

23.29 An entity shall recognise revenue on the following bases:

(a) Interest shall be recognised using the **effective interest method** as described in paragraphs 11.15 to 11.20. When calculating the **effective interest rate**, an entity shall include any related fees, finance charges paid or received (such as 'points'), **transaction costs** and other premiums or discounts.

(b) Royalties shall be recognised on an **accrual basis** in accordance with the substance of the relevant agreement.

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

Disclosures

General disclosures about revenue

23.30 An entity shall disclose:

(a) the **accounting policies** adopted for the recognition of revenue, including the methods adopted to determine the stage of completion of transactions involving the rendering of services; and

(b) the amount of each category of revenue recognised during the period, showing separately, at a minimum, revenue arising from:

(i) the sale of goods;

(ii) the rendering of services;

(iii) interest;

(iv) royalties;

(v) dividends;

(vi) commissions;

(vii) grants; and

(viii) any other significant types of revenue.

Disclosures relating to revenue from construction contracts

23.31 An entity shall disclose the following:

(a) the amount of contract revenue recognised as revenue in the period;

(b) the methods used to determine the contract revenue recognised in the period; and

(c) the methods used to determine the stage of completion of contracts in progress.

23.32 An entity shall present:

(a) the gross amount due from customers for contract work, as an asset; and

(b) the gross amount due to customers for contract work, as a **liability**.

23.33 The gross amount due from customers for contract work is the net amount of:

(a) costs recognised as contract expenses plus recognised profits; less

(b) the sum of recognised losses and progress billings,

for all contracts in progress for which contract expenses plus recognised profits (less recognised losses) exceed progress billings.

23.34 The gross amount due to customers for contract work is the net amount of:

(a) costs recognised as contract expenses plus recognised profits; less

(b) the sum of recognised losses and progress billings

for all contracts in progress for which progress billings exceed contract expenses plus recognised profits (less recognised losses).

23.35 Costs incurred less costs recognised as contract expenses shall be presented as contract work in progress within **inventories**, unless an entity has chosen to adapt its **statement of financial position** in accordance with paragraph 4.2A.

Appendix to Section 23
Example of revenue recognition under the principles in Section 23

This appendix accompanies, but is not part of, Section 23. It provides guidance for applying the requirements of Section 23 in recognising revenue.

23A.1 The following examples focus on particular aspects of a transaction and are not a comprehensive discussion of all the relevant factors that might influence the recognition of revenue. The examples generally assume that the amount of revenue can be measured reliably, it is probable that the economic benefits will flow to the entity and the costs incurred or to be incurred can be measured reliably.

Sale of goods

23A.2 The law in different countries may cause the recognition criteria in Section 23 to be met at different times. In particular, the law may determine the point in time at which the entity transfers the significant risks and rewards of ownership. Therefore, the examples in this appendix need to be read in the context of the laws relating to the sale of goods in the country in which the transaction takes place.

Example 1 'Bill and hold' sales, in which delivery is delayed at the buyer's request but the buyer takes title and accepts billing

23A.3 The seller recognises revenue when the buyer takes title, provided:

(a) it is probable that delivery will be made;

(b) the item is on hand, identified and ready for delivery to the buyer at the time the sale is recognised;

(c) the buyer specifically acknowledges the deferred delivery instructions; and

(d) the usual payment terms apply.

Revenue is not recognised when there is simply an intention to acquire or manufacture the goods in time for delivery.

Example 2 Goods shipped subject to conditions: installation and inspection

23A.4 The seller normally recognises revenue when the buyer accepts delivery, and installation and inspection are complete. However, revenue is recognised immediately upon the buyer's acceptance of delivery when:

(a) the installation process is simple, for example the installation of a factory-tested television receiver that requires only unpacking and connection of power and antennae; or

(b) the inspection is performed only for the purposes of final determination of contract prices, for example, shipments of iron ore, sugar or soya beans.

Example 3 Goods shipped subject to conditions: on approval when the buyer has negotiated a limited right of return

23A.5 If there is uncertainty about the possibility of return, the seller recognises revenue when the shipment has been formally accepted by the buyer or the goods have been delivered and the time period for rejection has elapsed.

Example 4 Goods shipped subject to conditions: consignment sales under which the recipient (buyer) undertakes to sell the goods on behalf of the shipper (seller)

23A.6 The shipper recognises revenue when the goods are sold by the recipient to a third party.

Example 5 Goods shipped subject to conditions: cash on delivery sales

23A.7 The seller recognises revenue when delivery is made and cash is received by the seller or its agent.

Example 6 Layaway sales under which the goods are delivered only when the buyer makes the final payment in a series of instalments

23A.8 The seller recognises revenue from such sales when the goods are delivered. However, when experience indicates that most such sales are consummated, revenue may be recognised when a significant deposit is received, provided the goods are on hand, identified and ready for delivery to the buyer.

Example 7 Orders when payment (or partial payment) is received in advance of delivery for goods not currently held in inventory, for example, the goods are still to be manufactured or will be delivered direct to the buyer from a third party

23A.9 The seller recognises revenue when the goods are delivered to the buyer.

Example 8 Sale and repurchase agreements (other than swap transactions) under which the seller concurrently agrees to repurchase the same goods at a later date, or when the seller has a call option to repurchase, or the buyer has a put option to require the repurchase, by the seller, of the goods

23A.10 For a sale and repurchase agreement on an asset other than a financial asset, the seller must analyse the terms of the agreement to ascertain whether, in substance, the risks and rewards of ownership have been transferred to the buyer. If they have been transferred, the seller recognises revenue. When the seller has retained the risks and rewards of ownership, even though legal title has been transferred, the transaction is a financing arrangement and does not give rise to revenue. For a sale and repurchase agreement on a financial asset, the derecognition provisions of Section 11 *Basic Financial Instruments* apply.

Example 9 Sales to intermediate parties, such as distributors, dealers or others for resale

23A.11 The seller generally recognises revenue from such sales when the risks and rewards of ownership have been transferred. However, when the buyer is acting, in substance, as an agent, the sale is treated as a consignment sale.

Example 10 Subscriptions to publications and similar items

23A.12 When the items involved are of similar value in each time period, the seller recognises revenue on a straight-line basis over the period in which the items are dispatched. When the items vary in value from period to period, the seller recognises revenue on the basis of the sales value of the item dispatched in relation to the total estimated sales value of all items covered by the subscription.

Example 11 Instalment sales, under which the consideration is receivable in instalments

23A.13 The seller recognises revenue attributable to the sales price, exclusive of interest, at the date of sale. The sale price is the present value of the consideration, determined by discounting the instalments receivable at the imputed rate of interest. The seller recognises the interest element as revenue using the effective interest method.

Example 12 Agreements for the construction of real estate

23A.14 An entity that undertakes the construction of real estate, directly or through subcontractors, and enters into an agreement with one or more buyers before construction is complete, shall account for the agreement using the percentage of completion method, only if:

(a) the buyer is able to specify the major structural elements of the design of the real estate before construction begins and/or specify major structural changes once construction is in progress (whether it exercises that ability or not); or

(b) the buyer acquires and supplies construction materials and the entity provides only construction services.

23A.15 If the entity is required to provide services together with construction materials in order to perform its contractual obligation to deliver real estate to the buyer, the agreement shall be accounted for as the sale of goods. In this case, the buyer does not obtain control or the significant risks and rewards of ownership of the work in progress in its current state as construction progresses. Rather, the transfer occurs only on delivery of the completed real estate to the buyer.

Example 13 Sale with customer loyalty award

23A.16 An entity sells product A for CU100. Purchasers of product A get an award credit enabling them to buy product B for CU10. The normal selling price of product B is CU18. The entity estimates that 40 per cent of the purchasers of product A will use their award to buy product B at CU10. The normal selling price of product A, after taking into account discounts that are usually offered but that are not available during this promotion, is CU95.

23A.17 The fair value of the award credit is 40 per cent $\times$ [CU18 – CU10] = CU3.20. The entity allocates the total revenue of CU100 between product A and the award credit by reference to their relative fair values of CU95 and CU3.20 respectively. Therefore:

(a) Revenue for product A is CU100 $\times$ [CU95 / (CU95 + CU3.20)] = CU96.74

(b) Revenue for product B is CU100 $\times$ [CU3.20 / (CU95 + CU3.20)] = CU3.26

Rendering of services

Example 14 Installation fees

23A.18 The seller recognises installation fees as revenue by reference to the stage of completion of the installation, unless they are incidental to the sale of a product, in which case they are recognised when the goods are sold.

Example 15 Servicing fees included in the price of the product

23A.19 When the selling price of a product includes an identifiable amount for subsequent servicing (eg after sales support and product enhancement on the sale of software), the seller defers that amount and recognises it as revenue over the period during which the service is performed. The amount deferred is that which will cover the expected costs of the services under the agreement, together with a reasonable profit on those services.

Example 16 Advertising commissions

23A.20 Media commissions are recognised when the related advertisement or commercial appears before the public. Production commissions are recognised by reference to the stage of completion of the project.

Example 17 Insurance agency commissions

23A.21 Insurance agency commissions received or receivable that do not require the agent to render further service are recognised as revenue by the agent on the effective commencement or renewal dates of the related policies. However, when it is probable that the agent will be required to render further services during the life of the policy, the agent defers the commission, or part of it, and recognises it as revenue over the period during which the policy is in force.

Example 17A Financial services fees

23A.21A The recognition of revenue for financial service fees depends on the purposes for which the fees are assessed and the basis of accounting for any associated financial instrument. The description of fees for financial services may not be indicative of the nature and substance of the services provided. Therefore it is necessary to distinguish between fees that are an integral part of the effective interest rate of a financial instrument, fees that are earned as services are provided, and fees that are earned on the execution of a significant act.

Example 18 Admission fees

23A.22 The seller recognises revenue from artistic performances, banquets and other special events when the event takes place. When a subscription to a number of events is sold, the seller allocates the fee to each event on a basis that reflects the extent to which services are performed at each event.

Example 19 Tuition fees

23A.23 The seller recognises revenue over the period of instruction.

Example 20 Initiation, entrance and membership fees

23A.24 Revenue recognition depends on the nature of the services provided. If the fee permits only membership, and all other services or products are paid for separately, or if there is a separate annual subscription, the fee is recognised as revenue when no significant uncertainty about its collectability exists. If the fee entitles the member to services or publications to be provided during the membership period, or to purchase goods or services at prices lower than those charged to non-members, it is recognised on a basis that reflects the timing, nature and value of the benefits provided.

Franchise fees

23A.25 Franchise fees may cover the supply of initial and subsequent services, equipment and other tangible assets, and know-how. Accordingly, franchise fees are recognised as revenue on a basis that reflects the purpose for which the fees were charged. The following methods of franchise fee recognition are appropriate.

Example 21 Franchise fees: Supplies of equipment and other tangible assets

23A.26 The franchisor recognises the fair value of the assets sold as revenue when the items are delivered or title passes.

Example 22 Franchise fees: Supplies of initial and subsequent services

23A.27 The franchisor recognises fees for the provision of continuing services, whether part of the initial fee or a separate fee, as revenue as the services are rendered. When the separate fee does not cover the cost of continuing services together with a reasonable profit, part of the initial fee, sufficient to cover the costs of continuing services and to provide a reasonable profit on those services, is deferred and recognised as revenue as the services are rendered.

23A.28 The franchise agreement may provide for the franchisor to supply equipment, inventories, or other tangible assets at a price lower than that charged to others or a price that does not provide a reasonable profit on those sales. In these circumstances, part of the initial fee, sufficient to cover estimated costs in excess of that price and to provide a reasonable profit on those sales, is deferred and recognised over the period the goods are likely to be sold to the franchisee. The balance of an initial fee is recognised as revenue when performance of all the initial services and other obligations required of the franchisor (such as assistance with site selection, staff training, financing and advertising) has been substantially accomplished.

23A.29 The initial services and other obligations under an area franchise agreement may depend on the number of individual outlets established in the area. In this case, the fees attributable to the initial services are recognised as revenue in proportion to the number of outlets for which the initial services have been substantially completed.

23A.30 If the initial fee is collectible over an extended period and there is a significant uncertainty that it will be collected in full, the fee is recognised as cash instalments are received.

Example 23 Franchise fees: Continuing franchise fees

23A.31 Fees charged for the use of continuing rights granted by the agreement, or for other services provided during the period of the agreement, are recognised as revenue as the services are provided or the rights used.

Example 24 Franchise fees: Agency transactions

23A.32 Transactions may take place between the franchisor and the franchisee that, in substance, involve the franchisor acting as agent for the franchisee. For example, the franchisor may order supplies and arrange for their delivery to the franchisee at no profit. Such transactions do not give rise to revenue.

Example 25 Fees from the development of customised software

23A.33 The software developer recognises fees from the development of customised software as revenue by reference to the stage of completion of the development, including completion of services provided for post-delivery service support.

Interest, royalties and dividends

Example 26 Licence fees and royalties

23A.34 The licensor recognises fees and royalties paid for the use of an entity's assets (such as trademarks, patents, software, music copyright, record masters and motion picture films) in accordance with the substance of the agreement. As a practical matter, this may be on a straight-line basis over the life of the agreement, for example, when a licensee has the right to use specified technology for a specified period of time.

23A.35 An assignment of rights for a fixed fee or non-refundable guarantee under a non-cancellable contract that permits the licensee to exploit those rights freely and the licensor has no remaining obligations to perform is, in substance, a sale. An example is a licensing agreement for the use of software when the licensor has no obligations after delivery. Another example is the granting of rights to exhibit a motion picture film in markets in which the licensor has no control over the distributor and expects to receive no further revenues from the box office receipts. In such cases, revenue is recognised at the time of sale.

23A.36 In some cases, whether or not a licence fee or royalty will be received is contingent on the occurrence of a future event. In such cases, revenue is recognised only when it is probable that the fee or royalty will be received, which is normally when the event has occurred.

Recognition and measurement

Example 27 Determining whether an entity is acting as a principal or as an agent

23A.37 Determining whether an entity is acting as a principal or as an agent requires judgement and consideration of all relevant facts and circumstances.

23A.38 An entity is acting as a principal when it has exposure to the significant risks and rewards associated with the sale of goods or the rendering of services. Features that indicate that an entity is acting as principal include:

(a) the entity has the primary responsibility for providing the goods or services to the customer or for fulfilling the order, for example by being responsible for the acceptability of the products or services ordered or purchased by the customer;

(b) the entity has inventory risk before or after the customer order, during shipping or on return;

(c) the entity has latitude in establishing prices, either directly or indirectly, for example by providing additional goods or services; and

(d) the entity bears the customer's credit risk for the amount receivable from the customer.

23A.39 An entity is acting as an agent when it does not have exposure to the significant risks and rewards associated with the sale of goods or the rendering of services. One feature indicating that an entity is acting as agent is that the amount the entity earns is predetermined, being either a fixed fee per transaction or a stated percentage of the amount billed to the customer.

23A.40 When an entity has entered into a contract as an undisclosed agent, it is normally acting as principal.

23A.41 The amounts collected by an agent on behalf of a principal are not revenue. Instead, revenue is the amount of commission.

Section 24
Government Grants

Scope of this section

24.1 This section applies to **government grants**.

PBE24.1A The accounting for incoming resources from **non-exchange transactions** other than government grants is addressed in paragraphs PBE34.64 to PBE34.74 and Appendix B to Section 34 *Specialised Activities*.

24.2 Government grants exclude those forms of government assistance that cannot reasonably have a value placed upon them and transactions with government that cannot be distinguished from the normal trading transactions of the entity.

24.3 This section does not cover government assistance that is provided for an entity in the form of benefits that are available in determining **taxable profit (tax loss)**, or are determined or limited on the basis of **income tax** liability. Examples of such benefits are income tax holidays, investment tax credits, accelerated depreciation allowances and reduced income tax rates. Section 29 *Income Tax* covers accounting for taxes based on **income**.

Recognition and measurement

24.3A Government grants, including non-monetary grants shall not be recognised until there is reasonable assurance that:

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

(b) the grants will be received.

24.4 An entity shall recognise grants either based on the performance model or the accrual model. This policy choice shall be applied on a class-by-class basis.

24.5 An entity shall measure grants at the **fair value** of the **asset** received or receivable.

24.5A Where a grant becomes repayable it shall be recognised as a **liability** when the repayment meets the definition of a liability.

Performance model

24.5B An entity applying the performance model shall recognise grants as follows:

(a) A grant that does not impose specified future **performance-related conditions** on the recipient is recognised in income when the grant proceeds are received or receivable.

(b) A grant that imposes specified future performance-related conditions on the recipient is recognised in income only when the performance-related conditions are met.

(c) Grants received before the **revenue recognition** criteria are satisfied are recognised as a liability.

Accrual model

24.5C An entity applying the accrual model shall classify grants either as a grant relating to revenue or a grant relating to assets.

24.5D Grants relating to revenue shall be recognised in income on a systematic basis over the periods in which the entity recognises the related costs for which the grant is intended to compensate.

24.5E A grant that becomes receivable as compensation for **expenses** or losses already incurred or for the purpose of giving immediate financial support to the entity with no future related costs shall be recognised in income in the period in which it becomes receivable.

24.5F Grants relating to assets shall be recognised in income on a systematic basis over the expected **useful life** of the asset.

24.5G Where part of a grant relating to an asset is deferred it shall be recognised as deferred income and not deducted from the **carrying amount** of the asset.

Disclosures

24.6 An entity shall disclose the following:

(a) the **accounting policy** adopted for grants in accordance with paragraph 24.4;

(b) the nature and amounts of grants recognised in the **financial statements**;

(c) unfulfilled conditions and other contingencies attaching to grants that have been recognised in income; and

(d) an indication of other forms of government assistance from which the entity has directly benefited.

24.7 For the purpose of the disclosure required by paragraph 24.6(d), government assistance is action by government designed to provide an economic benefit specific to an entity or range of entities qualifying under specified criteria. Examples include free technical or marketing advice and the provision of guarantees.

Section 25
Borrowing Costs

Scope of this section

25.1 This section applies to **borrowing costs**. Borrowing costs include:

(a) interest expense calculated using the **effective interest method** as set out in Section 11 *Basic Financial Instruments*;

(b) finance charges in respect of **finance leases** as set out in Section 20 *Leases*; and

(c) exchange differences arising from foreign currency borrowings to the extent that they are regarded as an adjustment to interest costs.

Recognition

25.2 An entity may adopt a policy of capitalising borrowing costs that are directly attributable to the acquisition, construction or production of a **qualifying asset** as part of the cost of that **asset**. Where an entity adopts a policy of capitalisation of borrowing costs, it shall be applied consistently to a class of qualifying assets. Where an entity does not adopt a policy of capitalising borrowing costs, all borrowing costs shall be recognised as an **expense** in **profit or loss** in the period in which they are incurred.

25.2A The borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset are those borrowing costs that would have been avoided if the expenditure on the qualifying asset had not been made.

25.2B To the extent that an entity borrows funds specifically for the purpose of obtaining a qualifying asset, the entity shall determine the amount of borrowing costs eligible for capitalisation as the actual borrowing costs incurred on that borrowing during the period less any investment income on the temporary investment of those borrowings.

25.2C To the extent that funds applied to obtain a qualifying asset form part of the entity's general borrowings, the amount of borrowing costs eligible for capitalisation are determined by applying a capitalisation rate to the expenditure on that asset. For this purpose the expenditure on the asset is the average **carrying amount** of the asset during the period, including borrowing costs previously capitalised. The capitalisation rate used in an accounting period shall be the weighted average of rates applicable to the entity's general borrowings that are outstanding during the period. This excludes borrowings by the entity that are specifically for the purpose of obtaining other qualifying assets. The amount of borrowing costs that an entity capitalises during a period shall not exceed the amount of borrowing costs it incurred during that period.

25.2D An entity shall:

(a) capitalise borrowing costs as part of the cost of a qualifying asset from the point when it first incurs both expenditure on the asset and borrowing costs, and undertakes activities necessary to prepare the asset for its intended use or sale;

(b) suspend capitalisation during extended periods where active development of the asset has paused; and

(c) cease capitalisation when substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are complete.

Disclosures

25.3 Paragraph 5.5 sets out the presentation requirements for items of profit or loss, including interest payable. Paragraph 11.48(b) requires disclosure of total interest expense (using the effective interest method) for **financial liabilities** that are not at **fair value** through profit or loss. When a policy of capitalising borrowing costs is not adopted, this section does not require any additional disclosure.

25.3A Where a policy of capitalisation is adopted, an entity shall disclose:

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

(b) the capitalisation rate used.

Section 26
Share-based Payment

Scope of this section

26.1 This section applies to **share-based payment transactions** including:

(a) **equity-settled share-based payment transactions**;

(b) **cash-settled share-based payment transactions**; and

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

In the absence of specifically identifiable goods or services, other circumstances may indicate that goods or services have been (or will be) received, in which case this section applies.

26.1A A share-based payment transaction may be settled by another **group** entity (or a shareholder of any group entity) on behalf of the entity receiving or acquiring the goods or services. Paragraph 26.1 also applies to an entity that:

(a) receives goods or services when another entity in the same group (or shareholder of any group entity) has the obligation to settle the share-based payment transaction; or

(b) has an obligation to settle a share-based payment transaction when another entity in the same group receives the goods or services

unless the transaction is clearly for a purpose other than payment for goods or services supplied to the entity receiving them.

26.2 Cash-settled share-based payment transactions include share appreciation rights. For example, an entity might grant share appreciation rights to employees as part of their remuneration package, whereby the employees will become entitled to a future cash payment (rather than an equity instrument), based on the increase in the entity's share price from a specified level over a specified period of time. Or an entity might grant to its employees a right to receive a future cash payment by granting to them a right to shares (including shares to be issued upon the exercise of **share options**) that are redeemable, either mandatorily (eg upon cessation of employment) or at the employee's option.

26.2A The entity settling a share-based payment transaction when another entity in the group receives the goods or services shall recognise the transaction as an equity-settled share-based payment transaction only if it is settled in its own equity instruments. Otherwise, the transaction shall be recognised as a cash-settled share-based payment transaction.

Recognition

26.3 An entity shall recognise the goods or services received or acquired in a share-based payment transaction when it obtains the goods or as the services are received. The entity shall recognise a corresponding increase in **equity** if the goods or services were received in an equity-settled share-based payment transaction, or a **liability** if the goods or services were acquired in a cash-settled share-based payment transaction.

26.4 When the goods or services received or acquired in a share-based payment transaction do not qualify for **recognition** as assets, the entity shall recognise them as **expenses**.

Recognition when there are vesting conditions

26.5 If the **share-based payments** granted **vest** immediately, the counterparty is not required to complete a specified period of service before becoming unconditionally entitled to those share-based payments. In the absence of evidence to the contrary, the entity shall presume that services rendered by the counterparty as consideration for the share-based payments have been received. In this case, on **grant date** the entity shall recognise the services received in full, with a corresponding increase in equity or liabilities.

26.6 If the share-based payments do not vest until the counterparty completes a specified period of service, the entity shall presume that the services to be rendered by the counterparty as consideration for those share-based payments will be received in the future, during the **vesting period**. The entity shall account for those services as they are rendered by the counterparty during the vesting period, with a corresponding increase in equity or liabilities.

Measurement of equity-settled share-based payment transactions

Measurement principle

26.7 For equity-settled share-based payment transactions, an entity shall measure the goods or services received, and the corresponding increase in equity, at the **fair value** of the goods or services received, unless that fair value cannot be estimated reliably. If the entity cannot estimate reliably the fair value of the goods or services received, the entity shall measure their value, and the corresponding increase in equity, by reference to the fair value of the equity instruments granted measured in accordance with paragraphs 26.10 and 26.11. To apply this requirement to transactions with employees and others providing similar services, the entity shall measure the fair value of the services received by reference to the fair value of the equity instruments granted, because typically it is not possible to estimate reliably the fair value of the services received.

26.8 For transactions with employees (including others providing similar services), the fair value of the equity instruments shall be measured at grant date. For transactions with parties other than employees, the measurement date is the date when the entity obtains the goods or the counterparty renders service.

26.9 A grant of equity instruments might be conditional upon satisfying specified **vesting conditions** related to service or performance. An example of a **service condition** is when a grant of shares or share options is conditional on the employee remaining in the entity's employ for a specified period of time. Examples of **performance conditions** are when a grant of shares or share options is conditional on the entity achieving a specified growth in profit (a non-market vesting condition) or a specified increase in the entity's share price (a **market condition**). Vesting conditions and conditions that are not vesting conditions (such as a condition that an employee contributes to a savings plan) are accounted for as follows:

(a) Vesting conditions, other than market conditions, shall not be taken into account when estimating the fair value of the shares or share options at the measurement date. Instead, such vesting conditions shall be taken into account in estimating the number of equity instruments expected to vest. Subsequently, the entity shall revise that estimate, if new information indicates that the number of equity instruments expected to vest differs from previous estimates. On the vesting date, the entity shall revise the estimate to equal the number of equity instruments that ultimately vested.

(b) All **market vesting conditions** and conditions that are not vesting conditions shall be taken into account when estimating the fair value of the equity instruments granted at the measurement date, with no subsequent adjustment to the estimated fair value, irrespective of the outcome of the market condition or condition that is not a vesting condition, provided that all other vesting conditions are satisfied.

Shares

26.10 An entity shall measure the fair value of shares (and the related goods or services received) using the following three-tier measurement hierarchy:

(a) If an observable market price is available for the equity instruments granted, use that price.

(b) If an observable market price is not available, measure the fair value of equity instruments granted using entity-specific observable market data such as:

(i) a recent transaction in the entity's shares; or

(ii) a recent independent fair valuation of the entity or its principal assets.

(c) If an observable market price is not available and obtaining a reliable **measurement** of fair value under (b) is **impracticable**, indirectly measure the fair value of the shares using a valuation method that uses market data to the greatest extent practicable to estimate what the price of those equity instruments would be on the grant date in an arm's length transaction between knowledgeable, willing parties. The entity's directors shall use their judgement to apply a generally accepted valuation methodology for valuing equity instruments that is appropriate to the circumstances of the entity.

Share options and equity-settled share appreciation rights

26.11 An entity shall measure the fair value of share options and equity-settled share appreciation rights (and the related goods or services received) using the following three-tier measurement hierarchy:

(a) If an observable market price is available for the equity instruments granted, use that price.

(b) If an observable market price is not available, measure the fair value of share options and share appreciation rights granted using entity-specific observable market data such as for a recent transaction in the share options.

(c) If an observable market price is not available and obtaining a reliable measurement of fair value under (b) is impracticable, indirectly measure the fair value of share options or share appreciation rights using an alternative valuation methodology such as an option pricing model. The inputs for an option pricing model (such as the weighted average share price, exercise price, expected volatility, option life, expected dividends and the risk-free interest rate) shall use market data to the greatest extent possible. Paragraph 26.10 provides guidance on determining the fair value of the shares used in determining the weighted average share price. The entity shall derive an estimate of expected volatility consistent with the valuation methodology used to determine the fair value of the shares.

Modifications to the terms and conditions on which equity instruments were granted

26.12 An entity might modify the terms and conditions on which equity instruments are granted in a manner that is beneficial to the employee, for example, by reducing the exercise price of an option or reducing the vesting period or by modifying or eliminating a performance condition. Alternatively, an entity might modify the terms and conditions in a manner that is not beneficial to the employee, for example, by increasing the vesting period or adding a performance condition. The entity shall take the modified vesting conditions into account in accounting for the share-based payment transaction, as follows:

(a) If the modification increases the fair value of the equity instruments granted (or increases the number of equity instruments granted) measured immediately before and after the modification, the entity shall include the incremental fair value granted in the measurement of the amount recognised for services received as consideration for the equity instruments granted. The incremental fair value granted is the difference between the fair value of the modified equity instrument and that of the original equity instrument, both estimated as at the date of the modification. If the modification occurs during the vesting period, the incremental fair value granted is included in the measurement of the amount recognised for services received over the period from the modification date until the date when the modified equity instruments vest, in addition to the amount based on the grant date fair value of the original equity instruments, which is recognised over the remainder of the original vesting period.

(b) If the modification reduces the total fair value of the **share-based payment arrangement**, or apparently is not otherwise beneficial to the employee, the entity shall nevertheless continue to account for the services received as consideration for the equity instruments granted as if that modification had not occurred.

The requirements in this paragraph are expressed in the context of share-based payment transactions with employees. The requirements also apply to share-based payment transactions with parties other than employees if these transactions are measured by reference to their fair value of the equity instruments granted, but reference to the grant date refers to the date that the entity obtains the goods or the counterparty renders service.

Cancellations and settlements

26.13 An entity shall account for a cancellation or settlement of an equity-settled share-based payment transaction as an acceleration of vesting, and therefore shall recognise immediately the amount that otherwise would have been recognised for services received over the remainder of the vesting period.

Cash-settled share-based payment transactions

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

Share-based payment transactions with cash alternatives

26.15 Some share-based payment transactions give either the entity or the counterparty a choice of settling the transaction in cash (or other assets) or by the transfer of equity instruments.

26.15A When the entity has a choice of settlement of the transaction in cash (or other assets) or by the transfer of equity instruments, the entity shall account for the transaction as a wholly equity-settled share-based payment transaction in accordance with paragraphs 26.7 to 26.13 unless:

(a) the choice of settlement in equity instruments has no commercial substance (eg because the entity is legally prohibited from issuing shares); or

(b) the entity has a past practice or a stated policy of settling in cash, or generally settles in cash whenever the counterparty asks for cash settlement.

In circumstances (a) and (b) the entity shall account for the transaction as a wholly cash-settled transaction in accordance with paragraph 26.14.

26.15B Except as set out in paragraph 26.15C, when the counterparty has a choice of settlement of the transaction in cash (or other assets) or by the transfer of equity instruments, the entity shall account for the transaction as a wholly cash-settled share-based payment transaction in accordance with paragraph 26.14.

26.15C If the choice of settlement in cash (or other assets) has no commercial substance because the cash settlement amount (or value of the other assets) bears no relationship to, and is likely to be lower in value than, the fair value of the equity instruments, the entity shall account for the transaction as a wholly equity-settled transaction in accordance with paragraphs 26.7 to 26.13.

Group plans

26.16 If a share-based payment is granted by an entity to the employees of one or more group entities, the group entities are permitted, as an alternative to the treatment set out in paragraphs 26.7 to 26.15C, to measure the share-based payment expense on the basis of a reasonable allocation of the expense for the group, calculated in accordance with this FRS, IFRS 2 *Share-based Payment* or on an equivalent basis.

Government-mandated plans

26.17 Some jurisdictions have programmes established under law by which equity investors (such as employees) are able to acquire equity without providing goods or services that can be specifically identified (or by providing goods or services that are clearly less than the fair value of the equity instruments granted). This indicates that other consideration has been or will be received (such as past or future employee services). These are equity-settled share-based payment transactions within the scope of this section. The entity shall measure the unidentifiable goods or services received (or to be received) as the difference between the fair value of the equity instrument and the fair value of any identifiable goods or services received (or to be received) measured at the grant date.

Disclosures

26.18 An entity shall disclose the following information about the nature and extent of share-based payment arrangements that existed during the period:

(a) A description of each type of share-based payment arrangement that existed at any time during the period, including the general terms and conditions of each arrangement, such as vesting requirements, the maximum term of options granted, and the method of settlement (eg whether in cash or equity). An entity with substantially similar types of share-based payment arrangements may aggregate this information.

(b) The number and weighted average exercise prices of share options for each of the following groups of options:

(i) outstanding at the beginning of the period;

(ii) granted during the period;

(iii) forfeited during the period;

(iv) exercised during the period;

(v) expired during the period;

(vi) outstanding at the end of the period; and

(vii) exercisable at the end of the period.

26.19 For equity-settled share-based payment arrangements, an entity shall disclose information about how it measured the fair value of goods or services received or the value of the equity instruments granted. If a valuation methodology was used, the entity shall disclose the method and its reason for choosing it.

26.20 For cash-settled share-based payment arrangements, an entity shall disclose information about how the liability was measured.

26.21 For share-based payment arrangements that were modified during the period, an entity shall disclose an explanation of those modifications.

26.22 If the entity is part of a group share-based payment arrangement, and it measures its share-based payment expense on the basis of a reasonable allocation of the expense for the group, it shall disclose that fact and the basis for the allocation (see paragraph 26.16).

26.23 An entity shall disclose the following information about the effect of share-based payment transactions on the entity's profit or loss for the period and on its **financial position**:

(a) the total expense recognised in profit or loss for the period; and

(b) the total **carrying amount** at the end of the period for liabilities arising from share-based payment transactions.

Section 27
Impairment of Assets

Objective and scope

27.1 This section applies to the impairment of assets and the **recognition** of **impairment losses** except in relation to:

(a) **assets** arising from **construction contracts** (see Section 23 *Revenue*);

(b) **deferred tax assets** (see Section 29 *Income Tax*);

(c) assets arising from **employee benefits** (see Section 28 *Employee Benefits*);

(d) **financial assets** within the scope of Section 11 *Basic Financial Instruments* or Section 12 *Other Financial Instruments Issues*;

(e) **investment property** measured at **fair value** (see Section 16 *Investment Property*);

(f) **biological assets** related to **agricultural activity** measured at fair value less estimated costs to sell (see Section 34 *Specialised Activities*); and

(g) **deferred acquisition costs** and **intangible assets** arising from contracts within the scope of **FRS 103**.

27.1A [Moved to paragraph 27.1(g)]

Impairment of inventories

Selling price less costs to complete and sell

27.2 An entity shall assess at each **reporting date** whether any **inventories** are impaired. The entity shall make the assessment by comparing the **carrying amount** of each item of inventory (or group of similar items – see paragraph 27.3) with its selling price less costs to complete and sell. If an item of inventory (or group of similar items) is impaired, the entity shall reduce the carrying amount of the inventory (or the group) to its selling price less costs to complete and sell. That reduction is an impairment loss and it is recognised immediately in **profit or loss**.

27.3 If it is **impracticable** to determine the selling price less costs to complete and sell for inventories item by item, the entity may group items of inventory relating to the same product line that have similar purposes or end uses and are produced and marketed in the same geographical area for the purpose of assessing impairment.

Reversal of impairment

27.4 An entity shall make a new assessment of selling price less costs to complete and sell at each subsequent reporting date. When the circumstances that previously caused inventories to be impaired no longer exist or when there is clear evidence of an increase in selling price less costs to complete and sell because of changed economic circumstances, the entity shall reverse the amount of the impairment (ie the reversal is limited to the amount of the original impairment loss) so that the new carrying amount is the lower of the cost and the revised selling price less costs to complete and sell.

Impairment of assets other than inventories

General principles

27.5 If, and only if, the **recoverable amount** of an asset is less than its carrying amount, the entity shall reduce the carrying amount of the asset to its recoverable amount. That reduction is an impairment loss. Paragraphs 27.11 to 27.20A provide guidance on measuring recoverable amount.

27.6 An entity shall recognise an impairment loss immediately in profit or loss, unless the asset is carried at a revalued amount in accordance with another section of this FRS (for example, in accordance with the revaluation model in Section 17 *Property, Plant and Equipment*). Any impairment loss of a revalued asset shall be treated as a revaluation decrease in accordance with that other section.

Indicators of impairment

27.7 An entity shall assess at each reporting date 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. If there is no indication of impairment, it is not necessary to estimate the recoverable amount.

27.8 If it is not possible to estimate the recoverable amount of the individual asset, an entity shall estimate the recoverable amount of the **cash-generating unit** to which the asset belongs. This may be the case because measuring recoverable amount requires forecasting **cash flows**, and sometimes individual assets do not generate cash flows by themselves. An asset's cash-generating unit is the smallest identifiable group of assets that includes the asset and generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets.

27.9 In assessing whether there is any indication that an asset may be impaired, an entity shall consider, as a minimum, the following indications:

External sources of information

(a) During the period, an asset's market value has declined significantly more than would be expected as a result of the passage of time or normal use.

(b) Significant changes with an adverse effect on the entity have taken place during the period, or will take place in the near future, in the technological, market, economic or legal environment in which the entity operates or in the market to which an asset is dedicated.

(c) Market interest rates or other market rates of return on investments have increased during the period, and those increases are likely to affect materially the discount rate used in calculating an asset's **value in use** and decrease the asset's **fair value less costs to sell**.

(d) The carrying amount of the net assets of the entity is more than the estimated fair value of the entity as a whole (such an estimate may have been made, for example, in relation to the potential sale of part or all of the entity).

Internal sources of information

(e) Evidence is available of obsolescence or physical damage of an asset.

(f) Significant changes with an adverse effect on the entity have taken place during the period, or are expected to take place in the near future, in the extent to which, or manner in which, an asset is used or is expected to be used. These changes include the asset becoming idle, plans to discontinue or restructure the operation to which an asset belongs, plans to dispose of an asset before the previously expected date, and reassessing the **useful life** of an asset as finite rather than indefinite.

(g) Evidence is available from internal reporting that indicates that the economic performance of an asset is, or will be, worse than expected. In this context economic performance includes operating results and cash flows.

27.10 If there is an indication that an asset may be impaired, this may indicate that the entity should review the remaining useful life, the **depreciation (amortisation)** method or the **residual value** for the asset and adjust it in accordance with the section of this FRS applicable to the asset (eg Section 17 and Section 18 *Intangible Assets other than Goodwill*), even if no impairment loss is recognised for the asset.

Measuring recoverable amount

27.11 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. If it is not possible to estimate the recoverable amount of an individual asset, references to an asset in paragraphs 27.12 to 27.20A should be read as references also to an asset's cash-generating unit.

27.12 It is not always necessary to determine both an asset's fair value less costs to sell and its value in use. If either of these amounts exceeds the asset's carrying amount, the asset is not impaired and it is not necessary to estimate the other amount.

27.13 If there is no reason to believe that an asset's value in use materially exceeds its fair value less costs to sell, the asset's fair value less costs to sell may be used as its recoverable amount. This will often be the case for an asset that is held for disposal.

Fair value less costs to sell

27.14 Fair value less costs to sell is the amount obtainable from the sale of an asset in an arm's length transaction between knowledgeable, willing parties, less the costs of disposal. The best evidence of the fair value less costs to sell of an asset is a price in a binding sale agreement in an arm's length transaction or a market price in an **active market**. If there is no binding sale agreement or active market for an asset, fair value less costs to sell is based on the best information available to reflect the amount that an entity could obtain, at the reporting date, from the disposal of the asset in an arm's length transaction between knowledgeable, willing parties, after deducting the costs of disposal. In determining this amount, an entity considers the outcome of recent transactions for similar assets within the same industry.

27.14A When determining an asset's fair value less costs to sell, consideration shall be given to any restrictions imposed on that asset. Costs to sell shall also include the cost of obtaining relaxation of a restriction where necessary in order to enable the asset to be sold. If a restriction would also apply to any potential purchaser of an asset, the fair value of the asset may be lower than that of an asset whose use is not restricted.

Value in use

27.15 Value in use is the **present value** of the future cash flows expected to be derived from an asset. This present value calculation involves the following steps:

(a) estimating the future cash inflows and outflows to be derived from continuing use of the asset and from its ultimate disposal; and

(b) applying the appropriate discount rate to those future cash flows.

27.16 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.

27.17 In measuring value in use, estimates of future cash flows shall include:

(a) projections of cash inflows from the continuing use of the asset;

(b) projections of cash outflows that are necessarily incurred to generate the cash inflows from continuing use of the asset (including cash outflows to prepare the asset for use) and can be directly attributed, or allocated on a reasonable and consistent basis, to the asset; and

(c) net cash flows, if any, expected to be received (or paid) for the disposal of the asset at the end of its useful life in an arm's length transaction between knowledgeable, willing parties.

The entity may wish to use any recent financial budgets or forecasts to estimate the cash flows, if available. To estimate cash flow projections beyond the period covered by the most recent budgets or forecasts an entity may wish to extrapolate the projections based on the budgets or forecasts using a steady or declining growth rate for subsequent years, unless an increasing rate can be justified.

27.18 Estimates of future cash flows shall not include:

(a) cash inflows or outflows from **financing activities**; or

(b) **income tax** receipts or payments.

27.19 Future cash flows shall be estimated for the asset in its current condition. Estimates of future cash flows shall not include estimated future cash inflows or outflows that are expected to arise from:

(a) a future **restructuring** to which an entity is not yet committed; or

(b) improving or enhancing the asset's performance.

27.20 The discount rate (rates) used in the present value calculation shall be a pre-tax rate (rates) that reflect(s) current market assessments of:

(a) the time value of money; and

(b) the risks specific to the asset for which the future cash flow estimates have not been adjusted.

The discount rate (rates) used to measure an asset's value in use shall not reflect risks for which the future cash flow estimates have been adjusted, to avoid double-counting.

27.20A For assets held for their **service potential**, a cash flow driven valuation (such as value in use) may not be appropriate. In these circumstances **value in use (in respect of assets held for their service potential)** is determined by the present value of the asset's remaining service potential plus the net amount the entity will receive from its disposal. In some cases this may be taken to be costs avoided by possession of the asset. Therefore, **depreciated replacement cost**, may be a suitable measurement model but other approaches may be used where more appropriate.

Recognising and measuring an impairment loss for a cash-generating unit

27.21 An impairment loss shall be recognised for a cash-generating unit if, and only if, the recoverable amount of the unit is less than the carrying amount of the unit. The impairment loss shall be allocated to reduce the carrying amount of the assets of the unit in the following order:

(a) first, to reduce the carrying amount of any **goodwill** allocated to the cash-generating unit; and

(b) then, to the other assets of the unit pro rata on the basis of the carrying amount of each asset in the cash-generating unit.

27.22 However, an entity shall not reduce the carrying amount of any asset in the cash-generating unit below the highest of:

(a) its fair value less costs to sell (if determinable);

(b) its value in use (if determinable); and

(c) zero.

27.23 Any excess amount of the impairment loss that cannot be allocated to an asset because of the restriction in paragraph 27.22 shall be allocated to the other assets of the unit pro rata on the basis of the carrying amount of those other assets.

Additional requirements for impairment of goodwill

27.24 Goodwill, by itself, cannot be sold. Nor does it generate cash flows to an entity that are independent of the cash flows of other assets. As a consequence, the fair value of goodwill cannot be measured directly. Therefore, the fair value of goodwill must be derived from **measurement** of the fair value of the cash-generating unit(s) of which the goodwill is a part.

27.25 For the purpose of impairment testing, goodwill acquired in a **business combination** shall, from the **acquisition date**, be allocated to each of the acquirer's cash-generating units that are expected to benefit from the synergies of the combination, irrespective of whether other assets or **liabilities** of the acquiree are assigned to those units.

27.26 Part of the recoverable amount of a cash-generating unit is attributable to the **non-controlling interest** in goodwill. For the purpose of impairment testing of a non-wholly-owned cash-generating unit with goodwill, the carrying amount of that unit is notionally adjusted, before being compared with its recoverable amount, by grossing up the carrying amount of goodwill allocated to the unit to include the goodwill attributable to the non-controlling interest. This notionally adjusted carrying amount is then compared with the recoverable amount of the unit to determine whether the cash-generating unit is impaired.

27.27 If goodwill cannot be allocated to individual cash-generating units (or groups of cash-generating units) on a non-arbitrary basis, then for the purposes of testing goodwill the entity shall test the impairment of goodwill by determining the recoverable amount of either:

(a) the acquired entity in its entirety, if the goodwill relates to an acquired entity that has not been integrated. Integrated means the acquired **business** has been restructured or dissolved into the reporting entity or other **subsidiaries;** or

(b) the entire **group** of entities, excluding any entities that have not been integrated, if the goodwill relates to an entity that has been integrated.

In applying this paragraph, an entity will need to separate goodwill into goodwill relating to entities that have been integrated and goodwill relating to entities that have not been integrated. Also the entity shall follow the requirements for cash-generating units in this section when calculating the recoverable amount of, and allocating impairment losses and reversals to assets belonging to, the acquired entity or group of entities.

Reversal of an impairment loss

27.28 An impairment loss recognised for goodwill shall not be reversed in a subsequent period.

27.29 For all assets other than goodwill, if and only if the reasons for the impairment loss have ceased to apply, an impairment loss shall be reversed in a subsequent period. An entity shall assess at each reporting date whether there is any indication that an impairment loss recognised in prior periods may no longer exist or may have decreased. Indications that an impairment loss may have decreased or may no longer exist are generally the opposite of those set out in paragraph 27.9. If any such indication exists, the entity shall determine whether all or part of the prior impairment loss should be reversed. The procedure for making that determination will depend on whether the prior impairment loss on the asset was based on:

(a) the recoverable amount of that individual asset (see paragraph 27.30); or

(b) the recoverable amount of the cash-generating unit to which the asset belongs (see paragraph 27.31).

Reversal where recoverable amount was estimated for an individual impaired asset

27.30 When the prior impairment loss was based on the recoverable amount of the individual impaired asset, the following requirements apply:

(a) The entity shall estimate the recoverable amount of the asset at the current reporting date.

(b) If the estimated recoverable amount of the asset exceeds its carrying amount, the entity shall increase the carrying amount to recoverable amount, subject to the limitation described in (c) below. That increase is a reversal of an impairment loss. The entity shall recognise the reversal immediately in profit or loss unless the asset is carried at revalued amount in accordance with another section of this FRS (for example, the revaluation model in Section 17). Any reversal of an impairment loss of a revalued asset shall be treated as a revaluation increase in accordance with the relevant section of this FRS.

(c) The reversal of an impairment loss shall not increase the carrying amount of the asset above the carrying amount that would have been determined (net of amortisation or depreciation) had no impairment loss been recognised for the asset in prior years.

(d) After a reversal of an impairment loss is recognised, the entity shall adjust the depreciation (amortisation) charge for the asset in future periods to allocate the asset's revised carrying amount, less its residual value (if any), on a systematic basis over its remaining useful life.

Reversal when recoverable amount was estimated for a cash-generating unit

27.31 When the original impairment loss was based on the recoverable amount of the cash-generating unit to which the asset, including goodwill belongs, the following requirements apply:

(a) The entity shall estimate the recoverable amount of that cash-generating unit at the current reporting date.

(b) If the estimated recoverable amount of the cash-generating unit exceeds its carrying amount, that excess is a reversal of an impairment loss. The entity shall allocate the amount of that reversal to the assets of the unit, except for goodwill, pro rata with the carrying amounts of those assets, subject to the limitation described in (c) below. Those increases in carrying amounts shall be treated as reversals of impairment losses and recognised immediately in profit or loss unless an asset is carried at revalued amount in accordance with another section of this FRS (for example, the revaluation model in Section 17). Any reversal of an impairment loss of a revalued asset shall be treated as a revaluation increase in accordance with the relevant section of this FRS.

(c) In allocating a reversal of an impairment loss for a cash-generating unit, the reversal shall not increase the carrying amount of any asset above the lower of:

(i) its recoverable amount; and

(ii) the carrying amount that would have been determined (net of amortisation or depreciation) had no impairment loss been recognised for the asset in prior periods.

(d) Any excess amount of the reversal of the impairment loss that cannot be allocated to an asset because of the restriction in (c) above shall be allocated pro rata to the other assets of the cash-generating unit, except for goodwill.

(e) After a reversal of an impairment loss is recognised, if applicable, the entity shall adjust the depreciation (amortisation) charge for each asset in the cash-generating unit in future periods to allocate the asset's revised carrying amount, less its residual value (if any), on a systematic basis over its remaining useful life.

Disclosures

27.32 An entity shall disclose the following for each **class of assets** indicated in paragraph 27.33:

* (a) the amount of impairment losses recognised in profit or loss during the period and the line item(s) in the **statement of comprehensive income** (or in the **income statement**, if presented) in which those impairment losses are included; and

* (b) the amount of reversals of impairment losses recognised in profit or loss during the period and the line item(s) in the statement of comprehensive income (or in the income statement, if presented) in which those impairment losses are reversed.

27.33 An entity shall disclose the information required by paragraph 27.32 for each of the following classes of asset:

(a) inventories;

(b) **property, plant and equipment** (including investment property accounted for by the cost method);

(c) goodwill;

(d) intangible assets other than goodwill;

(e) investments in **associates**; and

(f) investments in **joint ventures**.

27.33A An entity shall disclose a description of the events and circumstances that led to the recognition or reversal of the impairment loss.

Section 28
Employee Benefits

Scope of this section

28.1 This section applies to **employee benefits**, except for **share-based payment transactions**, (see Section 26 *Share-based Payment*). Employee benefits include:

(a) short-term employee benefits, which are employee benefits (other than **termination benefits**) that are expected to be settled wholly before 12 months after the end of the **reporting period** in which the employees render the related service;

(b) **post-employment benefits**, which are employee benefits (other than termination benefits and short-term employee benefits) that are payable after the completion of employment;

(c) other long-term employee benefits, which are all employee benefits, other than short-term employee benefits, post-employment benefits and termination benefits; or

(d) termination benefits, which are employee benefits provided in exchange for the termination of an employee's employment as a result of either:

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

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

28.2 [Deleted]

General recognition principle for all employee benefits

28.3 An entity shall recognise the cost of all employee benefits to which its employees have become entitled as a result of service rendered to the entity during the reporting period:

(a) As a **liability**, after deducting amounts that have been paid either directly to the employees or as a contribution to an employee benefit fund[55]. If the amount paid exceeds the obligation arising from service before the **reporting date**, an entity shall recognise that excess as an **asset** to the extent that the prepayment will lead to a reduction in future payments or a cash refund.

(b) As an **expense**, unless another section of this FRS requires the cost to be recognised as part of the cost of an asset such as **inventories** (for example in accordance with paragraph 13.8) or **property, plant and equipment** (in accordance with paragraph 17.10).

[55] Contributions to an employee benefit fund that is an intermediate payment arrangement shall be accounted for in accordance with paragraphs 9.33 to 9.38, and as a result if the employer is a sponsoring entity the assets and liabilities of the intermediary will be accounted for by the sponsoring entity as an extension of its own business. In which case the payment to the employee benefit fund does not extinguish the liability of the employer.

Examples

28.4 Short-term employee benefits include items such as the following, if expected to be settled wholly before 12 months after the end of the annual reporting period in which the employees render the related service:

(a) wages, salaries and social security contributions;

(b) paid annual leave and paid sick leave;

(c) profit-sharing and bonuses; and

(d) non-monetary benefits (such as medical care, housing, cars and free or subsidised goods or services) for current employees.

Measurement of short-term benefits generally

28.5 When an employee has rendered service to an entity during the reporting period, the entity shall measure the amounts recognised in accordance with paragraph 28.3 at the undiscounted amount of short-term employee benefits expected to be paid in exchange for that service.

Recognition and measurement: Short-term compensated absences

28.6 An entity may compensate employees for absence for various reasons including annual leave and sick leave. Some short-term compensated absences accumulate – they can be carried forward and used in future periods if the employee does not use the current period's entitlement in full. Examples include annual leave and sick leave. An entity shall recognise the expected cost of **accumulating compensated absences** when the employees render service that increases their entitlement to future compensated absences. The entity shall measure the expected cost of accumulating compensated absences at the undiscounted additional amount that the entity expects to pay as a result of the unused entitlement that has accumulated at the end of the reporting period. The entity shall present this amount as falling due within one year at the reporting date.

28.7 An entity shall recognise the cost of other (non-accumulating) compensated absences when the absences occur. The entity shall measure the cost of non-accumulating compensated absences at the undiscounted amount of salaries and wages paid or payable for the period of absence.

Recognition: Profit-sharing and bonus plans

28.8 An entity shall recognise the expected cost of profit-sharing and bonus payments only when:

(a) the entity has a present legal or **constructive obligation** to make such payments as a result of past events (this means that the entity has no realistic alternative but to make the payments); and

(b) a reliable estimate of the obligation can be made.

Post-employment benefits: Distinction between defined contribution plans and defined benefit plans

28.9 Post-employment benefits include, for example:

(a) retirement benefits, such as pensions; and

(b) other post-employment benefits, such as post-employment life insurance and post-employment medical care.

Arrangements whereby an entity provides post-employment benefits are **post-employment benefit plans**. An entity shall apply this section to all such arrangements whether or not they involve the establishment of a separate entity to receive contributions and to pay benefits. In some cases, these arrangements are imposed by law rather than by action of the entity. In some cases, these arrangements arise from actions of the entity even in the absence of a formal, documented plan.

28.10 Post-employment benefit plans are classified as either **defined contribution plans** or **defined benefit plans**, depending on their principal terms and conditions:

(a) Defined contribution plans are post-employment benefit plans under which an entity pays fixed contributions into a separate entity (a fund) and has no legal or constructive obligation to pay further contributions or to make direct benefit payments to employees if the fund does not hold sufficient assets to pay all employee benefits relating to employee service in the current and prior periods. Thus, the amount of the post-employment benefits received by the employee is determined by the amount of contributions paid by an entity (and perhaps also the employee) to a post-employment benefit plan or to an insurer, together with investment returns arising from the contributions.

(b) Defined benefit plans are post-employment benefit plans other than defined contribution plans. Under defined benefit plans, the entity's obligation is to provide the agreed benefits to current and former employees, and actuarial risk (that benefits will cost more or less than expected) and investment risk (that returns on assets set aside to fund the benefits will differ from expectations) are borne, in substance, by the entity. If actuarial or investment experience is worse than expected, the entity's obligation may be increased, and vice versa if actuarial or investment experience is better than expected.

Multi-employer plans and state plans

28.11 **Multi-employer plans** and **state plans** are classified as defined contribution plans or defined benefit plans on the basis of the terms of the plan, including any constructive obligation that goes beyond the formal terms. However, if sufficient information is not available to use defined benefit accounting for a multi-employer plan that is a defined benefit plan, an entity shall account for the plan in accordance with paragraphs 28.13 and 28.13A as if it was a defined contribution plan and make the disclosures required by paragraphs 28.40 and 28.40A. An entity shall account for a state plan in the same way as for a multi-employer plan.

28.11A Where an entity participates in a defined benefit plan, which is a multi-employer plan that in accordance with paragraph 28.11 is accounted for as if the plan were a defined contribution plan, and the entity has entered into an agreement with the multi-employer plan that determines how the entity will fund a deficit, the entity shall recognise a liability for the contributions payable that arise from the agreement (to the extent that they relate to the deficit) and the resulting expense in **profit or loss** in accordance with paragraphs 28.13 and 28.13A.

28.11B When an entity participates in a defined benefit plan, which is a multi-employer plan that in accordance with paragraph 28.11 is accounted for as if the plan were a defined contribution plan, and sufficient information to use defined benefit accounting becomes available, the entity shall:

(a) apply defined benefit accounting in accordance with paragraphs 28.14 to 28.28 from the relevant date as defined in paragraph 28.11C; and

(b) recognise the difference between:

(i) its **net defined benefit liability** (after taking into account the effect of paragraph 28.22, if any) at the relevant date as defined in paragraph 28.11C; and

(ii) the carrying value at the relevant date of its liability for the contributions payable arising from an agreement to fund a deficit, if any, plus any liability recognised in accordance with paragraph 28.13(a);

as a separate item in **other comprehensive income**.

28.11C For the purposes of applying paragraph 28.11B, the relevant date is the later of the first day for which sufficient information to use defined benefit accounting becomes available, and the first day of the current reporting period (comparative information is not restated).

28.11D For the avoidance of doubt, the difference calculated in accordance with paragraph 28.11B(b) excludes the impact of any plan changes, curtailments or settlements occurring at the relevant date, which are accounted for in accordance with paragraphs 28.21 and 28.21A.

Insured benefits

28.12 An entity may pay insurance premiums to fund a post-employment benefit plan. The entity shall treat such a plan as a defined contribution plan unless the entity has a legal or constructive obligation either:

(a) to pay the employee benefits directly when they become due; or

(b) to pay further amounts if the insurer does not pay all future employee benefits relating to employee service in the current and prior periods.

A constructive obligation could arise indirectly through the plan, through the mechanism for setting future premiums, or through a **related party** relationship with the insurer. If the entity retains such a legal or constructive obligation, the entity shall treat the plan as a defined benefit plan.

Post-employment benefits: Defined contribution plans

Recognition and measurement

28.13 An entity shall recognise the contribution payable for a period:

(a) As a liability, after deducting any amount already paid. If contribution payments exceed the contribution due for service before the reporting date, an entity shall recognise that excess as an asset to the extent that the prepayment will lead to a reduction in future payments or a cash refund.

(b) As an expense, unless another section of this FRS requires the cost to be recognised as part of the cost of an asset such as inventories or property, plant and equipment.

28.13A When contributions to a defined contribution plan (or a defined benefit plan which, in accordance with paragraph 28.11, is accounted for as a defined contribution plan) are not expected to be settled wholly within 12 months after the end of the reporting period in which the employees render the related service, the liability shall be measured at the **present value** of the contributions payable using the methodology for selecting a discount rate specified in paragraph 28.17. The unwinding of the discount shall be recognised as a finance cost in profit or loss in the period in which it arises.

Post-employment benefits: Defined benefit plans

Recognition

28.14 In applying the general **recognition** principle in paragraph 28.3 to defined benefit plans, an entity shall recognise:

(a) a liability for its obligations under defined benefit plans net of **plan assets** – its 'net defined benefit liability' (see paragraphs 28.15 to 28.22); and

(b) the net change in that liability during the period as the cost of its defined benefit plans during the period (see paragraphs 28.23 to 28.27).

Measurement of the net defined benefit liability

28.15 An entity shall measure the net defined benefit liability for its obligations under defined benefit plans at the net total of the following amounts:

(a) the present value of its obligations under defined benefit plans (its **defined benefit obligation**) at the reporting date (paragraphs 28.16 to 28.21A provide guidance for measuring this obligation); minus

(b) the **fair value** at the reporting date of plan assets (if any) out of which the obligations are to be settled. The Appendix to Section 2 *Concepts and Pervasive Principles* provides guidance on determining the fair values of those plan assets, except that, if the asset is an insurance policy that exactly matches the amount and timing of some or all of the benefits payable under the plan, the fair value of the asset is deemed to be the present value of the related obligation.

28.15A Where an entity has measured its defined benefit obligation using the **projected unit credit method** (including the use of appropriate **actuarial assumptions**), as set out in paragraph 28.18, it shall not recognise any additional liabilities to reflect differences between these assumptions and those used for the most recent actuarial valuation of the plan for funding purposes. For the avoidance of doubt, no additional liabilities shall be recognised in respect of an agreement with the defined benefit plan to fund a deficit (such as a schedule of contributions).

Inclusion of both vested and unvested benefits

28.16 The present value of an entity's obligations under defined benefit plans at the reporting date shall reflect the estimated amount of benefit that employees have earned in return for their service in the current and prior periods, including benefits that are not yet **vested** (see paragraph 28.26) and including the effects of benefit formulas that give employees greater benefits for later years of service. This requires the entity to determine how much benefit is attributable to the current and prior periods on the basis of the plan's benefit formula and to make estimates (actuarial assumptions) about demographic variables (such as employee turnover and mortality) and financial variables (such as future increases in salaries and medical costs) that influence the cost of the benefit. The actuarial assumptions shall be unbiased (neither imprudent nor excessively conservative), mutually compatible, and selected to lead to the best estimate of the future **cash flows** that will arise under the plan.

Discounting

28.17 An entity shall measure its defined benefit obligation on a discounted present value basis. The entity shall determine the rate used to discount the future payments by reference to market yields at the reporting date on high quality corporate bonds. In countries with no deep market in such bonds, the entity shall use the market yields (at the reporting date) on government bonds. The currency and term of the corporate bonds or government bonds shall be consistent with the currency and estimated period of the future payments.

Actuarial valuation method

28.18 An entity shall use the projected unit credit method to measure its defined benefit obligation and the related expense. If defined benefits are based on future salaries, the projected unit credit method requires an entity to measure its defined benefit obligations on a basis that reflects estimated future salary increases. Additionally, the projected unit credit method requires an entity to make various actuarial assumptions in measuring the defined benefit obligation, including discount rates, employee turnover, mortality, and (for defined benefit medical plans) medical cost trend rates.

28.19 [Deleted]

28.20 This FRS does not require an entity to engage an independent actuary to perform the comprehensive actuarial valuation needed to calculate its defined benefit obligation. Nor does it require that a comprehensive actuarial valuation must be done annually. In the periods between comprehensive actuarial valuations, if the principal actuarial assumptions have not changed significantly the defined benefit obligation can be measured by adjusting the prior period measurement for changes in employee demographics such as number of employees and salary levels.

Plan introductions, changes, curtailments and settlements

28.21 If a defined benefit plan has been introduced or the benefits have changed in the current period, the entity shall increase or decrease its net defined benefit liability to reflect the change, and shall recognise the increase (decrease) as an expense (**income**) in measuring profit or loss in the current reporting period.

28.21A If a defined benefit plan has been curtailed (ie benefits or group of covered employees are reduced) or settled (the relevant part of the employer's obligation is completely discharged) in the current period, the defined benefit obligation shall be decreased or eliminated, and the entity shall recognise the resulting **gain** or loss in profit or loss in the current reporting period.

Defined benefit plan asset

28.22 If the present value of the defined benefit obligation at the reporting date is less than the fair value of plan assets at that date, the plan has a surplus. An entity shall recognise a plan surplus as a defined benefit plan asset only to the extent that it is able to recover the surplus either through reduced contributions in the future or through refunds from the plan.

Cost of a defined benefit plan

28.23 An entity shall recognise the cost of a defined benefit plan, except to the extent that another section of this FRS requires part or all of the cost to be recognised as part of the cost of an asset, as follows:

(a) the change in the net defined benefit liability arising from employee service rendered during the reporting period in profit or loss;

(b) net interest on the net defined benefit liability during the reporting period in profit or loss;

(c) the cost of plan introductions, benefit changes, curtailments and settlements in profit or loss (see paragraphs 28.21 and 28.21A); and

(d) remeasurement of the net defined benefit liability in other comprehensive income.

Some defined benefit plans require employees or third parties to contribute to the cost of the plan. Contributions by employees reduce the cost of the benefits to the entity.

28.24 The net interest on the net defined benefit liability shall be determined by multiplying the net defined benefit liability by the discount rate in paragraph 28.17, both as determined at the start of the annual reporting period, taking account of any changes in the net defined benefit liability during the period as a result of contribution and benefit payments.

28.24A The net interest on the net defined benefit liability can be viewed as comprising interest cost on the defined benefit obligation and interest income on plan assets excluding the effect of any surplus that is not recoverable in accordance with paragraph 28.22.

28.24B Interest income on plan assets, excluding the effect of any surplus that is not recoverable in accordance with paragraph 28.22, is a component of the return on plan assets, and is determined by multiplying the fair value of the plan assets by the discount rate specified in paragraph 28.17 both as determined at the start of the annual reporting period, taking account of any changes in the plan assets held during the period as a result of contribution and benefit payments. The difference between the interest income on plan assets and the return on plan assets is included in the remeasurement of the net defined benefit liability.

28.25 Remeasurement of the net defined benefit liability comprises:

(a) **actuarial gains and losses**;

(b) the return on plan assets, excluding amounts included in net interest on the net defined benefit liability; and

(c) any change in the amount of a defined benefit plan surplus that is not recoverable (see paragraph 28.22), excluding amounts included in net interest on the net defined benefit liability.

28.25A Remeasurement of the net defined benefit liability recognised in other comprehensive income shall not be reclassified to profit or loss in a subsequent period.

28.26 Employee service gives rise to an obligation under a defined benefit plan even if the benefits are conditional on future employment (in other words, they are not yet vested). Employee service before the vesting date gives rise to a constructive obligation because, at each successive reporting date, the amount of future service that an employee will have to render before becoming entitled to the benefit is reduced. In measuring its defined benefit obligation, an entity considers the probability that some employees may not satisfy vesting requirements. Similarly, although some post-employment benefits (such as post-employment medical benefits) become payable only if a specified event occurs when an employee is no longer employed (such as an illness), an obligation is created when the employee renders service that will provide entitlement to the benefit if the specified event occurs. The probability that the specified event will occur affects the **measurement** of the obligation, but does not determine whether the obligation exists.

28.27 If defined benefits are reduced for amounts that will be paid to employees under government-sponsored plans, an entity shall measure its defined benefit obligations on a basis that reflects the benefits payable under the government plans, but only if:

(a) those plans were enacted before the reporting date; or

(b) past history, or other reliable evidence, indicates that those state benefits will change in some predictable manner, for example, in line with future changes in general price levels or general salary levels.

Reimbursements

28.28 If an entity is virtually certain that another party will reimburse some or all of the expenditure required to settle a defined benefit obligation, the entity shall recognise its right to reimbursement as a separate asset. An entity shall treat that asset in the same way as plan assets. The cost of a defined benefit plan recognised in accordance with paragraph 28.23 may be presented net of the amounts relating to changes in the **carrying amount** of the right to reimbursement.

Other long-term employee benefits

28.29 Other long-term employee benefits include items such as the following, if not expected to be settled wholly before 12 months after the end of the annual reporting period in which the employees render the related service:

(a) long-term paid absences such as long-service or sabbatical leave;

(b) other long-service benefits;

(c) long-term disability benefits;

(d) profit-sharing and bonuses; and

(e) deferred remuneration.

28.30 An entity shall recognise a liability for other long-term employee benefits measured at the net total of the following amounts:

(a) the present value of the benefit obligation at the reporting date (calculated using the methodology for selecting a discount rate in paragraph 28.17); minus

(b) the fair value at the reporting date of plan assets (if any) out of which the obligations are to be settled directly.

An entity shall recognise the net change in the liability during the period in profit or loss, except to the extent that this FRS requires or permits their inclusion in the cost of an asset, such as inventory or property, plant and equipment.

Termination benefits

28.31 An entity may be committed, by legislation, by contractual or other agreements with employees or their representatives or by a constructive obligation based on business practice, custom or a desire to act equitably, to make payments (or provide other benefits) to employees when it terminates their employment. Such payments are termination benefits.

Recognition

28.32 Because termination benefits do not provide an entity with future economic benefits, an entity shall recognise them as an expense in profit or loss immediately.

28.33 When an entity recognises termination benefits, the entity may also have to account for a curtailment of retirement benefits or other employee benefits.

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

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

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

28.35 An entity is demonstrably committed to a termination only when the entity has a detailed formal plan for the termination[56] and is without realistic possibility of withdrawal from the plan.

Measurement

28.36 An entity shall measure termination benefits at the best estimate of the expenditure that would be required to settle the obligation at the reporting date. In the case of an offer made to encourage voluntary redundancy, the measurement of termination benefits shall be based on the number of employees expected to accept the offer.

28.37 When termination benefits are due more than 12 months after the end of the reporting period, they shall be measured at their discounted present value using the methodology for selecting a discount rate specified in paragraph 28.17.

Group plans

28.38 When an entity participates in a defined benefit plan that shares risks between entities under common control it shall obtain information about the plan as a whole measured in accordance with this FRS on the basis of assumptions that apply to the plan as a whole. If there is a contractual agreement or stated policy for charging the net defined benefit cost of a defined benefit plan as a whole measured in accordance with this FRS to individual **group** entities, the entity shall, in its **individual financial statements**, recognise the net defined benefit cost of a defined benefit plan so charged. If there is no such agreement or policy, the net defined benefit cost of a defined benefit plan shall be recognised in the individual financial statements of the group entity which is the sponsoring employer for the plan. The other group entities shall, in their individual financial statements, recognise a cost equal to their contribution payable for the period. As the net defined benefit cost is calculated by reference to both the defined obligation and the fair value of plan assets, recognising a net defined benefit cost requires the recognition of a corresponding net defined benefit asset or liability in the individual financial statements of any group entity recognising a net defined benefit cost.

[56] An example of the features of a detailed formal plan for restructuring, which may include termination benefits, is given in paragraph 21.11C.

Disclosures

Disclosures about short-term employee benefits

28.39 This section does not require specific disclosures about short-term employee benefits.

Disclosures about defined contribution plans

28.40 An entity shall disclose the amount recognised in profit or loss as an expense for defined contribution plans.

28.40A If an entity treats a defined benefit multi-employer plan as a defined contribution plan because sufficient information is not available to use defined benefit accounting (see paragraph 28.11) it shall:

* (a) disclose the fact that it is a defined benefit plan and the reason why it is being accounted for as a defined contribution plan, along with any available information about the plan's surplus or deficit and the implications, if any, for the entity;

* (b) include a description of the extent to which the entity can be liable to the plan for other entities' obligations under the terms and conditions of the multi-employer plan; and

(c) disclose how any liability recognised in accordance with paragraph 28.11A has been determined.

Disclosures about defined benefit plans

28.41 An entity shall disclose the following information about defined benefit plans (except for any multi-employer defined benefit plans that are accounted for as a defined contribution plan in accordance with paragraphs 28.11 and 28.11A, for which the disclosures in paragraphs 28.40 and 28.40A apply instead). If an entity has more than one defined benefit plan, these disclosures may be made in aggregate, separately for each plan, or in such groupings as are considered to be the most useful:

(a) A general description of the type of plan, including **funding** policy. This includes the amount and timing of the future payments to be made by the entity under any agreement with the defined benefit plan to fund a deficit (such as a schedule of contributions).

(b) [Deleted]

(c) [Deleted]

(d) The date of the most recent comprehensive actuarial valuation and, if it was not as of the reporting date, a description of the adjustments that were made to measure the defined benefit obligation at the reporting date.

(e) A reconciliation of opening and closing balances for each of the following:

(i) the defined benefit obligation;

(ii) the fair value of plan assets; and

(iii) any reimbursement right recognised as an asset.

(f) Each of the reconciliations in paragraph 28.41(e) shall show each of the following, if applicable:

(i) the change in the defined benefit liability arising from employee service rendered during the reporting period in profit or loss;

(ii) interest income or expense;

(iii) remeasurement of the defined benefit liability, showing separately actuarial gains and losses and the return on plan assets less amounts included in (ii) above; and

(iv) plan introductions, changes, curtailments and settlements.

(g) The total cost relating to defined benefit plans for the period, disclosing separately the amounts:

(i) recognised in profit or loss as an expense; and

(ii) included in the cost of an asset.

(h) For each major class of plan assets, which shall include, but is not limited to, equity instruments, debt instruments, property, and all other assets, the percentage or amount that each major class constitutes of the fair value of the total plan assets at the reporting date.

(i) The amounts included in the fair value of plan assets for:

(i) each class of the entity's own **financial instruments**; and

(ii) any property occupied by, or other assets used by, the entity.

(j) The return on plan assets.

(k) The principal actuarial assumptions used, including, when applicable:

(i) the discount rates;

(ii) [Deleted]

(iii) the expected rates of salary increases;

(iv) medical cost trend rates; and

(v) any other **material** actuarial assumptions used.

The reconciliations in (e) and (f) above need not be presented for prior periods.

28.41A If an entity participates in a defined benefit plan that shares risks between entities under common control (see paragraph 28.38) it shall disclose the following information:

(a) The contractual agreement or stated policy for charging the cost of a defined benefit plan or the fact that there is no policy.

(b) The policy for determining the contribution to be paid by the entity.

(c) If the entity accounts for an allocation of the net defined benefit cost, all the information required in paragraph 28.41.

* (d) If the entity accounts for the contributions payable for the period, the information about the plan as a whole required by paragraph 28.41(a), (d), (h) and (i).

This information can be disclosed by cross-reference to disclosures in another group entity's **financial statements** if:

(i) that group entity's financial statements separately identify and disclose the information required about the plan; and

(ii) that group entity's financial statements are available to users of the financial statements on the same terms as the financial statements of the entity and at the same time as, or earlier than, the financial statements of the entity.

Disclosures about other long-term benefits

28.42 For each category of other long-term benefits that an entity provides to its employees, the entity shall disclose the nature of the benefit, the amount of its obligation and the extent of funding at the reporting date.

Disclosures about termination benefits

28.43 For each category of termination benefits that an entity provides to its employees, the entity shall disclose the nature of the benefit, its **accounting policy**, and the amount of its obligation and the extent of funding at the reporting date.

28.44 When there is uncertainty about the number of employees who will accept an offer of termination benefits, a **contingent liability** exists. Section 21 *Provisions and Contingencies* requires an entity to disclose information about its contingent liabilities unless the possibility of an outflow in settlement is remote.

Section 29
Income Tax

Scope of this section

29.1 [Deleted]

29.2 This section applies to:

(a) **income tax** comprising:

(i) **current tax**; and

(ii) **deferred tax** including deferred tax in respect of **assets** (other than **goodwill**) and **liabilities** recognised as a result of a **business combination**; and

(b) value added tax (VAT) and other similar sales taxes, which are not income taxes.

29.2A [Moved to paragraph 29.2(b)]

Recognition and measurement of current tax

29.3 An entity shall recognise a current tax liability for tax payable on **taxable profit** for the current and past periods. If the amount of tax paid for the current and past periods exceeds the amount of tax payable for those periods, the entity shall recognise the excess as a current tax asset.

29.4 An entity shall recognise a current tax asset for the benefit of a tax loss that can be carried back to recover tax paid in a previous period.

29.5 An entity shall measure a current tax liability (asset) at the amount of tax it expects to pay (recover) using the tax rates and laws that have been enacted or **substantively enacted** by the **reporting date**.

Recognition of deferred tax

Timing differences

29.6 Deferred tax shall be recognised in respect of all **timing differences** at the reporting date, except as otherwise required by paragraphs 29.7 to 29.9 and 29.11A below. Timing differences are differences between taxable profits and **total comprehensive income** as stated in the **financial statements** that arise from the inclusion of **income** and **expenses** in tax assessments in periods different from those in which they are recognised in financial statements.

29.7 Unrelieved tax losses and other **deferred tax assets** shall be recognised only to the extent that it is **probable** that they will be recovered against the reversal of **deferred tax liabilities** or other future taxable profits (the very existence of unrelieved tax losses is strong evidence that there may not be other future taxable profits against which the losses will be relieved).

29.8 Deferred tax shall be recognised when the tax allowances for the cost of a **fixed asset** are received before or after the **depreciation** of the fixed asset is recognised in **profit or loss**. If and when all conditions for retaining the tax allowances have been met, the deferred tax shall be reversed.

29.9 Deferred tax shall be recognised when income or expenses from a **subsidiary**, **associate**, branch, or interest in **joint venture** have been recognised in the financial statements, and will be assessed to or allowed for tax in a future period, except where:

(a) the reporting entity is able to control the reversal of the timing difference; and

(b) it is probable that the timing difference will not reverse in the foreseeable future.

Such timing differences may arise, for example, where there are undistributed profits in a subsidiary, associate, branch or interest in a joint venture.

Permanent differences

29.10 **Permanent differences** arise because certain types of income and expenses are non-taxable or disallowable, or because certain tax charges or allowances are greater or smaller than the corresponding income or expense in the financial statements. Deferred tax shall not be recognised on permanent differences except for circumstances set out in paragraph 29.11.

Business combinations

29.11 When the amount that can be deducted for tax for an asset (other than goodwill) that is recognised in a business combination accounted for by applying the purchase method is less (more) than the value at which it is recognised, a deferred tax liability (asset) shall be recognised for the additional tax that will be paid (avoided) in respect of that difference. Similarly, a deferred tax asset (liability) shall be recognised for the additional tax that will be avoided (paid) because of a difference between the value at which a liability is recognised in a business combination accounted for by applying the purchase method and the amount that will be assessed for tax. The amount attributed to goodwill (or negative goodwill) shall be adjusted by the amount of deferred tax recognised.

29.11A In applying paragraph 29.11 and determining the amount that can be deducted for tax an entity shall consider the manner in which the entity expects, at the end of the **reporting period**, to recover or settle the **carrying amount** of the asset or liability.

Measurement of deferred tax

29.12 An entity shall measure a deferred tax liability (asset) using the tax rates and laws that have been enacted or substantively enacted by the reporting date that are expected to apply to the reversal of the timing difference.

29.13 When different tax rates apply to different levels of taxable profit, an entity shall measure deferred tax expense (income) and related deferred tax liabilities (assets) using the average enacted or substantively enacted rates that it expects to be applicable to the taxable profit (tax loss) of the periods in which it expects the deferred tax asset to be realised or the deferred tax liability to be settled.

29.14 In some jurisdictions, income taxes are payable at a higher or lower rate if part or all of the profit or retained earnings is paid out as a dividend to shareholders of the entity. In other jurisdictions, income taxes may be refundable or payable if part or all of the profit or retained earnings is paid out as a dividend to shareholders of the entity. In both of those circumstances, an entity shall measure current and deferred taxes at the tax rate applicable to undistributed profits until the entity recognises a liability to pay a dividend. When the entity recognises a liability to pay a dividend, it shall recognise the resulting current or deferred tax liability (asset), and the related **tax expense** (income).

29.14A As an exception, when:

(a) an entity is wholly-owned by one or more charitable[57] entities;

(b) it is probable that a gift aid payment will be made to a member of the same charitable **group**, or a charitable **venturer**, within nine months of the reporting date; and

(c) that payment will qualify to be set against profits for tax purposes,

the income tax effects of that gift aid payment shall be recognised at the reporting date. The income tax effects shall be measured consistently with the tax treatment planned to be used in the entity's income tax filings. A deferred tax liability shall not be recognised in relation to such a gift aid payment.

29.15 Deferred tax relating to a non-depreciable asset that is measured using the revaluation model in Section 17 *Property, Plant and Equipment* shall be measured using the tax rates and allowances that apply to the sale of the asset.

29.16 Deferred tax relating to **investment property** that is measured at **fair value** in accordance with Section 16 *Investment Property* shall be measured using the tax rates and allowances that apply to the sale of the asset, except for investment property that has a limited **useful life** and is held within a business model whose objective is to consume substantially all of the economic benefits embodied in the property over time.

Measurement of both current and deferred tax

29.17 An entity shall not discount current or deferred tax assets and liabilities.

Withholding tax on dividends

29.18 When an entity pays dividends to its shareholders, it may be required to pay a portion of the dividends to taxation authorities on behalf of shareholders. Outgoing dividends and similar amounts payable shall be recognised at an amount that includes any withholding tax but excludes other taxes, such as attributable tax credits.

29.19 Incoming dividends and similar income receivable shall be recognised at an amount that includes any withholding tax but excludes other taxes, such as attributable tax credits. Any withholding tax suffered shall be shown as part of the tax charge.

Value added tax (VAT) and other similar sales taxes

29.20 **Turnover** shown in profit or loss shall exclude VAT and other similar sales taxes on taxable outputs and VAT imputed under the flat rate VAT scheme. Expenses shall exclude recoverable VAT and other similar recoverable sales taxes. Irrecoverable VAT allocable to **fixed assets** and to other items disclosed separately in the financial statements shall be included in their cost where practicable and **material**.

[57] In this context, 'charitable' refers to an entity that has been recognised by HMRC as being eligible for certain tax reliefs because of its charitable purposes.

Presentation

Allocation in comprehensive income and equity

29.21 An entity shall present changes in a current tax liability (asset) and changes in a deferred tax liability (asset) as tax expense (income) with the exception of those changes arising on the initial **recognition** of a business combination which shall be dealt with in accordance with paragraphs 29.11 to 29.11A.

29.22 An entity shall present tax expense (income) in the same component of total comprehensive income (ie continuing or **discontinued operations**, and profit or loss or **other comprehensive income**) or **equity** as the transaction or other event that resulted in the tax expense (income).

29.22A As an exception to paragraph 29.22, an entity shall present the tax expense (income) effects of distributions to **owners** in profit or loss.

Presentation in the statement of financial position

29.23 An entity shall present deferred tax liabilities within provisions for liabilities and deferred tax assets within debtors, unless it has chosen to adapt its **statement of financial position** in accordance with paragraph 4.2A.

Offsetting

29.24 An entity shall offset current tax assets and current tax liabilities, if and only if, it has a legally enforceable right to set off the amounts and it intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

29.24A An entity shall offset deferred tax assets and deferred tax liabilities if, and only if:

(a) the entity has a legally enforceable right to set off current tax assets against current tax liabilities; and

(b) the deferred tax assets and deferred tax liabilities relate to income taxes levied by the same taxation authority on either the same taxable entity or different taxable entities which intend either to settle current tax liabilities and assets on a net basis, or to realise the assets and settle the liabilities simultaneously, in each future period in which significant amounts of deferred tax liabilities or assets are expected to be settled or recovered.

Disclosures

29.25 An entity shall disclose information that enables users of its financial statements to evaluate the nature and financial effect of the current and deferred tax consequences of recognised transactions and other events.

29.26 An entity shall disclose separately the major components of tax expense (income). Such components of tax expense (income) may include:

(a) current tax expense (income);

(b) any adjustments recognised in the period for current tax of prior periods;

(c) the amount of deferred tax expense (income) relating to the origination and reversal of timing differences;

(d) the amount of deferred tax expense (income) relating to changes in tax rates or the imposition of new taxes;

(e) adjustments to deferred tax expense (income) arising from a change in the tax status of the entity or its shareholders; and

(f) the amount of tax expense (income) relating to changes in **accounting policies** and material **errors** (see Section 10 *Accounting Policies, Estimates and Errors*).

29.27 An entity shall disclose the following separately:

* (a) the aggregate current and deferred tax relating to items that are recognised as items of other comprehensive income or equity;

(b) a reconciliation between:

(i) the tax expense (income) included in profit or loss; and

(ii) the profit or loss on ordinary activities before tax multiplied by the applicable tax rate;

(c) the amount of the net reversal of deferred tax assets and deferred tax liabilities expected to occur during the year beginning after the reporting period together with a brief explanation for the expected reversal;

(d) an explanation of changes in the applicable tax rate(s) compared with the previous reporting period;

(e) the amount of deferred tax liabilities and deferred tax assets at the end of the reporting period for each type of timing difference and the amount of unused tax losses and tax credits;

(f) the expiry date, if any, of timing differences, unused tax losses and unused tax credits; and

(g) in the circumstances described in paragraph 29.14, an explanation of the nature of the potential income tax consequences that would result from the payment of dividends to its shareholders.

Section 30
Foreign Currency Translation

Scope of this section

30.1 This section applies to:

(a) foreign currency transactions;

(b) **foreign operations**; and

(c) the translation of **financial statements** into a **presentation currency**.

30.1A This section does not apply to hedge accounting of foreign currency items (see Section 12 *Other Financial Instruments Issues*).

Functional currency

30.2 Each entity shall identify its **functional currency**. An entity's functional currency is the currency of the primary economic environment in which the entity operates.

30.3 The primary economic environment in which an entity operates is normally the one in which it primarily generates and expends **cash**. Therefore, the following are the most important factors an entity considers in determining its functional currency:

(a) the currency:

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

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

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

30.4 The following factors may also provide evidence of an entity's functional currency:

(a) the currency in which funds from **financing activities** (issuing debt and equity instruments) are generated; and

(b) the currency in which receipts from **operating activities** are usually retained.

30.5 The following additional factors are considered in determining the functional currency of a foreign operation, and whether its functional currency is the same as that of the reporting entity (the reporting entity, in this context, being the entity that has the foreign operation as its **subsidiary**, branch, **associate** or **joint venture**):

(a) Whether the activities of the foreign operation are carried out as an extension of the reporting entity, rather than being carried out with a significant degree of autonomy. An example of the former is when the foreign operation only sells goods imported from the reporting entity and remits the proceeds to it. An example of the latter is when the operation accumulates cash and other **monetary items**, incurs **expenses**, generates **income** and arranges borrowings, all substantially in its local currency.

(b) Whether transactions with the reporting entity are a high or a low proportion of the foreign operation's activities.

(c) Whether **cash flows** from the activities of the foreign operation directly affect the cash flows of the reporting entity and are readily available for remittance to it.

(d) Whether cash flows from the activities of the foreign operation are sufficient to service existing and normally expected debt obligations without funds being made available by the reporting entity.

Reporting foreign currency transactions in the functional currency

Initial recognition

30.6 A foreign currency transaction is a transaction that is denominated or requires settlement in a foreign currency, including transactions arising when an entity:

(a) buys or sells goods or services whose price is denominated in a foreign currency;

(b) borrows or lends funds when the amounts payable or receivable are denominated in a foreign currency; or

(c) otherwise acquires or disposes of **assets**, or incurs or settles **liabilities**, denominated in a foreign currency.

30.7 An entity shall record a foreign currency transaction, on initial **recognition** in the functional currency, by applying to the foreign currency amount the spot exchange rate between the functional currency and the foreign currency at the date of the transaction.

30.8 The date of a transaction is the date on which the transaction first qualifies for recognition in accordance with this FRS. For practical reasons, a rate that approximates the actual rate at the date of the transaction is often used, for example, an average rate for a week or a month might be used for all transactions in each foreign currency occurring during that period. However, if exchange rates fluctuate significantly, the use of the average rate for a period is inappropriate.

Reporting at the end of the subsequent reporting periods

30.9 At the end of each **reporting period**, an entity shall:

(a) translate foreign currency monetary items using the **closing rate**;

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

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

30.10 An entity shall recognise, in **profit or loss** in the period in which they arise, exchange differences arising on the settlement of monetary items or on translating monetary items at rates different from those at which they were translated on initial recognition during the period or in previous periods, except as described in paragraph 30.13.

30.11 When another section of this FRS requires a **gain** or loss on a non-monetary item to be recognised in **other comprehensive income**, an entity shall recognise any exchange component of that gain or loss in other comprehensive income. Conversely, when a gain or loss on a non-monetary item is recognised in profit or loss, an entity shall recognise any exchange component of that gain or loss in profit or loss.

Net investment in a foreign operation

30.12 An entity may have a monetary item that is receivable from or payable to a foreign operation. An item for which settlement is neither planned nor likely to occur in the foreseeable future is, in substance, a part of the entity's net investment in that foreign operation, and is accounted for in accordance with paragraph 30.13. Such monetary items may include long-term receivables or loans. They do not include trade receivables or trade payables.

30.13 Exchange differences arising on a monetary item that forms part of a reporting entity's **net investment in a foreign operation** shall be recognised in profit or loss in the **separate financial statements** of the reporting entity or the **individual financial statements** of the foreign operation, as appropriate, except that any unrealised gain shall be recognised in other comprehensive income. In the financial statements that include the foreign operation and the reporting entity (eg **consolidated financial statements** when the foreign operation is a subsidiary), such exchange differences shall be recognised in other comprehensive income and accumulated in **equity**. They shall not be recognised in profit or loss on disposal of the net investment.

Change in functional currency

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

30.15 As noted in paragraphs 30.2 to 30.5, the functional currency of an entity reflects the underlying transactions, events and conditions that are relevant to the entity. Accordingly, once the functional currency is determined, it can be changed only if there is a change to those underlying transactions, events and conditions. For example, a change in the currency that mainly influences the sales prices of goods and services may lead to a change in an entity's functional currency.

30.16 The effect of a change in functional currency is accounted for prospectively. In other words, an entity translates all items into the new functional currency using the exchange rate at the date of the change. The resulting translated amounts for non-monetary items are treated as their historical cost.

Use of a presentation currency other than the functional currency

Translation to the presentation currency

30.17 An entity may present its financial statements in any currency (or currencies). If the presentation currency differs from the entity's functional currency, the entity shall translate its items of income and expense and **financial position** into the presentation currency. For example, when a **group** contains individual entities with different functional currencies, the items of income and expense and financial position of each entity are expressed in a common currency so that consolidated financial statements may be presented.

30.18 An entity whose functional currency is not the currency of a hyperinflationary economy shall translate its results and financial position into a different presentation currency using the following procedures:

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

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

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

30.19 For practical reasons, an entity may use a rate that approximates the exchange rates at the dates of the transactions, for example an average rate for the period to translate income and expense items. However, if exchange rates fluctuate significantly, the use of the average rate for a period is inappropriate.

30.20 The exchange differences referred to in paragraph 30.18(c) result from:

(a) translating income and expenses at the exchange rates at the dates of the transactions and assets and liabilities at the closing rate; and

(b) translating the opening net assets at a closing rate that differs from the previous closing rate.

When the exchange differences relate to a foreign operation that is consolidated but not wholly-owned, accumulated exchange differences arising from translation and attributable to the **non-controlling interest** are allocated to, and recognised as part of, non-controlling interest in the consolidated statement of financial position.

30.21 An entity whose functional currency is the currency of a hyperinflationary economy shall adjust its results and financial position using the procedures specified in Section 31 *Hyperinflation* before translating them into a different presentation currency using the following procedures:

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

(b) when amounts are translated into the currency of a non-hyperinflationary economy, comparative amounts shall be those that are presented as current period amounts in the relevant prior period financial statements.

Translation of a foreign operation into the investor's presentation currency

30.22 In incorporating the assets, liabilities, income and expenses of a foreign operation with those of the reporting entity, the entity shall follow normal consolidation procedures, such as the elimination of intragroup balances and intragroup transactions of a subsidiary (see Section 9 *Consolidated and Separate Financial Statements*) and the translation procedures set out in paragraphs 30.17 to 30.21. An intragroup monetary asset (or liability), whether short-term or long-term, cannot be eliminated against the corresponding intragroup liability (or asset) without showing the results of currency fluctuations in the consolidated financial statements. This is because the monetary item represents a commitment to convert one currency into another and exposes the reporting entity to a gain or loss through currency fluctuations. Accordingly, in the consolidated financial statements, a reporting entity continues to recognise such an exchange difference in profit or loss or, if it arises from the circumstances described in paragraph 30.13, the entity shall recognise it in other comprehensive income.

30.23 Any **goodwill** arising on the acquisition of a foreign operation and any fair value adjustments to the **carrying amounts** of assets and liabilities arising on the acquisition of that foreign operation shall be treated as assets and liabilities of the foreign operation. Thus, they shall be expressed in the functional currency of the foreign operation and shall be translated at the closing rate in accordance with paragraph 30.18.

Disclosures

30.24 In paragraphs 30.26 and 30.27, references to functional currency apply, in the case of a group, to the functional currency of the **parent**.

30.25 An entity shall disclose the following:

(a) the amount of exchange differences recognised in profit or loss during the period, except for those arising on **financial instruments** measured at fair value through profit or loss in accordance with Sections 11 *Basic Financial Instruments* and Section 12; and

(b) the amount of exchange differences recognised in other comprehensive income arising during the period.

30.26 An entity shall disclose the currency in which the financial statements are presented. When the presentation currency is different from the functional currency, an entity shall state that fact and shall disclose the functional currency and the reason for using a different presentation currency.

30.27 When there is a change in the functional currency of either the reporting entity or a significant foreign operation, the entity shall disclose that fact and the reason for the change in functional currency.

Section 31
Hyperinflation

Scope of this section

31.1 This section applies to an entity whose **functional currency** is the currency of a hyperinflationary economy. It requires such an entity to prepare **financial statements** that have been adjusted for the effects of hyperinflation.

Hyperinflationary economy

31.2 This section does not establish an absolute rate at which an economy is deemed hyperinflationary. An entity shall make that judgement by considering all available information including, but not limited to, the following possible indicators of hyperinflation:

(a) The general population prefers to keep its wealth in non-monetary assets or in a relatively stable foreign currency. Amounts of local currency held are immediately invested to maintain purchasing power.

(b) The general population regards monetary amounts not in terms of the local currency but in terms of a relatively stable foreign currency. Prices may be quoted in that currency.

(c) Sales and purchases on credit take place at prices that compensate for the expected loss of purchasing power during the credit period, even if the period is short.

(d) Interest rates, wages and prices are linked to a price index.

(e) The cumulative inflation rate over three years is approaching, or exceeds, 100 per cent.

Measuring unit in the financial statements

31.3 All amounts in the financial statements of an entity whose functional currency is the currency of a hyperinflationary economy shall be stated in terms of the measuring unit current at the end of the **reporting period**. The comparative information for the previous period required by paragraph 3.14, and any information presented in respect of earlier periods, shall also be stated in terms of the measuring unit current at the **reporting date**.

31.4 The restatement of financial statements in accordance with this section requires the use of a general price index that reflects changes in general purchasing power. In most economies there is a recognised general price index, normally produced by the government, that entities will follow.

Procedures for restating historical cost financial statements

Statement of financial position

31.5 **Statement of financial position** amounts not expressed in terms of the measuring unit current at the end of the reporting period are restated by applying a general price index.

31.6 **Monetary items** are not restated because they are expressed in terms of the measuring unit current at the end of the reporting period. Monetary items are money held and items to be received or paid in money.

31.7 **Assets** and **liabilities** linked by agreement to changes in prices, such as index-linked bonds and loans, are adjusted in accordance with the agreement and presented at this adjusted amount in the restated statement of financial position.

31.8 All other assets and liabilities are non-monetary:

(a) Some non-monetary items are carried at amounts current at the end of the reporting period, such as net realisable value and **fair value**, so they are not restated. All other non-monetary assets and liabilities are restated.

(b) Most non-monetary items are carried at cost or cost less **depreciation**; hence they are expressed at amounts current at their date of acquisition. The restated cost, or cost less depreciation, of each item is determined by applying to its historical cost and accumulated depreciation the change in a general price index from the date of acquisition to the end of the reporting period.

(bA) Some non-monetary items are carried at amounts that were current at dates other than that of acquisition or the reporting date, for example**, property, plant and equipment** that has been revalued at some earlier date. In these cases, the **carrying amounts** are restated by applying to the revalued amount the change in a general price index from the date of the revaluation.

(c) The restated amount of a non-monetary item is reduced, in accordance with Section 27 *Impairment of Assets*, when it exceeds its **recoverable amount**.

31.9 At the beginning of the first period of application of this section, the components of **equity**, except retained earnings and any revaluation surplus, are restated by applying a general price index from the dates the components were contributed or otherwise arose. Any revaluation surplus that arose in previous periods is not restated. Restated retained earnings are derived from all the other amounts in the restated statement of financial position.

31.10 At the end of the first period and in subsequent periods, all components of **owners**' equity are restated by applying a general price index from the beginning of the period or the date of contribution, if later. The changes for the period in owners' equity are disclosed in accordance with Section 6 *Statement of Changes in Equity and Statement of Income and Retained Earnings*.

Statement of comprehensive income and income statement

31.11 All items in the **statement of comprehensive income** (and in the **income statement**, if presented) shall be expressed in terms of the measuring unit current at the end of the reporting period. Therefore, all amounts need to be restated by applying the change in the general price index from the dates when the items of **income** and **expenses** were initially recognised in the financial statements. If general inflation is approximately even throughout the period, and the items of income and expense arose approximately evenly throughout the period, an average rate of inflation may be appropriate.

Statement of cash flows

31.12 An entity shall express all items in the **statement of cash flows** in terms of the measuring unit current at the end of the reporting period.

Gain or loss on net monetary position

31.13 In a period of inflation, an entity holding an excess of monetary assets over monetary liabilities loses purchasing power, and an entity with an excess of monetary liabilities over monetary assets gains purchasing power, to the extent the assets and liabilities are not linked to a price level. An entity shall include in **profit or loss** the **gain** or loss on the net monetary position, except that any unrealised gain shall be recognised in **other comprehensive income**. An entity shall offset the adjustment to those assets and liabilities linked by agreement to changes in prices made in accordance with paragraph 31.7 against the gain or loss on net monetary position.

Economies ceasing to be hyperinflationary

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

Disclosures

31.15 An entity to which this section applies shall disclose the following:

(a) the fact that financial statements and other prior period data have been restated for changes in the general purchasing power of the functional currency;

(b) the identity and level of the price index at the reporting date and changes during the current reporting period and the previous reporting period; and

(c) amount of gain or loss on monetary items.

Section 32
Events after the End of the Reporting Period

Scope of this section

32.1 This section applies to the **recognition**, **measurement** and disclosure of events after the end of the **reporting period**.

Events after the end of the reporting period defined

32.2 Events after the end of the reporting period are those events, favourable and unfavourable, that occur between the end of the reporting period and the date when the **financial statements** are authorised for issue. There are two types of events:

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

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

32.3 Events after the end of the reporting period include all events up to the date when the financial statements are authorised for issue, even if those events occur after the public announcement of **profit or loss** or other selected financial information.

Recognition and measurement

Adjusting events after the end of the reporting period

32.4 An entity shall adjust the amounts recognised in its financial statements, including related disclosures, to reflect adjusting events after the end of the reporting period.

32.5 The following are examples of adjusting events after the end of the reporting period that require an entity to adjust the amounts recognised in its financial statements, or to recognise items that were not previously recognised:

(a) The settlement after the end of the reporting period of a court case that confirms that the entity had a present obligation at the end of the reporting period. The entity adjusts any previously recognised **provision** related to this court case in accordance with Section 21 *Provisions and Contingencies* or recognises a new provision. The entity does not merely disclose a **contingent liability**. Rather, the settlement provides additional evidence to be considered in determining the provision that should be recognised at the end of the reporting period in accordance with Section 21.

(b) The receipt of information after the end of the reporting period indicating that an **asset** was impaired at the end of the reporting period, or that the amount of a previously recognised **impairment loss** for that asset needs to be adjusted. For example:

(i) the bankruptcy of a customer that occurs after the end of the reporting period usually confirms that a loss existed at the end of the reporting period on a trade receivable and that the entity needs to adjust the **carrying amount** of the trade receivable; and

(ii) the sale of **inventories** after the end of the reporting period may give evidence about their selling price at the end of the reporting period for the purpose of assessing impairment at that date.

(c) The determination after the end of the reporting period of the cost of assets purchased, or the proceeds from assets sold, before the end of the reporting period.

(d) The determination after the end of the reporting period of the amount of profit-sharing or bonus payments, if the entity had a legal or **constructive obligation** at the end of the reporting period to make such payments as a result of events before that date (see Section 28 *Employee Benefits*).

(e) The discovery of fraud or **errors** that show that the financial statements are incorrect.

Non-adjusting events after the end of the reporting period

32.6 An entity shall not adjust the amounts recognised in its financial statements to reflect non-adjusting events after the end of the reporting period.

32.7 Examples of non-adjusting events after the end of the reporting period include:

(a) A decline in market value of investments between the end of the reporting period and the date when the financial statements are authorised for issue. The decline in market value does not normally relate to the condition of the investments at the end of the reporting period, but reflects circumstances that have arisen subsequently. Therefore, an entity does not adjust the amounts recognised in its financial statements for the investments. Similarly, the entity does not update the amounts disclosed for the investments as at the end of the reporting period, although it may need to give additional disclosure in accordance with paragraph 32.10.

(b) An amount that becomes receivable as a result of a favourable judgement or settlement of a court case after the **reporting date** but before the financial statements are authorised for issued. This would be a **contingent asset** at the reporting date (see paragraph 21.13), and disclosure may be required by paragraph 21.16. However, agreement on the amount of damages for a judgement that was reached before the reporting date, but was not previously recognised because the amount could not be measured reliably, may constitute an adjusting event.

Further examples of non-adjusting events are set out in paragraph 32.11.

Going concern

32.7A An entity shall not prepare its financial statements on a **going concern** basis if management determines after the reporting period either that it intends to liquidate the entity or to cease trading, or that it has no realistic alternative but to do so.

32.7B Deterioration in operating results and **financial position** after the reporting period may indicate a need to consider whether the going concern assumption is still appropriate. If the going concern assumption is no longer appropriate, the effect is so pervasive that this section requires a fundamental change in the basis of accounting, rather than an adjustment to the amounts recognised within the original basis of accounting and therefore the disclosure requirements of paragraph 3.9 apply.

Dividends

32.8 If an entity declares dividends to holders of its equity instruments after the end of the reporting period, the entity shall not recognise those dividends as a **liability** at the end of the reporting period because no obligation exists at that time. The amount of the dividend may be presented as a segregated component of retained earnings at the end of the reporting period.

Disclosure

Date of authorisation for issue

32.9 An entity shall disclose the date the financial statements were authorised for issue and who gave that authorisation.

Non-adjusting events after the end of the reporting period

* 32.10 An entity shall disclose the following for each category of non-adjusting event after the end of the reporting period:

(a) the nature of the event; and

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

* 32.11 The following are examples of non-adjusting events after the end of the reporting period that would generally result in disclosure. The disclosures will reflect information that becomes known after the end of the reporting period but before the financial statements are authorised for issue:

(a) a major **business combination** or disposal of a major **subsidiary**;

(b) announcement of a plan to discontinue an operation;

(c) major purchases of assets, disposals or plans to dispose of assets, or expropriation of major assets by government;

(d) the destruction of a major production plant by a fire;

(e) announcement, or commencement of the implementation, of a major **restructuring**;

(f) issues or repurchases of an entity's debt or equity instruments;

(g) abnormally large changes in asset prices or foreign exchange rates;

(h) changes in tax rates or tax laws enacted or announced that have a significant effect on current and **deferred tax assets and liabilities**;

(i) entering into significant commitments or contingent liabilities, for example, by issuing significant guarantees; and

(j) commencement of major litigation arising solely out of events that occurred after the end of the reporting period.

Section 33
Related Party Disclosures

Scope of this section

33.1 This section requires an entity to include in its **financial statements** the disclosures necessary to draw attention to the possibility that its **financial position** and **profit or loss** have been affected by the existence of **related parties** and by transactions and outstanding balances with such parties.

33.1A Disclosures required by this section need not be given of transactions entered into between two or more members of a **group**, provided that any **subsidiary** which is a party to the transaction is wholly owned by such a member.

Related party defined

33.2 A related party is a person or entity that is related to the entity that is preparing its financial statements (the reporting entity).

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

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

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

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

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

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

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

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

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

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

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

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

(viii) the entity, or any member of a group of which it is a part, provides key management personnel services to the reporting entity or to the parent of the reporting entity.

33.3 In considering each possible related party relationship, an entity shall assess the substance of the relationship and not merely the legal form.

33.4 In the context of this FRS, the following are not related parties:

(a) Two entities simply because they have a director or other member of key management personnel in common or because a member of key management personnel of one entity has significant influence over the other entity.

(b) Two **venturers** simply because they share joint control over a joint venture.

(c) Any of the following simply by virtue of their normal dealings with an entity (even though they may affect the freedom of action of an entity or participate in its decision-making process):

(i) providers of finance;

(ii) trade unions;

(iii) public utilities; and

(iv) government departments and agencies.

(d) A customer, supplier, franchisor, distributor or general agent with whom an entity transacts a significant volume of **business**, merely by virtue of the resulting economic dependence.

33.4A In the definition of a related party, an associate includes subsidiaries of the associate and a joint venture includes subsidiaries of the joint venture. Therefore, for example, an associate's subsidiary and the investor that has significant influence over the associate are related to each other.

Disclosures

Disclosure of parent-subsidiary relationships

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

Disclosure of key management personnel compensation

33.6 Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly, including any director (whether executive or otherwise) of that entity. Compensation includes all **employee benefits** (as defined in Section 28 *Employee Benefits*) including those in the form of **share-based payments** (see Section 26 *Share-based Payment*). Employee benefits include all forms of consideration paid, payable or provided by the entity, or on behalf of the entity (eg by its parent or by a shareholder), in exchange for services rendered to the entity. It also includes such consideration paid on behalf of a parent of the entity in respect of goods or services provided to the entity.

33.7 An entity shall disclose key management personnel compensation in total.

33.7A When an entity is subject to a legal or regulatory requirement to disclose directors' remuneration (or equivalent), it is exempt from the requirements of paragraph 33.7 if the key management personnel and directors are the same.

Disclosure of related party transactions

33.8 A related party transaction is a transfer of resources, services or obligations between a reporting entity and a related party, regardless of whether a price is charged. Examples of related party transactions that are common to entities within the scope of this FRS include, but are not limited to:

(a) transactions between an entity and its principal **owner(s)**;

(b) transactions between an entity and another entity when both entities are under the common control of a single entity or person; and

(c) transactions in which an entity or person that controls the reporting entity incurs **expenses** directly that otherwise would have been borne by the reporting entity.

* 33.9 If an entity has related party transactions, it shall disclose the nature of the related party relationship as well as information about the transactions, outstanding balances and commitments necessary for an understanding of the potential effect of the relationship on the financial statements. Those disclosure requirements are in addition to the requirements in paragraph 33.7 to disclose key management personnel compensation.[58] At a minimum, disclosures shall include:

(a) The amount of the transactions.

(b) The amount of outstanding balances and:

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

* (ii) details of any guarantees given or received.

(c) Provisions for uncollectible receivables related to the amount of outstanding balances.

(d) The expense recognised during the period in respect of bad or doubtful debts due from related parties.

Such transactions could include purchases, sales, or transfers of goods or services, **leases**, guarantees and settlements by the entity on behalf of the related party or vice versa.

33.10 An entity shall make the disclosures required by paragraph 33.9 separately for each of the following categories:

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

(b) entities over which the entity has control, joint control or significant influence;

(c) key management personnel of the entity or its parent (in the aggregate);

(d) entities that provide key management personnel services to the entity; and

(e) other related parties.

33.11 An entity is exempt from the disclosure requirements of paragraph 33.9 in relation to:

(a) a **state** (a national, regional or local government) that has control, joint control or significant influence over the reporting entity; and

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

[58] When, in accordance with paragraph 33.7A, an entity takes advantage of the exemption from disclosing key management personnel compensation it is not required, by this paragraph, to provide additional disclosure about directors' share-based payment arrangements.

However, the entity must still disclose a parent-subsidiary relationship as required by paragraph 33.5.

33.12 The following are examples of transactions that shall be disclosed if they are with a related party:

(a) purchases or sales of goods (finished or unfinished);

(b) purchases or sales of property and other **assets**;

(c) rendering or receiving of services;

(d) leases;

(e) transfers of **research** and **development**;

(f) transfers under licence agreements;

(g) transfers under finance arrangements (including loans and equity contributions in **cash** or in kind);

(h) provision of guarantees or collateral;

(i) settlement of **liabilities** on behalf of the entity or by the entity on behalf of another party; and

(j) participation by a parent or subsidiary in a **defined benefit plan** that shares risks between group entities.

33.13 An entity shall not state that related party transactions were made on terms equivalent to those that prevail in arm's length transactions unless such terms can be substantiated.

* 33.14 An entity may disclose items of a similar nature in the aggregate except when separate disclosure is necessary for an understanding of the effects of related party transactions on the financial statements of the entity.

Section 34
Specialised Activities

Scope of this section

34.1 This section applies to the following types of specialised activities:

(a) Agriculture (see paragraphs 34.2 to 34.10A);

(b) Extractive Activities (see paragraphs 34.11 to 34.11C);

(c) Service Concession Arrangements (see paragraphs 34.12 to 34.16C);

(d) Financial Institutions (see paragraphs 34.17 to 34.33);

(e) Retirement Benefit Plans: Financial Statements (see paragraphs 34.34 to 34.48);

(f) Heritage Assets (see paragraphs 34.49 to 34.56);

(g) Funding Commitments (see paragraphs 34.57 to 34.63);

(h) Incoming Resources from Non-Exchange Transactions (see paragraphs PBE34.64 to PBE34.74);

(i) Public Benefit Entity Combinations (see paragraphs PBE34.75 to PBE34.86); and

(j) Public Benefit Entity Concessionary Loans (see paragraphs PBE34.87 to PBE34.97).

Agriculture

34.2 An entity that is engaged in **agricultural activity** shall determine an **accounting policy** for each class of **biological asset** and its related **agricultural produce.**

Recognition

34.3 An entity shall recognise a biological asset or an item of agricultural produce when, and only when:

(a) the entity controls the **asset** as a result of past events;

(b) it is **probable** that future economic benefits associated with the asset will flow to the entity; and

(c) the **fair value** or cost of the asset can be measured reliably.

Measurement

34.3A For each class of biological asset and its related agricultural produce an entity shall choose as its accounting policy either:

(a) the fair value model set out in paragraphs 34.4 to 34.7B; or

(b) the cost model set out in paragraphs 34.8 to 34.10A.

34.3B If an entity has chosen the fair value model for a class of biological asset and its related agricultural produce, it shall not subsequently change its accounting policy to the cost model.

Measurement – fair value model

34.4 An entity applying the fair value model shall measure a biological asset on initial **recognition** and at each **reporting date** at its **fair value less costs to sell**. Changes in fair value less costs to sell shall be recognised in **profit or loss**.

34.5 Agricultural produce harvested from an entity's biological assets shall be measured at the point of harvest at its fair value less costs to sell. Such **measurement** is the cost at that date when applying Section 13 *Inventories* or another applicable section of this FRS.

34.6 In determining fair value, an entity shall consider the following:

(a) If an **active market** exists for a biological asset or agricultural produce in its present location and condition, the quoted price in that market is the appropriate basis for determining the fair value of that asset. If an entity has access to different active markets, the entity shall use the price existing in the market that it expects to use.

(b) If an active market does not exist, an entity uses one or more of the following, when available, in determining fair value:

(i) the most recent market transaction price, provided that there has not been a significant change in economic circumstances between the date of that transaction and the end of the **reporting period**;

(ii) market prices for similar assets with adjustment to reflect differences; and

(iii) sector benchmarks such as the value of an orchard expressed per export tray, bushel, or hectare, and the value of cattle expressed per kilogram of meat.

(c) In some cases, the information sources listed in (b) may suggest different conclusions as to the fair value of a biological asset or an item of agricultural produce. An entity considers the reasons for those differences, to arrive at the most reliable estimate of fair value within a relatively narrow range of reasonable estimates.

(d) In some circumstances, fair value may be readily determinable even though market determined prices or values are not available for a biological asset in its present condition. An entity shall consider whether the **present value** of expected net **cash flows** from the asset discounted at a current market determined rate results in a reliable measure of fair value.

34.6A If the fair value of a biological asset cannot be measured reliably, the entity shall apply the cost model to that biological asset in accordance with paragraphs 34.8 and 34.10A until such time that the fair value can be reliably measured.

Disclosures – fair value model

34.7 An entity shall disclose the following for each class of biological asset measured using the fair value model:

(a) a description of each class of biological asset;

* (b) the methods and significant assumptions applied in determining the fair value of each class of biological asset;

* (c) a reconciliation of changes in the **carrying amount** of each class of biological asset between the beginning and the end of the current period. The reconciliation shall include:

* (i) the **gain** or loss arising from changes in fair value less costs to sell;

(ii) increases resulting from purchases;

(iii) decreases attributable to sales;

(iv) decreases resulting from harvest;

(v) increases resulting from **business combinations**; and

(vi) other changes.

This reconciliation need not be presented for prior periods.

34.7A If an entity measures any individual biological assets at cost in accordance with paragraph 34.6A, it shall explain why fair value cannot be reliably measured. If the fair value of such a biological asset becomes reliably measurable during the current period an entity shall explain why fair value has become reliably measurable and the effect of the change.

34.7B An entity shall disclose the methods and significant assumptions applied in determining the fair value at the point of harvest of each class of agricultural produce.

Measurement – cost model

34.8 An entity applying the cost model shall measure biological assets at cost less any accumulated **depreciation** (when relevant) and any accumulated **impairment losses**.

34.9 In applying the cost model, agricultural produce harvested from an entity's biological assets shall be measured at the point of harvest at either:

(a) the lower of cost and estimated selling price less costs to complete and sell; or

(b) its fair value less costs to sell. Any gain or loss arising on initial recognition of agricultural produce at fair value less costs to sell shall be included in profit or loss for the period in which it arises.

Such measurement is the cost at that date when applying Section 13 or another applicable section of this FRS.

Disclosures – cost model

34.10 An entity shall disclose the following for each class of biological asset measured using the cost model:

(a) a description of each class of biological asset;

(b) [Deleted]

(c) the depreciation method used;

(d) the useful lives or the depreciation rates used; and

* (e) a reconciliation of changes in the carrying amount of each class of biological asset between the beginning and the end of the current period. The reconciliation shall include:

(i) increases resulting from purchases;

(ii) decreases attributable to sales;

(iii) decreases resulting from harvest;

(iv) increases resulting from business combinations;

(v) impairment losses recognised or reversed in profit or loss in accordance with Section 27 *Impairment of Assets;* and

(vi) other changes.

This reconciliation need not be presented for prior periods.

34.10A An entity shall disclose, for any agricultural produce measured at fair value less costs to sell, the methods and significant assumptions applied in determining the fair value at the point of harvest of its agricultural produce.

Extractive Activities

34.11 An entity that is engaged in the exploration for and/or evaluation of mineral resources (extractive activities) shall apply the requirements of IFRS 6 *Exploration for and Evaluation of Mineral Resources* (as adopted in the relevant jurisdiction).

34.11A When applying the requirements of IFRS 6, references made to other IFRSs within that standard shall be taken to be references to the relevant section or paragraph within this FRS.

34.11B Notwithstanding the requirements of paragraph 34.11A, when applying paragraph 21 of IFRS 6, a **cash-generating unit** or group of cash-generating units shall be no larger than an **operating segment** and the reference to IFRS 8 *Operating Segments* shall be ignored**.**

34.11C On first-time adoption of this FRS if it is not practical to apply a particular requirement of paragraph 18 of IFRS 6 to previous comparative amounts, an entity shall disclose that fact.

Service Concession Arrangements

34.12 A **service concession arrangement** is an arrangement whereby a public sector body, or a **public benefit entity** (the grantor) contracts with a private sector entity (the operator) to construct (or upgrade), operate and maintain **infrastructure assets** for a specified period of time (concession period). The operator is paid for its services over the period of the arrangement. A common feature of a service concession arrangement is the public service nature of the obligation undertaken by the operator, whereby the arrangement contractually obliges the operator to provide services to, or on behalf of, the grantor for the benefit of the public.

34.12A Specifically an arrangement is a service concession arrangement when the following conditions apply:

(a) the grantor controls or regulates what services the operator must provide using the infrastructure assets, to whom, and at what price; and

(b) the grantor controls, through ownership, beneficial entitlement or otherwise, any significant **residual interest** in the **assets** at the end of the term of the arrangement.

Where the infrastructure assets have no significant **residual value** at the end of the term of the arrangement (ie the arrangement is for its entire **useful life**), then the arrangement shall be accounted for as a service concession if the conditions in (a) are met.

For the purpose of condition (b), the grantor's control over any significant residual interest should both restrict the operator's practical ability to sell or pledge the infrastructure assets and give the grantor a continuing right of use throughout the concession period.

34.12B A service concession arrangement shall be accounted for in accordance with the requirements of paragraphs 34.12E to 34.16C.

34.12C A service concession arrangement may contain a group of contracts and sub-arrangements as elements of the service concession arrangement as a whole. Such an arrangement shall be treated as a whole when the group of contracts and sub-arrangements are linked in such a way that the commercial effect cannot be understood without reference to them as a whole. Accordingly, the contractual terms of certain contracts or arrangements may meet both the scope requirements of paragraphs 34.12 and 34.12A, and Section 20 *Leases*. Where this is the case, the requirements of this section shall prevail.

34.12D Where an arrangement does not meet the requirements of paragraphs 34.12 and 34.12A, it shall be accounted for in accordance with Section 17 *Property, Plant and Equipment*, Section 18 *Intangible Assets other than Goodwill*, Section 20 or Section 23 *Revenue*, based on the nature of the arrangement.

Accounting by grantors – Finance lease liability model

34.12E The infrastructure assets shall be recognised as assets of the grantor together with a **liability** for its obligations under the service concession arrangement.

34.12F The grantor shall initially recognise the infrastructure assets and associated liability in accordance with paragraphs 20.9 and 20.10. If as a result of applying paragraphs 20.9 and 20.10 the grantor has not recognised a liability to make payments to the operator, it shall not recognise the infrastructure assets.

34.12G The liability shall be recognised as a finance lease liability and subsequently accounted for in accordance with paragraph 20.11.

34.12H The infrastructure assets shall be recognised as **property, plant and equipment** or as **intangible assets**, as appropriate, and subsequently accounted for in accordance with Section 17 or Section 18.

Accounting by operators

Treatment of the operator's rights over the infrastructure

34.12I Infrastructure assets shall not be recognised as property, plant and equipment by the operator because the contractual service arrangement does not convey the right to control the use of the public service assets to the operator. The operator has access to operate the infrastructure to provide the public service on behalf of the grantor in accordance with the terms specified in the arrangement.

Recognition and measurement of consideration

34.13 There are two principal categories of service concession arrangements:

(a) In one, the operator receives a **financial asset** - an unconditional contractual right to receive a specified or determinable amount of **cash** or another financial asset from, or at the direction of, the grantor in return for constructing (or upgrading) the infrastructure assets, and then operating and maintaining the asset for a specified period of time. This category includes guarantees by the grantor to pay for any shortfall between amounts received from users of the public service and specified or determinable amounts.

(b) In the other, the operator receives an intangible asset - a right to charge for use of the infrastructure assets that it constructs (or upgrades) and then operates and maintains for a specified period of time. A right to charge users is not an unconditional right to receive cash because the amounts are contingent on the extent to which the public uses the service.

Sometimes, a single arrangement may contain both types: to the extent that the grantor has given an unconditional guarantee of payment for the construction (or upgrade) of the infrastructure assets, the operator has a financial asset; to the extent that the operator receives a right to charge the public for using the service the operator has an intangible asset.

Accounting – financial asset model

34.14 The operator shall recognise a financial asset to the extent that it has an unconditional contractual right to receive cash or another financial asset from, or at the direction of, the grantor for the construction (or upgrade) services. The operator shall initially recognise the financial asset at **fair value** for the consideration received or receivable, based on the fair value of the construction (or upgrade) services provided. Thereafter, it shall account for the financial asset in accordance with Section 11 *Basic Financial Instruments* and Section 12 *Other Financial Instruments Issues*. In classifying the financial asset as basic or other, a payment being contingent on the operator ensuring that the infrastructure meets specified quality or efficiency requirements does not in itself prevent its classification as basic.

Accounting – intangible asset model

34.15 The operator shall recognise an intangible asset to the extent that it receives a right (a licence) to charge users of the public service. The operator shall initially recognise the intangible asset at fair value for the consideration received or receivable, based on the fair value of the construction (or upgrade) services provided. Thereafter, it shall account for the intangible asset in accordance with Section 18.

Operating services

34.16 The operator shall account for **revenue** in accordance with Section 23 for the operating services it performs.

Borrowing costs

34.16A **Borrowing costs** attributable to the arrangement shall be recognised as an **expense**, in accordance with Section 25 *Borrowing Costs*, in the period in which they are incurred unless the operator has an intangible asset. In this case borrowing costs attributable to the arrangement may be capitalised in accordance with Section 25 where a policy of capitalisation has been adopted in accordance with that section.

Disclosures

34.16B An operator and a grantor shall disclose information that enables users of the entity's **financial statements** to evaluate the nature and extent of relevant risks arising from service concession arrangements. This information shall typically include, but is not limited to, a description of the arrangement, including any rights, obligations or options arising, and any significant terms of arrangement that may affect the amount, timing and certainty of future **cash flows**.

34.16C An operator shall disclose the amount of revenue, profits or losses and other **income** recognised in the period on exchanging construction services for a financial asset or an intangible asset.

34.17 A **financial institution** applying this FRS shall, in addition to the disclosure requirements in Section 11 *Basic Financial Instruments* and Section 12 *Other Financial Instruments Issues*, provide the disclosures in paragraphs 34.19 to 34.33. The disclosures in paragraphs 34.19 to 34.33 are required to be provided in:

(a) the **individual financial statements** of a financial institution; and

(b) the **consolidated financial statements** of a **group** containing a financial institution when the **financial instruments** held by the financial institution are **material** to the group. Where this is the case, the disclosures apply regardless of whether the principal activity of the group is being a financial institution or not. The disclosures in paragraphs 34.19 to 34.33 only need to be given in respect of financial instruments held by entities within the group that are financial institutions.

34.18 [Deleted]

Disclosures

Significance of financial instruments for financial position and performance

34.19 A financial institution shall disclose information that enables users of its **financial statements** to evaluate the significance of financial instruments for its **financial position** and **performance**.

34.20 A financial institution shall disclose a disaggregation of the **statement of financial position** line item by class of financial instrument. A class is a grouping of financial instruments that is appropriate to the nature of the information disclosed and that takes into account the characteristics of those financial instruments.

Impairment

34.21 Unless a financial institution has made the **accounting policy** choice in paragraphs 11.2(c) and 12.2(c) to apply the **recognition** and **measurement** provisions of IFRS 9 *Financial Instruments* (as adopted in the relevant jurisdiction), when it uses a separate allowance account to record impairments, it shall disclose a reconciliation of changes in that account during the period for each class of **financial asset**.

34.21A When a financial institution has made the accounting policy choice in paragraphs 11.2(c) and 12.2(c) to apply the recognition and measurement provisions of IFRS 9, it shall disclose information that enables users of its financial statements to understand the effect of **credit risk** on the amount, timing and uncertainty of future **cash flows**. This shall include:

(a) An explanation of the financial institution's credit risk management practices and how they relate to the recognition and measurement of expected credit losses.

(b) A reconciliation from the opening balance to the closing balance of the loss allowance, in a table, showing separately the changes during the period for:

(i) the loss allowance measured at an amount equal to 12-month expected credit losses;

(ii) the loss allowance measured at an amount equal to lifetime expected credit losses (showing separately the amount relating to financial instruments for which credit risk has increased significantly since initial recognition); and

(iii) financial assets that are purchased or originated credit-impaired.

(c) By credit risk rating grade, the gross **carrying amount** of financial assets and the exposure to credit risk on loan commitments and **financial guarantee contracts** (showing separately information for financial instruments for which the loss allowance is measured at an amount equal to 12-month expected credit losses, for which the loss allowance is measured at an amount equal to lifetime expected credit losses, and that are purchased or originated credit-impaired **financial assets**).

Fair value

34.22 For financial instruments held at **fair value** in the statement of financial position, a financial institution shall disclose for each class of financial instrument, an analysis of the level in the following fair value hierarchy into which the fair value measurements are categorised. A fair value measurement is categorised in its entirety on the basis of the lowest level input that is significant to the fair value measurement in its entirety.

Level 1: The unadjusted quoted price in an **active market** for identical **assets** or **liabilities** that the entity can access at the measurement date.

Level 2: Inputs other than quoted prices included within Level 1 that are observable (ie developed using market data) for the asset or liability, either directly or indirectly.

Level 3: Inputs are unobservable (ie for which market data is unavailable) for the asset or liability.

Nature and extent of risks arising from financial instruments

34.23 A financial institution shall disclose information that enables users of its financial statements to evaluate the nature and extent of credit risk, **liquidity risk** and **market risk** arising from financial instruments to which the financial institution is exposed at the end of the **reporting period**.

34.24 For each type of risk arising from financial instruments, a financial institution shall disclose:

(a) the exposures to risk and how they arise;

(b) its objectives, policies and processes for managing the risk and the methods used to measure the risk; and

(c) any changes in (a) or (b) from the previous period.

Credit risk

34.25 For financial instruments within the scope of Section 11 or Section 12 to which the impairment requirements of IFRS 9 are not applied, a financial institution shall disclose by class of financial instrument:

(a) The amount that best represents its maximum exposure to credit risk at the end of the reporting period. This disclosure is not required for financial instruments whose carrying amount best represents the maximum exposure to credit risk.

(b) A description of collateral held as security and of other credit enhancements, and the extent to which these mitigate credit risk.

(c) The amount by which any related credit **derivatives** or similar instruments mitigate that maximum exposure to credit risk.

(d) Information about the credit quality of financial assets that are neither past due nor impaired.[59]

34.26 Unless a financial institution has made the accounting policy choice in paragraphs 11.2(c) and 12.2(c) to apply the recognition and measurement provisions of IFRS 9, it shall provide, by class of financial asset, an analysis of:

(a) the age of financial assets that are past due as at the end of the reporting period but not impaired; and

(b) the financial assets that are individually determined to be impaired as at the end of the reporting period, including the factors the financial institution considered in determining that they are impaired.

34.27 When a financial institution obtains financial or non-financial assets during the period by taking possession of collateral it holds as security or calling on other credit enhancements (eg guarantees), and such assets meet the recognition criteria in other sections, a financial institution shall disclose:

(a) the nature and carrying amount of the assets obtained; and

(b) when the assets are not readily convertible into cash, its policies for disposing of such assets or for using them in its operations.

Liquidity risk

34.28 A financial institution shall provide a maturity analysis for **financial liabilities** that shows the remaining contractual maturities at undiscounted amounts separated between derivative and non-derivative financial liabilities.

Market risk

34.29 A financial institution shall provide a sensitivity analysis for each type of market risk (eg interest rate risk, currency risk, other price risk) it is exposed to, showing the impact on **profit or loss** and **equity**. Details of the methods and assumptions used should be provided.

34.30 If a financial institution prepares a sensitivity analysis, such as value-at-risk, that reflects interdependencies between risk variables (eg interest rates and exchange rates) and uses it to manage **financial risks**, it may use that sensitivity analysis instead.

Capital

34.31 A financial institution shall disclose information that enables users of its financial statements to evaluate the entity's objectives, policies and processes for managing capital. A financial institution shall disclose the following:

(a) Qualitative information about its objectives, policies and processes for managing capital, including:

   (i) a description of what it manages as capital;

   (ii) when an entity is subject to externally imposed capital requirements, the nature of those requirements and how those requirements are incorporated into the management of capital; and

   (iii) how it is meeting its objectives for managing capital.

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[59] Sub-paragraph (d) does not apply to financial institutions that have made the accounting policy choice in paragraphs 11.2(c) and 12.2(c) to apply the recognition and measurement provisions of IFRS 9 *Financial Instruments*.

(b) Summary quantitative data about what it manages as capital. Some entities regard some financial liabilities (eg some forms of subordinated debt) as part of capital. Other entities regard capital as excluding some components of equity (eg components arising from cash flow hedges).

(c) Any changes in (a) and (b) from the previous period.

(d) Whether during the period it complied with any externally imposed capital requirements to which it is subject.

(e) When the entity has not complied with such externally imposed capital requirements, the consequences of such non-compliance.

A financial institution bases these disclosures on the information provided internally to **key management personnel**.

34.32 A financial institution may manage capital in a number of ways and be subject to a number of different capital requirements. For example, a conglomerate may include entities that undertake insurance activities and banking activities and those entities may operate in several jurisdictions. When an aggregate disclosure of capital requirements and how capital is managed would not provide useful information or would distort a financial statement user's understanding of the financial institution's capital resources, the financial institution shall disclose separate information for each capital requirement to which the entity is subject.

Reporting cash flows on a net basis

34.33 A financial institution that presents a **statement of cash flows** in accordance with Section 7 *Statement of Cash Flows* may report cash flows arising from each of the following activities on a net basis:

(a) cash receipts and payments for the acceptance and repayment of deposits with a fixed maturity date;

(b) the placement of deposits with and withdrawal of deposits from other financial institutions; and

(c) cash advances and loans made to customers and the repayment of those advances and loans.

This paragraph does not impose a requirement to produce a cash flow statement.

Retirement Benefit Plans: Financial Statements

34.34 An entity applying this FRS that is a **retirement benefit plan** shall also apply the requirements of paragraphs 34.35 to 34.48. A retirement benefit plan may be a **defined benefit plan**, a **defined contribution plan**, or have both defined benefit and defined contribution elements. The **financial statements** shall distinguish between defined benefit and defined contribution elements, where **material**.

Requirements applicable to both defined benefit plans and defined contribution plans

34.35 A retirement benefit plan need not comply with the requirements of paragraph 3.17. The financial statements of a retirement benefit plan shall contain as part of the financial statements:

(a) a statement of changes in **net assets available for benefits** (which can also be called a Fund Account) (see paragraph 34.37);

(b) a statement of net assets available for benefits (see paragraph 34.38); and

(c) **notes**, comprising its significant **accounting policies** and other explanatory information.

34.36 At each **reporting date**, the net assets available for benefits shall be measured in accordance with paragraph 28.15(b). Changes in **fair value** shall be recognised in the statements of changes in net assets available for benefits.

Statement of changes in net assets available for benefits (Fund Account)

34.37 The financial statements of a retirement benefit plan, whether defined contribution or defined benefit, shall present the following in the statement of changes in net assets available for benefits:

(a) employer contributions;

(b) employee contributions;

(c) investment income such as interest and dividends;

(d) other **income**;

(e) benefits paid or payable (analysed, for example, as retirement, death and disability benefits, and lump sum payments);

(f) administrative expenses;

(g) other expenses;

(h) taxes on income;

(i) profits and losses on disposal of investments and changes in value of investments;

(j) transfers in; and

(k) payments to and on account of leavers.

Statement of net assets available for benefits

34.38 The financial statements of a retirement benefit plan, whether defined contribution or defined benefit, shall present the following in the statement of net assets available for benefits:

(a) **assets** at the end of the period suitably classified; and

(b) **liabilities** other than the actuarial **present value** of promised retirement benefits.

The basis of valuation of assets shall be presented in the **notes** to the financial statements.

Disclosures

Assets other than financial instruments held at fair value

34.39 Where a retirement benefit plan holds assets other than **financial instruments** at fair value in accordance with paragraph 34.36, it shall apply the disclosure requirements of the relevant section of this FRS, for example in relation to **investment property** it shall provide the disclosures required by paragraph 16.10.

Significance of financial instruments for financial position and performance

34.40 A retirement benefit plan shall disclose information that enables users of its financial statements to evaluate the significance of financial instruments for its **financial position** and **performance**.

34.41 A retirement benefit plan shall disclose a disaggregation of the statement of net assets available for benefits by class of financial instrument. A class is a grouping of financial instruments that is appropriate to the nature of the information disclosed and that takes into account the characteristics of those financial instruments.

Fair value

34.42 For financial instruments held at fair value in the statement of net assets available for benefits, a retirement benefit plan shall disclose for each class of financial instrument, an analysis of the level in the following fair value hierarchy into which the fair value measurements are categorised. A fair value measurement is categorised in its entirety on the basis of the lowest level input that is significant to the fair value measurement in its entirety.

Level 1: The unadjusted quoted price in an **active market** for identical assets or liabilities that the entity can access at the measurement date.

Level 2: Inputs other than quoted prices included within Level 1 that are observable (ie developed using market data) for the asset or liability, either directly or indirectly.

Level 3: Inputs are unobservable (ie for which market data is unavailable) for the asset or liability.

Nature and extent of risks arising from financial instruments

34.43 A retirement benefit plan shall disclose information that enables users of its financial statements to evaluate the nature and extent of **credit risk** and **market risk** arising from financial instruments to which the retirement benefit plan is exposed at the end of the **reporting period**.

34.44 For each type of credit and market risk arising from financial instruments, a retirement benefit plan shall disclose:

(a) the exposures to risk and how they arise;

(b) its objectives, policies and processes for managing the risk and the methods used to measure the risk; and

(c) any changes in (a) or (b) from the previous period.

In relation to credit risk, a retirement benefit plan shall, in addition, provide the disclosures set out in paragraphs 34.45 and 34.46.

Credit risk

34.45 A retirement benefit plan shall disclose by class of financial instrument:

(a) The amount that best represents its maximum exposure to credit risk at the end of the reporting period. This disclosure is not required for financial instruments whose **carrying amount** best represents the maximum exposure to credit risk.

(b) A description of collateral held as security and of other credit enhancements, and the extent to which these mitigate credit risk.

(c) The amount by which any related credit **derivatives** or similar instruments mitigate that maximum exposure to credit risk.

(d) Information about the credit quality of **financial assets** that are neither past due nor impaired.

34.46 When a retirement benefit plan obtains financial or non-financial assets during the period by taking possession of collateral it holds as security or calling on other credit enhancements (eg guarantees), and such assets meet the **recognition** criteria in other sections, a retirement benefit plan shall disclose:

(a) the nature and carrying amount of the assets obtained; and

(b) when the assets are not readily convertible into **cash**, its policies for disposing of such assets or for retaining them.

Defined benefit plans – actuarial liabilities

34.47 A defined benefit plan is not required to recognise a liability in relation to the promised retirement benefits.

34.48 A defined benefit plan shall disclose, in a report alongside the financial statements, information regarding the actuarial present value of promised retirement benefits including:

(a) a statement of the actuarial present value of promised retirement benefits, based on the most recent valuation of the scheme;

(b) the date of the most recent valuation of the scheme; and

(c) the significant **actuarial assumptions** made and the method used to calculate the actuarial present value of promised retirement benefits.

Heritage Assets

34.49 All **heritage assets** shall be accounted for in accordance with the requirements of paragraphs 34.50 to 34.56. These paragraphs do not apply to **investment property**, **property, plant and equipment** or **intangible assets** which fall within the scope of Section 16 *Investment Properties*, Section 17 *Property, Plant and Equipment* and Section 18 *Intangible Assets other than Goodwill*.

34.50 Works of art and similar objects are sometimes held by commercial entities but are not heritage assets because they are not maintained principally for their contribution to knowledge and culture. These **assets** shall therefore be accounted for in accordance with Section 17. Heritage assets used by the entity itself, for example historic buildings used for teaching by education establishments, shall also be accounted for in accordance with Section 17. This is based on the view that an operational perspective is likely to be most relevant for most users of **financial statements**. However, entities that use historic buildings and similar assets may wish to consider whether it is appropriate to apply the disclosures required by paragraphs 34.55 and 34.56.

Recognition and measurement

34.51 An entity shall recognise and measure heritage assets in accordance with Section 17 or Section 18, as appropriate (ie using the cost model or revaluation model), subject to the requirements set out in paragraphs 34.52 to 34.53 below.

34.52 Heritage assets shall be recognised in the **statement of financial position** separately from other assets.

34.53 Where heritage assets have previously been capitalised or are recently purchased, information on the cost or value of the asset will be available. Where this information is not available, and cannot be obtained at a cost which is commensurate with the benefits to users of the financial statements, the assets shall not be recognised in the statement of financial position, but must be disclosed in accordance with the requirements below.

34.54 At each **reporting date**, an entity shall apply Section 27 *Impairment of Assets* to determine whether a heritage asset is impaired and, if so, how to recognise and measure the **impairment loss**. A heritage asset may be impaired, for example where it has suffered physical deterioration, breakage or doubts arise as to its authenticity.

Disclosure

34.55 An entity shall disclose the following for all heritage assets it holds:

(a) An indication of the nature and scale of heritage assets held by the entity.

(b) The policy for the acquisition, preservation, management and disposal of heritage assets (including a description of the records maintained by the entity of its collection of heritage assets and information on the extent to which access to the assets is permitted).

(c) The **accounting policies** adopted for heritage assets, including details of the **measurement** bases used.

(d) For heritage assets that have not been recognised in the statement of financial position, the **notes** to the financial statements shall:

(i) explain the reasons why;

(ii) describe the significance and nature of those assets; and

(iii) disclose information that is helpful in assessing the value of those heritage assets.

* (e) Where heritage assets are recognised in the statement of financial position the following disclosure is required:

(i) the **carrying amount** of heritage assets at the beginning of the **reporting period** and the reporting date, including an analysis between classes or groups of heritage assets recognised at cost and those recognised at valuation; and

* (ii) where assets are recognised at valuation, sufficient information to assist in understanding the valuation being recognised (date of valuation, method used, whether carried out by external valuer and if so their qualification and any significant limitations on the valuation).

* (f) A summary of transactions relating to heritage assets for the reporting period and each of the previous four reporting periods disclosing:

(i) the cost of acquisitions of heritage assets;

(ii) the value of heritage assets acquired by donations;

(iii) the carrying amount of heritage assets disposed of in the period and proceeds received; and

(iv) any impairment recognised in the period.

The summary shall show separately those transactions included in the statement of financial position and those that are not.

(g) In exceptional circumstances where it is **impracticable** to obtain a valuation of heritage assets acquired by donation the reason shall be stated.

Disclosures can be aggregated for groups or classes of heritage assets, provided this does not obscure significant information.

34.56 Where it is impracticable to do so, the disclosures required by paragraph 34.55(f) need not be given for any accounting period earlier than the previous comparable period, and a statement to the effect that it is impracticable shall be made.

Funding Commitments

34.57 An entity that commits to provide resources to other entities shall apply the requirements of paragraphs 34.58 to 34.63 and the accompanying guidance at Appendix A to this section, except for commitments to make a loan to which entities shall apply Section 11 *Basic Financial Instruments* or Section 12 *Other Financial Instruments Issues*, as applicable.

34.58 When applying these paragraphs, the requirements of Section 2 *Concepts and Pervasive Principles* and Section 21 *Provisions and Contingencies* shall also be taken into consideration.

Recognition

34.59 An entity shall recognise a **liability** and, usually, a corresponding **expense**, when it has made a commitment that it will provide resources to another party, if, and only if:

(a) the definition and **recognition** criteria for a liability have been satisfied;

(b) the obligation (which may be a **constructive obligation**) is such that the entity cannot realistically withdraw from it; and

(c) the entitlement of the other party to the resources does not depend on the satisfaction of **performance-related conditions**.

34.60 Commitments that are performance-related will be recognised when those performance-related conditions are met.

Measurement

34.61 An entity shall measure any recognised liability at the **present value** of the resources committed.

Disclosure

* 34.62 An entity that has made a commitment shall disclose the following:

(a) the commitment made;

(b) the time-frame of that commitment;

(c) any performance-related conditions attached to that commitment; and

(d) details of how that commitment will be funded.

34.63 The above disclosures may be made in aggregate, providing that such aggregation does not obscure significant information. However, separate disclosure shall be made for recognised and unrecognised commitments.

Incoming Resources from Non-Exchange Transactions

PBE34.64 The requirements for **government grants** are set out in Section 24 *Government Grants.*

PBE34.65 Paragraphs PBE34.67 to PBE34.74 and the accompanying guidance at Appendix B to this section apply to other resources received from **non-exchange transactions** by **public benefit entities** or entities within a **public benefit entity group**. A non-exchange transaction is a transaction whereby an entity receives value from another entity without directly giving approximately equal value in exchange or gives value to another entity without directly receiving approximately equal value in exchange.

PBE34.66 Non-exchange transactions include, but are not limited to, donations (of **cash**, goods, and services) and legacies.

Recognition and measurement

PBE34.67 An entity shall recognise receipts of resources from non-exchange transactions as follows:

(a) Transactions that do not impose specified future performance-related conditions on the recipient are recognised in **income** when the resources are received or receivable.

(b) Transactions that do impose specified future performance-related conditions on the recipient are recognised in income only when the performance-related conditions are met.

(c) Where resources are received before the **revenue recognition** criteria are satisfied, a **liability** is recognised.

PBE34.68 The existence of a **restriction** does not prohibit a resource from being recognised in income when receivable.

PBE34.69 When applying the requirements of paragraph PBE34.67, an entity must take into consideration whether the resource can be measured reliably and whether the benefits of recognising the resource outweigh the costs.

PBE34.70 Therefore, where it is **impracticable** to estimate the value of the resource with sufficient **reliability**, the income shall be included in the financial period when the resource is sold.

PBE34.71 An entity shall recognise a liability for any resource that has previously been received and recognised in income when, as a result of a subsequent failure to meet restrictions or performance-related conditions attached to it, repayment becomes **probable**.

PBE34.72 Donations of services that can be reasonably quantified will usually result in the recognition of income and an **expense**. An **asset** will be recognised only when those services are used for the production of an asset and the services received will be capitalised as part of the cost of that asset.

PBE34.73 An entity shall measure incoming resources from non-exchange transactions as follows:

(a) Donated services and facilities, that would otherwise have been purchased, shall be measured at the value to the entity.

(b) All other incoming resources from non-exchange transactions shall be measured at the **fair value** of the resources received or receivable.

Disclosure

PBE34.74 An entity shall disclose the following:

(a) the nature and amounts of resources receivable from non-exchange transactions recognised in the **financial statements**;

(b) any unfulfilled conditions or other contingencies attaching to resources from non-exchange transactions that have not been recognised in income; and

(c) an indication of other forms of resources from non-exchange transactions from which the entity has benefited.

Public Benefit Entity Combinations

PBE34.75 Paragraphs PBE34.76 to PBE34.86 apply to **public benefit entities** entering into the following **entity combinations** which involve a whole entity or parts of an entity combining with another entity:

(a) combinations at nil or nominal consideration which are in substance a gift; and

(b) combinations which meet the definition and criteria of a **merger**.

PBE34.76 Combinations which are determined to be acquisitions shall be accounted for in accordance with Section 19 *Business Combinations and Goodwill*.

Combinations that are in substance a gift

Accounting treatment and disclosure

PBE34.77 A **combination that is in substance a gift** shall be accounted for in accordance with Section 19 except for the matters addressed in paragraphs PBE34.78 and PBE34.79 below.

PBE34.78 Any excess of the **fair value** of the **assets** received over the fair value of the **liabilities** assumed is recognised as a **gain** in **income and expenditure**. This gain represents the gift of the value of one entity to another and shall be recognised as **income**.

PBE34.79 Any excess of the fair value of the liabilities assumed over the fair value of the assets received is recognised as a loss in income and expenditure. This loss represents the net obligations assumed, for which the receiving entity has not received a financial reward and shall be recognised as an **expense**.

Combinations that are a merger

PBE34.80 Unless it is not permitted by the statutory framework under which a public benefit entity reports, an entity combination that is a merger shall apply merger accounting as prescribed below. If merger accounting is not permitted, an entity combination shall be accounted for as an acquisition in accordance with Section 19.

PBE34.81 Any entity combination:

(a) which is neither a combination that is in substance a gift nor a merger; or

(b) for which merger accounting is not permitted by the statutory framework under which the public benefit entity reports

shall be accounted for as an acquisition in accordance with Section 19.

Accounting treatment

PBE34.82 Under merger accounting the carrying value of the assets and liabilities of the parties to the combination are not adjusted to fair value, although adjustments shall be made to achieve uniformity of **accounting policies** across the combining entities.

PBE34.83 The results and **cash flows** of all the combining entities shall be brought into the **financial statements** of the newly formed entity from the beginning of the financial period in which the merger occurs.

PBE34.84 The comparative amounts shall be restated by including the results for all the combining entities for the previous accounting period and their **statement of financial positions** for the previous **reporting date**. The comparative figures shall be marked as ‘combined’ figures.

PBE34.85 All costs associated with the merger shall be charged as an expense in the period incurred.

Disclosure

PBE34.86 For each entity combination accounted for as a merger in the **reporting period** the following shall be disclosed in the newly formed entity’s financial statements:

(a) the names and descriptions of the combining entities or **businesses**;

(b) the date of the merger;

(c) an analysis of the principal components of the current year’s **total comprehensive income** to indicate:

  (i) the amounts relating to the newly formed merged entity for the period after the date of the merger; and

  (ii) the amounts relating to each party to the merger up to the date of the merger.

(d) an analysis of the previous year’s total comprehensive income between each party to the merger;

(e) the aggregate carrying value of the net assets of each party to the merger at the date of the merger; and

(f) the nature and amount of any significant adjustments required to align accounting policies and an explanation of any further adjustments made to net assets as a result of the merger.

Public Benefit Entity Concessionary Loans

PBE34.87 Paragraphs PBE34.89 to PBE34.97 apply to **public benefit entity concessionary loans** within the **financial statements** of **public benefit entities** or entities within a **public benefit entity group**.

PBE34.88 Public benefit entity concessionary loans are loans made or received between a public benefit entity or an entity within the public benefit entity group, and another party at below the **prevailing market rate** of interest that are not repayable on demand and are for the purposes of furthering the objectives of the public benefit entity or public benefit entity **parent**.

Accounting treatment

PBE34.89 Entities making or receiving public benefit entity concessionary loans shall use either:

(a) the **recognition**, **measurement** and disclosure requirements in Section 11 *Basic Financial Instruments* or Section 12 *Other Financial Instruments Issues* (for example, Section 11 requires initial measurement at **fair value** and subsequent measurement at **amortised cost** using the **effective interest method**); or

(b) the accounting treatment set out in paragraphs PBE34.90 to PBE34.97 below.

A public benefit entity or an entity within a public benefit entity group shall apply the same **accounting policy** to concessionary loans both made and received.

Initial measurement

PBE34.90 A public benefit entity or an entity within a public benefit entity group making or receiving concessionary loans shall initially measure these arrangements at the amount received or paid and recognise them in the **statement of financial position**.

Subsequent measurement

PBE34.91 In subsequent years, the **carrying amount** of concessionary loans in the financial statements shall be adjusted to reflect any accrued interest payable or receivable.

PBE34.92 To the extent that a loan that has been made is irrecoverable, an **impairment loss** shall be recognised in **income and expenditure**.

Presentation and disclosure

PBE34.93 The entity shall present concessionary loans made and concessionary loans received either as a separate line items on the face of the statement of financial position or in the **notes** to the financial statements.

PBE34.94 Concessionary loans shall be presented separately between amounts repayable or receivable within one year and amounts repayable or receivable after more than one year.

PBE34.95 The entity shall disclose in its significant accounting policies the measurement basis used for concessionary loans and any other accounting policies which are relevant to the understanding of these transactions within the financial statements.

PBE34.96 The entity shall disclose the following:

(a) the terms and conditions of concessionary loan arrangements, for example the interest rate, any security provided and the terms of the repayment; and

(b) the value of concessionary loans which have been committed but not taken up at the year end.

PBE34.97 Concessionary loans made or received shall be disclosed separately. However multiple loans made or received may be disclosed in aggregate, providing that such aggregation does not obscure significant information.

Appendix A to Section 34
Guidance on funding commitments (paragraphs 34.57 to 34.63)

This appendix is an integral part of Section 34.

34A.1 Entities often make commitments to provide cash or other resources to other entities. In such a case, it is necessary to determine whether the commitment should be recognised as a liability. The definition of a liability requires that there be a present obligation, and not merely an expectation of a future outflow.

34A.2 A general statement that the entity intends to provide resources to certain classes of potential beneficiaries in accordance with its objectives does not in itself give rise to a liability, as the entity may amend or withdraw its policy, and potential beneficiaries do not have the ability to insist on their fulfilment. Similarly, a promise to provide cash conditional on the receipt of future income in itself may not give rise to a liability where the entity cannot be required to fulfil it if the future income is not received and it is probable that the economic benefits will not be transferred.

34A.3 A liability is recognised only for a commitment that gives the recipient a valid expectation that payment will be made and from which the grantor cannot realistically withdraw. One of the implications of this is that a liability only exists where the commitment has been communicated to the recipient.

34A.4 Commitments are not recognised if they are subject to performance-related conditions. In such a case, the entity is required to fulfil its commitment only when the performance-related conditions are met and no liability exists until that time.

34A.5 A commitment may contain conditions that are not performance-related conditions. For example, a requirement to provide an annual financial report to the grantor may serve mainly as an administrative tool because failure to comply would not release the grantor from its commitment. This may be distinguished from a requirement to submit a detailed report for review and consideration by the grantor of how funds will be utilised in order to secure payment. A mere restriction on the specific purpose for which funds are to be used does not in itself constitute a performance-related condition.

34A.6 For funding commitments that are not recognised, it is important that full and informative disclosures are made of their existence and of the sources of funding for these unrecognised commitments.

Appendix B to Section 34
Guidance on incoming resources from non-exchange transactions (paragraphs PBE34.64 to PBE34.74)

This appendix is an integral part of Section 34.

Recognition

PBE34B.1 The receipt of resources will usually result in an entity recognising an asset and corresponding income for the fair value of resources when those resources become received or receivable. Instances when this may differ include where:

(a) an entity received those resources in the form of services (see paragraphs PBE34B.8 to PBE34B.12); or

(b) there are performance-related conditions attached to the resources, which have yet to be fulfilled (see paragraphs PBE34B.13 to PBE34B.14).

PBE34B.2 Resources shall only be recognised when the fair value of the incoming resources can be measured reliably.

PBE34B.3 The concepts of materiality (see paragraph 2.6), and balance between benefit and cost (see paragraph 2.13) should be considered when deciding which resources received shall be recognised in the financial statements.

PBE34B.4 When it is impracticable to recognise resources from non-exchange transactions, the income is recognised in the period in which the resources are sold or distributed. The most common example is that of high volume, low value second-hand goods donated for resale.

Legacies

PBE34B.5 Donations in the form of legacies are recognised when it is probable that the legacy will be received and its value can be measured reliably. These criteria will normally be met following probate once the executor(s) of the estate has established that there are sufficient assets in the estate, after settling liabilities, to pay the legacy.

PBE34B.6 Evidence that the executor(s) has determined that a payment can be made, may arise on the agreement of the estate's accounts or notification that payment will be made. Where notification is received after the year-end but it is clear that the executor(s) has agreed prior to the year-end that the legacy can be paid, the legacy is accrued in the financial statements. The certainty and measurability of the receipt may be affected by subsequent events such as valuations and disputes.

PBE34B.7 Entities that are in receipt of numerous immaterial legacies for which individual identification would be burdensome may take a portfolio approach.

Services

PBE34B.8 Donated services that can be reasonably quantified shall be recognised in the financial statements when they are received.

PBE34B.9 Donated services that are consumed immediately are usually recognised as an expense. However, there may be circumstances when a service is used in the production of an asset, for example erecting a building. In these cases, the associated donated service (eg plumbing and electrical services) would be recognised as a part of the cost of that asset.

PBE34B.10 Donated services that can be reasonably quantified include donated facilities, such as office accommodation, services that would otherwise have been purchased and services usually provided by an individual or an entity as part of their trade or profession for a fee.

PBE34B.11 It is expected that contributions made by volunteers cannot be reasonably quantified and therefore these services shall not be recognised.

PBE34B.12 Paragraph PBE34.74(c) requires an entity to disclose other forms of resources from non-exchange transactions from which the entity has benefited. This will include the disclosure of unrecognised volunteer services.

Performance-related conditions

PBE34B.13 Some resources are given with performance-related conditions attached which require the recipient to use the resources to provide a specified level of service in order to be entitled to retain the resources. An entity will not recognise income from those resources until these performance-related conditions have been met.

PBE34B.14 However, some requirements are stated so broadly that they do not actually impose a performance-related condition on the recipient. In these cases the recipient will recognise income on receipt of the transfer of resources.

Measurement

PBE34B.15 Paragraph PBE34.73(a) requires donated services and facilities to be measured at the value to the entity. This requirement only applies to those services and facilities that would otherwise have been purchased by the entity. The value placed on these services and facilities should be the estimated value to the entity of the service or facility received, this will be the price the entity estimates it would pay in the open market for a service or facility of equivalent utility to the entity.

PBE34B.16 Paragraph PBE34.73(b) requires resources received or receivable, that are not services or facilities, to be measured at their fair value. These fair values are usually the price that the entity would have to pay on the open market for an equivalent resource.

PBE34B.17 When there is no direct evidence of an open market value for an equivalent item a value may be derived from sources such as:

(a) the cost of the item to the donor; or

(b) in the case of goods that are expected to be sold, the estimated resale value (which may reflect the amount actually realised) after deducting the cost to sell the goods.

PBE34B.18 Donated services are recognised as income and an equivalent amount shall be recognised as an expense in income and expenditure, unless the expense can be capitalised as part of the cost of an asset.

Section 35
Transition to this FRS

Scope of this section

35.1 This section applies to a **first-time adopter of this FRS**, regardless of whether its previous financial reporting framework was **adopted IFRS** or another set of generally accepted accounting principles (GAAP) such as its national accounting standards, or another framework such as the local **income tax** basis.

35.2 Notwithstanding the requirements in paragraphs 35.3 and 35.4, an entity that has applied **FRS 102** in a previous **reporting period**, but whose most recent previous annual **financial statements** did not contain an explicit and unreserved statement of compliance with this FRS, must either apply this section or else apply FRS 102 retrospectively in accordance with Section 10 *Accounting Policies, Changes in Estimates and Errors* as if the entity had never stopped applying this FRS.

First-time adoption

35.3 A first-time adopter of this FRS shall apply this section in its first financial statements that conform to this FRS.

35.4 An entity's first financial statements that conform to this FRS are the first financial statements[60] in which the entity makes an explicit and unreserved statement in those financial statements of compliance with this FRS. Financial statements prepared in accordance with this FRS are an entity's first such financial statements if, for example, the entity:

(a) did not present financial statements for previous periods;

(b) presented its most recent previous financial statements under previous UK and Republic of Ireland requirements that are not consistent with this FRS in all respects; or

(c) presented its most recent previous financial statements in conformity with adopted IFRS.

35.5 Paragraph 3.17 defines a complete set of financial statements.

35.6 Paragraph 3.14 requires an entity to disclose, in a complete set of financial statements, comparative information in respect of the preceding period for all amounts presented in the financial statements, as well as specified comparative narrative and descriptive information. An entity may present comparative information in respect of more than one preceding period. Therefore, an entity's **date of transition** to this FRS is the beginning of the earliest period for which the entity presents full comparative information in accordance with this FRS in its first financial statements that comply with this FRS.

[60] This excludes interim financial statements.

Procedures for preparing financial statements at the date of transition

35.7 Except as provided in paragraphs 35.9 to 35.11B, an entity shall, in its opening **statement of financial position** as of its date of transition to this FRS (ie the beginning of the earliest period presented):

(a) recognise all **assets** and **liabilities** whose **recognition** is required by this FRS;

(b) not recognise items as assets or liabilities if this FRS does not permit such recognition;

(c) reclassify items that it recognised under its previous financial reporting framework as one type of asset, liability or component of **equity**, but are a different type of asset, liability or component of equity under this FRS; and

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

This section does not require the opening statement of financial position to be presented.

35.8 The **accounting policies** that an entity uses in its opening statement of financial position under this FRS may differ from those that it used for the same date using its previous financial reporting framework. The resulting adjustments arise from transactions, other events or conditions before the date of transition to this FRS. Therefore, an entity shall recognise those adjustments directly in retained earnings (or, if appropriate, another category of equity) at the date of transition to this FRS.

35.9 On first-time adoption of this FRS, an entity shall not retrospectively change the accounting that it followed under its previous financial reporting framework for any of the following transactions:

(a) ***Derecognition*** *of* ***financial assets*** *and* ***financial liabilities***:

Financial assets and liabilities derecognised under an entity's previous financial reporting framework before the date of transition shall not be recognised upon adoption of this FRS. Conversely, for financial assets and liabilities that would have been derecognised under this FRS in a transaction that took place before the date of transition, but that were not derecognised under an entity's previous financial reporting framework, an entity may choose:

(i) to derecognise them on adoption of this FRS; or

(ii) to continue to recognise them until disposed of or settled.

(b) [Deleted]

(c) *Accounting estimates*.

(d) [Deleted]

(e) *Measuring* ***non-controlling interests***:

The requirements:

(i) to allocate **profit or loss** and **total comprehensive income** between non-controlling interest and **owners** of the **parent**;

(ii) for accounting for changes in the parent's ownership interest in a **subsidiary** that do not result in a loss of **control**; and

(iii) for accounting for a loss of control over a subsidiary

shall be applied **prospectively** from the date of transition to this FRS (or from such earlier date as this FRS is applied to restate **business combinations** – see paragraph 35.10(a)).

35.10 An entity may use one or more of the following exemptions in preparing its first financial statements that conform to this FRS:

(a) ***Business combinations, including group reconstructions***

A first-time adopter may elect not to apply Section 19 *Business Combinations and Goodwill* to business combinations that were effected before the date of transition to this FRS. However, if a first-time adopter restates any business combination to comply with Section 19, it shall restate all later business combinations. If a first-time adopter does not apply Section 19 retrospectively, the first-time adopter shall recognise and measure all its assets and liabilities acquired or assumed in a past business combination at the date of transition to this FRS in accordance with paragraphs 35.7 to 35.9 or if applicable, with paragraphs 35.10(b) to (v) except for:

(i) **intangible assets** other than **goodwill** – intangible assets subsumed within goodwill shall not be separately recognised; and

(ii) goodwill – no adjustment shall be made to the carrying value of goodwill.

(b) ***Share-based payment transactions***

A first-time adopter is not required to apply Section 26 *Share-based Payment* to equity instruments (including the equity component of **share-based payment transactions** previously treated as compound instruments) that were granted before the date of transition to this FRS, or to liabilities arising from share-based payment transactions that were settled before the date of transition to this FRS. Except that a first-time adopter previously applying FRS 20 *(IFRS 2) Share-based Payment* or IFRS 2 *Share-based Payment* shall, in relation to equity instruments (including the equity component of share-based payment transactions previously treated as compound instruments) that were granted before the date of transition to this FRS, apply either FRS 20/IFRS 2 (as applicable) or Section 26 of this FRS at the date of transition.

In addition, for a **small entity** that first adopts this FRS for an accounting period that commences before 1 January 2017, this exemption is extended to equity instruments that were granted before the start of the first reporting period that complies with this FRS, provided that the small entity did not previously apply FRS 20 or IFRS 2.

A small entity that chooses to apply this exemption shall provide disclosures in accordance with paragraph 1AC.31.

(c) ***Fair value as deemed cost***

A first-time adopter may elect to measure an:

(i) item of **property, plant and equipment**;

(ii) **investment property**; or

(iii) intangible asset which meets the recognition criteria and the criteria for revaluation in Section 18 *Intangible Assets other than Goodwill*

on the date of transition to this FRS at its **fair value** and use that fair value as its **deemed cost** at that date.

(d) ***Revaluation as deemed cost***

A first-time adopter may elect to use a revaluation determined under its previous financial reporting framework of an:

(i) item of property, plant and equipment;

(ii) investment property; or

(iii) intangible asset which meets the recognition criteria and the criteria for revaluation in Section 18

at, or before, the date of transition to this FRS as its deemed cost at the revaluation date.

(e) [Deleted]

(f) ***Individual and separate financial statements***

When an entity prepares individual or **separate financial statements**, paragraphs 9.26, 14.4 and 15.9 require the entity to account for its investments in subsidiaries, **associates**, and **jointly controlled entities** either at cost less impairment or at fair value.

If a first-time adopter measures such an investment at cost, it shall measure that investment at one of the following amounts in its individual or separate opening statement of financial position, as appropriate, prepared in accordance with this FRS:

(i) cost determined in accordance with Section 9 *Consolidated and Separate Financial Statements*, Section 14 *Investments in Associates* or Section 15 *Investments in Joint Ventures* at the date of transition; or

(ii) deemed cost, which shall be the **carrying amount** at the date of transition as determined under the entity's previous financial reporting framework.

(g) ***Compound financial instruments***

Paragraph 22.13 requires an entity to split a **compound financial instrument** into its liability and equity components at the date of issue. A first-time adopter need not separate those two components if the liability component is not outstanding at the date of transition to this FRS.

(h) [Deleted]

(i) ***Service concession arrangements – Accounting by operators***

A first-time adopter is not required to apply paragraphs 34.12I to 34.16A to **service concession arrangements** that were entered into before the date of transition to this FRS. Such service concession arrangements shall continue to be accounted for using the same accounting policies being applied at the date of transition to this FRS.

(j) ***Extractive activities***

A first-time adopter that under its previous financial reporting framework accounted for exploration and development costs for oil and gas properties in the development or production phases, in cost centres that included all properties in a large geographical area may elect to measure oil and gas assets at the date of transition to this FRS on the following basis:

(i) Exploration and evaluation assets at the amount determined under the entity's previous financial reporting framework.

(ii) Assets in the development or production phases at the amount determined for the cost centre under the entity's previous financial reporting framework. The entity shall allocate this amount to the cost centre's underlying assets pro rata using reserve volumes or reserve values as of that date.

The entity shall test exploration and evaluation assets and assets in the development and production phases for impairment at the date of transition to this FRS in accordance with Section 34 *Specialised Activities* or Section 27 *Impairment of Assets* of this FRS respectively, and if necessary, reduce the amount determined in accordance with (i) or (ii) above. For the purposes of this paragraph, oil and gas assets comprise only those assets used in the exploration, evaluation, development or production of oil and gas.

(k) ***Arrangements containing a lease***

A first-time adopter may elect to determine whether an arrangement existing at the date of transition to this FRS contains a **lease** (see paragraph 20.3A) on the basis of facts and circumstances existing at that date, rather than when the arrangement was entered into.

(l) ***Decommissioning liabilities included in the cost of property, plant and equipment***

Paragraph 17.10(c) states that the cost of an item of property, plant and equipment includes the initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located, the obligation for which an entity incurs either when the item is acquired or as a consequence of having used the item during a particular period for purposes other than to produce **inventories** during that period. A first-time adopter may elect to measure this component of the cost of an item of property, plant and equipment at the date of transition to this FRS, rather than on the date(s) when the obligation initially arose.

(m) ***Dormant companies***

A company within the Companies Act definition of a dormant company may elect to retain its accounting policies for reported assets, liabilities and equity at the date of transition to this FRS until there is any change to those balances or the company undertakes any new transactions.

(n) ***Deferred development costs as a deemed cost***

A first-time adopter may elect to measure the carrying amount at the date of transition to this FRS for **development** costs deferred in accordance with SSAP 13 *Accounting for* research *and development* as its deemed cost at that date.

(o) ***Borrowing costs***

An entity electing to adopt an accounting policy of capitalising **borrowing costs** as part of the cost of a **qualifying asset** may elect to treat the date of transition to this FRS as the date on which capitalisation commences.

(p) ***Lease incentives***

A first-time adopter is not required to apply paragraphs 20.15A and 20.25A to **lease incentives** provided the term of the lease commenced before the date of transition to this FRS. The first-time adopter shall continue to recognise any residual benefit or cost associated with these lease incentives on the same basis as that applied at the date of transition to this FRS.

(q) ***Public benefit entity combinations***

A first-time adopter may elect not to apply paragraphs PBE34.75 to PBE34.86 relating to **public benefit entity combinations** to combinations that were effected before the date of transition to this FRS. However, if on first-time adoption a **public benefit entity** restates any entity combination to comply with this section, it shall restate all later entity combinations.

(r) ***Assets and liabilities of subsidiaries, associates and joint ventures***

If a subsidiary becomes a first-time adopter later than its parent, the subsidiary shall in its financial statements measure its assets and liabilities at either:

(i) the carrying amounts that would be included in the parent's **consolidated financial statements**, based on the parent's date of transition to this

FRS, if no adjustments were made for consolidation procedures and for the effects of the business combination in which the parent acquired the subsidiary; or

(ii) the carrying amounts required by the rest of this FRS, based on the subsidiary's date of transition to this FRS. These carrying amounts could differ from those described in (i) when:

(a) the exemptions in this FRS result in measurements that depend on the date of transition to this FRS; or

(b) the accounting policies used in the subsidiary's financial statements differ from those in the consolidated financial statements. For example, the subsidiary may use as its accounting policy the cost model in Section 17 *Property, Plant and Equipment*, whereas the **group** may use the revaluation model.

A similar election is available to an associate or **joint venture** that becomes a first-time adopter later than an entity that has **significant influence** or **joint control** over it.

However, if an entity becomes a first-time adopter later than its subsidiary (or associate or joint venture) the entity shall, in its consolidated financial statements, measure the assets and liabilities of the subsidiary (or associate or joint venture) at the same carrying amounts as in the financial statements of the subsidiary (or associate or joint venture), after adjusting for consolidation (and equity accounting) adjustments and for the effects of the business combination in which the entity acquired the subsidiary (or transaction in which it acquired the associate or joint venture). Similarly, if a parent becomes a first-time adopter for its separate financial statements earlier or later than for its consolidated financial statements, it shall measure its assets and liabilities at the same amounts in both financial statements, except for consolidation adjustments.

(s) ***Designation of previously recognised financial instruments***

This FRS permits a **financial instrument** (provided it meets certain criteria) to be designated on initial recognition as a financial asset or financial liability at fair value through profit or loss. Despite this an entity is permitted to designate, as at the date of transition to this FRS, any financial asset or financial liability at fair value through profit or loss provided the asset or liability meets the criteria in paragraph 11.14(b) at that date.

(t) ***Hedge accounting***

(i) ***A hedging relationship existing on the date of transition***

A first-time adopter may choose to apply hedge accounting to a hedging relationship of a type described in paragraph 12.19 which exists on the date of transition between a **hedging instrument** and a **hedged item**, provided the conditions of paragraphs 12.18(a) to (c) are met on the date of transition to this FRS and the conditions of paragraphs 12.18(d) and (e) are met no later than the date the first financial statements that comply with this FRS are authorised for issue. This choice applies to each hedging relationship existing on the date of transition.

Hedge accounting as set out in Section 12 *Other Financial Instruments Issues* of this FRS may commence from a date no earlier than the conditions of paragraphs 12.18(a) to (c) are met. In a fair value hedge the cumulative **hedging gain or loss** on the hedged item from the date hedge accounting commenced to the date of transition, shall be recognised in retained earnings (or if appropriate, another category of equity). In a cash flow hedge and net investment hedge, the lower of the following (in absolute amounts) shall be recognised in equity (in respect of cash flow hedges in the cash flow hedge reserve):

(a) the cumulative gain or loss on the hedging instrument from the date hedge accounting commenced to the date of transition; and

(b) the cumulative change in fair value (ie the **present value** of the cumulative change of expected future **cash flows**) on the hedged item from the date hedge accounting commenced to the date of transition.

(ii) ***A hedging relationship that ceased to exist before the date of transition because the hedging instrument has expired, was sold, terminated or exercised prior to the date of transition***

A first-time adopter may elect not to adjust the carrying amount of an asset or liability for previous financial reporting framework effects of a hedging relationship that has ceased to exist.

A first-time adopter may elect to account for amounts deferred in equity in a cash flow hedge under a previous financial reporting framework, as described in paragraph 12.23(d) from the date of transition. Any amounts deferred in equity in relation to a hedge of a **net investment in a foreign operation** under a previous financial reporting framework shall not be reclassified to profit or loss on disposal or partial disposal of the **foreign operation**.

(iii) ***A hedging relationship that commenced after the date of transition***

A first-time adopter may elect to apply hedge accounting to a hedging relationship of a type described in paragraph 12.19 that commenced after the date of transition between a hedging instrument and a hedged item, starting from the date the conditions of paragraphs 12.18(a) to (c) are met, provided that the conditions of paragraphs 12.18(d) and (e) are met no later than the date the first financial statements that comply with this FRS are authorised for issue.

The choice applies to each hedging relationship that commenced after the date of transition.

(iv) ***Entities taking the accounting policy choice under paragraphs 11.2(b) or (c) or paragraphs 12.2(b) or (c) to apply IAS 39 Financial Instruments: Recognition and Measurement or IFRS 9 Financial Instruments***

A first-time adopter adopting an accounting policy set out in paragraphs 11.2(b) or (c) or paragraphs 12.2(b) or (c) shall not apply the transitional provisions of paragraphs (i) to (iii) above. Such a first-time adopter shall apply the transitional requirements applicable to hedge accounting in IFRS 1 *First–time adoption of International Financial Reporting Standards*, paragraphs B4 to B6, except that the designation and documentation of a hedging relationship may be completed after the date of transition, and no later than the date the first financial statements that comply with this FRS are authorised for issue, if the hedging relationship is to qualify for hedge accounting from the date of transition.

A first-time adopter adopting an accounting policy set out in paragraphs 11.2(b) or (c) or paragraphs 12.2(b) or (c) that has entered into a hedging relationship as described in IAS 39 or IFRS 9 in the period between the date of transition and the **reporting date** for the first financial statements that comply with this FRS may elect to apply hedge accounting prospectively from the date all qualifying conditions for hedge accounting in IAS 39 *Financial Instruments: Recognition and*

Measurement or IFRS 9 *Financial Instruments* are met, except that an entity shall complete the formal designation and documentation of a hedging relationship no later than the date the first financial statements that comply with this FRS are authorised for issue.

(u) ***Small entities – fair value measurement of financial instruments***

A small entity that first adopts this FRS for an accounting period that commences before 1 January 2017 need not restate comparative information to comply with the fair value measurement requirements of Section 11 *Basic Financial Instruments* or Section 12, unless those financial instruments were measured at fair value in accordance with the small entity's previous financial reporting framework.

A small entity that chooses to present comparative information that does not comply with the fair value measurement requirements of Sections 11 and 12 in its first year of adoption:

(a) shall apply its existing accounting policies to the relevant financial instruments in the comparative information and is encouraged to disclose this fact;

(b) shall disclose the accounting policies applied (in accordance with paragraph 1AC.3); and

(c) shall treat any adjustment between the statement of financial position at the comparative period's reporting date and the statement of financial position at the start of the first reporting period that complies with Sections 11 and 12 as an adjustment, in the current reporting period, to opening equity.

(v) ***Small entities – financing transactions involving related parties***

A small entity that first adopts this FRS for an accounting period that commences before 1 January 2017 need not restate comparative information to comply with the requirements of paragraph 11.13 only insofar as they related to financing transactions involving **related parties**.

A small entity that chooses to present comparative information that does not comply with the financing transaction requirements of Section 11 in its first year of adoption:

(a) shall apply its existing accounting policies to the relevant financial instruments in the comparative information and is encouraged to disclose this fact;

(b) shall disclose the accounting policies applied (in accordance with paragraph 1AC.3); and

(c) shall treat any adjustment between the statement of financial position at the comparative period's reporting date and the statement of financial position at the start of the first reporting period that complies with paragraph 11.13 as an adjustment, in the current reporting period, to opening equity. The present value of the financial asset or financial liability at the start of the first reporting period that complies with this FRS may be determined on the basis of the facts and circumstances existing at that date, rather than when the arrangement was entered into.

35.11 If it is **impracticable** for an entity to make one or more of the adjustments required by paragraph 35.7 at the date of transition, the entity shall apply paragraphs 35.7 to 35.10 for such adjustments in the earliest period for which it is practicable to do so, and shall identify which amounts in the financial statements have not been restated. If it is impracticable for an entity to provide any disclosures required by this FRS for any period before the period in which it prepares its first financial statements that conform to this FRS, the omission shall be disclosed.

35.11A Where applicable to the transactions, events or arrangements affected by applying these exemptions, an entity may continue to use the exemptions that are applied at the date of transition to this FRS when preparing subsequent financial statements, until such time when the assets and liabilities associated with those transactions, events or arrangements are derecognised.

35.11B When there is subsequently a significant change in the circumstances or conditions associated with transactions, events or arrangements that existed at the date of transition, to which an exemption has been applied, an entity shall reassess the appropriateness of applying that exemption in preparing subsequent financial statements in order to maintain a true and fair view in accordance with Section 3 *Financial Statement Presentation*.

Disclosures

Explanation of transition to this FRS

35.12 An entity shall explain how the transition from its previous financial reporting framework to this FRS affected its reported **financial position** and financial **performance**.

35.12A An entity that has applied this FRS in a previous reporting period but not in its most recent annual financial statements, as described in paragraph 35.2, shall disclose:

(a) the reason it stopped applying this FRS;

(b) the reason it is resuming the application of this FRS; and

(c) whether it has applied this section or has applied this FRS retrospectively in accordance with Section 10.

Reconciliations

35.13 To comply with paragraph 35.12, an entity's first financial statements prepared using this FRS shall include:

(a) A description of the nature of each change in accounting policy.

(b) Reconciliations of its equity determined in accordance with its previous financial reporting framework to its equity determined in accordance with this FRS for both of the following dates:

  (i) the date of transition to this FRS; and

  (ii) the end of the latest period presented in the entity's most recent annual financial statements determined in accordance with its previous financial reporting framework.

(c) A reconciliation of the profit or loss determined in accordance with its previous financial reporting framework for the latest period in the entity's most recent annual financial statements to its profit or loss determined in accordance with this FRS for the same period.

35.14 If an entity becomes aware of **errors** made under its previous financial reporting framework, the reconciliations required by paragraphs 35.13(b) and (c) shall, to the extent practicable, distinguish the correction of those errors from changes in accounting policies.

35.15 If an entity did not present financial statements for previous periods, it shall disclose that fact in its first financial statements that conform to this FRS.

Appendix I
Glossary

This appendix is an integral part of this FRS.

accounting policies	The specific principles, bases, conventions, rules and practices applied by an entity in preparing and presenting **financial statements**.
accrual basis (of accounting)	The effects of transactions and other events are recognised when they occur (and not as **cash** or its equivalent is received or paid) and they are recorded in the accounting records and reported in the **financial statements** of the periods to which they relate.
accumulating compensated absences	Compensated absences that are carried forward and can be used in future periods if the current period's entitlement is not used in full.
acquisition date	The date on which the acquirer obtains **control** of the acquiree.
Act	The Companies Act 2006
active market	A market in which all the following conditions exist: (a) the items traded in the market are homogeneous; (b) willing buyers and sellers can normally be found at any time; and (c) prices are available to the public.
actuarial assumptions	An entity's unbiased and mutually compatible best estimates of the demographic and financial variables that will determine the ultimate cost of providing **post-employment benefits**.
actuarial gains and losses	Changes in the **present value** of the **defined benefit obligation** resulting from: (a) experience adjustments (the effects of differences between the previous **actuarial assumptions** and what has actually occurred); and (b) the effects of changes in actuarial assumptions.
adopted IFRS	**IFRS** that have been adopted in the relevant jurisdiction. In the UK, this refers to **UK-adopted international accounting standards**. In the Republic of Ireland, this refers to **EU-adopted IFRS**.
agent	An entity is acting as an agent when it does not have exposure to the significant risks and rewards associated with the sale of goods or the rendering of services. One feature indicating that an entity is acting as an agent is that the amount the entity earns is predetermined, being either a fixed fee per transaction or a stated percentage of the amount billed to the customer.
agricultural activity	The management by an entity of the biological transformation of **biological assets** for sale, into **agricultural produce** or into additional biological assets.

agricultural produce	The harvested product of the entity's **biological assets**.
amortisation	The systematic allocation of the **depreciable amount** of an **asset** over its **useful life**.
amortised cost (of a financial asset or financial liability)	The amount at which the **financial asset** or **financial liability** is measured at initial **recognition** minus principal repayments, plus or minus the cumulative **amortisation** using the **effective interest method** of any difference between that initial amount and the maturity amount, and minus any reduction (directly or through the use of an allowance account) for impairment or uncollectability.
asset	A resource controlled by the entity as a result of past events and from which future economic benefits are expected to flow to the entity.
asset held by a long-term employee benefit fund	An **asset** (other than non-transferable **financial instruments** issued by the reporting entity) that: (a) is held by an entity (a fund) that is legally separate from the reporting entity and exists solely to pay or fund **employee benefits**; and (b) is available to be used only to pay or fund employee benefits, is not available to the reporting entity's own creditors (even in bankruptcy), and cannot be returned to the reporting entity, unless either: (i) the remaining assets of the fund are sufficient to meet all the related employee benefit obligations of the plan or the reporting entity; or (ii) the assets are returned to the reporting entity to reimburse it for employee benefits already paid.
associate	An entity, including an unincorporated entity such as a partnership, over which the investor has **significant influence** and that is neither a **subsidiary** nor an interest in a **joint venture**.
biological asset	A living animal or plant.
borrowing costs	Interest and other costs incurred by an entity in connection with the borrowing of funds.
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.
business combination	The bringing together of separate entities or **businesses** into one reporting entity.

carrying amount	The amount at which an **asset** or **liability** is recognised in the **statement of financial position**.
cash	Cash on hand and demand deposits.
cash equivalents	Short-term, highly liquid investments that are readily convertible to known amounts of **cash** and that are subject to an insignificant risk of changes in value.
cash flows	Inflows and outflows of **cash** and **cash equivalents**.
cash-generating unit	The smallest identifiable group of **assets** that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets.
cash-settled share-based payment transaction	A **share-based payment transaction** in which the entity acquires goods or services by incurring a **liability** to transfer **cash** or other **assets** to the supplier of those goods or services for amounts that are based on the price (or value) of the **equity** instruments (including shares and **share options**) of the entity or another **group** entity.
change in accounting estimate	An adjustment of the **carrying amount** of an **asset** or a **liability**, or the amount of the periodic consumption of an asset, that results from the assessment of the present status of, and expected future benefits and obligations associated with, assets and liabilities. Changes in accounting estimates result from new information or new developments and, accordingly, are not corrections of **errors**.
class of assets	A grouping of **assets** of a similar nature and use in an entity's operations.
close members of the family of a person	Those family members who may be expected to influence, or be influenced by, that person in their dealings with the entity including: (a) that person's children and spouse or domestic partner; (b) children of that person's spouse or domestic partner; and (c) dependants of that person or that person's spouse or domestic partner.
closing rate	The spot exchange rate at the end of the **reporting period**.
combination that is in substance a gift	A combination carried out at nil or nominal consideration that is not a **fair value** exchange but in substance the gift of one entity to another.
commencement of lease term	The date from which the lessee is entitled to exercise its right to use the leased asset. It is the date of initial **recognition** of the **lease** (ie the recognition of the **assets**, **liabilities**, **income** or **expenses** resulting from the lease, as appropriate).
component of an entity	Operations and **cash flows** that can be clearly distinguished, operationally and for financial reporting purposes, from the rest of the entity.
compound financial instrument	A **financial instrument** that, from the issuer's perspective, contains both a **liability** and an **equity** element.

consolidated financial statements	The **financial statements** of a **parent** and its **subsidiaries** presented as those of a single economic entity.
construction contract	A contract specifically negotiated for the construction of an **asset** or a combination of assets that are closely interrelated or interdependent in terms of their design, technology and function or their ultimate purpose or use.
constructive obligation	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.
contingent asset	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.
contingent liability	A contingent liability is either: (a) a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity; or (b) a present obligation that arises from past events but is not recognised because: (i) it is not **probable** that an outflow of resources embodying economic benefits will be required to settle the obligation; or (ii) the amount of the obligation cannot be measured with sufficient **reliability**.
contingent rent	That portion of the lease payments that is not fixed in amount but is based on the future amount of a factor that changes other than with the passage of time (eg percentage of future sales, amount of future use, future price indices, and future market rates of interest).
control (of an entity)	The power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.
credit risk	The risk that one party to a **financial instrument** will cause a financial loss for the other party by failing to discharge an obligation.
current assets	**Assets** of an entity which: (a) for an entity choosing to apply paragraph 1A(1) of Schedule 1 to the **Regulations**, are not **non-current assets**; or (b) for all other entities, are not **fixed assets**.

current liabilities (for the purposes of an entity applying paragraph 1A(1) of Schedule 1 to the Regulations)	**Liabilities** of the entity which: (a) it expects to settle in its normal operating cycle; (b) it holds primarily for the purpose of trading; (c) are due to be settled within 12 months after the **reporting period**; or (d) it does not have an unconditional right to defer settlement for at least 12 months after the reporting period.
current tax	The amount of **income tax** payable (refundable) in respect of the **taxable profit (tax loss)** for the current period or past **reporting periods**.
date of transition	The beginning of the earliest period for which an entity presents full comparative information in a given standard in its first **financial statements** that comply with that standard.
deemed cost	An amount used as a surrogate for cost or depreciated cost at a given date. Subsequent **depreciation** or **amortisation** assumes that the entity had initially recognised the **asset** or **liability** at the given date and that its cost was equal to the deemed cost.
deferred acquisition costs	Costs arising from the conclusion of **insurance contracts** that are incurred during a **reporting period** but which relate to a subsequent reporting period.
deferred tax	**Income tax** payable (recoverable) in respect of the **taxable profit (tax loss)** for future **reporting periods** as a result of past transactions or events.
deferred tax assets	**Income tax** recoverable in future **reporting periods** in respect of: (a) future tax consequences of transactions and events recognised in the **financial statements** of the current and previous periods; (b) the carry forward of unused tax losses; and (c) the carry forward of unused tax credits.
deferred tax liabilities	**Income tax** payable in future **reporting periods** in respect of future tax consequences of transactions and events recognised in the **financial statements** of the current and previous periods.
defined benefit obligation (present value of)	The **present value**, without deducting any **plan assets**, of expected future payments required to settle the obligation resulting from employee service in the current and prior periods.
defined benefit plans	**Post-employment benefit plans** other than **defined contribution plans**.
defined contribution plans	**Post-employment benefit plans** under which an entity pays fixed contributions into a separate entity (a fund) and has no legal or **constructive obligation** to pay further contributions or to make direct benefit payments to employees if the fund does not hold sufficient **assets** to pay all **employee benefits** relating to employee service in the current and prior periods.

depreciable amount	The cost of an **asset**, or other amount substituted for cost (in the **financial statements**), less its **residual value**.
depreciated replacement cost	The most economic cost required for the entity to replace the **service potential** of an **asset** (including the amount that the entity will receive from its disposal at the end of its **useful life**) at the **reporting date**.
depreciation	The systematic allocation of the **depreciable amount** of an **asset** over its **useful life**.
derecognition	The removal of a previously recognised **asset** or **liability** from an entity's **statement of financial position**.
derivative	A **financial instrument** or other contract with all three of the following characteristics: (a) its value changes in response to the change in a specified interest rate, financial instrument price, commodity price, foreign exchange rate, index of prices or rates, credit rating or credit index, or other variable (sometimes called the 'underlying'), provided in the case of a non-financial variable that the variable is not specific to a party to the contract; (b) it requires no initial net investment or an initial net investment that is smaller than would be required for other types of contracts that would be expected to have a similar response to changes in market factors; and (c) it is settled at a future date.
development	The application of **research** findings or other knowledge to a plan or design for the production of new or substantially improved materials, devices, products, processes, systems or services before the start of commercial production or use.
discontinued operation	A **component of an entity** that has been disposed of and: (a) represented a separate major line of **business** or geographical area of operations; (b) was part of a single co-ordinated plan to dispose of a separate major line of business or geographical area of operations; or (c) was a **subsidiary** acquired exclusively with a view to resale.
discretionary participation feature	A contractual right to receive, as a supplement to guaranteed benefits, additional benefits: (a) that are likely to be a significant portion of the total contractual benefits; (b) whose amount or timing is contractually at the discretion of the issuer; and (c) that are contractually based on: (i) the performance of a specified pool of contracts or a specified type of contract; (ii) realised and/or unrealised investment returns on a specified pool of **assets** held by the issuer; or (iii) the **profit or loss** of the company, fund or other entity that issues the contract.

disposal group	A group of **assets** to be disposed of, by sale or otherwise, together as a group in a single transaction, and **liabilities** directly associated with those assets that will be transferred in the transaction. The group includes **goodwill** acquired in a **business combination** if the group is a **cash-generating unit** to which goodwill has been allocated in accordance with the requirements of paragraphs 27.24 to 27.27 of this FRS.
effective interest method	A method of calculating the **amortised cost** of a **financial asset** or a **financial liability** (or a group of financial assets or financial liabilities) and of allocating the interest income or interest expense over the relevant period.
effective interest rate	The rate that exactly discounts estimated future cash payments or receipts through the expected life of the **financial instrument** or, when appropriate, a shorter period to the **carrying amount** of the **financial asset** or **financial liability**.
employee benefits	All forms of consideration given by an entity in exchange for service rendered by employees.
entity combination	See **business combination**.
equity	The residual interest in the **assets** of the entity after deducting all its **liabilities**.
equity-settled share-based payment transaction	A **share-based payment transaction** in which the entity: (a) receives goods or services as consideration for its own equity instruments (including shares or **share options**); or (b) receives goods or services but has no obligation to settle the transaction with the supplier.
errors	Omissions from, and misstatements in, the entity's **financial statements** for one or more prior periods arising from a failure to use, or misuse of, reliable information that: (a) was available when financial statements for those periods were authorised for issue; and (b) could reasonably be expected to have been obtained and taken into account in the preparation and presentation of those financial statements.
EU-adopted IFRS	**IFRS** that have been adopted in the European Union in accordance with EU Regulation 1606/2002.
expenses	Decreases in economic benefits during the **reporting period** in the form of outflows or depletions of **assets** or incurrences of **liabilities** that result in decreases in **equity**, other than those relating to distributions to equity investors.
fair value	The amount for which an **asset** could be exchanged, a **liability** settled, or an equity instrument granted could be exchanged, between knowledgeable, willing parties in an arm's length transaction. In the absence of any specific guidance provided in the relevant section of this FRS, the guidance in the Appendix to Section 2 *Concepts and Pervasive Principles* shall be used in determining fair value.

fair value less costs to sell	The amount obtainable from the sale of an **asset** or **cash-generating unit** in an arm's length transaction between knowledgeable, willing parties, less the costs of disposal.
finance lease	A **lease** that transfers substantially all the risks and rewards incidental to ownership of an **asset**. Title may or may not eventually be transferred. A lease that is not a finance lease is an **operating lease**.
financial asset	Any **asset** that is: (a) **cash**; (b) an equity instrument of another entity; (c) a contractual right: (i) to receive cash or another financial asset from another entity, or (ii) to exchange financial assets or **financial liabilities** with another entity under conditions that are potentially favourable to the entity; or (d) a contract that will or may be settled in the entity's own equity instruments and is: (i) a non-derivative for which the entity is or may be obliged to receive a variable number of the entity's own equity instruments; or (ii) a **derivative** that will or may be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the entity's own equity instruments. For this purpose the entity's own equity instruments do not include instruments that are themselves contracts for the future receipt or delivery of the entity's own equity instruments.
financial guarantee contract	A contract that requires the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due in accordance with the original or modified terms of a debt instrument.
financial institution	Any of the following: (a) a bank which is: (i) a firm with a Part 4A permission[61] which includes accepting deposits and: (a) which is a credit institution; or (b) whose Part 4A permission includes a requirement that it complies with the rules in the General Prudential sourcebook and the Prudential sourcebook for Banks, Building Societies and Investment Firms relating to banks, but which is not a building society, a friendly society or a credit union; (ii) an EEA bank which is a full credit institution;

[61] As defined in section 55A of the *Financial Services and Markets Act 2000* or references to equivalent provisions of any successor legislation.

	(b) a building society which is defined in section 119(1) of the Building Societies Act 1986 as a building society incorporated (or deemed to be incorporated) under that act; (c) a credit union, being a body corporate registered under the Co-operative and Community Benefit Societies Act 2014 as a credit union in accordance with the Credit Unions Act 1979, which is an authorised person; (d) a custodian bank or broker-dealer; (e) an entity that undertakes the **business** of effecting or carrying out **insurance contracts**, including general and life assurance entities; (f) an incorporated friendly society incorporated under the Friendly Societies Act 1992 or a registered friendly society registered under section 7(1)(a) of the Friendly Societies Act 1974 or any enactment which it replaced, including any registered branches; (g) an investment trust, Irish investment company, venture capital trust, mutual fund, exchange traded fund, unit trust, open-ended investment company (OEIC); or (h) [Deleted] (i) any other entity whose principal activity is similar to those listed above but is not specifically included in that list. A **parent** entity whose sole activity is to hold investments in other **group** entities is not a financial institution.
financial instrument	A contract that gives rise to a **financial asset** of one entity and a **financial liability** or equity instrument of another entity.
financial liability	Any **liability** that is: (a) a contractual obligation: (i) to deliver **cash** or another **financial asset** to another entity; or (ii) to exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavourable to the entity; or (b) a contract that will or may be settled in the entity's own equity instruments and is: (i) a non-derivative for which the entity is or may be obliged to deliver a variable number of the entity's own equity instruments; or (ii) a **derivative** that will or may be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the entity's own equity instruments. For this purpose the entity's own equity instruments do not include instruments that are themselves contracts for the future receipt or delivery of the entity's own equity instruments.
financial position	The relationship of the **assets**, **liabilities** and **equity** of an entity as reported in the **statement of financial position**.

financial risk	The risk of a possible future change in one or more of a specified interest rate, **financial instrument** price, commodity price, foreign exchange rate, index of prices or rates, credit rating or credit index or other variable, provided in the case of a non-financial variable that the variable is not specific to a party to the contract.
financial statements	Structured representation of the **financial position**, financial **performance** and **cash flows** of an entity.
financing activities	Activities that result in changes in the size and composition of the contributed **equity** and borrowings of the entity.
firm commitment	A binding agreement for the exchange of a specified quantity of resources at a specified price on a specified future date or dates.
first-time adopter of this FRS	An entity that presents its first annual **financial statements** that conform to this FRS, regardless of whether its previous financial reporting framework was **adopted IFRS** or another set of accounting standards.
fixed assets	**Assets** of an entity which are intended for use on a continuing basis in the entity's activities.
forecast transaction	An uncommitted but anticipated future transaction.
foreign operation	An entity that is a **subsidiary**, **associate**, **joint venture** or branch of a reporting entity, the activities of which are based or conducted in a country or currency other than those of the reporting entity.
FRS 100	FRS 100 *Application of Financial Reporting Requirements*
FRS 101	FRS 101 *Reduced Disclosure Framework*
FRS 102	FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland*
FRS 103	FRS 103 *Insurance Contracts*
FRS 104	FRS 104 *Interim Financial Reporting*
FRS 105	FRS 105 *The Financial Reporting Standard applicable to the Micro-entities Regime*
functional currency	The currency of the primary economic environment in which the entity operates.
funding (of post-employment benefits)	Contributions by an entity, and sometimes its employees, into an entity, or fund, that is legally separate from the reporting entity and from which the **employee benefits** are paid.
gains	Increases in economic benefits that meet the definition of **income** but are not **revenue**.

general purpose financial statements (generally referred to simply as financial statements)	**Financial statements** directed to the general financial information needs of a wide range of users who are not in a position to demand reports tailored to meet their particular information needs.
going concern	An entity is a going concern unless management either intends to liquidate the entity or to cease trading, or has no realistic alternative but to do so.
goodwill	Future economic benefits arising from **assets** that are not capable of being individually identified and separately recognised.
government grant	Assistance by government in the form of a transfer of resources to an entity in return for past or future compliance with specified conditions relating to the **operating activities** of the entity. Government refers to government, government agencies and similar bodies whether local, national or international.
grant date	The date at which the entity and another party (including an employee) agree to a **share-based payment arrangement**, being when the entity and the counterparty have a shared understanding of the terms and conditions of the arrangement. At grant date the entity confers on the counterparty the right to **cash**, other **assets**, or equity instruments of the entity, provided the specified **vesting conditions**, if any, are met. If that agreement is subject to an approval process (for example, by shareholders), grant date is the date when that approval is obtained.
gross investment in a lease	The aggregate of: (a) the **minimum lease payments** receivable by the lessor under a **finance lease**; and (b) any unguaranteed **residual value** accruing to the lessor.
group	A **parent** and all its **subsidiaries**.
group reconstruction	Any one of the following arrangements: (a) the transfer of an equity holding in a **subsidiary** from one group entity to another; (b) the addition of a new **parent** entity to a **group**; (c) the transfer of equity holdings in one or more subsidiaries of a group to a new entity that is not a group entity but whose equity holders are the same as those of the group's parent; (d) the combination into a group of two or more entities that before the combination had the same equity holders; (e) the transfer of the **business** of one group entity to another; or (f) the transfer of the business of one group entity to a new entity that is not a group entity but those equity holders are the same as those of the group's parent.

hedging gain or loss	The change in **fair value** of a hedged item that is attributable to the hedged risk.
held as part of an investment portfolio	An interest is held as part of an investment portfolio if its value to the investor is through **fair value** as part of a directly or indirectly held basket of investments rather than as media through which the investor carries out **business**. A basket of investments is indirectly held if an investment fund holds a single investment in a second investment fund which, in turn, holds a basket of investments. In some circumstances, it may be appropriate for a single investment to be considered an investment portfolio, for example when an investment fund it first being established and is expected to acquire additional investments.
held exclusively with a view to subsequent resale	An interest: (a) for which a purchaser has been identified or is being sought, and which is reasonably expected to be disposed of within approximately one year of its date of acquisition; or (b) that was acquired as a result of the enforcement of a security, unless the interest has become part of the continuing activities of the **group** or the holder acts as if it intends the interest to become so; or (c) which is **held as part of an investment portfolio**.
heritage assets	Tangible and **intangible assets** with historic, artistic, scientific, technological, geophysical, or environmental qualities that are held and maintained principally for their contribution to knowledge and culture.
highly probable	Significantly more likely than **probable**.
IAS / IFRS	Standards and interpretations issued (or adopted) by the International Accounting Standards Board (IASB). They comprise: (a) International Financial Reporting Standards; (b) International Accounting Standards; and (c) Interpretations developed by the IFRS Interpretations Committee (Interpretations Committee) (IFRIC) or the former Standing Interpretations Committee (SIC).
IAS Regulation	EU Regulation 1606/2002
impairment loss	The amount by which the **carrying amount** of an **asset** exceeds: (a) in the case of **inventories**, its selling price less costs to complete and sell; or (b) in the case of other assets, its **recoverable amount**.
impracticable	Applying a requirement is impracticable when the entity cannot apply it after making every reasonable effort to do so.
imputed rate of interest	The more clearly determinable of either: (a) the prevailing rate for a similar instrument of an issuer with a similar credit rating; or

	(b) a rate of interest that discounts the nominal amount of the instrument to the current cash sales price of the goods or services.
inception of the lease	The earlier of the date of the **lease** agreement and the date of commitment by the parties to the principal provisions of the lease.
income	Increases in economic benefits during the **reporting period** in the form of inflows or enhancements of **assets** or decreases of **liabilities** that result in increases in **equity**, other than those relating to contributions from equity investors.
income and expenditure	The total of **income** less **expenses**, excluding the components of **other comprehensive income**. In the for-profit sector this is known as **profit or loss.**
income statement	**Financial statement** that presents all items of **income** and **expense** recognised in a **reporting period**, excluding the items of **other comprehensive income** (referred to as the profit and loss account in the **Act**).
income tax	All domestic and foreign taxes that are based on **taxable profits**. Income tax also includes taxes, such as withholding taxes, that are payable by a **subsidiary**, **associate** or **joint venture** on distributions to the reporting entity.
individual financial statements	The accounts that are required to be prepared by an entity in accordance with the **Act** or relevant legislation, for example: (a) 'individual accounts', as set out in section 394 of the Act; (b) 'statement of accounts', as set out in section 132 of the Charities Act 2011; or (c) 'individual accounts', as set out in section 72A of the Building Societies Act 1986. **Separate financial statements** are included in the meaning of this term.
infrastructure assets	Infrastructure for public services, such as roads, bridges, tunnels, prisons, hospitals, airports, water distribution facilities, energy supply and telecommunications networks.
insurance contract	A contract under which one party (the insurer) accepts significant insurance risk from another party (the policyholder) by agreeing to compensate the policyholder if a specified uncertain future event (the insured event) adversely affects the policyholder.
intangible asset	An identifiable non-monetary **asset** without physical substance. Such an asset is identifiable when: (a) it is separable, ie capable of being separated or divided from the entity and sold, transferred, licensed, rented or exchanged, either individually or together with a related contract, asset or **liability**; or (b) it arises from contractual or other legal rights, regardless of whether those rights are transferable or separable from the entity or from other rights and obligations.

interest rate implicit in the lease	The discount rate that, at the **inception of the lease**, causes the aggregate **present value** of: (a) the **minimum lease payments**; and (b) the unguaranteed **residual value** to be equal to the sum of: (i) the **fair value** of the leased **asset**; and (ii) any initial direct costs of the lessor.
interim financial report	A financial report containing either a complete set of **financial statements** or a set of condensed financial statements for an **interim period**.
interim period	A financial **reporting period** shorter than a full financial year.
intrinsic value	The difference between the **fair value** of the shares to which the counterparty has the (conditional or unconditional) right to subscribe or which it has the right to receive, and the price (if any) the counterparty is (or will be) required to pay for those shares. For example, a **share option** with an exercise price of CU15, on a share with a fair value of CU20, has an intrinsic value of CU5.
inventories	**Assets**: (a) held for sale in the ordinary course of **business**; (b) in the process of production for such sale; or (c) in the form of materials or supplies to be consumed in the production process or in the rendering of services.
inventories held for distribution at no or nominal consideration	**Assets** that are: (a) held for distribution at no or nominal consideration in the ordinary course of operations; (b) in the process of production for distribution at no or nominal consideration in the ordinary course of operations; or (c) in the form of material or supplies to be consumed in the production process or in the rendering of services at no or nominal consideration.
investing activities	The acquisition and disposal of long-term assets and other investments not included in **cash equivalents**.
investment property	Property (land or a building, or part of a building, or both) held by the owner or by the lessee under a **finance lease** to earn rentals or for capital appreciation or both, rather than for: (a) use in the production or supply of goods or services or for administrative purposes, or (b) sale in the ordinary course of **business**.
joint control	The contractually agreed sharing of **control** over an economic activity. It exists only when the strategic financial and operating decisions relating to the activity require the unanimous consent of the parties sharing control (the **venturers**).

joint venture	A contractual arrangement whereby two or more parties undertake an economic activity that is subject to **joint control**. Joint ventures can take the form of jointly controlled operations, jointly controlled assets, or **jointly controlled entities**.
jointly controlled entity	A **joint venture** that involves the establishment of a corporation, partnership or other entity in which each **venturer** has an interest. The entity operates in the same way as other entities, except that a contractual arrangement between the venturers establishes **joint control** over the economic activity of the entity.
key management personnel	Those persons having authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly, including any director (whether executive or otherwise) of that entity.
lease	An agreement whereby the lessor conveys to the lessee in return for a payment or series of payments the right to use an **asset** for an agreed period of time.
lease incentives	Incentives provided by the lessor to the lessee to enter into a new or renew an **operating lease**. Examples of such incentives include up-front cash payments to the lessee, the reimbursement or assumption by the lessor of costs of the lessee (such as relocation costs, leasehold improvements and costs associated with pre-existing lease commitments of the lessee), or initial periods of the **lease** provided by the lessor rent-free or at a reduced rent.
lease term	The non-cancellable period for which the lessee has contracted to **lease** the **asset** together with any further terms for which the lessee has the option to continue to lease the asset, with or without further payment, when at the **inception of the lease** it is reasonably certain that the lessee will exercise the option.
lessee's incremental borrowing rate (of interest)	The rate of interest the lessee would have to pay on a similar **lease** or, if that is not determinable, the rate that, at the **inception of the lease**, the lessee would incur to borrow over a similar term, and with a similar security, the funds necessary to purchase the **asset**.
liability	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.
liquidity risk	The risk that an entity will encounter difficulty in meeting obligations associated with **financial liabilities** that are settled by delivering **cash** or another **financial asset**.
LLP Regulations	The Large and Medium-sized Limited Liability Partnerships (Accounts) Regulations 2008 (SI 2008/1913)
loans payable	**Financial liabilities** other than short-term trade payables on normal credit terms.
market vesting condition	A condition upon which the exercise price, vesting or exercisability of an equity instrument depends that is related to the market price of the entity's equity instruments, such as attaining a specified share price or a specified amount of **intrinsic value** of a **share option**, or achieving a specified target that is based on the market price of the entity's

	equity instruments relative to an index of market prices of equity instruments of other entities.
market risk	The risk that the **fair value** or future **cash flows** of a **financial instrument** will fluctuate because of changes in market prices. Market risk comprises three types of risk: currency risk, interest rate risk and other price risk. Interest rate risk – the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. Currency risk – the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. Other price risk – the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices (other than those arising from interest rate risk or currency risk), whether those changes are caused by factors specific to the financial instrument or its issuer, or factors affecting all similar financial instruments traded in the market.
material	Omissions or misstatements of items are material if they could, individually or collectively, influence the economic decisions of users taken on the basis of the **financial statements**. Materiality depends on the size and nature of the omission or misstatement judged in the surrounding circumstances. The size or nature of the item, or a combination of both, could be the determining factor.
measurement	The process of determining the monetary amounts at which the elements of the **financial statements** are to be recognised and carried in the **statement of financial position** and **statement of comprehensive income**.
merger	An **entity combination** that results in the creation of a new reporting entity formed from the combining parties, in which the controlling parties of the combining entities come together in a partnership for the mutual sharing of risks and benefits of the newly formed entity and in which no party to the combination in substance obtains **control** over any other, or is otherwise seen to be dominant. All of the following criteria must be met for an entity combination to meet the definition of a merger: (a) no party to the combination is portrayed as either acquirer or acquiree, either by its own board or management or by that of another party to the combination; (b) there is no significant change to the classes of beneficiaries of the combining entities or the purpose of the benefits provided as a result of the combination; and (c) all parties to the combination, as represented by the members of the board, participate in establishing the management structure of the combined entity and in selecting the management personnel, and such decisions are made on the basis of a consensus between the parties to the combination rather than purely by exercise of voting rights.

minimum lease payments	The payments over the **lease term** that the lessee is or can be required to make, excluding **contingent rent**, costs for services and taxes to be paid by and reimbursed to the lessor, together with: (a) for a lessee, any amounts guaranteed by the lessee or by a party related to the lessee; or (b) for a lessor, any **residual value** guaranteed to the lessor by: (i) the lessee; (ii) a party related to the lessee; or (iii) a third party unrelated to the lessor that is financially capable of discharging the obligations under the guarantee. However, if the lessee has an option to purchase the **asset** at a price that is expected to be sufficiently lower than **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, the minimum lease payments comprise the minimum payments payable over the lease term to the expected date of exercise of this purchase option and the payment required to exercise it.
monetary items	Units of currency held and **assets** and **liabilities** to be received or paid in a fixed or determinable number of units of currency.
multi-employer (benefit) plans	**Defined contribution plans** (other than **state plans**) or **defined benefit plans** (other than state plans) that: (a) pool the **assets** contributed by various entities that are not under common control, and (b) use those assets to provide benefits to employees of more than one entity, on the basis that contribution and benefit levels are determined without regard to the identity of the entity that employs the employees concerned.
net assets available for benefits	The **assets** of a plan less **liabilities** other than the actuarial **present value** of promised retirement benefits.
net debt	Net debt consists of the borrowings of an entity, together with any related **derivatives** and obligations under **finance leases**, less any **cash** and **cash equivalents**.
net defined benefit liability	The **present value** of the **defined benefit obligation** at the **reporting date** minus the **fair value** at the reporting date of **plan assets** (if any) out of which the obligations are to be settled.
net investment in a foreign operation	The amount of the reporting entity's interest in the net assets of that operation.
net investment in a lease	The **gross investment in a lease** discounted at the **interest rate implicit in the lease**.
non-controlling interest	The **equity** in a **subsidiary** not attributable, directly or indirectly, to a **parent**.

non-current assets	**Assets** of the entity which: (a) it does not expect to realise, or intend to sell or consume, in its normal operating cycle; (b) it does not hold primarily for the purpose of trading; (c) it does not expect to realise within 12 months after the **reporting period**; or (d) are **cash** or **cash equivalents** restricted from being exchanged or used to settle a **liability** for at least 12 months after the reporting period.
non-current liabilities	**Liabilities** of the entity which are not **current liabilities.**
non-exchange transaction	A transaction whereby an entity receives value from another entity without directly giving approximately equal value in exchange, or gives value to another entity without directly receiving approximately equal value in exchange.
notes (to financial statements)	Notes contain information in addition to that presented in the **statement of financial position**, **statement of comprehensive income**, **income statement** (if presented), combined **statement of income and retained earnings** (if presented), **statement of changes in equity** and **statement of cash flows**. Notes provide narrative descriptions or disaggregations of items presented in those statements and information about items that do not qualify for **recognition** in those statements.
objective of financial statements	To provide information about the **financial position**, **performance** and, when required to be presented, **cash flows** of an entity that is useful for economic decision-making by a broad range of users who are not in a position to demand reports tailored to meet their particular information needs.
onerous contract	A contract in which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it.
operating activities	The principal revenue-producing activities of the entity and other activities that are not investing or **financing activities**.
operating lease	A **lease** that does not transfer substantially all the risks and rewards incidental to ownership. A lease that is not an operating lease is a **finance lease**.
operating segment	An operating segment is a **component of an entity**: (a) that engages in **business** activities from which it may earn **revenues** and incur **expenses** (including revenues and expenses relating to transactions with other components of the same entity); (b) whose operating results are regularly reviewed by the entity's chief operating decision maker to make decisions about resources to be allocated to the segment and assess its **performance**; and (c) for which discrete financial information is available.

ordinary share	An equity instrument that is subordinate to all other classes of equity instrument.
other comprehensive income	Items of **income** and **expense** (including reclassification adjustments) that are not recognised in **profit or loss** as required or permitted by this FRS or by law.
owners	Holders of instruments classified as **equity**.
parent	An entity that has one or more **subsidiaries**.
performance	The relationship of the **income** and **expenses** of an entity, as reported in the **statement of comprehensive income**.
performance condition (in respect of share-based payment arrangements)	A **vesting condition** that requires: (a) the counterparty to complete a specified period of service (ie a **service condition**); the service requirement can be explicit or implicit; and (b) specified performance target(s) to be met while the counterparty is rendering the service required in (a). The period of achieving the performance target(s): (a) shall not extend beyond the end of the service period; and (b) may start before the service period on the condition that the commencement date of the performance target is not substantially before the commencement of the service period. A performance target is defined by reference to: (a) the entity's own operations (or activities) or the operations or activities of another entity in the same **group** (ie a non-market condition); or (b) the price (or value) of the entity's **equity instruments** or the equity instruments of another entity in the same group (including shares and **share options**) (ie a **market condition**). A performance target might relate either to the performance of the entity as a whole or to some part of the entity (or part of the group), such as a division or an individual employee.
performance-related condition (in respect of funding commitments)	A condition that requires the performance of a particular level of service or units of output to be delivered, with payment of, or entitlement to, the resources conditional on that performance.
permanent differences	Differences between an entity's **taxable profits** and its **total comprehensive income** as stated in the **financial statements**, other than **timing differences**.
plan assets (of an employee benefit plan)	Plan assets (of an employee benefit plan) are: (a) **assets held by a long-term employee benefit fund**; and (b) **qualifying insurance policies**.

post-employment benefits	**Employee benefits** (other than **termination benefits** and short-term employee benefits) that are payable after the completion of employment.
post-employment benefit plans	Formal or informal arrangements under which an entity provides **post-employment benefits** for one or more employees.
potential ordinary share	A **financial instrument** or other contract that may entitle its holder to **ordinary shares**.
present value	A current estimate of the present discounted value of the future net **cash flows** in the normal course of **business**.
presentation currency	The currency in which the **financial statements** are presented.
prevailing market rate	The rate of interest that would apply to the entity in an open market for a similar **financial instrument**.
principal	An entity is acting as a principal when it has exposure to the significant risks and rewards associated with the sale of goods or the rendering of services. Features that indicate that an entity is acting as a principal include: (a) the entity has the primary responsibility for providing the goods or services to the customer or for fulfilling the order, for example by being responsible for the acceptability of the products or services ordered or purchased by the customer; (b) the entity has **inventory** risk before or after the customer order, during shipping or on return; (c) the entity has latitude in establishing prices, either directly or indirectly, for example by providing additional goods or services; and (d) the entity bears the customer's **credit risk** for the amount receivable from the customer.
probable	More likely than not.
profit or loss	The total of **income** less **expenses**, excluding the components of **other comprehensive income**.
projected unit credit method	An actuarial valuation method that sees each period of service as giving rise to an additional unit of benefit entitlement and measures each unit separately to build up the final obligation (sometimes known as the accrued benefit method pro-rated on service or as the benefit/years of service method).
property, plant and equipment	Tangible assets that: (a) are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes, and (b) are expected to be used during more than one period.
prospectively (applying a change in accounting policy)	Applying the new **accounting policy** to transactions, other events and conditions occurring after the date as at which the policy is changed.

provision	A **liability** of uncertain timing or amount.
prudence	The inclusion of a degree of caution in the exercise of the judgements 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.
public benefit entity	An entity whose primary objective is to provide goods or services for the general public, community or social benefit and where any **equity** is provided with a view to supporting the entity's primary objectives rather than with a view to providing a financial return to equity providers, shareholders or members.[62]
public benefit entity concessionary loan	A loan made or received between a **public benefit entity** or an entity within a **public benefit entity group** and another party: (a) at below the **prevailing market rate** of interest; (b) that is not repayable on demand; and (c) is for the purposes of furthering the objectives of the public benefit entity or public benefit entity **parent**.
public benefit entity group	A **public benefit entity parent** and all of its wholly-owned **subsidiaries**.
publicly traded (debt or equity instruments)	Traded, or in process of being issued for trading, in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets).
qualifying asset	An **asset** that necessarily takes a substantial period of time to get ready for its intended use or sale. Depending on the circumstances any of the following may be qualifying assets: (a) **inventories**; (b) manufacturing plants; (c) power generation facilities; (d) **intangible assets**; and (e) **investment properties**. **Financial assets**, and inventories that are produced over a short period of time, are not qualifying assets. Assets that are ready for their intended use or sale when acquired are not qualifying assets.

[62] The term 'public benefit entity' does not necessarily imply that the purpose of the entity is for the benefit of the public as a whole. For example, many PBEs exist for the direct benefit of a particular group of people, although it is possible that society as a whole also benefits indirectly. The important factor is what the primary purpose of such an entity is, and that it does not exist primarily to provide economic benefit to its investors. Organisations such as mutual insurance companies, other mutual co-operative entities and clubs that provide dividends or other economic benefits directly and proportionately to their owners, members or participants are not PBEs.

Some PBEs undertake certain activities that are intended to make a surplus in order to fund their primary activities. Consideration should be given to the primary purpose of an entity's (or group's) activities in assessing whether it meets the definition of a PBE.

PBEs may have received contributions in the form of equity, even though the entity does not have a primary profit motive. However, because of the fundamental nature of public benefit entities, any such contributions are made by the equity holders of the entity primarily to enable the provision of goods or services to beneficiaries rather than with a view to a financial return for themselves. This is different from the position of lenders; loans do not fall into the category of equity.

qualifying entity (for the purposes of this FRS)	A member of a **group** where the **parent** of that group prepares publicly available **consolidated financial statements** which are intended to give a true and fair view (of the **assets**, **liabilities**, **financial position** and **profit or loss**) and that member is included in the consolidation[63].
qualifying insurance policies	An insurance policy[64] issued by an insurer that is not a **related party** of the reporting entity, if the proceeds of the policy: (a) can be used only to pay or fund **employee benefits** under a **defined benefit plan**; and (b) are not available to the reporting entity's own creditors (even in bankruptcy) and cannot be paid to the reporting entity, unless either: (i) the proceeds represent surplus **assets** that are not needed for the policy to meet all the related employee benefit obligations; or (ii) the proceeds are returned to the reporting entity to reimburse it for employee benefits already paid.
recognition	The process of incorporating in the **statement of financial position** or **statement of comprehensive income** an item that meets the definition of an **asset**, **liability**, **equity**, **income** or **expense** and satisfies the following criteria: (a) it is **probable** that any future economic benefit associated with the item will flow to or from the entity; and (b) the item has a cost or value that can be measured with **reliability**.
recoverable amount	The higher of an **asset's** (or **cash-generating unit's**) **fair value less costs to sell** and its value in use.
Regulations	The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (SI 2008/410)
reinsurance contract	An **insurance contract** issued by one insurer (the reinsurer) to compensate another insurer (the cedant) for losses on one or more contracts issued by the cedant.
related party	A related party is a person or entity that is related to the entity that is preparing its **financial statements** (the reporting entity). (a) A person or a **close member of that person's family** is related to a reporting entity if that person: (i) has **control** or **joint control** over the reporting entity; (ii) has **significant influence** over the reporting entity; or (iii) is a member of the **key management personnel** of the reporting entity or of a **parent** of the reporting entity.

[63] As set out in section 474(1) of the Act.
[64] A qualifying insurance policy is not necessarily an insurance contract.

	(b) An entity is related to a reporting entity if any of the following conditions apply: (i) the entity and the reporting entity are members of the same **group** (which means that each parent, **subsidiary** and fellow subsidiary is related to the others). (ii) one entity is an **associate** or **joint venture** of the other entity (or of a member of a group of which the other entity is a member). (iii) both entities are joint ventures of the same third entity. (iv) one entity is a joint venture of a third entity and the other entity is an associate of the third entity. (v) the entity is a **post-employment benefit plan** for the benefit of employees of either the reporting entity or an entity related to the reporting entity. If the reporting entity is itself such a plan, the sponsoring employers are also related to the reporting entity. (vi) the entity is controlled or jointly controlled by a person identified in (a). (vii) a person identified in (a)(i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity). (viii) the entity, or any member of a group of which it is a part, provides key management personnel services to the reporting entity or to the parent of the reporting entity.
related party transaction	A transfer of resources, services or obligations between a reporting entity and a **related party**, regardless of whether a price is charged.
relevance	The quality of information that allows it to influence the economic decisions of users by helping them evaluate past, present or future events or confirming, or correcting, their past evaluations.
reliability	The quality of information that makes it free from **material error** and bias and represents faithfully that which it either purports to represent or could reasonably be expected to represent.
reporting date	The end of the latest period covered by **financial statements** or by an **interim financial report**.
reporting period	The period covered by **financial statements** or by an **interim financial report**.
research	Original and planned investigation undertaken with the prospect of gaining new scientific or technical knowledge and understanding.
residual value (of an asset)	The estimated amount that an entity would currently obtain from disposal of an **asset**, after deducting the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its **useful life**.
restriction	A requirement that limits or directs the purposes for which a resource may be used that does not meet the definition of a **performance-related condition**.

restructuring	A restructuring is a programme that is planned and controlled by management and materially changes either: (a) the scope of a **business** undertaken by an entity; or (b) the manner in which that business is conducted.
retirement benefit plan	Arrangements whereby an entity provides benefits for employees on or after termination of service (either in the form of an annual **income** or as a lump sum) when such benefits, or the contributions towards them, can be determined or estimated in advance of retirement from the provisions of a document or from the entity's practice.
retrospective application (of an accounting policy)	Applying a new **accounting policy** to transactions, other events and conditions as if that policy had always been applied.
revenue	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.
separate financial statements	Those presented by a **parent** in which the investments in **subsidiaries**, **associates** or **jointly controlled entities** are accounted for either at cost or **fair value** rather than on the basis of the reported results and net assets of the investees. Separate financial statements are included within the meaning of **individual financial statements**.
service concession arrangement	An arrangement whereby a public sector body or a **public benefit entity** (the grantor) contracts with a private sector entity (the operator) to construct (or upgrade), operate and maintain **infrastructure assets** for a specified period of time (the concession period).
service condition	A **vesting condition** that requires the counterparty to complete a specified period of service during which services are provided to the entity. If the counterparty, regardless of the reason, ceases to provide service during the **vesting period**, it has failed to satisfy the condition. A service condition does not require a performance target to be met.
service potential	The capacity to provide services that contribute to achieving an entity's objectives. Service potential enables an entity to achieve its objectives without necessarily generating net cash inflows.
share-based payment	The equity instruments (including shares and **share options**), **cash** or other **assets** to which a counterparty may become entitled in a **share-based payment transaction**.
share-based payment arrangement	An agreement between the entity (or another **group** entity or any shareholder of any group entity) and another party (including an employee) that entitles the other party to receive: (a) **cash** or other **assets** of the entity for amounts that are based on the price (or value) of equity instruments (including shares or **share options**) of the entity or another group entity; or (b) equity instruments (including shares or share options) of the entity or another group entity, provided the specified **vesting conditions**, if any, are met.

share-based payment transaction	A transaction in which the entity: (a) receives goods or services from the supplier of those goods or services (including an employee) in a **share-based payment arrangement**; or (b) incurs an obligation to settle the transaction with the supplier in a share-based payment arrangement when another **group** entity receives those goods or services.
share option	A contract that gives the holder the right, but not the obligation, to subscribe to the entity's shares at a fixed or determinable price for a specific period of time.
significant influence	Significant influence is the power to participate in the financial and operating policy decisions of the **associate** but is not **control** or **joint control** over those policies.
Small Companies Regulations	The Small Companies and Groups (Accounts and Directors' Report) Regulations 2008 (SI 2008/409)
small entity	A small entity is: (a) a company meeting the definition of a small company as set out in section 382 or 383 of the **Act**[65], and not excluded from the small companies regime by section 384 of the Act; (b) an LLP qualifying as small and not excluded from the small LLPs regime, as set out in **LLP Regulations**; or (c) any other entity that would have met the criteria in (a) had it been a company incorporated under company law.
Small LLP Regulations	The Small Limited Liability Partnership (Accounts) Regulations 2008 (SI 2008/1912)
Statement of Recommended Practice (SORP)	An extant Statement of Recommended Practice developed in accordance with *Policy on Developing Statements of Recommended Practice (SORPs)*. SORPs recommend accounting practices for specialised industries or sectors. They supplement accounting standards and other legal and regulatory requirements in the light of the special factors prevailing or transactions undertaken in a particular industry or sector.
state	A national, regional, or local government.
state (employee benefit) plan	Employee benefit plans established by legislation to cover all entities (or all entities in a particular category, for example a specific industry) and operated by national, regional or local government or by another body (for example an autonomous agency created specifically for this purpose) which is not subject to control or influence by the reporting entity.

[65] Irish small entities (including qualifying partnerships that are required to comply with Part 6 of the *Companies Act 2014*, in accordance with the *European Union (Qualifying Partnerships: Accounting and Auditing) Regulations 2019* (SI No. 597 of 2019)) shall refer to sections 280A and 280B of the *Companies Act 2014*.

statement of cash flows	**Financial statement** that provides information about the changes in **cash** and **cash equivalents** of an entity for a period, showing separately changes during the period from operating, investing and **financing activities**.
statement of comprehensive income	**Financial statement** that presents all items of **income** and **expense** recognised in a period, including those items recognised in determining **profit or loss** (which is a subtotal in the statement of comprehensive income) and items of **other comprehensive income**. If an entity chooses to present both an **income statement** and a statement of comprehensive income, the statement of comprehensive income begins with profit or loss and then displays the items of other comprehensive income.
statement of financial position	**Financial statement** that presents the relationship of an entity's **assets**, **liabilities** and **equity** as of a specific date (referred to as the balance sheet in the **Act**).
statement of income and retained earnings	**Financial statement** that presents the **profit or loss** and changes in retained earnings for a **reporting period**.
subsidiary	An entity, including an unincorporated entity such as a partnership, that is **controlled** by another entity (known as the **parent**).
substantively enacted	Tax rates shall be regarded as substantively enacted when the remaining stages of the enactment process historically have not affected the outcome and are unlikely to do so. A UK tax rate shall be regarded as having been substantively enacted if it is included in either: (a) a Bill that has been passed by the House of Commons and is awaiting only passage through the House of Lords and Royal Assent; or (b) a resolution having statutory effect that has been passed under the Provisional Collection of Taxes Act 1968. (Such a resolution could be used to collect taxes at a new rate before that rate has been enacted. In practice, corporation tax rates are now set a year ahead to avoid having to invoke the Provisional Collection of Taxes Act for the quarterly payment system.) A Republic of Ireland tax rate can be regarded as having been substantively enacted if it is included in a Bill that has been passed by the Dáil.
tax expense	The aggregate amount included in **total comprehensive income** or **equity** for the **reporting period** in respect of **current tax** and **deferred tax**.
taxable profit (tax loss)	The profit (loss) for a **reporting period** upon which **income taxes** are payable or recoverable, determined in accordance with the rules established by the taxation authorities. Taxable profit equals taxable income less amounts deductible from taxable income.

termination benefits	**Employee benefits** provided in exchange for the termination of an employee's employment as a result of either: (a) an entity's decision to terminate an employee's employment before the normal retirement date; or (b) an employee's decision to accept voluntary redundancy in exchange for those benefits.
timing differences	Differences between **taxable profits** and **total comprehensive income** as stated in the **financial statements** that arise from the inclusion of **income** and **expenses** in tax assessments in periods different from those in which they are recognised in financial statements.
timeliness	Providing the information in **financial statements** within the decision time frame.
total comprehensive income	The change in **equity** during a period resulting from transactions and other events, other than those changes resulting from transactions from equity participants (equal to the sum of **profit or loss** and **other comprehensive income**).
transaction costs (financial instruments)	Incremental costs that are directly attributable to the acquisition, issue or disposal of a **financial asset** or **financial liability**, or the issue or reacquisition of an entity's own equity instrument. An incremental cost is one that would not have been incurred if the entity had not acquired, issued or disposed of the financial asset or financial liability, or had not issued or reacquired its own equity instrument.
treasury shares	An entity's own equity instruments, held by that entity or other members of the consolidated **group**.
turnover	The amounts derived from the provision of goods and services after deduction of: (a) trade discounts; (b) value added tax; and (c) any other taxes based on the amounts so derived.
UK-adopted international accounting standards	**IAS** that have been adopted for use within the UK in accordance with the International Accounting Standards and European Public Limited-Liability Company (Amendment etc.) (EU Exit) Regulations 2019 (SI 2019/685).
understandability	The presentation of information in a way that makes it comprehensible by users who have a reasonable knowledge of **business** and economic activities and accounting and a willingness to study the information with reasonable diligence.
useful life	The period over which an **asset** is expected to be available for use by an entity or the number of production or similar units expected to be obtained from the asset by an entity.
value in use	The **present value** of the future **cash flows** expected to be derived from an **asset** or **cash-generating unit**.

value in use (in respect of assets held for their service potential)	When the future economic benefits of an **asset** are not primarily dependent on the asset's ability to generate net cash inflows, **value in use** (in respect of assets held for their **service potential**) is the **present value** to the entity of the asset's remaining service potential if it continues to be used, plus the net amount that the entity will receive from its disposal at the end of its **useful life**.
venturer	A party to a **joint venture** that has **joint control** over that joint venture.
vest	Become an entitlement. Under a **share-based payment arrangement**, a counterparty's right to receive **cash**, other **assets** or equity instruments of the entity vests when the counterparty's entitlement is no longer conditional on the satisfaction of any **vesting conditions**.
vested benefits	Benefits, the rights to which, under the conditions of a **retirement benefit plan**, are not conditional on continued employment.
vesting conditions	The conditions that determine whether the entity receives the services that entitle the counterparty to receive **cash**, other **assets** or equity instruments of the entity, under a **share-based payment arrangement**. Vesting conditions are either **service conditions** or **performance conditions**.
vesting period	The period during which all the specified **vesting conditions** of a **share-based payment arrangement** are to be satisfied.

Appendix II
Table of equivalence for company law terminology

The following table compares both UK and Irish company law terminology with broadly equivalent terminology used in FRS 102.

Company law terminology	**FRS 102 terminology**
Accounting reference date	Reporting date
Accounts	Financial statements
Associated undertaking	Associate
Balance sheet	Statement of financial position
Capital and reserves	Equity
Cash at bank and in hand	Cash[66]
Debtors	Trade receivables
Diminution in value [of assets]	Impairment
Entity [financial statements]	Individual [financial statements]
Financial year	Reporting period
Financial year end date	Reporting date
Group [accounts/ financial statements]	Consolidated [financial statements]
Holding undertaking	Parent
IAS/IFRS	Adopted IFRS
Individual [accounts]	Individual [financial statements]
Interest payable and similar expenses	Finance costs
Interest receivable and similar income	Finance income/Investment income
Minority interests	Non-controlling interest
Net realisable value [of any current asset]	Estimated selling price less costs to complete and sell
Parent undertaking	Parent
Profit and loss account	Income statement (under the two-statement approach) Part of the statement of comprehensive income (under the single-statement approach)
Related undertakings[67]	Subsidiaries, associates and joint ventures
Stocks	Inventories
Subsidiary undertaking	Subsidiary
Tangible assets	Includes: Property, plant equipment; Investment property
Trade creditors	Trade payables

[66] FRS 102 requires the cash flow statement to reconcile the movement in 'cash and cash equivalents'. Disclosure is required of reconciliation between amounts presented in the statement of financial position (ie cash) and 'cash and cash equivalents'.

[67] This would also include entities in which a company has at least a 20 per cent holding, but which are not a subsidiary, joint venture or an associate. A shareholding of 20 per cent is presumed to give significant influence to the holder, such that the investment would be classified as an associate, therefore in practice there are unlikely to be many related undertakings that are not subsidiaries, joint ventures or associates.

Appendix III
Note on legal requirements

Introduction

A3.1 This appendix provides an overview of how the requirements in FRS 102 address United Kingdom company law requirements. It is therefore written from the perspective of a company to which the *Companies Act 2006* applies.[68] Appendix IV discusses the Republic of Ireland legal references.

A3.2 Many entities that are not constituted as companies apply accounting standards promulgated by the FRC for the purposes of preparing financial statements that present a true and fair view[69]. A brief consideration of the legal framework for some other entities can be found at A3.41 and A3.42. For those entities that are within the scope of a Statement of Recommended Practice (SORP), the relevant SORP will provide more details on the legal framework.

A3.3 References to the Act in this appendix are to the *Companies Act 2006*. References to the Regulations are to *The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008* (SI 2008/410). References to specific provisions are to Schedule 1 to the Regulations; entities applying Schedules 2, 3 or 6 should read them as referring to the equivalent paragraph in those schedules; and small entities applying the Small Companies Regulations should read them as referring to the equivalent paragraph in Schedule 1 to the Small Companies Regulations. Similar provisions generally also apply to limited liability partnerships applying the Small LLP Regulations or the LLP Regulations.

Applicable accounting framework

A3.4 Group accounts of certain parent entities (those with securities admitted to trading on a UK regulated market on their balance sheet date) are required by section 403(1) of the Act to be prepared in accordance with UK-adopted international accounting standards.[70]

A3.5 All other entities, except those that are eligible to apply FRS 105 *The Financial Reporting Standard applicable to the Micro-entities Regime*, must apply[71] either FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland*, UK-adopted international accounting standards or FRS 101 *Reduced Disclosure Framework* (if the financial statements are the individual financial statements of a qualifying entity eligible to apply FRS 101).

A3.6 Section 395(1) of the Act states:

'A company's individual accounts may be prepared—

(a) in accordance with section 396 ("Companies Act individual accounts"), or

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[68] Some charities are also companies, and are therefore required to apply the requirements of both the *Companies Act 2006* and the *Charities Act 2011*.

[69] More information about the 'true and fair' concept can be found on the FRC website.

[70] Group accounts of Irish parent entities, with securities admitted to trading on a regulated market in an EU Member State on their balance sheet date, are required by Article 4 of EU Regulation 1606/2002 (IAS Regulation) to be prepared in accordance with EU-adopted IFRS.

[71] Under company law in the Republic of Ireland, certain entities are permitted to prepare 'Companies Act financial statements' under a financial reporting framework based on accounting standards other than those issued by the FRC. Please refer to Appendix IV for further details.

(b) in accordance with international accounting standards ("IAS individual accounts").'

Section 403(2) of the Act states:

'The group accounts of other companies may be prepared—

(a) in accordance with section 404 ("Companies Act group accounts"), or

(b) in accordance with international accounting standards ("IAS group accounts").'

A3.7 Accounts prepared in accordance with FRS 102 are classified as either 'Companies Act individual accounts', including those of qualifying entities applying FRS 102, or 'Companies Act group accounts' and are therefore required to comply with the applicable provisions of Parts 15 and 16 of the Act and with the Regulations.

Consistency of financial reporting within groups

A3.8 Section 407 of the Act requires that the directors of the parent company secure that individual accounts of a parent company and each of its subsidiaries are prepared using the same financial reporting framework, except to the extent that in the directors' opinion there are good reasons for not doing so.

In addition, consistency is not required in the following situations:

(a) when the parent company does not prepare consolidated financial statements; or

(b) when some subsidiaries are charities (consistency is not needed between the framework used for these and for other subsidiaries).

Where the directors of a parent company prepare IAS group accounts and IAS individual accounts, there only has to be consistency across the individual financial statements of the subsidiaries.

A3.9 All companies, other than those which elect or are required to prepare IAS individual accounts in accordance with the Act, prepare Companies Act individual accounts.

A3.9A When a group includes insurers, the fact that some group entities are excluded from the scope of FRS 101 may be a factor that the directors take into account when considering whether there are good reasons for not preparing all subsidiary accounts using the same financial reporting framework.

Application of FRS 102

Compliance with company law

A3.10 The FRS has been developed for application in the UK and Republic of Ireland, using the IFRS for SMEs as a basis. Part of that development process included making amendments to the IFRS for SMEs to ensure compliance with the Act and the Regulations. For example, changes were made to eliminate options that are not permitted by company law. However, FRS 102 is not intended to be a one-stop-shop for all accounting and legal requirements, and although the FRC believes FRS 102 is not inconsistent with company law, compliance with FRS 102 alone will often be insufficient to ensure compliance with all the disclosure requirements set out in the Act and the Regulations. As a result preparers will continue to be required to have regard to the requirements of company law in addition to accounting standards.

A3.11 This appendix does not list every legal requirement, but instead focuses on those areas where greater judgement might be required in determining compliance with the law.

Small companies

A3.11A The definition of a small company is contained in sections 382 and 383 of the Act; certain companies are excluded from the small companies regime by section 384. Subject to certain conditions and exclusions, the qualifying conditions are met by a company in a year in which it does not exceed two or more of the following criteria:

(a)	Turnover	£10.2 million
(b)	Balance sheet total	£5.1 million
(c)	Average number of employees	50

A3.11B A parent company qualifies as a small company in relation to a financial year only if the group that it heads qualifies as small (as set out in section 383 of the Act).

A3.11C The Small Companies Regulations set out the small companies regime. Although FRS 102 was developed on the basis of the Regulations (which apply to large and medium-sized companies) the recognition and measurement requirements of FRS 102 should also be consistent with the Small Companies Regulations.

A3.11D In accordance with section 393 of the Act the directors of any company, including a small company, must not approve accounts unless they are satisfied that they give a true and fair view of the assets, liabilities, financial position and profit or loss of the company. In order to achieve this, a company, including a small company, may need to provide disclosures additional to those required by company law. In relation to small companies, paragraph 1A.16 of FRS 102 reflects this requirement and paragraph 1A.17 encourages a small company to consider all other disclosures in FRS 102 to determine any additional disclosures to provide.

A3.11E The Small Companies Regulations include options for small companies to prepare an abridged balance sheet and an abridged profit and loss account. In order to take this option small companies must comply with the additional legal requirement that all members of the company have given consent to the drawing up of abridged financial statements (which may only be given in respect of the preceding financial year). In accordance with paragraph 1A(4) of Schedule 1 to the Small Companies Regulations this option is not available to small entities that are charities. When a small entity that is not a company chooses to prepare abridged financial statements it should ensure that:

(a) similar consent is obtained from the members of its governing body, taking into account its legal form; and

(b) abridged financial statements would not be prohibited by relevant laws or regulation.

Financial instruments measured at fair value

A3.12 All preparers of Companies Act accounts must comply with the requirements of paragraph 36 of Schedule 1 to the Regulations, which provides that:

‘(1) Subject to sub-paragraphs (2) to (5), financial instruments (including derivatives) may be included at fair value.

(2) Sub-paragraph (1) does not apply to financial instruments that constitute liabilities unless—

(a) they are held as part of a trading portfolio,

(b) they are derivatives, or

(c) they are financial instruments falling within sub-paragraph (4).

(3) Unless they are financial instruments falling within sub-paragraph (4), sub-paragraph (1) does not apply to –

(a) financial instruments (other than derivatives) held to maturity,

(b) loans and receivables originated by the company and not held for trading purposes,

(c) interests in subsidiary undertakings, associated undertakings and joint ventures,

(d) equity instruments issued by the company,

(e) contracts for contingent consideration in a business combination, or

(f) other financial instruments with such special characteristics that the instruments, according to generally accepted accounting principles or practice, should be accounted for differently from other financial instruments.

(4) Financial instruments which under UK-adopted international accounting standards may be included in accounts at fair value, may be so included, provided that the disclosures required by such accounting standards are made.

(5) [...]'

A3.12A In limited circumstances, an entity applying this FRS to its financial instruments that are classified as non-basic in accordance with Section 11 *Basic Financial Instruments* may be prohibited, by paragraph 36 of Schedule 1 to the Regulations, from measuring those financial instruments at fair value through profit or loss in accordance with the requirements of this FRS. The Regulations prohibit the measurement of certain financial instruments at fair value through profit or loss, unless the instruments could be designated for such measurement under UK-adopted international accounting standards. UK-adopted international accounting standards permit designation at fair value through profit or loss upon initial recognition for financial instruments where: doing so eliminates or reduces a measurement or recognition inconsistency; or a group of financial instruments is managed and their performance evaluated on a fair value basis; or for a hybrid financial instrument which contains a component that, if recognised separately, would meet the definition of a derivative. Paragraph 12.8(c) of this FRS is applicable to the measurement of financial instruments prohibited under the Regulations from being measured at fair value through profit or loss and requires them to be measured at amortised cost.

A3.12B [Deleted]

A3.12C Paragraph 40 of Schedule 1 to the Regulations requires companies to include fair value gains and losses on financial instruments measured at fair value in the profit and loss account, except when the financial instrument is a hedging instrument or an available for sale security. Therefore, for those companies making the accounting policy choice, in accordance with paragraph 11.2(c) and 12.2(c) of FRS 102, to apply the recognition and measurement requirements of IFRS 9 *Financial Instruments*, recording fair value gains and losses attributable to changes in credit risk in other comprehensive income in accordance with IFRS 9 will usually be a departure from the requirement of paragraph 40 of Schedule 1 to the Regulations, for the overriding purpose of giving a true and fair view.

A3.12D Entities that are preparing Companies Act accounts must provide the disclosures required by paragraph 55 of Schedule 1 to the Regulations, which sets out requirements relating to financial instruments measured at fair value through profit or loss. Most of these disclosures will be satisfied by equivalent requirements of FRS 102, but entities will need to take care to ensure appropriate disclosure of derivatives is provided.

A3.13 An entity applying this FRS and holding financial instruments measured at fair value may be required to provide the disclosures required by paragraph 36(4) of Schedule 1 to the Regulations. The disclosures as required by paragraph 36(4) have been incorporated into Section 11. Some of the Section 11 disclosure requirements apply to all financial instruments measured at fair value, whilst others (see paragraph 11.48A of FRS 102) apply only to certain financial instruments (this does not include financial liabilities held as part of a trading portfolio nor derivatives). The disclosure requirements of paragraph 11.48A will predominantly apply to certain financial liabilities, however, there may be instances where paragraph 36(3) of Schedule 1 to the Regulations requires that the disclosures must also be provided in relation to financial assets, for example investments in subsidiaries, associates or jointly controlled entities measured at fair value (see paragraph 9.27B of FRS 102).

Requirement to present financial statements

A3.14 FRS 102 does not prescribe which entities prepare financial statements and preparers should apply the requirements of the Act in determining whether financial statements (either individual or consolidated) are required. FRS 102 sets out the requirements for a complete set of financial statements that give a true and fair view of the financial position, financial performance and cash flows of an entity (if presented), where these are required by law, or other regulation or requirement.

A3.15 A parent company preparing consolidated financial statements under section 434(2) of the Act must publish its company financial statements together with the consolidated financial statements, although section 408 of the Act provides an exemption from including the company's individual profit and loss account.

Subsidiaries excluded from consolidation

A3.16 Paragraph 9.9(b) of Section 9 *Consolidated and Separate Financial Statements* requires a group to exclude subsidiaries from consolidation on the grounds that they are held exclusively with a view to subsequent resale. By defining 'held exclusively with a view to subsequent resale' in FRS 102 to include those interests that are held as part of an investment portfolio, subsidiaries held as part of such an investment portfolio are excluded from consolidation in accordance with section 405(3) of the Act and an entity will not need to apply the true and fair override in this circumstance.

A3.17 Paragraph 9.9C(a) requires a group to measure subsidiaries excluded from consolidation by virtue of paragraph 9.9(b) and held as part of an investment portfolio, at fair value through profit or loss. The measurement at fair value through profit and loss, in circumstances where it would not be required by IFRS 10 *Consolidated Financial Statements*, is a departure from the requirements of paragraph 36 of Schedule 1 to the Regulations, for the overriding purpose of giving a true and fair view in the consolidated financial statements. In this circumstance entities must provide, in the notes to the financial statements, the 'particulars of the departure, the reasons for it and its effect' (paragraph 10(2) of Schedule 1 to the Regulations).

Calculation of goodwill where a business combination is achieved in stages

A3.18 Paragraph 9 of Schedule 6 to the Regulations sets out the requirements for the acquisition method of accounting, which results in goodwill (or negative goodwill) being calculated as the difference between:

(a) the fair value of the group's share of identifiable assets and liabilities of the subsidiary at the date control is achieved; and

(b) the total acquisition cost of the interests held by the group in that subsidiary.

This applies even where part of the acquisition cost arises from purchases at earlier dates.

A3.19 In most cases, this method provides a practical means of applying acquisition accounting because it does not require retrospective assessments of the fair value of the identifiable assets and liabilities of the subsidiary. In certain circumstances, however, not using fair values at the dates of earlier purchases while using acquisition costs which in part relate to earlier purchases may result in accounting that is inconsistent with the way the investment has been treated previously and, for that reason, may fail to give a true and fair view.

A3.20 For example, an undertaking that has been treated as an associate may then be acquired by that group as a subsidiary. Using the method required by the Regulations and paragraph 9.19B of FRS 102 to calculate goodwill on such an acquisition has the effect that the group's share of profits or losses and reserve movements of its associate becomes reclassified as goodwill (usually negative goodwill). A similar problem may arise where the group has substantially restated its investment in an undertaking that subsequently becomes its subsidiary. For example, where such an investment has been written down because it is impaired, the effect of applying the Regulations' method of acquisition accounting would be to increase reserves and create an asset (goodwill).

A3.21 In the rare cases where the method for calculating goodwill set out in the Regulations and in paragraph 9.19B of FRS 102 would be misleading, the goodwill should be calculated as the sum of goodwill arising from each purchase of an interest in the relevant undertaking adjusted as necessary for any subsequent impairment. Goodwill arising on each purchase should be calculated as the difference between the cost of that purchase and the fair value at the date of that purchase of the identifiable assets and liabilities attributable to the interest purchased. The difference between the goodwill calculated using this method and that calculated using the method provided by the Regulations and FRS 102 is shown in reserves. Section 404(5) of the Act sets out the disclosures required in cases where the statutory requirement is not applied. Paragraph 3.5 of FRS 102 sets out the disclosures when an entity departs from a requirement of FRS 102 or from a requirement of applicable legislation.

Netting

A3.22 FRS 102 permits an expense relating to a provision to be presented net of the amount recognised for a reimbursement (which may only be recognised if it is virtually certain it will be received) (see paragraph 21.9 of FRS 102). Paragraph 8 of Schedule 1 to the Regulations requires that 'Amounts in respect of items representing assets or income may not be set off against amounts in respect of items representing liabilities or expenditure (as the case may be), or vice versa.' The reimbursement asset is recognised separately from the underlying obligation to reflect the fact that the entity often will continue to be liable if the third party from which the reimbursement is due fails to pay. On the other hand, the net presentation in the income statement reflects the cost to the entity and net presentation therefore does not conflict with the Regulations.

A3.23 FRS 102 requires that a financial asset and financial liability are offset and the net amount presented in the statement of financial position, if certain criteria are met (see paragraph 11.38A of FRS 102). The net presentation does not conflict with paragraph 8 of Schedule 1 to the Regulations, because provided the criteria for the net presentation are met, the presentation reflects the expected net cash flows from settling two or more separate financial instruments.

Recording investments at cost

A3.24 Paragraph 9.26 of FRS 102 requires that in an investor's separate financial statements its investments in subsidiaries are accounted for at cost less impairment, or at fair value. Where the cost model is applied, sections 611 to 615 of the Act set out the treatment where 'merger relief' or 'group reconstruction relief' are available. These reliefs reduce the amount required to be included in share premium; they also (in section 615) allow the initial carrying amount to be adjusted downwards so it is equal to either the previous carrying amount of the investment in the transferor's books or the nominal value of the shares issued, depending on which relief applies. If the fair value model in paragraph 9.26 is used, then the relief in section 615 is not available, so the investment's carrying value may not be reduced, although the provisions in sections 611 and 612 remain relevant in respect of amounts required to be recorded in share premium.

A3.24A Section 615 permits the relief to be reflected in determining the amount at which the shares or other consideration provided for the shares issued are recognised. Therefore, when applying the cost model, any other consideration transferred may also be measured at an amount that reflects the relief available.

Realised profits

A3.25 Paragraph 13(a) of Schedule 1 to the Regulations requires that only profits realised at the reporting date are included in profit or loss, a requirement modified from that in Article 31.1(c)(aa) of the Fourth Directive which refers to profits 'made' at the balance sheet date.

A3.26 Paragraph 36 and paragraph 39 of Schedule 1 to the Regulations allow financial instruments, stocks, investment property, and living animals and plants to be held at fair value in Companies Act accounts.

A3.27 Paragraph 40(2) of Schedule 1 to the Regulations then requires that movements in the value of financial instruments, investment properties and living animals and plants are recognised in the profit and loss account, notwithstanding the usual restrictions allowing only realised profits and losses to be included in the profit and loss account. Paragraph 40 of Schedule 1 to the Regulations thereby overrides the requirements of paragraph 13(a) of Schedule 1.

A3.28 Entities measuring financial instruments, investment properties, and living animals and plants at fair value should note that they may transfer such amounts to a separate non-distributable reserve, instead of a transfer to retained earnings, but are not required to do so. Presenting fair value movements, that are not distributable profits, in the separate reserve may assist with the identification of profits available for that purpose.

A3.29 The determination of profits available for distribution is a complex area where accounting and company law interface. In determining profits available for distribution an entity may refer to Technical Release 02/17BL *Guidance on realised and distributable profits under the Companies Act 2006* issued by the Institute of Chartered Accountants in England and Wales and the Institute of Chartered Accountants of Scotland, or any successor document, to determine profits available for distribution.

Merger accounting

A3.30 Paragraph 10 of Schedule 6 to the Regulations states:

'The conditions for accounting for an acquisition as a merger are—

(a) that the undertaking whose shares are acquired is ultimately controlled by the same party both before and after the acquisition,

(b) that the control referred to in paragraph (a) is not transitory, and

(c) that adoption of the merger method accords with generally accepted accounting principles or practice.'

Therefore, paragraph 10 of Schedule 6 to the Regulations permits the use of merger accounting in certain limited circumstances, which is generally consistent with paragraph 19.27 of FRS 102 (group reconstructions). If an entity considers that, for the overriding purpose of giving a true and fair view, merger accounting should be applied in circumstances other than those set out in paragraph 10 of Schedule 6 to the Regulations, it may do so providing the relevant disclosures are made in the notes to the financial statements.

A3.30A Section 34 *Specialised Activities* requires that combinations by public benefit entities meeting certain criteria are accounted for as a merger, unless this is not permitted by the relevant statutory framework. FRS 102 therefore does not extend the use of merger accounting beyond its applicability in company law, or other relevant statutory framework. If a public benefit entity that is a company considers that, for the overriding purpose of giving a true and fair view, merger accounting should be applied in circumstances other than those set out in paragraph 10 of Schedule 6 to the Regulations, it may do so providing the relevant disclosures are made in the notes to the financial statements.

Treasury shares

A3.31 Paragraph 22.16 of FRS 102 sets out the accounting requirements when an entity purchases its own equity instruments (ie treasury shares).

A3.32 Companies subject to the Act, need to comply with the accounting requirements of paragraph 22.16 as well as with the requirements of the Act when they purchase their own equity and hold it in treasury (sections 690 to 708 and 724 to 732, respectively).

Measurement of investments in associates and jointly controlled entities for an investor, which is not a parent

A3.33 Paragraph 36 of Schedule 1 to the Regulations sets out the fair value accounting rules and permits investments in associates and joint ventures to be measured at fair value through profit or loss only where they are permitted to be treated as financial instruments in accordance with UK-adopted international accounting standards. UK-adopted international accounting standards do allow investments in subsidiaries, associates and jointly controlled entities to be measured in accordance with IFRS 9 within separate financial statements (as set out in IAS 27 *Consolidated and Separate Financial Statements*).

A3.34 Therefore, where the fair value model is applied by an investor, changes in fair value may be recognised through profit or loss, or other comprehensive income. Under the alternative accounting rules set out in Section C of Schedule 1 to the Regulations, the initial recognition of the investment must include any expenses that are incidental to the acquisition of the investment.

Measurement of inventories held for distribution at no or nominal value

A3.35 Paragraph 24(1) of Schedule 1 to the Regulations requires that if the net realisable value of any current asset is lower than its purchase price or production cost, the amount to be included in respect of that asset must be the net realisable value. However, paragraph 39 permits stocks to be included at their fair value, when applying fair value accounting.

A3.36 Inventories held for distribution at no or nominal value include items that might be distributed to beneficiaries by public benefit entities and items such as advertising and promotional material. As the items will be distributed at no or nominal cost, the net realisable value will usually be lower than the purchase price.

A3.37 Paragraph 13.4A of FRS 102 requires inventories held for distribution at no or nominal cost to be measured at the lower of cost (adjusted for any loss in service potential) and replacement cost. This is an application of fair value accounting. For inventories, including those held for distribution at no or nominal value (particularly items distributed to beneficiaries by public benefit entities), there is unlikely to be a significant difference between replacement cost and fair value.

Amortisation of intangible assets

A3.37A Paragraph 22 of Schedule 1 to the Regulations requires intangible assets to be written off over their useful economic lives. This is broadly consistent with paragraph 18.21 of FRS 102, except that FRS 102 allows for the possibility that an intangible asset will have a residual value, in which case it is the depreciable amount that shall be amortised, not the cost (or revalued amount) of the intangible asset. In practice it will be uncommon for an intangible asset to have a residual value (paragraph 18.23 requires an entity to assume that the residual value is zero other than in specific circumstances). In those cases where an intangible asset has a residual value that is not zero, the amortisation of the depreciable amount of an intangible asset over its useful economic life is a departure from the requirements of paragraph 22 of Schedule 1 to the Regulations for the overriding purpose of giving a true and fair view. In these circumstances entities must provide, in the notes to the financial statements, the ‘particulars of the departure, the reasons for it and its effect’ (paragraph 10(2) of Schedule 1 to the Regulations).

Recognition of incoming resources from non-exchange transactions by charitable companies

A3.37B Paragraph PBE34.67 requires the receipt of resources from non-exchange transactions to be recognised in income. This includes situations when items of property, plant and equipment, or inventory, are received. The income will be measured at the fair value of the assets received, which are measured in accordance with paragraphs PBE34.73 and PBE34B.15 to PBE34B.18.

A3.37C Charities that are companies are required to comply with the requirements of the Regulations, and may need to consider whether any gains are unrealised. Unrealised gains cannot be recognised in profit or loss, and should be presented as part of other comprehensive income.

Other assets included at fair value

A3.37D Paragraphs 13.3, 16.4A, 16.4B and 34.2 to 34.10A permit an entity to subdivide inventory, investment property and biological assets into classes such that some classes may be measured at cost, and others at fair value. This is consistent with the most reasonable and common sense interpretation of paragraph 39 of Schedule 1 to the Regulations.

Accounts formats

A3.38 Sections 1A, 4 and 5 of FRS 102 require entities to apply one of the profit and loss account and balance sheet formats set out in the Small Companies Regulations, the Regulations, the Small LLP Regulations and the LLP Regulations, when preparing their statement of comprehensive income (single-statement approach) or income statement (two-statement approach) and statement of financial position, respectively. The *General Rules* preceding *The Required Formats for Accounts* include certain flexibilities for companies, this includes permitting adaptation of the formats, providing the adapted presentation is equivalent to that set out in the formats and that it is consistent with generally accepted accounting practice. For entities within its scope FRS 102 sets out a framework for the information to be presented by those entities choosing to adapt the formats.

Discontinued operations

A3.39 FRS 102 requires an entity with discontinued operations, to provide an analysis between continuing operations and discontinued operations of each of the line items on the face of the statement of comprehensive income, or income statement, up to and including post-tax profit or loss for the period and illustrates this presentation in a columnar format. This is in order to present the post-tax results of those operations, combined with the profit or loss on their disposal, as a single line item while still complying with the requirement of company law to show totals for ordinary activities of items such as turnover, profit or loss before taxation and tax.

Long-term debtors

A3.40 UITF Abstract 4 *Presentation of long-term debtors in current assets* addressed the inclusion of debtors due after more than one year within ‘current assets’; that UITF consensus has been withdrawn, but its conclusions remain valid and have been included in paragraph 4.4A of FRS 102.

Presentation of amounts due under contracts

A3.40A Paragraph 23.35 requires amounts due from customers for contract work to be presented as part of inventories when it represents work in progress (ie costs incurred are greater than costs recognised as expenses). This is in order to meet company law presentation requirements.

Presentation and disclosure when using fair value as deemed cost on transition to this FRS

A3.40B Paragraph 35.10(c) permits first-time adopters to use a fair value at the transition date as the deemed cost of an item of property, plant and equipment, an investment property or an intangible asset. Paragraph 1.19(a) provides a similar option for investment property rented to other group entities, which is accounted for as property, plant and equipment, on the first application of the *Triennial review 2017 amendments*.

A3.40C If an entity elects to take these transitional exemptions in relation to property, plant and equipment, intangible assets or investment property rented to another group entity, these assets are measured under the alternative accounting rules as they are no longer carried on a cost basis. Therefore, any fair value uplift on transition to this FRS must be recognised in a revaluation reserve and the additional disclosures required by paragraph 34 of Schedule 1 to the Regulations must be given.

Related party disclosures – exemption for wholly-owned subsidiaries

A3.40D Paragraph 33.1A repeats the legal exemption from disclosing certain related party transactions. It states that '*disclosures required by this section need not be given of transactions entered into between two or more members of a group, provided that any subsidiary which is a party to the transaction is wholly-owned by such a member*'. This exemption is derived from paragraph 72(4) of Schedule 1 to the Regulations.

A3.40E This exemption may be applied to transactions between entities within a sub-group where the transacting subsidiary is wholly-owned by the intermediate parent of that sub-group, even if that intermediate parent is not wholly-owned by the ultimate controlling parent.

A3.40F In our view, this exemption may not be applied to transactions between entities in an intermediate parent's sub-group (including the intermediate parent itself) and the entities in the larger group if the intermediate parent is not wholly-owned by the parent of that larger group. Otherwise related party transactions could be obscured by a partly-owned intermediate parent creating a wholly-owned subsidiary and passing transactions through it.

Entities not subject to company law

A3.41 Many entities that apply FRS 102 are not companies, but are nevertheless required by their governing legislation, or other regulation or requirement to prepare financial statements that present a true and fair view of the financial performance and financial position of the reporting entity. However, the FRC sets accounting standards within the framework of the Act and therefore it is the company law requirements that the FRC primarily considered when developing FRS 102. Entities preparing financial statements within other legal frameworks will need to satisfy themselves that FRS 102 does not conflict with any relevant legal obligations.

A3.42 However, the FRC notes the following:

Legislation	Overview of requirements
Building Societies Act 1986	The annual accounts of a building society shall give a true and fair view of the income and expenditure for the year and the balance sheet shall give a true and fair view of the state of affairs of the society at the end of the financial year. Regulations make further requirements about the form and content of building society accounts, which do not appear inconsistent with the requirement of FRS 102.

Legislation	Overview of requirements
Charity law in England and Wales: Charities Act 2011 and regulations made thereunder	All charities are required to prepare accounts. The regulations require financial statements (other than cash-based receipts and payments accounts prepared by smaller charities) to present a true and fair view of the incoming resources, application of resources and the balance sheet, and to be prepared in accordance with the SORP. Company charities prepare their accounts in accordance with UK company law to give a 'true and fair view'. The Charities SORP (FRS 102) is compatible with the legal requirements, clarifying how they apply to accounting by charities applying FRS 102. UK company law prohibits charities from preparing IAS accounts.
Charity law in Scotland: Charities and Trustee Investments Act (Scotland) 2005 and regulations made thereunder	All charities are required to prepare accounts. The regulations require financial statements (other than cash-based receipts and payments accounts prepared by smaller charities) to present a true and fair view of the incoming resources, application of resources and the balance sheet, and to be prepared in accordance with the SORP. These regulations apply equally to company charities.
Charity law in Northern Ireland: Charities Act (Northern Ireland) 2008	All charities are required to prepare accounts. The regulations require financial statements (other than cash-based receipts and payments accounts prepared by smaller charities) to present a true and fair view of the incoming resources, expenditure of resources and the balance sheet, and to be prepared in accordance with FRS 102 and the SORP. Company charities prepare their accounts in accordance with UK company law to give a 'true and fair view'.
Co-operative and Community Benefit Societies Act 2014	Every Society shall prepare a revenue account and a balance sheet giving a true and fair view of the income and expenditure and state of affairs of the Society. FRS 102 does not appear to give rise to any legal conflicts for Societies. However, Societies often carry out activities that are regulated and may be required to comply with additional regulations on top of the legal requirements and accounting standards. Some Societies fall within the scope of SORPs, which reflect the requirements of FRS 102.

Legislation	Overview of requirements
Friendly Societies Act 1992	Every society shall prepare a balance sheet and an income and expenditure account for each financial year giving a true and fair view of the affairs of the society and its income and expenditure for the year. The Regulations[72] make further requirements about the form and content of friendly society accounts, which do not appear inconsistent with the requirements of FRS 102.
The Occupational Pension Schemes (Requirement to obtain Audited Accounts and a Statement from the Auditor) Regulations 1996	The accounts of pension funds within the scope of the regulations should show a true and fair view of the transactions during the year, assets held at the end of the year and liabilities of the scheme, other than those to pay pensions and benefits. FRS 102 includes retirement benefit plans as a specialised activity.

A3.43 Limited liability partnerships (LLPs) will be applying this FRS in conjunction with the LLP Regulations or the Small LLP Regulations. In many cases these regulations are similar to the Regulations or the Small Companies Regulations, which reduces the situations in which legal matters relevant to the financial statements of LLPs are not addressed in this appendix.

A3.44–A3.47 [Deleted]

[72] *The Friendly Societies (Accounts and Related Provisions) Regulations 1994* (as amended)

Appendix IV
Republic of Ireland legal references

Introduction

A4.1 The tables below outline the provisions in the *Companies Act 2014* corresponding to the provisions of the [UK] *Companies Act 2006* (the Act) and *The* [UK] *Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008* (the Regulations) (SI 2008/410) referred to in this FRS, unless the UK legal reference in this FRS is already footnoted with an Irish reference, or written separately in an Irish context[73].

Company law is structured differently in the two jurisdictions. The *Companies Act 2014* consists of 27 'Parts' such that:

- Parts 1 to 14 (along with the relevant Schedules) apply to private companies limited by shares (LTDs);
- Parts 16 to 24 cover the other types of companies under the *Companies Act 2014* – eg designated activity companies (DACs), public limited companies (PLCs), and companies limited by guarantee (CLGs); and
- Parts 15, 25, 26 and 27 cover Functions of the Registrar and of Regulatory and Advisory Bodies; Miscellaneous provisions; reports on Payments to Governments; and Statutory Audit, respectively.

The provisions of Parts 1 to 14 also apply to the other types of companies, unless disapplied or modified by the relevant Part (eg Part 16 for DACs). References in the text of this FRS, including in the tables below, are to the primary source of requirements in Parts 1 to 14 of, and the relevant Schedules to, the *Companies Act 2014* as pertaining to a private company limited by shares. For other company types, reference should be made to the relevant Part of the *Companies Act 2014* as applicable.

A4.2 General references are made in this FRS to UK legislation such as the '*Companies Act 2006*', 'the Companies Act', 'the Act', '*The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008* (SI 2008/410)', 'the Regulations', '*The Companies, Partnerships and Groups (Accounts and Reports) Regulations 2015* (SI 2015/980)', 'the Small Companies Regulations' and '*The Small Companies and Groups (Accounts and Directors' Report) Regulations 2008* (SI 2008/409)'. In an Irish context reference should be made to the relevant sections and paragraphs of Irish company law. Such general references are not dealt with in the tables below. References in the text to 'IAS accounts' are to be read as 'IFRS financial statements' in Irish company law.

For the purposes of the tables below, where general references are made in the text of this FRS to Schedules to the Regulations, the approach taken is that the corresponding Schedule to the *Companies Act 2014* is referenced. For example, the corresponding reference used for Schedule 1 to the Regulations is Schedule 3 to the *Companies Act 2014* (Accounting principles, form and content of entity financial statements). Likewise, the corresponding Irish references used for Schedule 2 and for Schedule 3 to the Regulations are the following, respectively:

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[73] Similarly, corresponding Irish legal references are not provided for the UK legal references in Appendix C to Section 1A *Small Entities*. Appendix C to Section 1A sets out the disclosure requirements for small entities in the UK, based on the requirements of company law in the UK, while Appendix D to Section 1A sets out the disclosure requirements for small entities in the Republic of Ireland, based on the requirements of company law in the Republic of Ireland.

- the *European Union (Credit Institutions: Financial Statements) Regulations 2015* (SI No. 266 of 2015) (Credit Institutions Regulations 2015); and
- the *European Union (Insurance Undertakings: Financial Statements) Regulations 2015* (SI No. 262 of 2015), as amended by the *European Union (Insurance Undertakings: Financial Statements) (Amendment) Regulations 2016* (SI No. 213 of 2016) (Insurance Undertakings Regulations 2015 (as amended)).

Similar to the approach noted in paragraph A3.3 of Appendix III of this FRS, where reference is made in this appendix to Schedule 3 to the *Companies Act 2014*, Irish entities applying the Credit Institutions Regulations 2015, the Insurance Undertakings Regulations 2015 (as amended) or Schedule 4 to the *Companies Act 2014* should read the references as referring to the corresponding paragraphs in those regulations or that Schedule where applicable. Small entities applying the small companies regime should read them as referring to the corresponding paragraph in Schedule 3A (Accounting principles, form and content of entity financial statements of a company qualifying for the small companies regime) or Schedule 4A (Accounting principles, form and content of group financial statements for companies subject to the small companies regime) to the *Companies Act 2014*, where applicable. The requirements of Schedule 3 to the *Companies Act 2014* are not necessarily the same as those contained in the Credit Institutions Regulations 2015 or in the Insurance Undertakings Regulations 2015 (as amended) in all cases. References should be made to the specific requirement as appropriate.

Note: Schedule 6 to the [UK] Regulations contains group financial statements requirements for all entities, including credit institutions and insurance undertakings. For Irish credit institutions and insurance undertakings, reference should be made to the Credit Institutions Regulations 2015 and the Insurance Undertakings Regulations 2015 (as amended), respectively.

A4.3 The following Irish legislation is also referenced in the tables below:

- *Building Societies Act, 1989*;
- *Charities Act 2009*;
- *Friendly Societies (Amendment) Act, 1977*;
- *Friendly Societies Regulations, 1988* (SI No. 74 of 1988);
- *Industrial and Provident Societies (Amendment) Act, 1978*;
- *Pensions Act, 1990*;
- *Occupational Pension Schemes (Disclosure of Information) Regulations, 2006* (SI No. 301 of 2006);
- *Central Bank Act, 1971*;
- The Credit Union Acts 1997 to 2012; and
- The Friendly Societies Acts 1896 to 2014.

Companies Act financial statements under Irish company law

A4.4 Certain entities are permitted under Irish company law to prepare their Companies Act financial statements under a financial reporting framework based on accounting standards other than those issued by the Financial Reporting Council (FRC). Specifically, and subject to certain conditions:

- Pursuant to section 279 of the *Companies Act 2014*, relevant holding companies are permitted to prepare 'Companies Act entity financial statements' and/or 'Companies Act group financial statements' in accordance with US GAAP, as modified to ensure consistency with Irish company law.
- Investment companies subject to Part 24 of the *Companies Act 2014* or the *European Communities (Undertakings for Collective Investment in Transferable Securities) Regulations 2011* (SI No. 352 of 2011) may adopt an alternative body of accounting standards, being standards which apply in the United States of America, Canada or Japan in preparing 'Companies Act entity or group financial statements' or 'Companies Act entity financial statements' respectively.

A4.5 Such entities, therefore, may adopt standards other than those issued by the FRC in preparing Companies Act financial statements under Irish company law.

Small companies under Irish company law

A4.6 The *Companies (Accounting) Act 2017* amended the *Companies Act 2014* to introduce the small companies regime (which is similar but not identical to the UK small companies regime), into Irish company law. Where a company qualifies as a small company in accordance with section 280A or 280B (small holding company) of the *Companies Act 2014*, as may be appropriate, then different rules may be applied (referred to as the 'small companies regime' in the *Companies Act 2014*) by the company in respect of financial statements and reports for a financial year, in relation to which that company qualifies as a small company (section 280C of the *Companies Act 2014*).

The definitions of a small company and a small holding company are contained in sections 280A and 280B of the *Companies Act 2014*. These sections also detail certain companies that cannot qualify as a small company or small holding company and are therefore excluded from the small companies regime.

Subject to certain conditions and exclusions, the qualifying conditions are met by a company if, in relation to a financial year, it does not exceed two or more of the following criteria:

(a)	Turnover	€12 million
(b)	Balance sheet total	€6 million
(c)	Average number of employees	50

A newly incorporated company must meet the qualifying conditions in relation to its first financial year to qualify as a small company.

In relation to a subsequent financial year (referred to as a 'relevant year') the qualifying conditions must be met by a company (i) in respect of the relevant year and the financial year immediately preceding the relevant year; (ii) in respect of the relevant year and the company qualified as a small company in relation to the financial year immediately preceding the relevant year; or (iii) in the financial year immediately preceding the relevant year and the company qualified as a small company in relation to that preceding financial year.

A holding company can only qualify as a small company in relation to a financial year if the group that it heads qualifies as small (as set out in section 280B of the *Companies Act 2014*).

A holding company that qualifies for the small companies regime is exempt from the requirement to prepare group financial statements, but may however elect to prepare them.

Other notes

Financial Instruments measured at fair value

A4.7 There are a number of UK legal references, primarily in Appendix III, to paragraph 36 of Schedule 1 to the Regulations in respect of the measurement of financial instruments at fair value. The corresponding reference in the *Companies Act 2014* is paragraph 38 of Schedule 3 to the *Companies Act 2014*.

It should also be noted, however, that the wording in paragraphs 51 and 52 of Schedule 1 to the Credit Institutions Regulations 2015 and in paragraphs 46 and 47 of Schedule 1 to the Insurance Undertakings Regulations 2015 (as amended) differ to that used in Schedule 3 to the Companies Act 2014, and reference should be made to these paragraphs where applicable.

Accounting for changes in fair value of financial instruments

A4.8 Paragraph A3.12C in Appendix III to this FRS discusses a potential departure from UK law for the overriding purpose of giving a true and fair view. Paragraph 41(3) of Schedule 3 to the *Companies Act 2014*, as distinct from UK law, cross references the rules in respect of the accounting for changes in the fair value of financial instruments to IFRS, thereby allowing any changes in the fair value of financial instruments to be accounted for under any approach permitted under IFRS. Consequently, presenting fair value gains or losses attributable to changes in own credit risk in other comprehensive income in accordance with IFRS 9 will not require a true and fair override.

It should also be noted, however, that the wording in paragraph 56 of Schedule 1 to the Credit Institutions Regulations 2015 and in paragraph 51 of Schedule 1 to the Insurance Undertakings Regulations 2015 (as amended) differ to that used in Schedule 3 to the *Companies Act 2014*, and reference should be made to these paragraphs where applicable. Consequently, for entities applying those regulations, presenting fair value gains or losses attributable to changes in own credit risk in other comprehensive income in accordance with IFRS 9 will usually require a true and fair override.

Stock at fair value

A4.9 Paragraph 39 of Schedule 1 to the Regulations permits stocks to be included at their fair value, when applying fair value accounting. Irish company law does not permit stock to be included in the financial statements at fair value.

Paragraph 13.5A of FRS 102 states that ‘Where inventories are acquired through a non-exchange transaction, their cost shall be measured at their fair value as at the date of acquisition.’ This does not breach the prohibition against fair value accounting as the use of a fair value is a method of estimating cost at initial recognition.

Financial Institution

A4.10 A financial institution is defined in the Glossary to this FRS. With regard to the UK legal references included in the definition, the table below is intended as a reference guide to the corresponding or similar provisions in Irish law and does not purport to be complete. It should be noted that not all Irish legal provisions directly correspond to

UK legal provisions and reference should be made to Irish law for an understanding of the relevant requirements.

Glossary to FRS 102	UK references	RoI references
‘financial institution’ and Footnote 61	Part 4A permission; Section 55A of the Financial Services and Markets Act 2000	There is no corresponding legislation in Ireland to the Financial Services and Markets Act 2000. Banks in Ireland are licensed under Section 9 of the Central Bank Act, 1971.
‘financial institution’	Section 119(1) of the Building Societies Act 1986	Section 2(1) of the Building Societies Act, 1989
‘financial institution’	Co-operative and Community Benefit Societies Act 2014 and Credit Unions Act 1979	Credit Union Acts 1997 to 2012
‘financial institution’	Friendly Societies Act 1992; Section 7(1)(a) of the Friendly Societies Act 1974	Friendly Societies Acts 1896 to 2014

Qualifying partnerships

A4.11 There are a number of references in this FRS to limited liability partnerships (LLPs) and legislation relating thereto. The structure and scope of the legislation applicable to partnerships is different in the two jurisdictions, therefore no corresponding Irish legislation is referenced in the tables below.

A4.11A Irish partnerships that meet the definition of a qualifying partnership as set out in the *European Union (Qualifying Partnerships: Accounting and Auditing) Regulations 2019* (SI No. 597 of 2019) are required to apply Part 6 of the *Companies Act 2014* in accordance with Part 4 of those regulations. Irish qualifying partnerships are eligible to apply the small companies regime provided they meet the relevant conditions.

A4.11B Part 4 of the *European Union (Qualifying Partnerships: Accounting and Auditing) Regulations 2019* does not require qualifying partnerships to comply with the requirement in Part 6 of the *Companies Act 2014* to prepare financial statements in accordance with applicable accounting standards. However, Part 4 of those regulations does require qualifying partnerships to comply with the requirement in Part 6 of the *Companies Act 2014* to prepare financial statements that give a true and fair view of the assets, liabilities and financial position as at the financial year end date and of the profit or loss for the financial year. This FRS applies to financial statements intended to give a true and fair view.

Other

A4.12 The following tables are intended as a reference guide to the corresponding or similar provisions in Irish law and do not purport to be complete. As such, it may be necessary to make reference to other Irish law as appropriate. It should be noted too that not all Irish legal provisions directly correspond to UK legal provisions and reference should be made to Irish law for an understanding of the relevant requirements. For example, references to ‘UK-adopted international accounting standards’ in UK company law correspond to provisions in Irish law that refer to EU-adopted IFRS. It should also be noted that various sections and paragraphs referenced below may have been amended by legislation subsequent to the issuing of this FRS, and reference should be made to such amended text where applicable.

Section 1 *Scope*

	UK references	RoI references	
Paragraph	**Act and the Regulations (unless otherwise stated)**	**Companies Act 2014**	**Other legislative reference**
1.10	Section 399	Section 293	
1.10	Section 400 to 402	Sections 299 to 301	

Section 3 *Financial Statement Presentation*

	UK references	RoI references	
Paragraph	**Act and the Regulations (unless otherwise stated)**	**Companies Act 2014**	**Other legislative reference**
3.14A	Paragraph 51 of Schedule 1 to the Regulations	Paragraph 46 in Part IV of Schedule 3	

Section 4 *Statement of Financial Position* and Section 5 *Statement of Comprehensive Income and Income Statement*

	UK references	RoI references	
Paragraph	**Act and the Regulations (unless otherwise stated)**	**Companies Act 2014**	**Other legislative reference**
4.2, 5.5 and 5.7	Part 1 *General Rules and Formats* of Schedule 1 to the Regulations	Part II *General Rules and Formats* of Schedule 3	
4.2, 5.5 and 5.7	Part 1 *General Rules and Formats* of Schedule 2 to the Regulations		Part II *General Rules and Formats* of Schedule 1 to the Credit Institutions Regulations 2015
4.2, 5.5 and 5.7	Part 1 *General Rules and Formats* of Schedule 3 to the Regulations		Part II *General Rules and Formats* of Schedule 1 to the Insurance Undertakings Regulations 2015 (as amended)
4.2, 5.5 and 5.7	Schedule 6 to the Regulations	Schedule 4 Refer also to paragraph A4.2 of this appendix.	

	UK references	RoI references	
Paragraph	**Act and the Regulations (unless otherwise stated)**	**Companies Act 2014**	**Other legislative reference**
4.2, 5.5 and 5.7	Schedule 1 and 3 to the LLP Regulations	Refer to paragraph A4.11 of this appendix.	
4.2A, 4.2B, 4.4A and 4.7	Paragraph 1A(1) of Schedule 1 to the Regulations	Paragraph 2(2) in Section A of Part II of Schedule 3	
5.5B and 5.7A	Paragraph 1A(2) of Schedule 1 to the Regulations	Paragraph 2(3) in Section A of Part II of Schedule 3	

Section 7 *Statement of Cash Flows*

	UK references	RoI references	
Paragraph	**Act and the Regulations (unless otherwise stated)**	**Companies Act 2014**	**Other legislative reference**
7.20A	Part 1 *General Rules and Formats* of Schedule 2 to the Regulations		Part II *General Rules and Formats* of Schedule 1 to the Credit Institutions Regulations 2015

Section 9 *Consolidated and Separate Financial Statements*

	UK references	RoI references	
Paragraph	**Act and the Regulations (unless otherwise stated)**	**Companies Act 2014**	**Other legislative reference**
9.27B	Paragraph 36(4) of Schedule 1 to the Regulations	Refer to paragraph A4.7 of this appendix.	

Section 11 *Basic Financial Instruments*

	UK references	RoI references	
Paragraph	**Act and the Regulations (unless otherwise stated)**	**Companies Act 2014**	**Other legislative reference**
11.48A	Paragraph 36(4) of Schedule 1 to the Regulations	Refer to paragraph A4.7 of this appendix.	

Section 22 *Liabilities and Equity*

	UK references	RoI references	
Paragraph	**Act and the Regulations (unless otherwise stated)**	**Companies Act 2014**	**Other legislative reference**
22.8	Sections 611 to 615	Sections 72 to 75 Reference to 'merger relief' encompasses a reference to both section 72 and section 75.	

Appendix I *Glossary*

	UK references	RoI references	
Paragraph	**Act and the Regulations (unless otherwise stated)**	**Companies Act 2014**	**Other legislative reference**
'current assets'	Paragraph 1A(1) of Schedule 1 to the Regulations	Paragraph 2(2) in Section A of Part II of Schedule 3	
'current liabilities'	Paragraph 1A(1) of Schedule 1 to the Regulations	Paragraph 2(2) in Section A of Part II of Schedule 3	
'financial institution' and Footnote 61	Part 4A permission; Section 55A of the Financial Services and Markets Act 2000		There is no corresponding legislation in Ireland to the Financial Services and Markets Act 2000. Banks in Ireland are licensed under Section 9 of the Central Bank Act, 1971. Refer also to paragraph A4.10 of this appendix.
'financial institution'	Section 119(1) of the Building Societies Act 1986		Section 2(1) of the Building Societies Act, 1989 Refer also to paragraph A4.10 of this appendix.
'financial institution'	Co-operative and Community Benefit Societies Act 2014 and Credit Unions Act 1979		Credit Union Acts 1997 to 2012 Refer also to paragraph A4.10 of this appendix.
'financial institution'	Friendly Societies Act 1992; Section 7(1)(a) of the Friendly Societies Act 1974		Friendly Societies Acts 1896 to 2014 Refer also to paragraph A4.10 of this appendix.

	UK references	RoI references	
Paragraph	**Act and the Regulations (unless otherwise stated)**	**Companies Act 2014**	**Other legislative reference**
'individual financial statements'	Section 394	Section 290	
'individual financial statements'	Section 132 of the Charities Act 2011		Section 48 of the Charities Act 2009 provides that certain charities are to prepare an annual statement of accounts, the form and content of which can be prescribed by Regulations of the Minister. At the date of publication of this FRS, no Regulations regarding the form and content of charities' annual statements of accounts have been published. Charity companies are required to prepare financial statements, which give a true and fair view in accordance with the Companies Act. Sections 290(5) and 293(5) of the Companies Act 2014 respectively require that a company or a group 'not trading for the acquisition of gain by its members' must prepare Companies Act financial statements (ie not IFRS financial statements), and this provision may apply to many Irish charity companies.
'individual financial statements'	Section 72A of the Building Societies Act 1986		Section 77 of the Building Societies Act, 1989 requires the preparation of (a) an income and expenditure account giving a true and fair view of its income and expenditure for that year, (b) a balance sheet giving a true and fair view of the state of its affairs as at the end of that year, (c) a statement of the source and application of funds giving a true and fair view of the manner in which its business has been financed and in which its financial resources have been used during that year, and also requires (d) that the

	UK references	RoI references	
Paragraph	**Act and the Regulations (unless otherwise stated)**	**Companies Act 2014**	**Other legislative reference**
			annual accounts shall also contain, whether in the form of notes or otherwise, such supplementary information as is required by or under that Act.
'LLP Regulations'	The Large and Medium-sized Limited Liability Partnerships (Accounts) Regulations 2008 (SI 2008/1913)	Refer to paragraph A4.11 of this appendix.	
'qualifying entity' (Footnote 63)	Section 474(1)	Section 274(5)	
'Small LLP Regulations'	The Small Limited Liability Partnership (Accounts) Regulations 2008 (SI 2008/1912)	Refer to paragraph A4.11 of this appendix.	
'UK-adopted international accounting standards'	The International Accounting Standards and European Public Limited-Liability Company (Amendment etc.) (EU Exit) Regulations 2019 (SI 2019/685)		There is no corresponding legislation in Ireland

Appendix III *Note on legal requirements*

	UK references	RoI references	
Paragraph	**Act and the Regulations (unless otherwise stated)**	**Companies Act 2014**	**Other legislative reference**
A3.1 (Footnote 68)	Charities Act 2011		Section 48 of the Charities Act 2009 provides that certain charities are to prepare an annual statement of accounts, the form and content of which can be prescribed by Regulations of the Minister. At the date of publication of this FRS, no Regulations

	UK references	RoI references	
Paragraph	**Act and the Regulations (unless otherwise stated)**	**Companies Act 2014**	**Other legislative reference**
			regarding the form and content of charities' annual statements of accounts have been published. Charity companies are required to prepare financial statements, which give a true and fair view in accordance with the Companies Act. Sections 290(5) and 293(5) of the Companies Act 2014 respectively require that a company or a group 'not trading for the acquisition of gain by its members' must prepare Companies Act financial statements (ie not IFRS financial statements), and this provision may apply to many Irish charity companies.
A3.3	Schedule 1 to the Regulations	Schedule 3 Refer also to paragraph A4.2 of this appendix.	
A3.3	Schedule 2 to the Regulations		Credit Institutions Regulations 2015 Refer also to paragraph A4.2 of this appendix.
A3.3	Schedule 3 to the Regulations		Insurance Undertakings Regulations 2015 (as amended) Refer also to paragraph A4.2 of this appendix.
A3.3	Schedule 6 to the Regulations	Schedule 4 Refer also to paragraph A4.2 of this appendix.	
A3.3	Schedule 1 to the Small Companies Regulations	Schedule 3A Refer also to paragraph A4.2 of this appendix.	
A3.6	Section 395(1)	Sections 290(3), 290(4)	
A3.6	Section 396	Section 291	
A3.6	Section 403(2)	Sections 293(3), 293(4)	
A3.6	Section 404	Section 294	
A3.7	Parts 15 and 16 of the Act	Part 6	

	UK references	RoI references	
Paragraph	**Act and the Regulations (unless otherwise stated)**	**Companies Act 2014**	**Other legislative reference**
A3.8	Section 407	Section 296	
A3.11A	Sections 382 and 383; Section 384	Sections 280A and 280B Refer also to paragraph A4.6 of this appendix.	
A3.11B	Section 383	Section 280B Refer also to paragraph A4.6 of this appendix.	
A3.11D	Section 393	Section 289 Refer also to paragraph A4.6 of this appendix.	
A3.11E	Paragraph 1A(4) of Schedule 1 to the Small Companies Regulations	Irish company law does not provide for the preparation of abridged statutory financial statements. This is not the same as abridgment for filing purposes.	
A3.12 and A3.12A	Paragraph 36 of Schedule 1 to the Regulations	Refer to paragraph A4.7 of this appendix.	
A3.12C	Paragraph 40 of Schedule 1 to the Regulations	Paragraph 41 in Section D of Part III of Schedule 3 Refer also to paragraph A4.8 of this appendix.	
A3.12D	Paragraph 55 of Schedule 1 to the Regulations	Paragraph 49 in Part IV of Schedule 3	
A3.13	Paragraph 36(4) of Schedule 1 to the Regulations	Refer to paragraph A4.7 of this appendix.	
A3.13	Paragraph 36(3) of Schedule 1 to the Regulations	Refer to paragraph A4.7 of this appendix.	
A3.15	Section 434(2)	Section 340(2)	
A3.15	Section 408	Section 304	
A3.16	Section 405(3)	Section 303(3)	
A3.17	Paragraph 36 of Schedule 1 to the Regulations	Refer to paragraph A4.7 of this appendix.	

	UK references	RoI references	
Paragraph	**Act and the Regulations (unless otherwise stated)**	**Companies Act 2014**	**Other legislative reference**
A3.17	Paragraph 10(2) of Schedule 1 to the Regulations	Paragraph 19 in Section A of Part III of Schedule 3 and see also sections 291(6) and 294(6) of the Companies Act 2014.	
A3.18	Paragraph 9 of Schedule 6 to the Regulations	Paragraph 14 in Part III of Schedule 4 Refer also to paragraph A4.2 of this appendix.	
A3.21	Section 404(5)	Section 294(6)	
A3.22 and A3.23	Paragraph 8 of Schedule 1 to the Regulations	Paragraph 7 in Section A of Part II of Schedule 3	
A3.24	Sections 611 to 615	Sections 72 to 75 Reference to 'merger relief' encompasses a reference to both section 72 and section 75.	
A3.24A	Section 615	Section 74	
A3.25 and A3.27	Paragraph 13(a) of Schedule 1 to the Regulations	Paragraph 14(a) in Section A of Part III of Schedule 3	
A3.26	Paragraph 36 of Schedule 1 to the Regulations	Refer to paragraph A4.7 of this appendix.	
A3.26	Paragraph 39 of Schedule 1 to the Regulations	Paragraph 40 in Section D of Part III of Schedule 3 Refer also to paragraph A4.9 of this appendix.	
A3.27	Paragraphs 40 and 40(2) of Schedule 1 to the Regulations	Paragraph 41 in Section D of Part III of Schedule 3	
A3.30 and A3.30A	Paragraph 10 of Schedule 6 to the Regulations	Paragraph 15 in Part III of Schedule 4 Refer also to paragraph A4.2 of this appendix.	
A3.32	Sections 690 to 708 and 724 to 732	Sections 102 to 116 and 320(1) to (3)	
A3.33	Paragraph 36 of Schedule 1 to the Regulations	Refer to paragraph A4.7 of this appendix.	

	UK references	RoI references	
Paragraph	**Act and the Regulations (unless otherwise stated)**	**Companies Act 2014**	**Other legislative reference**
A3.34	Section C of Schedule 1 to the Regulations	Section C in Part III of Schedule 3	
A3.35	Paragraph 24(1) of Schedule 1 to the Regulations	Paragraph 27(1) in Section B of Part III of Schedule 3	
A3.35	Paragraph 39 of Schedule 1 to the Regulations	Paragraph 40 in Section D of Part III of Schedule 3 Refer also to paragraph A4.9 of this appendix.	
A3.37A	Paragraph 22 of Schedule 1 to the Regulations	Paragraph 25 in Section B of Part III of Schedule 3	
A3.37A	Paragraph 10(2) of Schedule 1 to the Regulations	Paragraph 19 in Section A of Part III of Schedule 3 and see also sections 291(6) and 294(6) of the Companies Act 2014.	
A3.37D	Paragraph 39 of Schedule 1 to the Regulations	Paragraph 40 in Section D of Part III of Schedule 3 Refer also to paragraph A4.9 of this appendix.	
A3.40C	Paragraph 34 of Schedule 1 to the Regulations	Paragraph 35 in Section C of Part III of Schedule 3	
A3.40D	Paragraph 72(4) of Schedule 1 to the Regulations	Paragraph 65(3) in Part IV of Schedule 3	
A3.42	Building Societies Act 1986		Building Societies Act, 1989
A3.42	Charities Act 2011 and regulations made thereunder		Section 48 of the Charities Act 2009 provides that certain charities are to prepare an annual statement of accounts, the form and content of which can be prescribed by Regulations of the Minister. At the date of publication of this FRS, no Regulations regarding the form and content of charities' annual statements of accounts have been published. Charity companies are required to prepare financial statements, which give a true and fair view

	UK references	RoI references	
Paragraph	**Act and the Regulations (unless otherwise stated)**	**Companies Act 2014**	**Other legislative reference**
			in accordance with the Companies Act. Sections 290(5) and 293(5) of the Companies Act 2014 respectively require that a company or a group 'not trading for the acquisition of gain by its members' must prepare Companies Act financial statements (ie not IFRS financial statements), and this provision may apply to many Irish charity companies.
A3.42	Co-operative and Community Benefit Societies Act 2014		Section 30 of Part IV of the Industrial and Provident Societies (Amendment) Act, 1978; Regulations 4 and 5 of the Friendly Societies Regulations, 1988, pursuant to Section 3 of the Friendly Societies (Amendment) Act, 1977
A3.42 and Footnote 72	Friendly Societies Act 1992 and Friendly Societies (Accounts and Related Provisions) Regulations 1994 (as amended)		Regulations 4 and 5 of the Friendly Societies Regulations, 1988, pursuant to Section 3 of the Friendly Societies (Amendment) Act, 1977
A3.42	The Occupational Pension Schemes (Requirement to obtain Audited Accounts and a Statement from the Auditor) Regulations 1996		Section 56 of the Pensions Act, 1990; Regulation 5 and paragraphs 1 and 2(a)(ii) of Schedule A to the Occupational Pension Schemes (Disclosure of Information) Regulations, 2006

Basis for Conclusions

	UK references	RoI references	
Paragraph	**Act and the Regulations (unless otherwise stated)**	**Companies Act 2014**	**Other legislative reference**
A.28(a)	Paragraph 29A of Schedule 1 to the Regulations	Paragraph 33(4) in Section C of Part III of Schedule 3	
A.28(b)	Paragraph 36 of Schedule 1 to the Regulations	Refer to paragraph A4.7 of this appendix.	
B9.7	Section 405(3)	Section 303(3)	
B11.29 (Footnote 81)	Paragraph 36(4) of Schedule 1 to the Regulations	Refer to paragraph A4.7 of this appendix.	
B34D.2	Section 467(1)	Section 275(1)	

Approval by the FRC

FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland* was approved for issue by the Financial Reporting Council on 5 March 2013.

Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Basic financial instruments and Hedge accounting was approved for issue by the Financial Reporting Council on 2 July 2014.

Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Pension obligations was approved for issue by the Financial Reporting Council on 25 February 2015.

Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Small entities and other minor amendments was approved for issue by the Financial Reporting Council on 1 July 2015.

Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Fair value hierarchy disclosures was approved for issue by the Financial Reporting Council on 3 March 2016.

Amendments to FRS 101 Reduced Disclosure Framework and FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Notification of shareholders was approved for issue by the Financial Reporting Council on 7 December 2016.

Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Directors' loans – optional interim relief for small entities was approved for issue by the Financial Reporting Council on 26 April 2017.

Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Triennial review 2017 – Incremental improvements and clarifications was approved for issue by the Financial Reporting Council on 6 December 2017.

Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Multi-employer defined benefit plans was approved for issue by the Financial Reporting Council on 9 May 2019.

Amendment to FRS 101 Reduced Disclosure Framework – 2018/19 cycle was approved for issue by the Financial Reporting Council on 4 July 2019.

Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Interest rate benchmark reform was approved for issue by the Financial Reporting Council on 20 November 2019.

Amendment to FRS 101 Reduced Disclosure Framework – 2019/20 cycle was approved for issue by the Financial Reporting Council on 20 May 2020.

Amendment to FRS 101 Reduced Disclosure Framework – Effective date of IFRS 17 was approved for issue by the Financial Reporting Council on 29 September 2020.

Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland and FRS 105 The Financial Reporting Standard applicable to the Micro-entities Regime – COVID-19-related rent concessions was approved for issue by the Financial Reporting Council on 7 October 2020.

Amendments to UK and Republic of Ireland accounting standards – UK exit from the European Union was approved for issue by the Financial Reporting Council on 2 December 2020.

Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Interest rate benchmark reform (Phase 2) was approved for issue by the Financial Reporting Council on 9 December 2020.

Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland and FRS 105 The Financial Reporting Standard applicable to the Micro-entities Regime – COVID-19-related rent concessions beyond 30 June 2021 was approved for issue by the Financial Reporting Council on 2 June 2021.

Basis for Conclusions
FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland*

This Basis for Conclusions[74] *accompanies, but is not part of, FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland and summarises the main issues considered by the Financial Reporting Council (FRC) in developing FRS 102.*

Feedback from a number of exposure drafts and consultation documents has been considered in the development of FRS 102. Unless otherwise stated, respondents to the consultations supported the proposals made; detailed feedback statements to all consultations are available on the FRC website. Table 1 at the end of this Basis for Conclusions sets out the relevant exposure drafts and consultations along with the corresponding publications in which those consultations were finalised.

The effective dates and any transitional arrangements for FRS 102, and any amendments made to it, are set out in the FRS and for ease of reference also summarised in Table 1.

1 FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland* replaced accounting standards applicable in the UK and Republic of Ireland with a single FRS developed from the IFRS for SMEs. FRS 102 applies to general purpose financial statements and the financial reporting of entities including those that are not constituted as companies and those that are not profit-oriented. FRS 102 applies to the financial statements of entities that are not applying adopted IFRS, FRS 101 *Reduced Disclosure Framework* or FRS 105 *The Financial Reporting Standard applicable to the Micro-entities Regime*.

2 This Basis for Conclusions is organised into two parts:

(a) Part A covers general issues relating to the development of the standard and overarching issues affecting the whole standard.

(b) Part B covers specific technical issues organised by section number.

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[74] This Basis for Conclusions replaces the Accounting Council's Advice and the Corporate Reporting Council's Advice included in previous editions of FRS 102. That Advice continues to be available on the FRC website as part of the original publications, including any dissenting opinions to that Advice.

Part A – Development and overarching issues

Objective

A.1 In developing financial reporting standards, the overriding objective of the FRC is to enable users of accounts to receive high-quality understandable financial reporting proportionate to the size and complexity of the entity and users' information needs.

A.2 In achieving this objective, the FRC aims to provide succinct financial reporting standards that:

(a) have consistency with global accounting standards through the application of an IFRS-based solution unless an alternative clearly better meets the overriding objective;

(b) balance improvement, through reflecting up-to-date thinking and developments in the way businesses operate and the transactions they undertake, with stability;

(c) balance consistent principles for accounting by all UK and Republic of Ireland entities with proportionate and practical solutions, based on size, complexity, public interest and users' information needs;

(d) promote efficiency within groups; and

(e) are cost-effective to apply.

Development of FRS 102

Initially using the IFRS for SMEs as a basis

A.3 The Accounting Standards Board[75] (ASB) first started to consider the future of UK and Republic of Ireland accounting standards following the EU decision to require consolidated accounts of listed companies to comply with IFRS. The long-held view was that there could be no justification for two different sets of accounting standards.

A.4 It was decided that the IFRS for SMEs would be used as a basis for the initial development of FRS 102 as it:

(a) was a way of achieving a consistent accounting framework, as it is a simplification of IFRS;

(b) reflected more up-to-date thinking and developments than previous accounting standards, especially for financial instruments;

(c) was a single standard setting out clear accounting requirements; and

(d) was a cost effective way of updating previous accounting standards.

A.5 In the early stages of development, respondents raised some concerns, most notably about the removal of certain accounting policy options, such as revaluation of property, plant and equipment, that were available in previous accounting standards and EU-adopted IFRS[76] but not available in the IFRS for SMEs. The following points were raised:

(a) The removal of the policy options was potentially an over-simplification for the UK and Republic of Ireland. The IFRS for SMEs had been developed by the IASB for

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[75] The Accounting Standards Board of the Financial Reporting Council was a prescribed body for issuing accounting standards in the UK prior to this role being transferred to the FRC in 2012.

[76] This reflects the standards referenced in UK company law at the time, prior to the UK exit from the European Union (see paragraph A.63 of this Basis for Conclusions).

countries that had a less developed financial reporting framework than the UK and Republic of Ireland. Respondents considered that when options existed in previous accounting standards, the simplification had not been justified.

(b) The removal of the policy options would reduce comparability between entities that apply EU-adopted IFRS and those applying FRS 102 for entities operating in the same market. For example, entities applying FRS 102 would not be permitted to revalue property, plant and equipment whereas entities applying EU-adopted IFRS could do so.

(c) Retaining the options that existed in previous accounting standards would reduce transitional costs and ease transition between the different standards and also with EU-adopted IFRS.

(d) The inability to include borrowing costs as part of the costs of property, plant and equipment may cause some housing associations to breach the terms and conditions of current financing arrangements.

A.6 In response to these concerns it was noted that some pragmatism was required in determining what amendments were to be made to the IFRS for SMEs and a set of guidelines was developed to assist in the process. These guidelines were as follows:

(a) changes were made to permit accounting treatments that exist in FRSs at the transition date that align with EU-adopted IFRS;

(b) changes were consistent with EU-adopted IFRS unless a non-IFRS-based solution clearly better met the objective of providing high-quality understandable financial reporting proportionate to the size and complexity of the entity and the users' information needs. In these cases elements of an IFRS-based solution may nevertheless have been retained;

(c) use was made, where possible, of existing exemptions in company law to avoid gold-plating; and

(d) changes were made to provide clarification, by reference to EU-adopted IFRS, that would avoid unnecessary diversity in practice.

A.7 Consequently, FRS 102 includes accounting options for:

(a) capitalisation of borrowing costs;

(b) revaluation of property, plant and equipment and intangible assets; and

(c) capitalisation of development costs, in certain circumstances.

A.8 Respondents also suggested areas where further clarification would be useful. A number of clarifications were made, including some made by reference to EU-adopted IFRS or previous UK and Ireland accounting standards. Examples include:

(a) Amending the disclosure requirements for discontinued operations for compliance with company law.

(b) Providing a cost or fair value option for the measurement of investments by an investor that is not a parent, but has an investment in one or more associates and/or jointly controlled entities.

(c) Clarifying that the life of goodwill, when an entity is otherwise unable to make a reliable estimate, shall not be in excess of five years and thereby consistent with company law (this was subsequently revised to 10 years when the EU Accounting Directive was implemented in 2015). The same also applies to intangible assets.

(d) Clarifying the accounting treatment of group share-based payments when the award is granted by the parent or another group entity.

Urgent Issue Task Force (UITF) Abstracts

A.9 Early consultations proposed withdrawing all UITF Abstracts except UITF Abstract 43 *The Interpretation of equivalence for the purposes of section 228A of the Companies Act*. Respondents suggested that in addition to UITF Abstract 43, some other UITF Abstracts should be retained. To be consistent with the objective of providing succinct financial reporting standards, the following UITF Abstracts were incorporated into FRS 102:

UITF Abstract		**Action**
4	*Presentation of long-term debtors in current assets*	Incorporated into the legal appendix.
31	*Exchange of businesses or other non-monetary assets for an interest in a subsidiary, joint venture or associate*	Additional paragraphs 9.31 and 9.32 were inserted.
32	*Employee benefit trusts and other intermediate payment arrangements*	Additional paragraphs were inserted into Section 9 *Consolidated and Separate Financial Statements*.
43	*The interpretation of equivalence for the purposes of section 228A of the Companies Act 1985*	The guidance was updated and included as Application Guidance to FRS 100.

A.10 UITF Abstract 48 *Accounting implications of the replacement of the retail prices index with the consumer prices index for retirement benefits* was withdrawn as the circumstance it addressed related to one time period which has now passed.

Scope of FRS 102

A.11 In the early stages of development, a differential financial reporting system was proposed based on three tiers of entities using public accountability as a differentiator; this would have required some entities to apply EU-adopted IFRS that would not otherwise have been required to do so. Several concerns were noted about this – the more significant included:

(a) the costs for those entities that would be required to apply EU-adopted IFRS could not be justified in relation to the benefit to users of those entities' financial statements;

(b) inconsistencies in the recognition and measurement requirements between EU-adopted IFRS and the proposals at the time for FRS 102 would reduce comparability between entities; and

(c) the application guidance addressing the definition of public accountability remained unclear despite the guidance being developed further from the earliest proposals.

A.12 As a result, public accountability was eliminated as a differentiator and FRS 102 is applicable to all entities that are not required to apply EU-adopted IFRS (or are eligible and choose to apply another UK and Ireland accounting standard).

A.13 As a consequence of this change, various entities that are outside the scope of the IFRS for SMEs are within the scope of FRS 102. There are areas not addressed by the IFRS for SMEs that would be relevant to the broader group of entities applying FRS 102. Specifically, additional requirements were developed for financial institutions and public benefit entities (see Section 34 *Specialised Activities*) and entities whose debt or equity instruments are publicly traded but not on a regulated market (see Section 1 *Scope*). Further details are outlined in Part B.

Interaction with company law

A.14 Consideration was given to whether accounting options that had been removed because of conflicts with company law should be available to entities that are not companies. For example, SSAP 4 *Accounting for government grants* contained an option that was not permitted by company law. It was concluded that all entities applying FRS 102 should follow the same requirements; therefore requirements that conflicted with company law would be removed from FRS 102 as this would promote consistency between reporting entities regardless of the legal framework under which the entities operate.

Formats of financial statements

A.15 It was noted that there are conflicts between the formats required by the IFRS for SMEs and those required by company law, specifically in regard to the definition of current assets. It was concluded that all entities applying FRS 102 would be required to follow company law formats as this would promote consistency between reporting entities regardless of the legal framework under which they operate.

Insurance contracts

A.16 In the early stages of development, it was proposed that entities with insurance contracts should apply IFRS 4 *Insurance Contracts* to those contracts, and insurance-related contracts not meeting the definition of an insurance contract should usually be accounted for as financial instruments in accordance with Section 11 *Basic Financial Instruments* and Section 12 *Other Financial Instruments Issues*.

A.17 The various options for setting out the requirements for entities engaged in insurance business were considered, and a separate accounting standard on insurance contracts, FRS 103 *Insurance Contracts*, was developed and issued in March 2014. The Basis for Conclusions for FRS 103 accompanies that standard.

Initial effective date of FRS 102

A.18 Early consultations proposed an effective date for accounting periods beginning on or after 1 July 2013, with early application being permitted. Respondents' views regarding these proposals were very mixed with some calling for earlier adoption and others for deferral.

A.19 Key points relevant to setting the initial effective date were:

(a) An 18-month period between the publication of the final standard and effective date should be retained as there are significant changes to the accounting requirements for financial instruments.

(b) The effective date needed to take into consideration the updating of the SORPs that was required.

A.20 It was concluded that the effective date of FRS 102 should be accounting periods beginning on or after 1 January 2015.

A.21 In relation to early application of FRS 102, it was noted that as FRS 102 represents an improvement in financial reporting it would not be appropriate to prevent early application of its requirements. Early application of FRS 102 was permitted for accounting periods ending on or after 31 December 2012, which was consistent with the first date at which it was likely to be practical for entities applying FRS 101 to apply that standard.

A.22 Given that the SORPs required updating for consistency with FRS 102, early application was permitted for entities applying a SORP provided that FRS 102 did not conflict with the requirements of a current SORP or legal requirements for the preparation of financial statements.

EU Accounting Directive (July 2015)

A.23 The EU Accounting Directive (Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013) was implemented in the UK in 2015 and in the Republic of Ireland in 2017. In doing so there were changes made to company law to reflect new requirements and, when considered appropriate, to take advantage of new options that were available. FRS 102 was amended in July 2015 to reflect these changes in UK company law. Additional amendments were made in December 2017 to reflect changes in Irish company law.

A.24 A new Section 1A *Small Entities* was inserted into FRS 102 and a new standard for micro-entities, FRS 105[77], was issued in July 2015. The *Financial Reporting Standard for Smaller Entities* (FRSSE) was also withdrawn with effect from 1 January 2016. The new regime requires small entities to apply the recognition and measurement requirements of FRS 102 and the presentation and disclosure requirements set out in Section 1A.

Scope of Section 1A

A.25 Whilst the financial statements of a small company must give a true and fair view, the new legal framework for small companies restricts the disclosures that can be mandated of small companies. As these restrictions do not apply to entities that are not companies, consideration was given to whether there should be two small entities regimes; one applying to companies and one to other entities. It was concluded that it would be confusing to have two different sets of presentation and disclosure requirements for small entities depending on their legal form, particularly when the overall objectives of the financial statements are the same (ie that they give a true and fair view). Therefore Section 1A applies to all entities meeting the relevant criteria.

A.26 Eligibility for the small companies regime is set out in company law. Section 1A applies to companies eligible for the small companies regime, LLPs eligible for the small LLPs regime and any other entity that would have met the criteria for the small companies regime had they been companies. This is broadly the same as the scope of the FRSSE. Initially, different thresholds applied to the small companies regime and the small LLPs regime, but these were aligned when *The Limited Liability Partnerships, Partnerships and Groups (Accounts and Audit) Regulations 2016* (SI 2016/575) were made in May 2016.

Company law disclosure requirements for larger entities

A.27 Section 1A includes all the disclosure requirements for small companies as set out in company law. Respondents queried whether the same approach could be taken for larger entities applying FRS 102. The approach for larger entities was not changed because this would increase the length of FRS 102 and make it potentially less

[77] The Basis for Conclusions for FRS 105 accompanies that standard.

user-friendly, especially as a significant number of larger entities applying FRS 102 are not companies and the additional disclosure requirements would not be applicable to them. This approach was reconsidered as part of the triennial review 2017. No further changes were made (see paragraphs A.51 and A.52).

New accounting policy options available in company law, but not implemented in FRS 102

A.28 In implementing the EU Accounting Directive, new accounting options were made available in law alongside existing requirements. Two new options considered were:

(a) **Equity method in individual accounts**
Paragraph 29A of Schedule 1 to the Regulations and the Small Companies Regulations permit participating interests to be accounted for in the financial statements of an investor using the equity method. FRS 102 already included a number of options for accounting for such investments (see paragraph 9.26), therefore this option was not introduced.

(b) **Contingent consideration in a business combination**
An amendment to paragraph 36 of Schedule 1 to the Regulations and the Small Companies Regulations permits contingent consideration in a business combination to be measured and remeasured at fair value, which would be consistent with EU-adopted IFRS (IFRS 3 *Business Combinations* (revised 2008)). It was noted that the requirements of FRS 102 are based on IFRS 3 (issued 2004), therefore the accounting for contingent consideration was not reconsidered.

Amendments to other sections of FRS 102

A.29 A small number of other amendments were made to FRS 102 to maintain consistency with company law following the implementation of the EU Accounting Directive, including the definitions of a 'related party' and 'turnover'. Other amendments are discussed under the relevant sections of Part B of this Basis for Conclusions.

A.30 Two further amendments were also made to improve clarity that were unrelated to the implementation of the EU Accounting Directive:

(a) Two of the examples following paragraph 11.13 were amended for clarity.

(b) The reduced disclosures for subsidiaries, set out in paragraphs 1.8 to 1.13, were amended in relation to financial instruments measured at fair value through profit or loss to ensure they are consistent with company law disclosure requirements.

Residents' Management Companies (July 2015)

A.31 In considering the feedback received from previous consultations, it was noted that no clear consensus existed amongst respondents on the appropriate basis of accounting in the statutory financial statements of residents' management companies[78] that hold service charge monies on trust in accordance with section 42 of the *Landlord and Tenant Act 1987*. However, there was general agreement that no change should be made to FRS 102, or any other relevant financial reporting standard (including FRS 105), to address such a narrow and sector-specific issue.

A.32 The case for further intervention by reference to the FRC's published *Principles for the development of Codes, Standards and Guidance*[79] and, in particular, the extent to

[78] An organisation which may be referred to in the lease, which is responsible for the provision of services, and manages and arranges maintenance of the property, but which does not necessarily have any legal interest in the property.

[79] This can be found on the FRC website.

which the anticipated benefits from any changes to current practices would outweigh the costs incurred by the entities involved, were considered. It was concluded that this matter does not merit a change in accounting standards, and therefore no changes were made to FRS 102 (or FRS 105) in this regard.

Triennial review 2017

A.33 When FRS 102 was issued in March 2013, the FRC indicated that it would be reviewed every three years. This triennial review process was an opportunity to review the implementation of FRS 102 and whether it had achieved its aims, as well as to make improvements. The triennial review involved considering a wide range of potential sources of improvements and clarifications including:

(a) feedback from stakeholders on areas where FRS 102 can be improved;

(b) areas identified by the FRC for review;

(c) the IASB's 2015 *Amendments to the IFRS for SMEs*; and

(d) changes in IFRS (both new IFRS and amendments to existing IFRS) and new interpretations (IFRICs).

A.34 Amongst other sources, the FRC received and considered feedback from stakeholders through a request for information, a consultation document on the approach to changes in IFRS and exposure drafts setting out proposed amendments to FRS 102 (see Table 1 at the end of this Basis for Conclusions).

A.35 FRS 102 is an IFRS-based solution that was developed from the IFRS for SMEs. Therefore amendments to the IFRS for SMEs remained a useful source for considering the development and maintenance of FRS 102. However, the scope of FRS 102 is wider than the scope of the IFRS for SMEs and the FRC takes into account the size and range of entities applying FRS 102 when considering potential amendments. This means changes in IFRS were also relevant to FRS 102 and the FRC seeks an overall IFRS-based solution, when relevant, rather than simply maintaining consistency with the IFRS for SMEs.

Have the new standards delivered benefits?

A.36 In their feedback, a number of stakeholders highlighted some of the benefits of FRS 102. These included simpler financial statements, time-savings in preparation, greater consistency with IFRS, increased transparency and an easily readable standard.[80] Stakeholders also identified areas for possible further improvement that were considered as part of this triennial review.

A.37 The FRC continued to believe that the new UK and Ireland accounting standards have addressed the concerns that led to their development by providing a consistent IFRS-based framework, for example by improving recognition and disclosure of financial instruments. Although the triennial review was primarily about FRS 102, the FRC considered whether the suite of UK and Ireland accounting standards, as a whole, had delivered benefits.

A.38 FRS 101 is an optional standard (entities applying it could alternatively have applied FRS 102 or EU-adopted IFRS). Feedback to the annual reviews of FRS 101 suggest that this standard is being applied in practice, suggesting this is a cost-effective option for some entities. FRS 101 will continue to be subject to an annual review to provide additional disclosure exemptions as IFRS evolves and to respond to stakeholder

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[80] See also University of Worcester Business School research on behalf of the Institute of Financial Accountants, Final Report (December 2016).

feedback about other possible improvements. For example, FRS 101 was made more cost-effective by the removal of the requirement to notify shareholders prior to taking advantage of the disclosure exemptions.

A.39 FRS 102 is considerably shorter than the accounting standards that preceded it, a benefit that was highlighted by stakeholders. The succinct nature of FRS 102 was retained.

A.40 The requirements of FRS 102 have resulted in more information being available to users about the financial instruments held by a reporting entity, and therefore should have improved users' understanding of the instruments and the associated risks. Stakeholder feedback suggested that this was one of the most challenging aspects of implementing FRS 102. As part of this triennial review a number of amendments were made to respond to stakeholder feedback in this area.

A.41 FRS 105 has only been effective since 1 January 2016, and it was too early to assess the full impact of the new legal regime and associated accounting standard.

Incremental improvements and clarifications

A.42 Respondents supported the idea that the triennial review should focus on incremental improvements and clarifications. Although these amendments are effective from 1 January 2019 (four years after the initial effective date of FRS 102 and three years after small entities were brought within its scope), at present many entities have prepared no more than one or two sets of financial statements applying FRS 102 and respondents supported and emphasised the importance of allowing FRS 102 to bed down and become more familiar before more fundamental changes are proposed.

A.43 The amendments to FRS 102 are intended to improve the quality of financial reporting, the usability of the standard and/or the cost-effectiveness of the standard.

Future reviews of FRS 102

A.44 Any amendments to FRS 102 to reflect major changes in IFRS will be considered on a case-by-case basis, including the appropriate timing. The FRC agrees with respondents that, in most cases, it will be preferable to learn from IFRS implementation experience in determining whether, and if so how and when, FRS 102 should be amended.

A.45 In addition, FRS 102 will continue to be subject to periodic reviews to consider stakeholder feedback, minor changes in IFRS and the IFRS for SMEs and other issues. These periodic reviews are likely to take place every four to five years, to allow time for experience of the most recent edition of FRS 102 to develop before seeking stakeholder feedback. However, the FRC will continue to assess emerging issues as they arise to determine whether action needs to be taken. When necessary this will include issuing amendments to standards outside regular review cycles.

Undue cost or effort

A.46 During the initial development of FRS 102 respondents suggested additional guidance on the application of the term 'undue cost or effort' was necessary. It was noted that Section 2 *Concepts and Pervasive Principles* discussed the balance between benefit and cost and that no further clarification was required.

A.47 Prior to the triennial review 2017, FRS 102 included a limited number of undue cost or effort exemptions. These stemmed from the IFRS for SMEs, although some undue cost or effort exemptions in the IFRS for SMEs were not reflected in FRS 102. Some stakeholders welcomed the concept of 'undue cost or effort', which they considered provided a proportionate solution for smaller entities. However, it was noted that entities needed to apply judgement in determining whether an exemption is available in their circumstances, which has led to the exemptions being applied inconsistently in similar circumstances and therefore different costs being incurred in the preparation of financial statements. It was noted that not all entities were applying sufficient rigour in assessing the availability of the undue cost or effort exemptions; it is not an accounting policy choice.

A.48 Although the International Accounting Standards Board (IASB) introduced guidance on the meaning of undue cost or effort as part of the 2015 *Amendments to the IFRS for SMEs*, in response to the issues identified above, the undue cost or effort exemptions that existed in FRS 102 were removed. These are discussed in more detail in the relevant sections of Part B *Technical issues by section* (see sections B14 *Investments in Associates*, B15 *Investments in Joint Ventures* and B16 *Investment Property*).

A.49 The IASB introduced four new undue cost or effort exemptions in the 2015 *Amendments to the IFRS for SMEs* as follows:

(a) Investments in equity instruments at fair value (Section 11).

(b) Intangible assets acquired in a business combination (Section 18 *Intangible assets other than Goodwill*).

(c) Fair value of non-cash consideration (Section 22 *Liabilities and Equity*).

(d) Offsetting tax assets and liabilities (Section 29 *Income Tax*).

A.50 Consistent with the removal of all undue cost or effort exemptions that were in FRS 102, these new exemptions were not introduced into FRS 102. However, stakeholders had provided feedback on implementation issues relating to intangible assets acquired in a business combination and amendments were made to address that feedback (see Section B18 *Intangible Assets other than Goodwill*).

Company law requirements

A.51 As part of the triennial review 2017, the Consultation Document noted that the FRC intended to review the disclosure requirements of FRS 102 with a view to seeking greater alignment with company law requirements, when possible, and to consider whether, in the light of experience, any disclosure requirements should be amended.

A.52 The inclusion and integration into FRS 102 of company law disclosure requirements for large companies was considered. It was concluded that it was not possible to achieve this without reducing the usability of FRS 102 or reducing the quality of disclosure, due to some differences in the requirements and inconsistent use of language between the two.

Small Entities in the Republic of Ireland

A.53 In June 2017 the Republic of Ireland implemented the EU Accounting Directive. The requirements are effective for accounting periods beginning on or after 1 January 2017, but early adoption is permitted for accounting periods beginning on or after 1 January 2015 provided that the financial statements have not yet been approved.

A.54 As a result, the new small entities regime, as reflected in Section 1A of FRS 102, became available in the Republic of Ireland, however there are some differences in the disclosure requirements applicable in the UK and the Republic of Ireland.

A.55 When Section 1A was developed, feedback from stakeholders was that Appendix C to Section 1A should reflect, as closely as possible, the company law requirements. Therefore, for a consistent approach, a new Appendix D to Section 1A was inserted reflecting the disclosure requirements for small entities in the Republic of Ireland.

A.56 As the small entities regime in the Republic of Ireland is effective for accounting periods beginning on or after 1 January 2017, this was reflected in the *Triennial review 2017 amendments*.

Other suggestions

A.57 Based on stakeholder feedback, some suggestions for areas where disclosures might be reduced were considered and a small number of disclosure requirements have been deleted. In relation to financial instruments and post-employment benefits, when the required disclosures were addressing potentially significant financial risks they were not reduced.

Editorial amendments

A.58 Various editorial amendments were made to FRS 102. These editorial amendments were not intended to change the requirements of FRS 102, but improve drafting, usability and update external cross-references. For example, they included:

(a) improving the consistency of the scope sections throughout the standard to make it clearer what is within and outside the scope of each section;

(b) removing defined terms from the main body of the standard to reduce its length, as defined terms are set out in Appendix I *Glossary*; and

(c) improving the consistency of terminology and language in some areas.

A.59 Appendix II *Significant differences between FRS 102 and the IFRS for SMEs* was deleted as it is likely to have been of limited use as the IFRS for SMEs is not available for use in the European Union.

A.60 Appendix V *Previous consultations* was removed. More detailed information on the early development of the standard can be found on the FRC website.

Effective date of the triennial review 2017 amendments

A.61 In general the triennial review 2017 amendments are effective for accounting periods beginning on or after 1 January 2019, with early application permitted provided all the amendments are applied together. The only exceptions are:

(a) The amendments to paragraphs 11.13A(a), 11.13B, 11.13C and 11.14(a)(i), which relate to directors' loans, for which early application is permitted without early application of the rest of the triennial review 2017 amendments. Separate early application was permitted in order to extend the interim relief granted in May 2017 to all circumstances within the scope of the exemption.

(b) The amendments to paragraphs 29.14A and 29.22A, which relate to gift aid payments made within charitable groups, for which early application is permitted without early application of the rest of the triennial review 2017 amendments. Separate early application was permitted following feedback from respondents.

(c) Small entities in the Republic of Ireland, for which the effective date is aligned with the implementation of the *Companies (Accounting) Act 2017* (see paragraph A.56).

A.62 As the amendments focused on incremental improvements and clarifications, there were only limited circumstances in which a significant change in accounting policy would result from applying the amendments. Transitional arrangements were provided to:

(a) permit entities to carry forward fair value as deemed cost for investment property that are rented to another group entity, when they are to be measured based on cost going forward – this made a choice available that would have existed on first-time adoption of FRS 102 if this investment property had not been measured at fair value in the meantime (previous UK and Ireland accounting standards would not have regarded such property as investment property); and

(b) require entities to continue to recognise separately any intangible assets separated from goodwill in business combinations effected since transition to FRS 102.

UK exit from the European Union

A.63 In January 2020 the UK exited the European Union. As a result, changes were required to UK company law to ensure that it continues to operate effectively. FRS 102 was amended in December 2020 to reflect these changes. This included amending the references to 'EU-adopted IFRS' to read 'adopted IFRS', which incorporates the accounting standards referred to in both UK and Irish company law (UK-adopted international accounting standards and EU-adopted IFRS, respectively).

A.64 Early application is permitted by entities in the UK, which is consistent with the transitional arrangement provided in UK company law for entities preparing 'IAS accounts'. Application of the amendments to an accounting period beginning before 1 January 2021 allows entities to use IAS that are adopted for use within the UK after 31 December 2020 in their individual accounts, which may be relevant when FRS 102 permits or requires the application of a specific IFRS (as adopted in the relevant jurisdiction).

Part B – Technical issues by section

B1 Section 1 *Scope*

Entities listed but not on a regulated market

B1.1 Users need additional information about entities that are listed but not on a regulated market, namely earnings per share and operating segments. These areas were not addressed in the IFRS for SMEs and therefore accounting requirements were set in this section by cross-reference to the relevant adopted IFRS to ensure that the standard remained succinct.

Reduced disclosures

B1.2 As part of the implementation of the EU Accounting Directive in July 2015 it was clarified in paragraph 1.12(c) that, because company law requires certain disclosures relating to financial instruments, a qualifying entity choosing to provide reduced disclosures will not be exempt from all the disclosure requirements of Sections 11 and 12. This was previously addressed in paragraph A4.10, which notes that preparers need to have regard to the requirements of company law in addition to accounting standards.

Notification of shareholders

B1.3 In December 2016, this section and FRS 101 *Reduced Disclosure Framework* were amended to remove the requirement to notify shareholders of the intention to take advantage of reduced disclosures.

B1.4 Complying with this requirement was considered no longer cost-effective in practice and sufficient information will continue to exist for minority shareholders to understand the effects of the reduced disclosure framework.

B1.5 In removing the requirement, it was noted that:

(a) The overall level of disclosure required is not less than that required by previous UK accounting standards, taking into account exemptions that were available for subsidiaries.

(b) The shareholders in an ultimate parent entity will receive the consolidated financial statements of the group as well as the parent entity's individual financial statements. These consolidated financial statements will include full disclosure in accordance with the relevant accounting framework.

(c) Notifying all shareholders of an ultimate parent entity in writing could lead to a significant cost being incurred.

(d) A shareholder that controls a qualifying entity can exercise that control in relation to the financial reporting of its subsidiary without the need for an additional opportunity to object.

(e) A qualifying entity is required to disclose a summary of the disclosure exemptions adopted. Any prospective shareholders will be aware of the use of the reduced disclosure framework from the prior period financial statements.

(f) Company law does not generally require shareholder agreement, or provide an opportunity to object, to disclosure exemptions. However, company law does provide shareholders with other rights to influence the company's actions and protections for minority shareholders.

B1.6 Some respondents suggested further consideration be given to retaining the right to object for shareholders holding a specified proportion of the voting rights. A specific right to object to the use of disclosure exemptions is not necessary given the information available to shareholders and their existing rights.

B1A Section 1A *Small Entities*

B1A.1 Section 1A *Small Entities* was inserted into FRS 102 in July 2015 following the implementation of the EU Accounting Directive.

True and fair view

B1A.2 A key feature of the new small companies regime is that it specifies the maximum disclosure that can be mandated for inclusion in a small company's financial statements. However, the financial statements of a small company must still give a true and fair view of the financial performance and financial position of the entity; this has been emphasised in Section 1A. The directors of a company will need to consider whether additional disclosures are necessary to give a true and fair view and, if so, provide those additional disclosures.

B1A.3 To help small entities applying Section 1A, the disclosures required by law are included and cross-referenced to the same or similar disclosures elsewhere in FRS 102. For UK small entities this is set out in Appendix C to Section 1A, for Irish small entities this is set out in Appendix D to Section 1A, which was added in December 2017 following the implementation of the EU Accounting Directive in Ireland in June 2017. The drafting of these disclosures is as close as possible to the relevant company law requirements, with a note of the source of the legal requirement, and an indication of which paragraphs of FRS 102 address similar requirements.

B1A.4 There are a small number of additional non-mandatory disclosures considered to be useful to users of the financial statements of a small entity; these are set out in Appendix E to Section 1A. Section 1A encourages small entities to provide these disclosures.

B1A.5 The disclosures required by FRS 102 of larger entities are those that are usually considered necessary (but not necessarily sufficient) for them to give a true and fair view, therefore small entities are encouraged to consider these disclosures in order to determine the additional disclosures necessary in their own circumstances.

Additional financial statements

B1A.6 Another feature of the small companies regime is that additional 'statements' may not be required of small companies. This includes a statement of comprehensive income, a statement of changes in equity and the cash flow statement. Section 1A makes it clear that such statements are not required of small entities, but that a statement of comprehensive income and a statement of changes in equity (or statement of income and retained earnings) will be useful to users of the financial statements of a small entity in explaining the financial performance for the reporting period and the effect that this has had on financial position. Section 1A encourages small entities to provide these statements.

B1A.7 Although the FRSSE encouraged the presentation of a cash flow statement by small entities, FRS 1 (Revised 1996) *Cash flow statements* exempted small entities from presenting a cash flow statement on the basis that it was not required by company law for a small company. The exemption from FRS 1 has been retained and, as a result, a small entity choosing to apply ‘full’ FRS 102 is not required to present a cash flow statement.

Recognition and measurement

B1A.8 Small entities are required to follow the same recognition and measurement requirements of FRS 102 as larger entities; this continues the application of the principle of consistency in accounting policies between those entities that are smaller and those that are larger that applied when the FRSSE was originally developed. This improved financial reporting by small entities by requiring, for example, the recognition of financial instruments that the FRSSE did not require, such as derivatives like interest rate swaps and forward foreign currency contracts.

B1A.9 Generally, all entities within the scope of FRS 102 should be subject to consistent recognition and measurement requirements, although occasional specific exemptions may be granted in order to meet the principle of providing proportionate and practical solutions. In May 2017, as an interim measure, and then as part of the *Triennial review 2017 amendments*, an exception was introduced, which allows small entities to apply simpler accounting for directors’ loans (see paragraphs B11.32 to B11.40).

Related party disclosures

B1A.10 Following the implementation of the EU Accounting Directive, company law restricts the disclosures that can be required of small companies in relation to related party transactions. Specifically, disclosure can only be required of transactions not conducted under normal market conditions. Respondents noted that it could be burdensome for a small entity to identify those related party transactions that were not conducted under normal market conditions, because a significant degree of judgement would be involved. Instead, disclosure of all transactions with the specified related parties would meet the legal disclosure requirement. It was noted that the Accounting Regulatory Committee reached a conclusion in 2007 that disclosing all related party transactions would comply with the requirement to disclose those not conducted under normal market conditions (as previously set out in paragraph 36 of Appendix IV to FRS 8 *Related Party Disclosures*). Therefore additional guidance is included in Appendix C and Appendix D to Section 1A to this effect.

Transitional arrangements for small entities

B1A.11 It was noted that FRS 102 already includes Section 35 *Transition to this FRS*, which applies to any first-time adopter of FRS 102, which has a significant number of optional exemptions from full retrospective application of FRS 102 that are designed to reduce the burden of first-time adoption. This is particularly useful when it may be difficult to restate historical transactions on the basis otherwise required by FRS 102 because the relevant data would not have been obtained at the time the transaction occurred.

B1A.12 A small number of respondents suggested that some additional transitional arrangements should be made available to small entities. These suggestions related to areas where additional burdens may be incurred in applying FRS 102 for the first time because an entity’s transition date to FRS 102 occurred before these amendments were finalised.

B1A.13 Consequently, additional transitional exemptions for all small entities applying FRS 102 for the first time for an accounting period that commences before 1 January 2017 were given. These related to equity-settled share-based payment arrangements, financial instruments measured at fair value and financing transactions with related parties. On first-time application they provided relief from the full application of FRS 102 in the comparative period.

B2 Section 2 *Concepts and Pervasive Principles*

B2.1 In December 2017, as part of the *Triennial review 2017 amendments*, the fair value guidance from Section 11 *Basic Financial Instruments* was moved to an appendix to Section 2 *Concepts and Pervasive Principles* (see section B11 Section 11 *Basic Financial Instruments*).

B3 Section 3 *Financial Statement Presentation*

'Fair presentation' and 'true and fair'

B3.1 In July 2015, as part of the implementation of the EU Accounting Directive, Section 3 *Financial Statement Presentation* was amended to more closely reflect the requirements of company law. These changes are not considered to have any substantive effect as 'true and fair' and 'presents fairly' are synonymous, being different articulations of the same concept, as confirmed by legal opinion.

Comparative information

B3.2 A small number of respondents to the triennial review 2017 outreach queried whether comparatives are always necessary for disclosures required only by a SORP (ie disclosure that is not required by FRS 102). Comparatives are intended to provide useful information to users, and FRS 102 only provides an exemption from comparatives in limited circumstances reflecting historical company law exemptions. Therefore, in accordance with paragraph 3.14, comparatives should be provided for disclosures required by SORPs.

B4 Section 4 *Statement of Financial Position*

B4.1 In July 2015, as part of the implementation of the EU Accounting Directive, Section 4 *Statement of Financial Position* was amended to allow greater flexibility in relation to the format of the balance sheet. This allows entities choosing this option to adopt a presentation that is closer to that applied by entities preparing 'IAS accounts'.

B5 Section 5 *Statement of Comprehensive Income and Income Statement*

Requirements from FRS 3

B5.1 As noted in paragraph A.15 there are conflicts between the formats required by the IFRS for SMEs and those required by company law, however the Companies Act formats on their own are not sufficient and should be supplemented to highlight a range of important components of financial performance to aid users' understanding of the performance of the entity. Therefore, additional requirements were included in FRS 102, after considering the requirements of FRS 3 *Reporting Financial Performance*:

(a) a requirement to disclose the post-acquisition revenue and profit or loss of an acquiree in a business combination in the notes to the financial statements; and

(b) an explicit requirement to disclose material items.

B5.2 In addition, although no mandatory requirement to disclose an operating profit line was included, guidance was provided on matters to consider when entities choose to present operating profit. However, the FRS 3 requirement to show profits or losses on sale or termination of an operation, costs of a fundamental reorganisation materially affecting the operation and profits and losses on disposal of fixed assets separately on the face of the profit and loss account was not included.

B5.3 In view of the company law requirement that turnover includes the turnover from discontinued operations, the Appendix to Section 5 *Statement of Comprehensive Income and Income Statement* sets out a practical, columnar approach to presenting this and the post-tax profit or loss on discontinued operations.

Greater flexibility

B5.4 In July 2015, as part of the implementation of the EU Accounting Directive, Section 5 was amended to allow greater flexibility in relation to the format of the profit and loss account. This allows entities choosing this option to adopt a presentation that is closer to that applied by entities preparing 'IAS accounts'.

Classification of expenditure

B5.5 As part of the *Triennial review 2017 amendments*, paragraph 5.11 was deleted because it effectively duplicated the requirements of paragraph 5.5, since the profit and loss account formats in the Regulations include requirements for the classification of expenditure. This change was not expected to significantly change the information presented in financial statements.

B7 Section 7 *Statement of Cash Flows*

Net debt reconciliation

B7.1 In January 2016, the IASB issued amendments to the requirements for cash flow statements in *Disclosure Initiative (Amendments to IAS 7)*. The amendments introduced requirements to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes.

B7.2 In considering whether to introduce these additional disclosures into FRS 102 as part of the triennial review 2017, it was noted that the previous requirement to disclose a reconciliation of net debt in paragraph 33 of FRS 1 (Revised 1996) *Cash Flow Statements* gives users better information as it takes into account cash balances as well as the borrowings of an entity. Although this is a departure from an IFRS-based solution, it clearly better meets the overriding objective and entities will already be familiar with the disclosure and therefore it will be more cost-effective to apply. As a result, FRS 102 was amended to include a requirement to produce a net debt reconciliation.

B9 Section 9 *Consolidated and Separate Financial Statements*

Definitions of control, parent and subsidiary

B9.1 The definitions of control, parent and subsidiary included in FRS 102 are consistent with the IFRS for SMEs (and based on EU-adopted IFRS prior to the issuing of IFRS 10 *Consolidated Financial Statements*), but differ from those used in previous accounting standards. Some respondents queried whether the definitions should be based on company law. This suggestion was rejected, but it was noted that by using the definitions from the IFRS for SMEs the application of control would be widened to include certain special purpose entities within the definition of a group. However, this does not include employee benefit trusts and ESOPs (which should continue to be accounted for as if they are assets and liabilities of the sponsoring entity).

Control model in IFRS 10 *Consolidated Financial Statements*

B9.2 As part of the triennial review 2017, the Consultation Document proposed making limited amendments to FRS 102 to update it for the control model in IFRS 10. It noted that the change would result in better financial reporting as it addresses concerns about the boundary of the reporting entity, but that for many entities, the changes would have no effect and that this could be determined quickly and cost-effectively, limiting the costs of implementation.

B9.3 Respondents disagreed with this proposal. Feedback received included the following:

(a) The cost of implementation would far outweigh the benefit given that there would be no practical effect for the vast majority of entities, yet all entities would still have to go through an exercise to determine that there is no change.

(b) The proposal did not meet with the new principle of balancing improvements with stability.

(c) A significant amount of additional implementation guidance would need to be added to FRS 102 to ensure the revised definition could be applied in practice.

(d) The main impact of implementing IFRS 10 has been felt in financial institutions that have complex structured entities.

B9.4 Consequently, no changes were made to FRS 102 regarding the entities to be included in consolidated financial statements, but an additional disclosure regarding unconsolidated structured entities (such as special purpose entities) was introduced to improve the information available to users about any such entities. This principle-based disclosure was derived from IFRS 12 *Disclosure of Interests in Other Entities*.

Employee benefit trusts, ESOPs and similar arrangements

B9.5 In clarifying the requirements for consolidation, including considering consistency with company law requirements, it was noted that the accounting treatment for employee benefit trusts, ESOPs or similar arrangements would give rise to a change in accounting from previous accounting standards. The withdrawal of UITF Abstract 38 *Accounting for ESOP trusts* would mean that such arrangements would no longer be included in individual financial statements but only in consolidated financial statements. Further, for an entity with such an arrangement, which is not a parent entity, a change in accounting requirements would lead to the preparation of 'group' financial statements when they would otherwise not have been required. Therefore the accounting treatment from UITF Abstract 32 *Employee benefit trusts and other intermediate payment arrangements* was included in Section 9 *Consolidated and Separate Financial Statements* of FRS 102.

Investment entities exemption from consolidation

B9.6 In September 2011 the IASB issued an exposure draft proposing to exempt qualifying investment entities from consolidating their investments. The accounting requirements were finalised and published as an amendment to IFRS 10, IFRS 12 and IAS 27 *Separate Financial Statements* in October 2012. The FRC noted that without a similar exemption in FRS 102, investment entities eligible to apply FRS 102 would need to elect to prepare EU-adopted IFRS in order to take advantage of the exemption. This was not considered to be a logical or meaningful outcome and therefore a solution was sought.

B9.7 Section 405(3) of the Act permits a subsidiary to be excluded from consolidation on the following grounds:

(a) severe long-term restrictions substantially hinder the exercise of the rights of the parent company over the assets or management of that subsidiary;

(b) the information necessary for the preparation of group accounts cannot be obtained without disproportionate expense or undue delay; or

(c) the interest of the parent company is held exclusively with a view to subsequent resale.

B9.8 FRS 102 was developed such that the definition of an interest held exclusively with a view to subsequent resale included interests held as part of an investment portfolio.

B9.9 Subsidiaries excluded from consolidation and held as part of an investment portfolio shall be measured at fair value through profit or loss. In some cases this will be a departure from the requirements of the Companies Act for the overriding purpose of giving a true and fair view in the consolidated financial statements (see paragraph A3.17).

Changes in stake and gains and losses on disposals

B9.10 It was noted that the requirements of the IFRS for SMEs in relation to changes in stake and gains and losses on disposals were not entirely coherent, being based partly on IFRS 3 *Business combinations* (issued 2004) and partly on IFRS 3 *Business combinations* (revised 2008), and further, some of the requirements are not consistent with company law on the recognition of unrealised gains.

B9.11 Therefore, a coherent model for increases and decreases in stakes held in another entity was required which was also consistent with company law. As a result, these requirements of FRS 102 are based on IFRS 3 (issued 2004).

B9.12 In 2017 as part of the triennial review it was confirmed that no changes will be made to FRS 102 for greater consistency with IFRS 3 (revised 2008).

Control in PBE sectors

B9.13 The issues of control and the indicators of control that may be specific to the PBE sectors were considered. The indicators of control set out in Section 9 focus on benefits, and in the PBE sectors, benefit can be in the form of indirect benefit through a PBE's beneficiaries or benefit which furthers a PBE's activities. It was concluded that FRS 102 can be interpreted and applied to PBEs and therefore no separate guidance for PBEs was considered necessary.

B11 Section 11 *Basic Financial Instruments* and Section 12 *Other Financial Instruments Issues*

Improvement in accounting for financial instruments

B11.1 One of the most significant changes introduced by FRS 102 related to the recognition, measurement and disclosure of financial instruments, including derivatives. Entities use derivatives to manage risk and it is important that financial statements recognise and provide disclosures about the effect of those instruments on the entity's performance and position. Previous accounting standards contained limited requirements on accounting for financial instruments for unlisted entities or those that do not apply the fair value accounting rules. This approach, where derivatives were not recognised, did not adequately reflect the risks arising from financial instruments. FRS 102 has led to an improvement in accounting for financial instruments.

B11.2 During the development of FRS 102, the concern, primarily from the social housing sector, that the measurement of derivatives used for hedging purposes at fair value may result in volatility in profit or loss, was noted. However, it was concluded that it would not be consistent with the objective of providing high-quality information, or the guidelines for amending the IFRS for SMEs, to change the recognition and measurement requirements for derivatives. Recognition and measurement of derivatives at fair value, with associated disclosure, provides relevant information to users about the risks an entity has in relation to its financial instruments.

Accounting policy choices

B11.3 In order to allow entities applying FRS 102 maximum flexibility, entities have a choice of either:

(a) applying the requirements of Section 11 *Basic Financial Instruments* and Section 12 *Other Financial Instruments Issues* of FRS 102;

(b) applying the recognition and measurement provisions of IAS 39 *Financial Instruments: Recognition and Measurement* (as adopted in the relevant jurisdiction) as the standard applies prior to the application of IFRS 9 *Financial Instruments*; or

(c) applying IFRS 9 (as far as it has replaced the requirements of IAS 39) and IAS 39 (as far it remains applicable if IFRS 9 is applied).

B11.4 By providing these accounting policy choices entities have the flexibility to apply the accounting requirements of IFRS 9 without delay should they wish to do so.

B11.5 As part of the triennial review 2017, the Consultation Document asked for feedback on the proposal to retain the accounting policy choice in Section 11 and Section 12 of FRS 102 to apply the recognition and measurement requirements of IAS 39 following the mandatory effective date of IFRS 9. FRS 102 was amended to retain that option, and it is available until the FRS 102 requirements for the impairment of financial assets have been amended to reflect IFRS 9, or it is otherwise decided not to amend FRS 102 further in relation to IFRS 9. The IAS 39 EU carve-out also continues to be available.

Scope

Financial guarantee contracts

B11.6 Financial guarantee contracts are within the scope of Section 21 *Provisions and Contingencies* unless an entity has chosen to apply IAS 39 and/or IFRS 9, or has an existing accounting policy of insurance contract accounting for financial guarantee contracts and chooses to continue to apply that policy under FRS 103 *Insurance Contracts*.

Use of the term 'derivatives'

B11.7 As part of the triennial review 2017, a number of minor changes were made to Sections 11 and 12 arising from comments received from stakeholders, including a more direct reference to 'derivatives' in the relevant paragraphs. Previously, these sections avoided the word creating ambiguity for stakeholders. Given that it is already defined in FRS 102, this change improved the drafting. One consequence of this is a change to the definition of a financial liability, but this is not expected to have any practical effects.

Classification of financial instruments

B11.8 In July 2014, amendments to Section 11 were made to address concerns raised in relation to the classification of financial instruments. After the publication of FRS 102, feedback from stakeholders indicated that the implementation of the accounting requirements of FRS 102 for loans with common contractual features could have unintended consequences for many entities because the conditions for classification as basic were overly restrictive.

B11.9 The classification of financial instruments as 'basic' or 'other' in FRS 102 is dependent on a list of prescriptive conditions. Consideration was given to whether a principles-based solution to relaxing the conditions, based on the principle articulated in IFRS 9 in respect of the classification of financial assets, would be more effective. However, the rules-based conditions of FRS 102 were retained for the following reasons:

(a) the IFRS 9 principle was as yet untested in practice and, at the time, the IASB was debating possible amendments to IFRS 9; and

(b) the IFRS 9 principle in relation to the classification of financial instruments only applies to financial assets. The classification conditions in FRS 102, however, apply equally to debt instruments that are assets or liabilities.

B11.10 The amendments were intended to ensure that common financial instruments can be measured at amortised cost, when measurement at amortised cost is appropriate. They also aligned FRS 102 more closely with the measurement requirements of IFRS.

B11.11 Paragraph 11.8 included a list of financial instruments that were classified as 'basic'. For some of these financial instruments, the classification as 'basic' or 'other' was further dependent on meeting a list of prescriptive conditions; for debt instruments these were set out in paragraph 11.9. Feedback from stakeholders, as part of the triennial review 2017, clearly highlighted that this rules-based classification caused significant problems for those applying FRS 102, highlighting a number of judgement areas and other implementation difficulties.

B11.12 As a result, as part of the *Triennial review 2017 amendments*, in addition to those debt instruments that meet the conditions in paragraph 11.9, a debt instrument shall be classified as 'basic' if it is consistent with a principle-based description of a 'basic' financial instrument. This description, set out in paragraph 11.9A, need only be considered for debt instruments that do not meet the detailed conditions in paragraph 11.9. Making such a change better articulated the principle for classification as 'basic' financial instruments and set the boundary for more complex debt instruments.

B11.13 The description requires a 'basic' debt instrument to give rise to cash flows on specified dates that constitute reasonable compensation for the time value of money, credit risk and other basic lending risks and costs. Such reasonable compensation is dependent on the prevailing economic conditions and monetary policies in operation.

B11.14 In addition, amendments were made to the examples following paragraph 11.9A, including the addition of new examples to address feedback from stakeholders.

Loans in the social housing sector

B11.15 A number of respondents from the social housing sector raised concerns about the classification of certain lending arrangements common within that sector. It was noted that a number of these arrangements were structured in different ways but often to achieve the same economic outcome. After detailed consideration it was concluded that a loan cannot be classified as basic if it includes contractual terms giving the lender the unilateral option to change the terms of that loan, for example from a pre-determined fixed rate to a variable rate or to a different fixed rate chosen by the lender, even if the holder can avoid it by repaying the loan.

Loans with two-way compensation clauses

B11.16 In June 2016 the FRC commented on issues arising in relation to accounting for social housing loans. This related to the classification of loans with two-way compensation clauses, and the FRC noted that the conditions set out in paragraph 11.9 would be reviewed as part of the triennial review 2017.

B11.17 As noted above, the conditions for the classification of a financial instrument as basic were reviewed, and a number of amendments made, notably the inclusion of paragraph 11.9A. In addition, the IASB has completed its project *Prepayment Features with Negative Compensation (Amendments to IFRS 9)*, which considered a similar issue, and the FRC was able to consider its solution.

B11.18 Respondents considered that the proposed inclusion of paragraph 11.9A did not adequately address this issue, which could be resolved by a simple amendment to paragraph 11.9(c) noting that compensation could be paid by either the holder or the issuer. This amendment was made.

Structured financial instruments

B11.19 A number of respondents raised questions about the classification of certain financial instruments that were structured in a complex way and requested that FRS 102 clarify their classification. It was noted that such structured financial instruments are not based on contracts that are standardised across an industry. As a result, the repayment of principal and interest on such loans can be impacted in a complex way by a number of different variables defined in the contractual terms. Therefore it was not possible to conclude on the classification of such financial instruments without a close reading of the individual contracts and an understanding of the detailed clauses. Therefore, the reporting entity's directors should apply their judgement to determine whether the contractual terms enable a financial instrument to be classified as basic in accordance with the requirements in FRS 102.

Classification subsequent to initial recognition

B11.20 The FRC noted that the initial classification assessment of a financial instrument should take into account the relevant clauses dealing with the returns and any subsequent contractual variations relating to returns, prepayments and extensions of terms etc. Once the classification of a financial instrument is determined at initial recognition, no re-assessment is required at subsequent dates unless there is a modification of contractual terms. From December 2017 this requirement has been reflected in paragraph 11.6A.

Measurement of financial instruments

Interaction with the Regulations or LLP Regulations on measurement of certain financial instruments

B11.21 The FRC was made aware of an issue in relation to a conflict between the Regulations and LLP Regulations and the requirements in FRS 102 (as originally issued in March 2013) regarding the measurement of some financial liabilities. The original text of FRS 102 could have resulted in the standard requiring certain financial liabilities to be measured at fair value when such measurement may be prohibited by the Regulations. The Regulations prohibit the measurement of financial liabilities at fair value, except for those held as part of a trading portfolio, that are derivatives or when permitted by UK-adopted international accounting standards.

B11.22 For example, the original text of FRS 102 would have required certain financial liabilities, where the cash outflows are linked to non-financial variables specific to one party to the contract, to be classified as other and measured at fair value. Fair value measurement is not permitted for such liabilities under UK-adopted international accounting standards and so would be prohibited by the Regulations.

B11.23 The FRC was aware that there were divergent views on what constitutes a 'non-financial variable' in other cases. For example, there is no clear consensus on whether measures of performance such as turnover, profits or EBITDA are 'non-financial variables ... specific to a party to the contract'. The FRC was unable to resolve this divergence as to do so would involve interpreting UK-adopted international accounting standards on an issue that the IFRS Interpretations Committee had so far not reached a definitive conclusion on.

B11.24 Similarly, FRS 102 would have required financial assets that are similarly linked to non-financial variables specific to one party to the contract, to be classified as other and measured at fair value through profit or loss. Although the Regulations permit financial assets to be measured at fair value, this measurement is only available as permitted by UK-adopted international accounting standards, which in some cases is restricted to fair value through other comprehensive income.

B11.25 The FRC also noted that there may be other non-basic financial assets and liabilities that UK-adopted international accounting standards, and hence the Regulations, would not permit to be measured at fair value through profit or loss although it expected that such instruments would be rare in practice.

B11.26 As a result, an exception is included in paragraph 12.8(c) in respect of financial instruments when the Regulations would not permit the use of fair value through profit or loss, instead requiring them to be measured at amortised cost. This exception would only be applicable to a small number of entities under a narrow set of circumstances.

Designation at fair value through profit or loss

B11.27 The original edition of FRS 102 (issued in March 2013), as a change from the IFRS for SMEs, included an option in Section 11 to designate debt instruments to be measured at fair value through profit or loss.

B11.28 Section 11 was further amended in July 2014 to allow the designation of loan commitments at fair value through profit or loss. This amendment allows economic hedge accounting when an entity balances the risks from an instrument by taking out a second which is measured at fair value; the entity can choose to measure the first instrument at fair value, thus matching the movements in profit or loss and reflecting, in financial reporting, the combined economic effect of the instruments.

Measurement at fair value

B11.29 In July 2015, as part of the implementation of the EU Accounting Directive, Section 11 was amended to reflect changes to certain requirements relating to financial instruments that are, or may be, measured at fair value. The new Accounting Directive permits measurement of certain financial instruments at fair value when it is in accordance with EU-adopted IFRS[81]; previously this was restricted to IFRS endorsed by 5 September 2006. The consequences of this change, as well as any interaction with IFRS 9 (issued in July 2014), were considered. The amendments that were made for compliance with company law are only likely to affect a minority of entities applying FRS 102. Appendix III *Note on legal requirements* advises that entities applying IFRS 9 will need to consider an override of the Regulations for the purposes of giving a true and fair view, in order to recognise certain fair value gains or losses in other comprehensive income.

Investments in shares

B11.30 Prior to the *Triennial review 2017 amendments*, FRS 102 required investments in non-convertible preference shares and non-puttable ordinary shares or preference shares to be measured at fair value (unless they cannot be measured reliably). This requirement was based on the legal form of the instruments and created an anomaly whereby certain preference shares that are liabilities of the issuer (and measured at amortised cost) were treated differently by the holder.

B11.31 The reference to such investments in shares was amended to non-derivative financial instruments that are equity of the issuer. This simplified the drafting, but also improved the accounting for those instruments that are liabilities of the issuer by requiring measurement at amortised cost (if the instrument is classified as 'basic').

Directors' loans

B11.32 Many stakeholders provided feedback on the accounting for directors' loans. Prior to the *Triennial review 2017 amendments*, FRS 102 required all financing transactions (except public benefit entity concessionary loans) to be measured at the present value of the future payments discounted at a market rate of interest for a similar debt instrument. This included directors' loans (ie loans from a director to a company in which that director is also a shareholder) that are non-interest bearing, or bear interest at a non-market rate. The FRC continues to believe that this is generally appropriate accounting which reflects the fact that such transactions contain both an interest-bearing loan and the transfer of value representing the saving compared to market rates of interest.

B11.33 However, concerns were raised about some of the practicalities of the accounting requirements, in particular that such loans are often made by directors, especially those of small companies, because commercial funding is unavailable and therefore it is difficult to determine an appropriate market rate for a similar debt instrument.

B11.34 These concerns, including comments about the nature of the transaction in the context of a small entity where the same individual is employee, director, shareholder and lender were considered. It was also noted that FRS 102 did include an

[81] Following the UK exit from the EU, paragraph 36(4) of Schedule 1 to the Regulations (and the equivalent requirements of the Small Companies Regulations, the Small LLP Regulations and the LLP Regulations) permits measurement of certain financial instruments at fair value when it is in accordance with UK-adopted international accounting standards.

exemption from the financing transaction requirements for public benefit entity concessionary loans, which had been provided on the basis of difficulties in measuring such loans at fair value and the information that users might find useful.

B11.35 Generally, all entities within the scope of FRS 102 should be subject to consistent recognition and measurement requirements, although occasional specific exemptions may be granted in order to meet the principle of providing proportionate and practical solutions.

B11.36 The FRC considered possible solutions to the issues raised and, for small entities, proposed a more proportionate accounting solution for a loan from a director who is a natural person and a shareholder in the small entity (or a close member of the family of that person), which would permit the loan to be initially measured at transaction price. Initial reactions to the proposal were favourable and, with small entities mandatorily coming within the scope of FRS 102 from 1 January 2016, stakeholders requested earlier application in order to prevent small entities making adjustments to directors' loans for one year only for this to be reversed when the amendments to FRS 102 were finalised. As a result, in May 2017 the FRC made an interim amendment to FRS 102 to allow immediate relief for small entities pending a permanent solution. This was included in paragraph 1.15A, which has now been deleted.

B11.37 Respondents agreed with the proposals, but a number of respondents suggested that the exemption should apply to additional transactions, such an intragroup transactions and loans from all directors or all shareholders. The FRC considered these suggestions and the reasons for the exemption. The exemption is intended to provide relief to small owner-managed businesses. Transactions between entities within a group are subject to other considerations, including the nature of transactions between the entities and when a distribution or investment has occurred. Therefore the exemption was not extended to transactions between group entities.

B11.38 The FRC considered how to define 'owner-managed' for the purposes of this exemption. Some small businesses are operated and financed by a group of family members, who may have varying interests in the business. This had been recognised in the proposal by permitting loans from a close family member of a director-shareholder to qualify for the exemption. However, this did not necessarily include all situations where relief was intended. Therefore relief is now available for loans to small entities from a directors' group of close family members (which includes the director), when that group also includes a shareholder in the entity. As a result, a loan from a director, who is not a shareholder and has no close family members that are shareholders, will not qualify for the relief.

B11.39 Relief has also been extended, on a similar basis, to small LLPs.

B11.40 Loans from directors, or shareholders with a participating interest, to a small entity that are non-interest bearing, or bear interest at a non-market rate, fall within the disclosure requirements of paragraphs 1AC.35 or 1AD.51. Small entities are encouraged to consider whether disclosure about such loans from other parties is necessary for the purposes of giving a true and fair view.

Fair value measurement guidance

B11.41 Prior to the *Triennial review 2017 amendments*, FRS 102 contained guidance on fair value measurement in paragraphs 11.27 to 11.32. These paragraphs were cross-referenced from a number of sections of FRS 102 when fair value measurement was permitted or required.

B11.42 As these paragraphs are of general application, rather than relevant only to financial instruments, and illustrate a measurement basis described in Section 2 *Concepts and Pervasive Principles*, they were moved to a new appendix to Section 2. This did not change the scope and application of the guidance, although some improvements were made to the guidance.

B11.43 The Consultation Document suggested that key definitions in FRS 102 relating to fair value and paragraph 11.27 (now paragraph 2A.1), which sets out the process for estimating fair values, may be amended for greater consistency with IFRS 13 *Fair Value Measurement*.

B11.44 Respondents' feedback highlighted that incorporating the IFRS 13 definition of fair value may lead to unintended consequences. That definition, anchored as it is in the market approach, may lead to changes that would be particularly significant for certain entities that have only recently implemented the FRS 102 fair value requirements.

B11.45 Stakeholders have previously provided feedback that although the fair value measurement guidance hierarchy in FRS 102 is not identical to the disclosure hierarchy for financial institutions and retirement benefit plans, a change to paragraph 11.27 was not essential as it simply provides a methodology for approaching fair value measurement.

B11.46 As a result, the definition of fair value was not amended, and only minor changes were made to paragraph 11.27, for example to emphasise that it is a methodology and give further practical guidance.

Impairment

B11.47 Originally it was planned to amend FRS 102 prior to its effective date in respect of the requirements relating to the impairment of financial assets, once the IASB's project on impairment was completed. However, the IASB's work on the expected credit loss model was not completed until July 2014 and therefore the FRC's consultation on introducing equivalent requirements in FRS 102 was deferred. Respondents to FRED 51 requested the exemption of certain entities from the requirement to adopt the impairment accounting requirements in FRS 102 until any new impairment requirements in FRS 102 are finalised.

B11.48 The FRC deliberated on the likely impact of the adoption of the impairment accounting requirements in FRS 102. It concluded that the incurred loss impairment model in FRS 102 is consistent with UK GAAP, as applicable prior to the introduction of FRS 102. The FRC considered that it was therefore unnecessary to provide a temporary relief from the impairment accounting requirements in FRS 102.

B11.49 In 2017, as part of the triennial review, it was confirmed that further evidence-gathering and analysis will be undertaken before a decision is made on reflecting the principles of the expected credit loss model of IFRS 9 in FRS 102, if at all.

Interest rate benchmark reform (Phase 2)

B11.49A Interest rate benchmarks such as the London Interbank Offered Rate (LIBOR) are being reformed, and it is anticipated that LIBOR will not be available after 2021. As a consequence, entities have to amend contractual terms referenced to LIBOR and other interest rate benchmarks and switch to new alternative benchmark rates. Whilst changes to financial assets or financial liabilities are common, the financial reporting implications for changes that are required by interest rate benchmark reform could not have been foreseen when FRS 102 was developed.

B11.49B Therefore FRS 102 was amended in December 2020 to deal with the financial reporting implications associated with the replacement of interest rate benchmarks as part of the international interest rate benchmark reforms. These amendments are referred to as Phase 2 of the interest rate benchmark reform related amendments to FRS 102. The Phase 1 amendments relate to hedge accounting (see paragraphs B11.69 to B11.75).

B11.49C For the purposes of these amendments, interest rate benchmark reform refers to the market-wide reform of an interest rate benchmark, including the replacement of an interest rate benchmark with an alternative benchmark rate such as that resulting from the recommendations set out in the Financial Stability Board's July 2014 report *Reforming Major Interest Rate Benchmarks*.

B11.49D Similarly to Phase 1, as this is a global systemic issue, the FRC did not want to develop a financial reporting solution in isolation from other relevant developments. Therefore these amendments are based on the IASB's *Interest Rate Benchmark Reform – Phase 2 Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16*. Changes were made to reflect existing differences between IFRS and FRS 102. The amendments were supported by respondents.

B11.49E FRS 102 permits an accounting policy choice between the requirements of Section 11 and Section 12 of FRS 102 and the recognition and measurement requirements of IFRS 9 or IAS 39. The amendments to FRS 102 ensure that equivalent relief is available to all entities applying FRS 102, regardless of their accounting policy choice in relation to financial instruments.

B11.49F A new practical expedient requires entities to account for changes to contractual cash flows required by interest rate benchmark reform, as if they were a re-estimation of the cash flows of a variable rate financial instrument. The re-estimation of the cash flows is not expected to change the carrying amount of the financial asset or financial liability. This practical expedient applies exclusively to changes to cash flows required as a direct consequence of interest rate benchmark reform. Other changes to financial assets or financial liabilities continue to be assessed in accordance with the existing requirements in FRS 102 (for example paragraphs 11.19, 11.20 or 11.37).

B11.49G Some additional disclosures were introduced to assist users of financial statements to better understand the impact and risks associated with interest rate benchmark reform.

B11.49H Application of the amendments is mandatory and effective for accounting periods beginning on or after 1 January 2021, with early application permitted. An end date is not specified for the Phase 2 amendments, although they are temporary in nature. These amendments are designed to address financial reporting issues associated with the replacement of interest rate benchmarks, and their use ends when this process is complete.

Disclosures

B11.50 FRS 102 contains an option for entities to apply the recognition and measurement provisions of either IAS 39 or IFRS 9 instead of the recognition and measurement provisions of Sections 11 and 12. Paragraph 11.42 requires an entity to disclose information that enables users of its financial statements to evaluate the significance of financial instruments for its financial position and performance. In order to comply with this, an entity that has taken the accounting policy choice to apply the recognition and measurement provisions of IAS 39 or IFRS 9 may need to consider additional disclosure based on IFRS 7 *Financial Instruments: Disclosure*, as it relates to the recognition and measurement policies applied.

B11.51 As IFRS 9 was finalised, amendments were made to IFRS 7 to reflect the new requirements of IFRS 9. In relation to the impairment of financial assets, many changes were made to IFRS 7 to reflect the recognition of expected credit losses. As a result, some of the disclosure requirements of FRS 102 would be inconsistent with the application of the recognition and measurement requirements of IFRS 9. This particularly applied to the disclosure requirements for financial institutions.

B11.52 Therefore a number of changes have been made to the disclosure requirements to ensure that entities applying the recognition and measurement requirements of IFRS 9 are providing relevant information about the impairment of financial assets.

Hedge accounting

B11.53 The original edition of FRS 102 (issued in March 2013) contained requirements for hedge accounting based on the requirements of IAS 39. At the time, the FRC noted that the IASB was reviewing its hedge accounting requirements and therefore was reluctant to propose new accounting requirements in respect of this area before the IASB's project was finalised. The FRC also noted that the proposed first triennial review of FRS 102 was too far in the future and consequential amendments to FRS 102 may therefore be untimely for entities that would like to apply the new IFRS 9 accounting requirements without undue delay. For that reason the FRC noted that a proposed amendment to FRS 102 would be issued for public consultation once the IASB has completed the hedge accounting projects.

B11.54 The IASB completed its work on updating IFRS 9 in November 2013 and amendments to the hedge accounting requirements in FRS 102 were issued in July 2014. These amendments were based on the hedge accounting requirements in IFRS 9.

B11.55 The previous hedge accounting requirements in FRS 102 narrowly defined the types of arrangements that may qualify for hedge accounting, which was not necessarily representative of an entity's risk management objectives and hedging practices.

B11.56 The aim of these amendments was to develop hedge accounting requirements that allow for a reflection of an entity's hedging activities in the financial statements that are consistent with the entity's risk management objectives and are, as far as appropriate for entities applying FRS 102, consistent with IFRS.

B11.57 The amendments to FRS 102 substantively adopted the terminology and hedge accounting requirements in IFRS 9, with notable exceptions described in more detail below. The requirements in IFRS 9 deal with hedging transactions that can be far more complex than those typically entered into by entities applying FRS 102, therefore the departures from the requirements in IFRS 9 are intended to simplify the application of hedge accounting.

Qualifying hedge accounting conditions

B11.58 There are qualifying conditions for applying hedge accounting, including that an economic relationship between the hedged item and the hedging instrument has to exist. These conditions have been simplified when compared to the criteria set out in IFRS 9, with the aim of making hedge accounting easier to apply.

B11.59 It was noted that although a quantitative assessment of hedge effectiveness is not required by FRS 102, it is nevertheless important for entities to identify the different factors that affect the valuation of the hedging instrument and hedged item, including factors that may be a source of hedge ineffectiveness. Entities are therefore required to identify and document causes of hedge ineffectiveness before they commence hedge accounting, to ensure that ineffectiveness is properly captured in profit or loss.

B11.60 Entities are required to document a hedging relationship, to avoid hedge accounting being misused. The hedging documentation requirements are, however, relatively informal and undemanding and should not be an administrative burden for entities in practice.

Discontinuing hedge accounting

B11.61 Entities may discontinue hedge accounting voluntarily. This is a departure from IFRS 9. The FRC considered the restrictions in IFRS 9 on discontinuation unnecessarily onerous, and instead retained the existing option of voluntary discontinuation. An entity must document the election to discontinue hedge accounting, which is consistent with the requirement for documentation at the start of hedge accounting.

Disclosure

B11.62 The amendments retained substantially the original disclosure requirements of FRS 102. The disclosure requirements in IFRS focus on risks and risk mitigation through hedging. The FRC noted that risk disclosures are not generally required in FRS 102, except for financial institutions.

Transitional arrangements for hedge accounting for first-time adopters of FRS 102

B11.63 The FRC's aim was to develop transitional arrangements that are consistent with the permissive hedge accounting regime of FRS 102 and give entities a choice over whether to commence, continue or end hedge accounting on transition to FRS 102. Some respondents were concerned that this flexibility may be abused, as it allows entities to apply a degree of hindsight. The FRC was mindful of this possible exploitation of the transitional arrangements, nevertheless, on balance it believed that in the interests of the majority of entities, especially entities that have not applied hedge accounting before, flexibility should take precedence over restrictions aimed at preventing abuse.

B11.64 The FRC was conscious that entities may have applied diverse hedge accounting practices before the adoption of FRS 102. Entities may have applied the hedge accounting requirements of FRS 26 (IAS 39) *Financial Instruments: Recognition and Measurement* or may have applied synthetic accounting practices permitted under SSAP 20 *Foreign currency translation*. Accommodating these different accounting practices introduced complexity that the transitional arrangements needed to address. Under the transitional arrangements, regardless of which accounting practices were applied previously, entities have the choice to apply hedge accounting in accordance with FRS 102, provided the conditions for hedge accounting are met. Entities that elect not to apply the FRS 102 hedge accounting requirements have to comply with the applicable measurement requirements for assets and liabilities set out elsewhere in FRS 102 from the date of transition.

B11.65 These amendments were issued after the date of transition to FRS 102 for many entities. The transitional arrangements take this into account by providing an extended deadline for hedge documentation on first-time adoption.

Fair value hedging for a portfolio of financial instruments (macro hedging)

B11.66 Respondents requested reconsideration of the exclusion of macro hedging provisions from FRS 102. After consideration of the specific concerns of respondents that raised this as an issue, the FRC concluded that in the interests of developing straight-forward hedge accounting requirements that are relevant for a majority of entities, entities wishing to apply the IFRS macro hedging provisions are able to make the accounting policy choice in FRS 102 to apply IAS 39 and/or IFRS 9.

B11.67 As part of the triennial review 2017, the issue of macro hedging was reconsidered. General feedback from certain UK entities was that they liked the succinct nature of FRS 102 but chose to apply the recognition and measurement provisions of IAS 39 solely in order to have access to macro hedging.

B11.68 Given the lack of progress on the IASB's macro hedging project, it is expected that the IASB will retain the macro hedging requirements of IAS 39 for the foreseeable future. The IFRS 9 section on hedge accounting also cross-refers to the relevant IAS 39 paragraphs and the associated guidance on macro hedging. Therefore in order to address this 'gap' in FRS 102, the macro hedging requirements were incorporated into FRS 102 by cross-reference to the IAS 39 requirements, rather than by importing them directly into FRS 102. This enables entities to apply macro hedging with the recognition and measurement requirements of Sections 11 and 12 of FRS 102.

Interest rate benchmark reform (Phases 1 and 2)

B11.69 For the purposes of these amendments, interest rate benchmark reform refers to the market-wide reform of an interest rate benchmark, including the replacement of an interest rate benchmark with an alternative benchmark rate such as that resulting from the recommendations set out in the Financial Stability Board's July 2014 report *Reforming Major Interest Rate Benchmarks*.

B11.70 Interest rate benchmarks such as the London Interbank Offered Rate (LIBOR) are being reformed, and it is anticipated that LIBOR will not be available after 2021. There is increasing uncertainty about the long-term viability of some interest rate benchmarks and this gives rise to issues affecting financial reporting in the period before the reform, particularly in relation to hedge accounting.

B11.71 Interest rate benchmark reform will affect some entities applying FRS 102. In relation to financial instruments, FRS 102 permits entities an accounting policy choice to apply the recognition and measurement requirements of Section 11 and Section 12 of FRS 102, IFRS 9 or IAS 39. The IASB has made amendments to IFRS 9 and IAS 39 in response to the reform of interest rate benchmarks.

Interest rate benchmark reform (Phase 1)

B11.72 In December 2019, Section 12 was amended to include temporary amendments to specific hedge accounting requirements to provide relief during the period of uncertainty before the interest rate benchmark is reformed. In considering the issue, the FRC noted that interest rate benchmark reform is an international and systemic issue and it did not want to develop a financial reporting solution in isolation from other relevant developments. The IASB's *Interest Rate Benchmark Reform (Amendments to IFRS 9, IAS 39 and IFRS 7)* was identified as a suitable basis for the development of similar amendments to FRS 102. In deciding to base the amendments to FRS 102 on similar amendments to IFRS 9 the FRC made a number of changes including simplifications and changes to reflect existing differences between IFRS 9 and FRS 102. The amendments were supported by respondents.

B11.73 As a result of these amendments, entities will apply specific hedge accounting requirements assuming that the interest rate benchmark relevant to the hedge accounting is not altered as a result of interest rate benchmark reform.

B11.74 The temporary amendments to specific hedge accounting requirements are not intended to change the requirement that entities measure and recognise hedge ineffectiveness, which should continue to be measured and recognised in accordance with FRS 102 (or IFRS 9 or IAS 39 depending on the accounting policy choice made by the entity). Entities should continue to apply assumptions that are consistent with those applied to the hedged risk of the hedged item. For example, if an entity designated interest rate benchmark-based cash flows as the hedged item in a cash flow hedge, the entity would not assume, for the purposes of measuring hedge ineffectiveness, that the expected replacement of the interest rate benchmark with an alternative benchmark rate will result in zero cash flows after the replacement.

B11.75 The effective date is accounting periods beginning on or after 1 January 2020, with early application permitted.

Interest rate benchmark reform (Phase 2)

B11.76 In December 2020 additional amendments were made to address the accounting implications associated with the replacement of interest rate benchmarks, referred to as Phase 2 of the interest rate benchmark reform related amendments. See also paragraph B11.49D.

B11.77 The amendments apply when the Phase 1 hedge accounting reliefs end, ie when the uncertainties about the timing and amount of interest rate benchmark referenced cash flows are resolved by the replacement with alternative benchmark rates.

B11.78 A new temporary relief relating to hedge documentation will prevent the discontinuation of hedge accounting when hedge documentation is updated to reflect the switch to alternative benchmark rates. To ease the operational burden entities are allowed to make the necessary changes to their hedge documentation by the end of the reporting period, rather than immediately. This period has been extended to the date the financial statements are authorised for issue on first-time application of the amendments, to provide even greater flexibility to entities, particularly those that adopt these amendments early. Other amendments provide specific reliefs for cash flow hedges, hedges of groups of items and non-contractually specified risk components. All other unamended hedge accounting requirements of FRS 102 continue to apply.

B11.79 The amendments are mandatory, although the application of hedge accounting remains optional. The effective date of the amendments is accounting periods beginning on or after 1 January 2021, with early application permitted. An end date is not specified for the Phase 2 amendments, although they are temporary in nature. These amendments are designed to address financial reporting issues associated with the replacement of interest rate benchmarks, and their use ends when this process is complete.

B14 Section 14 *Investments in Associates*

B14.1 Prior to the *Triennial review 2017 amendments*, the undue cost or effort exemption in relation to investments in associates only applied in situations where the reporting entity had chosen to measure these items at fair value in its individual financial statements and it had subsequently become impracticable to do so. Reporting entities already had the choice to use the cost model in this situation, therefore this exemption served no practical purpose and was removed. No amendments were made to the accounting policy choice to measure investments in associates using the cost model or fair value.

B15 Section 15 *Investments in Joint Ventures*

B15.1 Prior to the *Triennial review 2017 amendments*, the undue cost or effort exemption in relation to investments in joint ventures only applied in situations where the reporting entity had chosen to measure these items at fair value in its individual financial statements and it had subsequently become impracticable to do so. Reporting entities already had the choice to use the cost model in this situation, therefore this exemption served no practical purpose and was removed. No amendments were made to the accounting policy choice to measure investments in joint ventures using the cost model or fair value.

B16 Section 16 *Investment Property*

Investment properties including those rented to another group entity

B16.1 Prior to the *Triennial review 2017 amendments*, FRS 102 required only investment property that could be measured at fair value without undue cost or effort, to be measured at fair value; any that could not were accounted for as property, plant and equipment using the cost model in Section 17 *Property, Plant and Equipment*. In the UK, entities should generally be able to obtain a fair value for an investment property, without undue cost or effort, which would provide useful, decision-relevant information to users of the financial statements. Therefore as part of the triennial review 2017 the undue cost or effort exemption in relation to investment property was removed.

B16.2 However, a significant amount of feedback from stakeholders suggested that the cost of obtaining a fair value for an investment property that is rented to another group entity far outweighs the benefit, as the information is of little use when the investment property would be treated as property, plant and equipment in the consolidated financial statements.

B16.3 To address this significant implementation issue, an accounting policy choice was introduced for entities that rent investment property to another group entity, whereby they can choose to measure that investment property either at cost (less depreciation and impairment) or at fair value.

B16.4 A small number of respondents were concerned about the impact of the change on the small number of properties for which a reliable measure of fair value is not available. The FRC notes that prior to the introduction of FRS 102 such properties were required to be measured at open market value and that the Appendix to Section 2 *Concepts and Pervasive Principles* provides guidance on situations when a reliable measure of fair value is not available.

B17 Section 17 *Property, Plant and Equipment*

Property held for the provision of social benefits

B17.1 The requirements for property held for the provision of social benefits apply to all entities applying FRS 102 and are not restricted to PBEs.

B17.2 Consideration was given to whether properties that are held for the provision of social benefits meet the definition of an investment property. The definition of investment property includes properties held to earn rentals and/or for capital appreciation but excludes properties held for use in the production or supply of goods and services or for administrative purposes.

B17.3 It was noted that although many PBEs that engage in the provision of social housing receive rental income, their primary purpose is to provide social benefits. Provision of social housing is akin to supplying a service and, therefore, property held for the primary purpose of providing social benefits is excluded from the scope of investment property and should be accounted for as property, plant and equipment.

B17.4 PBEs may hold investment properties, being those that are not held primarily to provide social benefits, but return market value rentals and/or are held for their capital appreciation. FRS 102 requires those properties to be accounted for as investment properties.

B18 Section 18 *Intangible Assets other than Goodwill*

Useful life of intangible assets

B18.1 In July 2015, as part of implementing the EU Accounting Directive, Section 18 *Intangible Assets other than Goodwill* was amended to revise the maximum period over which intangible assets may be amortised to 10 years, in those exceptional cases when an entity is unable to make a reliable estimate of the asset's useful economic life. As this only applies in exceptional cases, the change in the maximum period so soon after it was introduced in the first edition of FRS 102 should have a limited impact in practice.

Intangible assets acquired in a business combination

B18.2 In the triennial review 2017, stakeholders provided feedback on the practical issues arising from applying paragraph 18.8 of FRS 102 in recognising and measuring intangible assets acquired in a business combination; in particular, the meaning and purpose of the phrase 'immeasurable variables'. Further difficulties arose from the use of language that was similar to IFRS 3 *Business Combinations*, which notes that intangible assets acquired in a business combination can always be measured reliably.

B18.3 Various options for improving FRS 102 were considered, including:

(a) allowing an undue cost or effort exemption as per the revised IFRS for SMEs;

(b) moving towards an IFRS 3 approach whereby all intangible assets are recognised separately from goodwill; or

(c) reverting back to an approach similar to FRS 10 *Goodwill and Intangible Assets* whereby some but not all intangibles are recognised separately.

B18.4 Research indicated that some investors saw a distinction between those intangible assets that are 'wasting' (ie those that are separable from the entity, have finite useful lives and lead to identifiable future revenue streams) and those that are 'organically replaced' (ie those that are unlikely to be separable, to have reliably determined useful lives or to be a source of future economic benefits that could be distinguished from the business as a whole). Some investors argued that those intangibles that are 'wasting' assets should be recognised separately from goodwill, whereas those that are 'organically replaced' should be subsumed into goodwill.

B18.5 It was also noted that FRS 102 requires goodwill to be amortised over its useful life, which is consistent with the accounting treatment of intangible assets. Therefore, the impetus to separate intangible assets from goodwill is less than it may be under IFRS, where goodwill is not amortised.

B18.6 Amendments to FRS 102 were made so that entities are required to recognise some but not all intangible assets acquired in a business combination separately from goodwill. This was achieved by requiring entities to recognise intangible assets separately if they:

(a) meet the recognition criteria; and

(b) are separable and arise from contractual or other legal rights.

B18.7 This should not give rise to particular measurement difficulties in practice.

B18.8 In addition, an entity may choose to separately recognise other intangible assets acquired in a business combination that meet the recognition criteria and are either separable or arise from contractual or other legal rights. This is a proportionate solution that permits the separate recognition of a larger number of intangible assets when this information provides useful information to the reporting entity and the users of its financial statements. This choice, when exercised, must be applied consistently to the relevant class of intangible assets. This will result in comparability over time in the entity's financial statements. In addition, a new disclosure was introduced that requires disclosure of the nature of the additional intangible assets separated from goodwill and the reason why, which will assist users in drawing comparisons between different entities.

B18.9 Some respondents expressed reservations about the extent of choice available to entities and the potential for inconsistency between different entities. Nevertheless, the option will enable more information to be provided to users in some circumstances and additional disclosure will assist in drawing comparisons. Therefore, the FRC believes these amendments will lead to proportionate reporting.

B18.10 Some respondents requested further guidance on which intangible assets are expected to meet the criteria for separate recognition in a business combination. The FRC considers that examples of intangible assets that would normally satisfy all three criteria include licences, copyrights, trademarks, internet domain names, patented technology and legally protected trade secrets, and examples of intangible assets that would not normally satisfy all three criteria include customer lists, customer relationships and unprotected trade secrets (such as secret recipes or formulas) as no contractual or legal right exists that would give rise to expected future economic benefits.

B19 Section 19 *Business Combinations and Goodwill*

Group reconstructions

B19.1 FRS 102 retains the accounting permitted by FRS 6 *Acquisitions and mergers* for group reconstructions. It was noted that whilst EU-adopted IFRS does not provide accounting requirements for business combinations under common control, the accounting required by FRS 6 is well understood and provides useful information. Therefore these requirements were carried forward into FRS 102. In practice, the introduction of FRS 102 was not expected to change the accounting for group reconstructions.

B19.2 As part of the triennial review 2017, amendments were made to the definition of a group reconstruction to incorporate, in certain circumstances, the transfer of a business, in addition to the transfer of equity holdings.

Useful life of goodwill

B19.3 In July 2015, as part of implementing the EU Accounting Directive, Section 19 *Business Combinations and Goodwill* was amended to revise the maximum period over which goodwill may be amortised to 10 years, in those exceptional cases when an entity is unable to make a reliable estimate of the asset's useful economic life and to prohibit the reversal of impairment losses for goodwill. As the revision to the maximum amortisation period for goodwill only applies in exceptional cases, this change should have a limited impact in practice.

Other minor amendments

B19.4 As part of the triennial review 2017, amendments were made to clarify the steps involved in applying the purchase method to a business combination.

B20 Section 20 *Leases*

Leases with non-typical contractual terms

B20.1 All leases are within the scope of Section 20 *Leases*, except for those leases that could result in a loss to the lessor or the lessee as a result of non-typical contractual terms, for example those that are unrelated to:

(a) changes in the price of the leased asset;

(b) changes in foreign exchange rates; or

(c) a default by one of the counterparties.

Such leases are within the scope of Section 12.

B20.2 It was noted that the reference to 'changes in the price of the leased asset' is framed widely and in practice not many leases are expected to fall within the scope of Section 12 *Other Financial Instruments Issues*.

Lease disclosures

B20.3 As part of the triennial review 2017, the Consultation Document proposed that lease disclosures in FRS 102 were enhanced, in advance of any revised requirements based on IFRS 16 *Leases*. The aim was to improve the information available to users.

B20.4 Respondents did not support this approach. It would be difficult for entities to provide more information about obligations arising from operating leases without first determining a detailed approach to updating FRS 102 for IFRS 16, and IFRS 16 itself does not require enhanced disclosure in the run up to implementation.

B20.5 Having considered this further, FRS 102 was not amended in this respect. Further evidence-gathering and analysis will be undertaken before a decision is made on reflecting the principles of IFRS 16 in FRS 102, if at all.

COVID-19-related rent concessions

B20.6 In October 2020, FRS 102 was amended to require entities to recognise changes in operating lease payments that occur as a direct consequence of the COVID-19 pandemic, and meet specified conditions, on a systematic basis over the periods that the change in lease payments is intended to compensate.

B20.7 This was to address concerns about how the relevant requirements of FRS 102 should be applied to temporary rent concessions granted in response to the COVID-19 pandemic. Specifically, there were differences of opinion over how the previous requirements of FRS 102 should be applied to forgiven payments in operating lease agreements. If this had led to different accounting treatments for changes in lease payments that had arisen under similar circumstances it would have been unhelpful to users of financial statements.

B20.8 Although concerns about the treatment of forgiven lease payments were raised predominantly from the perspective of lessees, because of the similarities between the relevant recognition requirements of FRS 102, the accounting by both lessees and lessors was addressed.

B20.9 The amendments were intended to reflect the particular circumstances that had resulted in these changes in lease payments occurring, where there had typically been a temporary reduction in the lessee's benefit from the use of the leased asset. Requiring entities to recognise the impact of changes in lease payments over the periods that the change is intended to compensate was considered to generally reflect the economic substance of the intended benefit of these concessions and their temporary nature, and provide more relevant information for users. The requirements were based on the accrual model for government grants as set out in Section 24 *Government Grants*.

B20.10 The criteria for applying the requirements were intended to restrict the treatment to those concessions when it was generally considered to be reflective of the substance of the concession. This minimises the risk of the requirements being applied when it may be more appropriate to recognise changes in lease payments on another basis. The requirements apply only to rent concessions that occur as a direct consequence of the COVID-19 pandemic and:

(a) result in revised consideration for the lease that is less than the consideration for the lease immediately preceding the change. Deferred lease payments do not change the consideration for the lease but change only the timing of individual payments. The requirements therefore do not apply to changes in lease payments that result from rent deferrals. These changes are accounted for under the existing requirements of FRS 102, which are considered to provide useful information to users of financial statements.

(b) result in a reduction to only lease payments originally due on or before 30 June 2022[82]. A related increase in lease payments that extends beyond 30 June 2022 would not prevent a rent concession from meeting this condition. In contrast, if reductions in lease payments extend beyond 30 June 2022, the rent concession in its entirety would not be within scope. The economic effects of the COVID-19 pandemic could continue for some time. If the requirements were not limited to a particular timeframe, an entity could conclude that many future changes in lease payments are a consequence of the COVID-19 pandemic. The chosen timeframe was intended to limit the requirements to apply to those concessions where the treatment is expected to be reflective of the substance of the concession and achieve consistency over this period.

(c) introduce no significant change to other terms and conditions of the lease. A concession that incorporates significant changes to a lease agreement which are unrelated to the COVID-19 pandemic, but negotiated at the same time as those related changes, would not meet this condition.

[82] *Amendments to FRS 102 and FRS 105 – COVID-19-related rent concessions beyond 30 June 2021* was issued in June 2021 which amended the date in paragraph 20.15D of FRS 102 from 30 June 2021 to 30 June 2022 (see paragraph B20.11A).

B20.11 FRS 102 already requires lessees to disclose operating lease payments recognised as an expense. Therefore, to ensure that the impact of any temporary rent concessions occurring as a direct consequence of the COVID-19 pandemic is distinguishable from any other changes in lease payments, paragraph 20.16(c) requires lessees to disclose the amount of the change in lease payments recognised in profit or loss in accordance with paragraph 20.15C. Paragraph 20.30(c) requires lessors to provide a general description of their significant leasing arrangements. Information about rent concessions granted would be expected to be included within this disclosure. Given this existing requirement and the current level of disclosure required for revenue in FRS 102, no additional disclosures have been required of lessors.

COVID-19-related rent concessions beyond 30 June 2021

B20.11A In June 2021, FRS 102 was amended to extend the requirements of paragraphs 20.15C and 20.25B so that they apply to rent concessions for which any reduction in lease payments affects only payments originally due on or before 30 June 2022, provided the other conditions in paragraph 20.15D are met. Extending the time condition by 12 months was necessary to allow the requirements to be applied consistently to concessions that are similar in substance to those covered by the original requirements, reflecting the continued impact of the COVID-19 pandemic on operating lease agreements. The extended timeframe was considered to be sufficient to cover those periods where concessions will be granted in circumstances similar to those that existed when the original requirements were developed.

Interest rate benchmark reform (Phase 2)

B20.12 The FRC assessed whether specific reliefs were needed for lease accounting when there is a change in the basis for determining future lease payments or receipts required by interest rate benchmark reform. The FRC would not expect that changes to future lease payments or receipts required by interest rate benchmark reform would alter the carrying amounts of receivables recognised by a lessor or payables recognised by a lessee arising under a finance lease. The FRC also believes that the existing requirements for operating leases are not onerous to apply and will provide useful information in the context of interest rate benchmark reform. The FRC notes that the IASB made changes to IFRS 16 *Leases* as part of its Phase 2 amendments to IFRS (see paragraph B11.49D), but they relate to specific lease modification requirements that do not exist in FRS 102. The FRC therefore decided that no specific amendments to FRS 102 were needed. A consequential amendment was made to paragraph 20.11 to reflect changes made to Section 11 *Basic Financial Instruments*.

B21 Section 21 *Provisions and Contingencies*

Seriously prejudicial exemption

B21.1 In July 2015, as part of implementing the EU Accounting Directive, Section 21 *Provisions and Contingencies* was amended in relation to the 'seriously prejudicial' exemption that applies, in extremely rare circumstances, to disclosure of provisions and contingencies. It was noted that company law requires certain disclosures in relation to provisions and contingencies, and that disclosure by entities that are companies and those that are not should be consistent. Therefore the 'seriously prejudicial' exemption was amended to remind companies of the legal disclosure requirements and ensure that equivalent disclosures are provided by all entities.

B22 Section 22 *Liabilities and Equity*

Distribution of non-cash assets to owners

B22.1 Respondents asked for clarification that the distribution of non-cash assets to owners did not apply to distributions within groups. In considering this requirement, a distinction between the disposal of an asset at fair value followed by a distribution to shareholders of the profit, and making a distribution of the asset to shareholders, was noted. A distribution to shareholders does not generate a profit, whereas a disposal does generate a profit that may then be distributed to shareholders. The requirement in the IFRS for SMEs to recognise a liability to pay a dividend for a non-cash asset at fair value was removed and a requirement to disclose the fair value of the assets distributed to shareholders was included.

Debt for equity swaps

B22.2 Prior to the *Triennial review 2017 amendments*, FRS 102 was silent on the accounting for debt for equity swaps. Although it required equity instruments to be initially recognised at fair value, resulting in equivalent accounting to that required by IFRIC 19 *Extinguishing Financial Liabilities with Equity Instruments*, it contained no scope exemptions for transactions that would not be within the scope of IFRIC 19 (such as common control transactions) or the conversion of convertible debt.

B22.3 Feedback from stakeholders suggested that this was an area that would benefit from more explicit guidance as, when they occur, such transactions can be significant. FRS 102 was amended with the insertion of paragraph 22.8A.

Option to purchase own equity instruments

B22.4 It was proposed as part of the triennial review 2017 that a new example be inserted in Section 22 *Liabilities and Equity* relating to a written option to purchase own equity instruments. Some respondents raised concerns about the possibility of unintended consequences, and after considering those comments the example was not included in FRS 102. The FRC may review this issue again in the future.

B23 Section 23 *Revenue*

Transactions including separately identifiable goods and services

B23.1 Amendments to FRS 102 were proposed as part of the triennial review 2017 to provide greater clarity to the requirements for the recognition of revenue from separately identifiable goods and services provided under a single transaction. Respondents did not support this approach noting that Section 23 *Revenue* was not causing any notable implementation issues to date and the section should be considered in more detail when the incorporation of IFRS 15 *Revenue from Contracts with Customers* is considered. Consequently, FRS 102 was not amended in this respect.

B23.2 It was also confirmed that further evidence-gathering and analysis will be undertaken before a decision is made on reflecting the principles of IFRS 15 in FRS 102, if at all.

Agent and principal

B23.3 As part of the *Triennial review 2017 amendments*, further guidance on how to determine whether an entity is acting as an agent or a principal was inserted into Section 23 following feedback that the standard was not sufficiently clear. The additional guidance is based on the guidance included in IAS 18 *Revenue*.

B24 Section 24 *Government Grants*

Performance model and accrual model

B24.1 A number of respondents, particularly from the public benefit entity sector, raised concerns about the proposed changes to the recognition of income from grants when an entity fulfilled the performance criteria stipulated in the grant (the performance model). This would have been a change from both previous accounting standards and EU-adopted IFRS, which both attempt to match grant income with the related expenditure (the accruals model).

B24.2 The performance model could have been supplemented with additional application guidance on performance outcome. However, this approach would have required a research project to be undertaken and caused delay to the finalisation of FRS 102. An alternative approach would have been to align FRS 102 with EU-adopted IFRS and defer a research project on the accounting for grants until after the publication of FRS 102. However, respondents noted that some entities, mainly in the public benefit entity sector, already applied the performance model and that reverting to the accruals model would introduce a change for these entities. The FRC did not wish to implement a change for entities that might subsequently be reversed, therefore FRS 102 permits a choice between the performance model and accruals model.

B24.3 In 2017 as part of the triennial review it was noted that inconsistency in practice has continued, and without an internationally accepted solution this is likely to continue. Therefore although the FRC would like to improve consistency of accounting in this area, the time is not right for significant change.

Grants from other sources

B24.4 Respondents further commented that as Section 24 *Government Grants* is restricted to government grants, grants received by public benefit entities from other sources will be accounted for in accordance with Section 34 *Specialised Activities*, and there is now the possibility that the accounting for grants depends on the source of the grant, rather than whether or not the underlying terms and conditions of the grants differ. Whilst this is not ideal, the accrual model for government grants has been permitted in accordance with the guidelines for amending the IFRS for SMEs, as an interim solution to avoid changes in accounting that might be reversed in the future.

Capital grants

B24.5 For those entities that apply the performance model to capital grants, either as an accounting policy choice for government grants, or through applying Section 34 to grants from other sources, it was noted that there may be a change in accounting treatment, which may lead to greater volatility in the income statement. The effect of this volatility can be explained in the notes to the financial statements.

B26 Section 26 *Share-based Payment*

Option pricing models

B26.1 Previously, entities in the UK and Republic of Ireland[83] that entered into share-based payment transactions were required to apply FRS 20 (IFRS 2) *Share-based Payment*. However, it was noted that for unlisted entities it may be difficult to apply option pricing models and the benefits may outweigh the costs. Therefore, as set out

[83] Other than those applying the FRSSE.

in paragraph 26.10(c), directors shall apply judgement by using models that are appropriate to the entity's circumstances.

Share-based payment arrangements with cash alternatives

B26.2 In July 2015, FRS 102 was amended so that share-based payment arrangements with cash alternatives are accounted for as equity-settled share-based payment arrangements unless the option to settle in equity has no commercial substance or the entity has created a valid expectation that it would settle in cash.

B26.3 It was noted that the requirement to account for such transactions as cash-settled was more onerous than the requirements of EU-adopted IFRS, under which they would generally be treated as equity-settled, since it requires the measurement of the obligation at fair value at each reporting date.

B26.4 In some schemes the recipient may have an option to request settlement in cash or equity instruments. If an entity cannot avoid settling in cash should the recipient request it, FRS 102 requires the entity to account for the transaction as cash-settled by measuring the goods or services acquired at the fair value of the liability unless the cash settlement option has no commercial substance. It was noted that this requirement is different to EU-adopted IFRS which requires the separate recognition of debt and equity components. The simpler requirements of FRS 102 provide a practical and proportionate solution for those applying the standard and are generally consistent with the requirements of the IFRS for SMEs. The exemption from cash-settled accounting when the option to settle in cash has no commercial substance was retained in FRS 102.

B26.5 The proposal set out additional amendments that would have resulted in cash-settled treatment for all share-based payment arrangements with terms that could result in the transfer of cash on the occurrence of an event outside the control of either party to the transaction. Some respondents commented that this could result in the recognition of a liability in situations when the probability of settlement in cash is remote. FRS 102 was not amended in this regard.

B26.6 No additional transitional exemptions for entities that had chosen to early adopt FRS 102 and had granted awards under share-based payment arrangements that would be affected by these changes were given as such instances would be very rare and early adopters would have had the benefit of the transitional exemption for awards granted before the date of transition.

B26.7 The transitional exemption in paragraph 35.10(b) of FRS 102 was amended to clarify that the reference to equity instruments includes the equity component of compound instruments accounted for in accordance with FRS 20/IFRS 2. It was noted that the transitional exemption was intended to alleviate the costs of transition in respect of equity-settled share-based payment arrangements for companies that had previously applied the FRSSE, where such arrangements were not recognised, and for companies that had previously applied FRS 20/IFRS 2 should FRS 102 require different accounting.

B26.8 It was also noted that there was no need for transitional exemptions to be added for liabilities not settled at the transition date, including those arising from arrangements previously treated as compound instruments, because the liability will not continue to be measured in the same way under FRS 102.

Cost-effectiveness of applying Section 26 by private companies

B26.9 As part of the triennial review 2017, the Consultation Document asked for feedback regarding the cost-effectiveness of applying Section 26 *Share-based Payment* by private companies.

B26.10 Feedback from respondents was mixed. Some noted that the requirements had been in place for some 10 years, were well embedded and reflected a cost to the company, and therefore no changes should be made. Some noted sympathy with the difficulties faced by small private companies in obtaining a reliable and meaningful fair value measurement for share-based payment arrangements. Some suggested that a disclosure-only approach for small entities could be considered in the future should the legislative landscape change. It was not possible to do this as additional disclosures cannot be mandated of small entities under the EU Accounting Directive.

B26.11 Consequently, no wholesale changes were made to Section 26 but minor improvements were made to align some of the definitions used in the section with IFRS 2 *Share-based Payment*. However, it was noted that the issue should be revisited in the future if company law changes such that disclosures could be mandated for small companies.

B27 Section 27 *Impairment of Assets*

Impairment of assets held for service potential

B27.1 FRS 102 requires impaired assets to be measured at the lower of their fair value less costs to sell and their value in use. In a for-profit context, value in use is determined by measuring the present value of the cash flows derived from the asset. However, often PBE assets are held for their service potential rather than their ability to generate cash flows. In such a case it is sometimes impossible to determine value in use by reference to cash flows and it is more appropriate to regard value in use as the present value of future service potential.

B27.2 IPSAS 21 *Impairment of Non-Cash Generating Assets* permits value in use to be determined by any of three approaches:

(a) depreciated replacement cost (DRC);

(b) restoration cost; or

(c) the service units approach.

B27.3 Restoration cost and the service units approach are applications of DRC as DRC is used as the starting point. DRC reflects the cash outflows that are saved through ownership of an asset and is likely to be widely applicable and appropriate for PBEs. Therefore FRS 102 permits a service potential driven valuation to be used for assets held for their service potential.

B27.4 The use of DRC is not mandated; other methods that value service potential rather than cash flows may be used if those methods are more appropriate in the particular circumstances.

B27.5 Consideration was also given to whether a restriction on the use of an asset would affect its fair value. As an asset's fair value is based on the amount that an entity could obtain, restrictions might impact on the fair value when they prevent a purchaser from using the asset for another purpose that would be more valuable than that required by the restriction. In addition, the costs to sell should include the costs of breaking the restriction.

B27.6 The indicators of impairment provided in FRS 102 are mainly linked to the expected cash flow from an asset and as such may not necessarily be relevant to some PBE assets; however, they must, as a minimum, be considered by PBEs as possible indicators of impairment.

B27.7 In addition, it was noted that other accounting literature (eg IPSAS 21 and SORPs) identified other indicators of impairment including:

(a) cessation, or near cessation, of the demand or need for services provided by the asset;

(b) social, demographic or environmental changes resulting in a reduction of beneficiaries; and

(c) a major loss of key employees associated with particular activities.

B27.8 It was concluded that it would not be appropriate to include these indicators in FRS 102, as they are not exclusively relevant to PBEs and because the indicators given in FRS 102 will continue to apply to PBEs. Therefore, their inclusion would make such entities subject to a confusing list of overlapping indicators.

B27.9 Consideration was also given to whether FRS 102 should specify that an indicator of impairment was present when an asset's service potential was not fully utilised. It was noted that an entity may require standby or surplus capacity to ensure that it has adequate capacity to provide services at all times. For example, a building that provides accommodation for the homeless may not be used to full capacity during the summer months but is utilised fully during winter. In this circumstance, the surplus capacity is part of the required service potential of the asset and the asset is not impaired. For this reason, it was concluded that it would be inappropriate to specify that the unutilised capacity should be treated as an indicator of impairment.

B28 Section 28 *Employee Benefits*

Cost of a defined benefit plan

B28.1 Respondents noted that the presentation requirements for post-employment benefit plans were not clear in earlier proposals. Specifically, a request was made to clarify where the difference between the actual return on plan assets and expected return on plan assets should be presented. It was noted that the presentation requirements in IAS 19 *Employee Benefits* had been amended in 2011 which was consistent with the ASB's recommendations in its report following the consultation document *The Financial Reporting of Pensions*. In view of this, the requirements of FRS 102 are consistent with the revised IAS 19, which requires an entity to recognise the net change in the defined benefit liability as follows:

(a) the change in the defined benefit liability arising from employee service rendered during the reporting period in profit or loss;

(b) net interest on the net defined benefit liability in profit or loss; and

(c) remeasurement of the net defined benefit liability in other comprehensive income.

Group defined benefit pension plans

B28.2 It was noted that the accounting requirements in the IFRS for SMEs for group pension plan arrangements were more stringent than those set out in IAS 19 (revised 2011), therefore these requirements were aligned to be consistent with the IAS 19 (revised 2011).

B28.3 Consistently with IAS 19 (revised 2011), paragraph 28.38 of FRS 102 requires entities participating in a group defined benefit pension plan to recognise the net defined benefit cost in their individual financial statements when a relevant agreement or policy exists. Otherwise the entity that is the sponsoring employer for the group pension plan will recognise the entire net defined benefit cost in its individual financial statements. It was noted that although this paragraph only refers explicitly to the cost of the pension plan, the net defined benefit cost is calculated by reference to both the defined benefit obligation and the fair value of plan assets. Therefore paragraph 28.38 requires the recognition of the relevant net defined benefit liability in the individual financial statements of any group entities recognising a net defined benefit cost, and it was updated to clarify this as part of the *Triennial review 2017 amendments*.

Multi-employer defined benefit plans

Multi-employer defined benefit plans accounted for as defined contribution plans

B28.4 In October 2012 the FRC issued an exposure draft of additional proposals, including amendments to Section 28 *Employee Benefits*. These amendments related to multi-employer defined benefit plans that are accounted for as defined contribution plans. Differences in accounting practice had arisen in relation to whether entities, that participate in a defined benefit multi-employer plan, account for that plan as a defined contribution plan and have entered into a funding agreement for future payments relating to past service liabilities, recognise a liability in relation to the deficit in the plan in their financial statements.

B28.5 The relevant requirement from IAS 19 was incorporated into FRS 102. The IASB's Basis for Conclusions states that 'In relation to the funding of a deficit, [...] this principle [is] consistent with the recognition of a provision in accordance with IAS 37'.

B28.6 The measurement requirements for such a liability were also clarified. In the circumstances that the entity has entered into a funding agreement for future payments relating to past service it shall recognise those future payments as a liability, discounted using the methodology for selecting a discount rate for post-employment benefit liabilities.

B28.7 Some respondents disagreed with the proposed amendment or requested a delay in implementation; however, a liability exists and its recognition provides useful information to users and therefore these requirements were mandatory from the effective date of FRS 102.

B28.8 Some respondents suggested that FRS 102 should also address situations where a multi-employer pension plan was in surplus, and had entered into an agreement to distribute that surplus to the participating employers. Although it was noted that this was addressed in IAS 19, it is expected that the situation would arise rarely in practice, and that entities would be able to determine the appropriate accounting using the principles set out in FRS 102. Therefore no amendment was made for this.

Transition from defined contribution accounting to defined benefit accounting

B28.8A In May 2019 FRS 102 was amended to provide clear and unambiguous requirements for the transition from defined contribution accounting to defined benefit accounting when sufficient information becomes available.

B28.8B Some multi-employer defined benefit plans had been carrying out exercises with a view to being able to provide sufficient information to participating employers in the future, which generated debate over the relevant requirements of FRS 102. There were differences of opinion over how the previous requirements of FRS 102 should be applied in this circumstance, with at least three alternative treatments being proposed. If this had led to differences in accounting practice by employers participating in the same multi-employer defined benefit plan it would have been unhelpful to users of financial statements.

B28.8C Sufficient information could become available at any time; it will not necessarily become available at the start of a reporting period, and therefore the accounting needs to address the possibility that the transition may take place part way through a reporting period.

B28.8D In accordance with paragraph 28.11, whilst sufficient information is not available an entity shall account for the plan as if it were a defined contribution plan, and the fact that information subsequently becomes available does not render the accounting during the earlier period invalid. If information becomes available:

(a) for a date during the current period, the change in accounting shall take place from that date, which may not be the first day of a reporting period, in order that the benefits to users of defined benefit accounting are not delayed;

(b) for a date during a prior period, after the financial statements for that period have been authorised for issue, the change in accounting shall take place from the first day of the current period, with no restatement of comparatives as those financial statements were prepared on the basis of the information available at the time; and

(c) for a date during the prior period, before those financial statements have been authorised for issue, the change in accounting shall take place from that date (as an adjusting event after the end of the reporting period).

B28.8E When an entity accounts for a multi-employer defined benefit plan as if it were a defined contribution plan, paragraph 28.11A requires it to recognise a liability for any contributions payable that arise from an agreement to fund a deficit. The change to defined benefit accounting can then be seen as a change to an improved measurement basis, using more complete information, to measure the same underlying obligation, and the amount to be recognised in the statement of financial position is likely to change, creating a ‘difference’ to be recognised on transition.

B28.8F Items can only be recognised in other comprehensive income when FRS 102 specifically requires or permits it. Following the amendment made in May 2019, the difference between any existing liability arising from a schedule of contributions and the net defined benefit liability (which is a defined term and could also be an asset), at the date of transition shall be recognised in other comprehensive income. This means that the existing provision is not derecognised through profit and loss and the change is recognised in a way analogous with the recognition and presentation of actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions. This is a pragmatic solution to achieve consistency in accounting practices that results in the costs recognised in profit or loss for the period being solely those usually required by the respective accounting approaches, and the impact of the change in approach being presented as a single line in other comprehensive income.

B28.8G The difference to be recognised in other comprehensive income shall be limited to the effects of the transition and excludes:

(a) any changes in the liability for the contributions payable arising from an agreement to fund a deficit, which arise, and shall be accounted for, prior to the relevant date (such changes might relate to payments made, interest on the liability and changes to the underlying agreement);

(b) the impact of any plan changes, curtailments or settlements occurring at the relevant date (see paragraph 28.11D); and

(c) the impact of any plan changes, curtailments or settlements that occur between the relevant date and the reporting date.

B28.8H Paragraph 5.5A(a) requires items in other comprehensive income to be classified by nature. Therefore, to ensure that the effect of the transition from defined contribution accounting to defined benefit accounting is distinguishable from any other items relating to post-employment benefits, paragraph 28.11B(b) requires the difference on transition to be presented separately in other comprehensive income. FRS 102 already includes disclosure requirements that are relevant to the transition from defined contribution accounting to defined benefit accounting, such as those relating to accounting policies, significant judgements, defined benefit plans, amounts to be recognised in other comprehensive income and general requirements to provide information that is relevant to an understanding of the financial statements. Therefore, no additional disclosures have been required.

Defined benefit plans (February 2015)

B28.9 After the publication of FRS 102 in March 2013 the FRC issued, in October 2013, a Press Notice addressing the accounting in accordance with EU-adopted IFRS for a 'schedule of contributions' payable by an entity to a defined benefit pension plan. Subsequently the FRC received enquiries about the accounting for similar circumstances by entities applying FRS 102.

B28.10 The issue concerns whether or not an entity applying FRS 102 should have regard to the principles of IFRIC 14 *IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction* when it might be relevant to its circumstances. Amendments to FRS 102 were issued in February 2015 to address this, and two other issues.

Proportionate measurement of the net defined benefit liability for a defined benefit plan

B28.11 Consideration was given to whether FRS 102 required an entity with a defined benefit plan to consider the principles of IFRIC 14 in interpreting its requirements to measure the net defined benefit liability. It was noted that there appeared to be uncertainty over this issue and that there was the possibility of significant differences arising in accounting practice, particularly because the amounts that might (or might not) be recognised could be very significant.

B28.12 For entities applying FRS 102, the recognition of the net defined benefit liability or asset (which may be limited by paragraph 28.22) for a defined benefit pension plan as the net total of the present value of the obligations under the plan and the fair value of the plan assets is a proportionate way to measure the present obligation to employees as a result of service rendered. It was noted that in some circumstances IFRIC 14 would result in an additional liability being recognised in relation to a schedule of contributions that had been agreed with the defined benefit plan in order to address a deficit that had arisen on the basis of the funding assumptions. Further, the measurement of the present value of the obligations under the plan for funding purposes differs from the measurement for accounting purposes, but they are different measurements of the same obligation, not separate obligations.

B28.13 Therefore, as a practical and proportionate solution, in measuring its defined benefit obligation an entity need not include the present value of contributions payable that arise from an agreement with the defined benefit plan to fund a deficit. Section 28 explicitly states that no additional liabilities shall be recognised in respect of an agreement with the defined benefit plan to fund a deficit (such as a schedule of contributions). This should ensure there are no divergent interpretations of the scope of Section 21 *Provisions and Contingencies* in relation to a schedule of contributions, because they are clearly within the scope of Section 28, and therefore outside the scope of Section 21.

B28.14 Consideration was given to whether removing the restriction on recognising a defined benefit plan asset in some circumstances might be an alternative solution. However, this option was rejected because it could have the unintended consequence of permitting an asset to be recognised when other factors would indicate the reporting entity was not able to recover the surplus.

B28.15 These amendments to FRS 102 do not affect the accounting for a schedule of contributions or other funding agreement between a reporting entity and a multi-employer plan, which is set out in paragraph 28.11A of FRS 102. When an entity participates in a defined benefit plan that is a multi-employer plan accounted for as if it were a defined contribution plan, it shall recognise a liability for the contributions payable that arise from the agreement (to the extent that they relate to a deficit). This is the most cost-effective way of recognising the entity's obligation to employees as a result of service rendered. This contrasts with the approach for defined benefit plans because the obligation has already been recognised as the net defined benefit liability.

Effect of a restriction on the recoverability of a plan surplus

B28.16 Initially FRS 102 did not specify where an entity shall recognise the effects of a restriction on the recoverability of a plan surplus, and therefore FRS 102 would require it to be recognised in profit or loss. A plan surplus may be irrecoverable because the entity is not able to recover the surplus through reduced contributions in the future or through refunds from the plan (see paragraph 28.22 of FRS 102). Except for any amount included in net interest on the net defined benefit liability, the effect of any such restriction should be recognised in other comprehensive income and therefore paragraph 28.25 was amended so that any such amounts are part of remeasurements, and recognised in other comprehensive income. This is consistent with IAS 19.

Disclosures

B28.17 Some respondents commented that the disclosure of information about the amount and timing of payments intended to fund a deficit in a defined benefit plan would be useful information for users of financial statements. Although this was already covered by the requirement to describe the funding policy, paragraph 28.41(a) was amended to clarify this.

B29 Section 29 Income Tax

'*Timing differences plus' approach*

B29.1 The income tax section of the IFRS for SMEs (2009) was not consistent with IAS 12 *Income Taxes*; the IASB had based the requirements of the IFRS for SMEs on proposals which were subsequently abandoned. In an early exposure draft the FRC proposed that the income tax section of FRS 102 should be replaced by the requirements of IAS 12. Respondents agreed that the IFRS for SMEs requirements should not be retained but also did not support the proposal to replace it with IAS 12.

B29.2 In developing an alternative solution, the findings of the ASB's research work with EFRAG in developing the Discussion Paper *Improving the Financial Reporting of Income Tax* (issued in December 2011), as well as the FRC's commitment to an IFRS-based solution and the requirements of FRS 19 *Deferred Tax* from which entities would be transitioning, were considered. The proposal set out an alternative approach that based the recognition requirements on timing differences, with additional recognition requirements for certain temporary differences that are not timing differences; a 'timing differences plus' approach. The advantages of this approach were that it would:

(a) provide useful information to users of financial statements; and

(b) provide the simple solution preparers were looking for that was close to previous accounting standards and that would give the same answers as IFRS in most cases.

B29.3 The most significant change to the requirements in previous accounting standards is that the 'timing differences plus' approach requires the recognition of the deferred tax implications of the revaluation of assets. Gains and losses recognised on a revaluation are timing differences and the tax effects should be recognised. Such a requirement is consistent with IAS 12 and the IFRS for SMEs.

B29.4 Another significant change from previous accounting standards is that discounting of current and deferred tax is not allowed which is consistent with IAS 12 and the IFRS for SMEs.

B29.5 Under IAS 12 deferred tax is not generally recognised on the initial recognition of an asset, except that of assets and liabilities arising from a business combination. No specific exception for this is necessary under the 'timing differences plus' approach as no timing difference arises.

B29.6 IAS 12 requires that deferred tax is recognised in respect of the difference between the amount recognised on a business combination for assets and liabilities (other than goodwill) and the amount that will be allowed for or assessed to tax in respect of such assets and liabilities. These differences are not timing differences. In order to maintain consistency with IAS 12, the timing differences approach is supplemented with a requirement to recognise deferred tax on business combinations.

B29.7 FRS 102 does not permit the recognition of deferred tax:

(a) when the tax deduction (or estimated future deduction) for share-based payment exceeds the cumulative amount of the related remuneration expense; and

(b) in some cases, when the tax basis of an asset is changed, for example when legislation changes the amount of future tax relief relating to the asset.

B29.8 However, it is considered that differences with IAS 12 are likely to be relatively rare and that in such cases the relevance of the information produced in accordance with IAS 12 would be unclear.

B29.9 The requirement to disclose differences between the current tax charge and a standard rate of tax for the next three years, was replaced by a requirement to disclose expected net reversals of timing differences for the next year. The requirement to disclose is on a net basis, which takes account of both the reversal of existing timing differences and the origination of new ones. The net basis provides information that is relevant to the entity's future cash flows, and hence is more relevant than disclosure on a gross basis. The additional benefit of disclosure on a net basis outweighs the cost to preparers of forecasting future new timing differences.

Gift aid

B29.10 The FRC was made aware of significant differences in accounting treatment arising in practice in relation to the accounting for payments made, or expected to be made, by a subsidiary to its charitable parent that will qualify for gift aid (expected gift aid payments). This includes charitable parents that are exempt charities, eg they are not regulated by the Charity Commission, but have another principal regulator.

B29.11 Many charitable entities, including registered providers of social housing and higher education institutions, carry out trading activities through a non-charitable subsidiary. Profits from the non-charitable subsidiary might be distributed to the parent charity (or venturer in a joint venture) in a tax-efficient manner as a donation which is eligible for corporation tax relief under the gift aid rules, provided it is made during the relevant reporting period or during the following nine months.

Distribution to owners

B29.12 Although such payments are donations for tax purposes, they are a distribution from the entity to its owners for company law purposes (see ICAEW Technical release TECH 16/14BL REVISED *Guidance on donations by a company to its parent charity*).

B29.13 As a result, FRS 102 requires the gift aid payment to be accounted for as a distribution to owners. FRS 102 contains some specific requirements that are relevant to distributions to owners, for example paragraph 22.17 requires distributions to owners to be recognised in equity. When there are no specific requirements, paragraph 10.5 requires an entity to first have regard to any requirements dealing with similar and related issues. In this case, this would be requirements relating to dividends, which are also distributions to owners. Therefore paragraph 32.8 should be applied to gift aid payments, and an expected gift aid payment shall not be accrued unless a legal obligation to make the payment exists at the reporting date. A board decision to make a gift aid payment to a parent charity, that has been taken prior to the reporting date, is not sufficient to create a legal obligation.

B29.14 Just over half the respondents to this issue considered that a liability should be recognised at the reporting date for an expected gift aid payment, for example when there was past practice of making such payments. This is not consistent with FRS 102 and the FRC was not persuaded that this better reflects the substance of the transaction which, for accounting purposes, is a distribution to owners, and therefore no amendment has been made to FRS 102 in this regard.

B29.15 Some respondents suggested that additional disclosure requirements be added to FRS 102 in order to provide information about any expected gift aid payment. The FRC considers that the current disclosure requirements of FRS 102, including those relating to tax, are sufficient and no additional disclosure requirements have been added.

Tax effects

B29.16 When a subsidiary does not have a legal obligation to distribute its profits to its owners at the reporting date, it would have taxable profits and need to recognise a tax expense because paragraph 29.14 prevents the tax effects of dividends being recognised before the dividend itself has been recognised.

B29.17 Respondents agreed that, in order to provide more relevant information to users of the financial statements, a pragmatic exception to paragraph 29.14 should be made to permit the tax effects of the gift aid payment to be taken into account when it is probable that the gift aid payment will be made within nine months of the reporting date. This is consistent with the way in which the gift aid relief works for corporation tax purposes in that relief is provided automatically against the taxable profits of the previous period when the gift aid payment is made within nine months of the reporting date.

B29.18 One respondent requested greater relief from recognising current and deferred tax expense (income) on the basis that ultimately any profits will be eligible for relief. No further relief has been provided in FRS 102 because the exception in paragraph 29.14A is based on the tax relief expected for the reporting period. Any other tax effects should be recognised when relevant; for example, if an entity does not expect to distribute all of its taxable profits, or has revalued items of property, plant and equipment.

Presentation of the tax effects of distributions to owners

B29.19 In addition, an amendment has been made to Section 29 *Income Tax* to clarify that the tax effects of distributions to owners shall be presented in profit or loss, rather than the same component as the underlying transaction. This is because when there is a tax effect arising from the distribution, it affects taxable profits. This is consistent with an amendment proposed to IAS 12.

B29.20 This amendment will be relevant to the tax effects of expected gift aid payments, but may also have wider application.

B31 Section 31 *Hyperinflation*

B31.1 Section 31 *Hyperinflation* has been amended as part of the *Triennial review 2017 amendments* to address situations when non-monetary items, such as property, plant and equipment, have been revalued at an earlier date. The revaluation reserve shall not be restated when adjustments are made for the effects of hyperinflation. This is a difference from IAS 29 *Financial Reporting in Hyperinflationary Economies* and the IFRS for SMEs reflecting the company law requirement to maintain a revaluation reserve.

B33 Section 33 *Related Party Disclosures*

Intragroup related party transactions exemption

B33.1 In response to feedback from respondents, the company law exemption from disclosing intragroup related party transactions was included in FRS 102.

B33.2 Some respondents raised the issue of a possible exemption from the disclosure of outstanding balances as well as transactions. However, it was noted that there is a separate legal requirement, in relation to the format of the balance sheet which requires disclosure of outstanding balances in aggregate for group undertakings and, separately, for undertakings in which the company has a participating interest. As Section 33 *Related Party Disclosures* requires disclosure in aggregate for a category of related parties, one of which is 'entities over which the entity has control, joint control or significant influence', this should be met by compliance with the requirements of Section 4 *Statement of Financial Position*. As a result, it was not possible to provide an effective exemption from the disclosure of outstanding balances with group undertakings.

Key management personnel compensation

B33.3 Some stakeholders questioned whether it was necessary for entities to disclose key management personnel compensation in addition to directors' remuneration, when it is required by company law. There can be significant differences between key management personnel compensation and directors' remuneration, for example when the directors and key management personnel are different, and not all entities applying FRS 102 are subject to company law.

B33.4 Therefore the key management personnel disclosure requirement was retained as part of the triennial review 2017, but an exemption was introduced for entities when there is no difference between the key management personnel and directors. An entity that is not exempt from the requirement to disclose key management personnel compensation shall disclose the total key management personnel compensation, including that relating to the directors.

B33.5 It was noted that if there are transactions with directors that are not required to be disclosed as directors' remuneration, they may still require disclosure in accordance with paragraph 33.9.

B34 Section 34 *Specialised Activities*

(A) Agriculture

B34A.1 Respondents questioned the proposed requirements relating to agricultural activity, which were largely based on a fair value model, noting that previous accounting standards did not set out accounting requirements for these transactions and although the proposals included an exemption from applying fair value when there is undue cost or effort, the fair value information is inconsistent with the way most agricultural businesses are managed and would not benefit the users of financial statements.

B34A.2 Therefore an accounting policy choice between a cost model and a fair value model was introduced for biological assets.

B34A.3 It was noted that both the cost model and the fair value model, as set out in the IFRS for SMEs, require agricultural produce to be measured at the point of harvest at fair value less costs to sell. However, respondents in favour of the cost model would expect the cost model to mean that both biological assets and agricultural produce would be measured at cost.

B34A.4 Agricultural produce should be capable of measurement at fair value without undue cost or effort, and should provide more relevant information to users. However, respondents argued that agricultural businesses often manage their business on the basis of cost information and agricultural produce should be permitted to be measured at cost. Therefore use of the cost model for agricultural produce is limited to those entities that chose the cost model for biological assets; however, these entities should also have the option of using the fair value model for agricultural produce.

(B) Extractive Activities

B34B.1 Respondents noted that the requirements of the IFRS for SMEs in relation to extractive activities were not consistent with IFRS 6 *Exploration for and Evaluation of*

Mineral Resources, and the application of the IFRS for SMEs requirements, in conjunction with other elements of FRS 102, would significantly change accounting practices. It would be likely that no assets could be recognised from the costs of exploration activities, yet entities applying EU-adopted IFRS would be permitted to recognise such assets. Therefore the requirements of IFRS 6 were incorporated into FRS 102 by cross-reference.

(C) Service Concession Arrangements

B34C.1 Respondents raised two main issues relating to the accounting for service concession arrangements. The first was that the requirements of the IFRS for SMEs in relation to the accounting by operators had been over-simplified when compared with IFRIC 12 *Service Concession Arrangements*. Therefore additional clarification of the principles of accounting by operators for service concession arrangements were developed from IFRIC 12 and added into FRS 102.

B34C.2 The second issue related to grantors, with some respondents noting that grantors might be within the scope of FRS 102. EU-adopted IFRS do not address accounting by grantors of service concession arrangements; grantors are expected to be outside their scope. As a result, accounting requirements for grantors were developed that were consistent with the principles underpinning the accounting by operators of service concession arrangements. The scope of IFRIC 12 is such that the grantor controls the residual interest in the infrastructure asset, and therefore for service concession arrangements meeting the definition in FRS 102, the grantor recognises its interest in the infrastructure asset usually as property, plant and equipment, with a corresponding liability measured using a finance lease model.

B34C.3 It was noted that the International Public Sector Accounting Standards Board (IPSASB) had issued a standard IPSAS 32 *Service Concession Arrangements: Grantor*, which includes two models for accounting by the grantor, depending on the terms of the arrangement with the operator. In addition to the finance lease model, IPSAS 32 includes a 'grant of right to the operator model' which applies to 'user-pays' arrangements. Some respondents suggested that this model should be permitted, but this FRS does not permit the application of this model because it results in the recognition of liabilities of amounts that may not meet the definition of a liability.

B34C.4 The need for transitional arrangements for grantors was considered. It was noted that for some grantors, the proposals would result in the recognition of assets and liabilities for infrastructure assets that would not previously have been recognised. It was considered that this provides more relevant information to users, and therefore no transitional arrangements were permitted. As a result, grantors are not permitted to apply the transitional exemptions that are available to operators, as set out in paragraph 35.10(i), by analogy.

(D) Financial Institutions

B34D.1 In broad terms, financial institutions are entities that hold assets in a fiduciary capacity or take deposits, including credit unions, building societies and investment entities. FRS 102 set out improvements from previous accounting standards for the recognition and measurement of financial instruments; however, the IFRS for SMEs had limited specific disclosure requirements for financial instruments held by financial institutions. A proportionate set of disclosures for financial institutions was developed from IFRS 7 *Financial Instruments: Disclosures*. Financial institutions applying reduced disclosures are not permitted to take exemptions from these additional disclosures.

B34D.2 Having identified a need to improve the disclosure requirements for financial institutions, a clear definition of a financial institution was developed. Various options were considered including the following:

(a) Using part of the definition of 'public accountability' from the IFRS for SMEs.

(b) Using the definition in section 467(1) of the Act.

(c) Listing the types of entity that are financial institutions. In this regard consideration was given to FRS 13 *Derivatives and Other Financial Instruments: Disclosures*, which applied a differential disclosure regime depending on the category of entity.

B34D.3 Prior to the *Triennial review 2017 amendments*, FRS 102 defined a financial institution by reference to a list of types of entities supported by a principle, intended to capture other similar entities.

B34D.4 The implementation of FRS 102 resulted in a number of queries about how the definition of a financial institution was applied in practice. Some stakeholders requested the removal of certain entities from the definition, whilst others requested amendments to the principle included in the definition to remove some uncertainties. Additionally, some perceived anomalies were highlighted during outreach.

B34D.5 After considering a number of options, the principle included in the financial institution definition was amended to remove references to 'generate wealth' and 'manage risk'. This change should help to reduce the interpretational difficulties in relation to implementing these concepts, and should reduce the number of entities meeting the definition of a financial institution.

B34D.6 In addition, retirement benefit plans were also removed from the definition, as they are not similar to the other entities specifically included in the list and FRS 102 already includes separate disclosure requirements for retirement benefit plans in Section 34 *Specialised Activities*.

B34D.7 Respondents noted that judgement will still need to be applied in determining whether an entity meets the definition of a financial institution, and that the inclusion of stockbrokers on the list will give rise to particular difficulties as they are generally dissimilar from the other entities, in that they do not hold financial instruments on behalf of others. Consequently, stockbrokers were removed from the list.

B34D.8 Respondents also noted the difficulties in applying the previous definition to group treasury companies. Some of these issues will have been alleviated by the change in the definition, but whether or not a group treasury company is a financial institution will depend on the individual facts and circumstances. Judgement will need to be applied in determining whether a group treasury company is similar to the other entities listed in the definition of a financial institution.

B34D.9 Further, bearing in mind the overall objective of entities providing information to enable users of financial statements to evaluate the significance of financial instruments held by the entity, paragraph 11.42 was amended to note that when the risks arising from financial instruments are particularly significant to the business, additional disclosure may be required. The disclosure requirements for financial institutions, set out in paragraphs 34.19 to 34.33, may be relevant in such cases.

Fair value hierarchy disclosures

B34D.10 In March 2016, amendments were made so that financial institutions and retirement benefit plans categorise fair value measurements into levels consistent with the fair value hierarchy set out in IFRS 13 *Fair Value Measurement*. This followed feedback from the representative bodies of some financial institutions and retirement benefit plans suggesting that the disclosure requirements for these entities could be made more cost-effective, whilst increasing their usefulness to users of the financial statements. For those users familiar with the IFRS disclosures, the consistency of disclosure with IFRS may also reduce costs or effort of comparison and the possibility of confusion.

B34D.11 It was noted that paragraphs 34.22 and 34.42 of FRS 102 required financial institutions and retirement benefit plans, respectively, to provide disclosures about financial instruments held at fair value analysed by the level of the fair value hierarchy in paragraph 11.27 of FRS 102 (now paragraph 2A.1). This hierarchy was not the same as the hierarchy set out in IFRS 13, and therefore the disclosures provided by a financial institution or retirement benefit plan applying FRS 102 would not be directly comparable to those provided by an entity applying EU-adopted IFRS. The SORPs for Authorised Funds, Investment Trust Companies and Pension Schemes require, or permit, additional disclosure from entities within their scope in order to improve this comparability. It was also noted that some financial institutions previously applied FRS 29 *Financial Instruments: Disclosures*, which required disclosure according to a fair value hierarchy that is consistent with IFRS 13, and therefore for these entities FRS 102 had introduced a departure from IFRS.

B34D.12 This amendment leaves an inconsistency within FRS 102, whereby the hierarchy described in paragraph 11.27 for the purposes of determining a process for estimating fair values is no longer consistent with the hierarchy used for disclosure purposes in Section 34.

B34D.13 As part of the *Triennial review 2017 amendments*, this issue was reviewed and further feedback from respondents was received. As discussed in paragraphs B11.42 to B11.47, only minor changes were made to paragraph 11.27, for example to emphasise that it is a methodology and give further practical guidance.

B34D.14 Amendments to the relevant SORPs were not necessary before any changes to FRS 102 could take effect because a change in accounting standards after a SORP has been issued means that any inconsistent provisions of a SORP cease to have effect.

(E) Retirement Benefit Plans: Financial Statements

B34E.1 Having decided to eliminate the definition of public accountability, retirement benefit plans fall within the scope of FRS 102; however, the IFRS for SMEs contains no specific requirements for retirement benefit plans.

B34E.2 One approach that was rejected, was to direct retirement benefit plans to IAS 26 *Accounting and Reporting by Retirement Benefit Plans* and request that the Statement of Recommended Practice (SORP) *Financial Reports of Pension Schemes* be updated to be consistent with IAS 26. Feedback from stakeholders suggested that the application of IAS 26 would be difficult for two reasons:

(a) legal accounting and reporting requirements in the UK are different to those in IAS 26; and

(b) IAS 26 itself makes references to other IFRSs and the interaction between those references and FRS 102 would be complicated.

B34E.3 A further complication would arise as the SORP would also provide application guidance for retirement benefit plans.

B34E.4 Following this feedback, accounting requirements for retirement benefit plans financial statements were developed that would be supplemented by the SORP.

B34E.5 In developing the proposals, the issue of whether the financial statements of retirement benefit plans need to provide disclosure regarding the pension liabilities and the related funding of the plan were considered. Feedback from respondents suggested that such information should not be disclosed in the financial statements, but provided alongside them, as was the case under previous accounting standards.

B34E.6 Initially, retirement benefit plans met the definition of a financial institution; however, not all of the disclosure requirements for financial institutions are relevant to retirement benefit plans. Therefore all the requirements for retirement benefit plans are provided in one sub-section for ease of use. In December 2017 retirement benefit plans were removed from the definition of a financial institution.

Fair value hierarchy disclosures

B34E.7 In March 2016, amendments were made so that financial institutions and retirement benefit plans categorise fair value measurements into levels consistent with the fair value hierarchy set out in IFRS 13. This followed feedback from the representative bodies of some financial institutions and retirement benefit plans suggesting that the disclosure requirements for these entities could be made more cost-effective, whilst increasing their usefulness to users of the financial statements. For those users familiar with the IFRS disclosures, the consistency of disclosure with IFRS may also reduce costs or effort of comparison and the possibility of confusion.

B34E.8 Further discussion of this amendment can be found in sub-section (D) *Financial Institutions* above.

(G) Funding Commitments

B34G.1 The *Statement of Principles: Interpretation for Public Benefit Entities* previously addressed the issue of when to recognise a commitment to provide funding in a non-exchange transaction. It was considered necessary to incorporate these details into FRS 102 to be used in conjunction with Section 2 *Concepts and Pervasive Principles* and Section 21 *Provisions and Contingencies*.

B34G.2 The issue was particularly important because many PBEs provide funding on an on-going basis and there is little guidance on how such multi-year commitments should be recognised.

B34G.3 Consideration was given to when a liability for such a commitment should be recognised and an entity shall only recognise a liability if the commitment to provide funding was made unconditionally, and the grantor could not realistically withdraw from the commitment. In this situation, an entity would recognise a liability for the present value of the total funding promised.

B34G.4 As this is an application of the principles in Section 2 and Section 21, it was concluded that the requirements for funding commitments should apply to all entities and not just PBEs.

(I) Incoming Resources from Non-exchange Transactions

B34I.1 The receipt of resources from non-exchange transactions is an inflow of resources that is highly significant for many PBEs: the receipt of donations, grants and legacies from non-exchange transactions is a major source of their funding and this issue is not addressed in the IFRS for SMEs apart from in Section 24 *Government Grants*.

B34I.2 FRS 102 requires, in principle, PBEs to value the resources they receive from non-exchange transactions at their fair value. Consideration was given to whether using fair value would overstate the value of a donation when the entity is unable to exploit an asset fully, and the equivalent service potential could be derived from a lower value asset. Being able to achieve the same service potential from a lower value asset might suggest that the value of the donated asset should be at the lower value. However, FRS 102 requires donated assets to be valued at their fair value as this reflects that the circumstances described above would rarely occur. In many cases, an entity would be able to sell the donated asset and, if appropriate, purchase a cheaper asset with the equivalent service potential.

B34I.3 Incorporating an exception for donated assets that may not be fully exploited would make the application of FRS 102 more onerous, as it would require all entities in receipt of donated assets (except those intended for resale) to consider whether they would be able to exploit the asset fully. This would be subjective and may incur the risk of understatement of the value of donated assets.

B34I.4 The FRC noted that when goods are donated for subsequent sale (for example donations to charity shops), it could be argued that the donated goods should be valued only when they are sold. This is not consistent with the accruals concept which requires the financial statements to recognise goods when they are received. However, on pragmatic grounds, FRS 102 requires that donated goods should only be recognised as income on receipt when the item is material, can be measured reliably and if the benefits of recognising the item outweigh the costs. Further, the same accounting may be applied by other wholly-owned entities in a public benefit entity group, to eliminate the need to restate goods donated for subsequent sale on consolidation (for example, where a charity operates its shops through a subsidiary that is a non-charitable company).

B34I.5 FRS 102 requires donated services that would otherwise have been purchased to be accounted for at their estimated value to the recipient. This is a pragmatic solution recognising that there are potential issues in determining a value for volunteer services and their contribution to the organisation and notes that quantifying this type of service may not be practicable. There is an argument to suggest that volunteer services could be measured by reference to a metric such as the minimum wage, however this measure does not take into consideration an organisation's requirements for volunteers. In addition, this would be attributing an arbitrary value to a volunteer's time which may not be reflective of their skills, experience or role and to determine a different method of valuation would be very subjective.

B34I.6 However, when a service is provided voluntarily for which the entity would otherwise have to pay (eg legal or financial advice), the value of that service should be recognised in the financial statements when, as will usually be the case, its value can be reasonably quantified.

(J) Public Benefit Entity Combinations

B34J.1 In considering the issue of entity combinations involving two or more public benefit entities, it was noted that there is some debate over whether the use of acquisition accounting for all combinations would be appropriate. In particular, whether acquisition accounting reflects the substance of a transaction if there is a gift of one entity to another in a combination at nil or nominal consideration, or where two or more organisations genuinely merge to form a new entity.

B34J.2 When there is a combination of entities at nil or nominal consideration which is in substance a gift, it is appropriate to follow the same accounting principles as donations of assets (as set out in Section 34 *Specialised Activities*) by recognising the fair value of the assets received and liabilities assumed as a gain or loss in income and expenditure.

B34J.3 Accounting for combinations that meet the definition of a merger requires a different methodology to acquisition accounting in order to reflect the true substance of the transaction. Whilst it is not anticipated that all combinations involving two or more public benefit entities are mergers or that merger accounting will generally be applicable to such combinations, it is considered appropriate to retain merger accounting in certain circumstances. In considering this matter it was noted that the accounting requirements for PBEs in some jurisdictions, for example, the US and Australia, had retained merger accounting for the public and not-for-profit sectors.

B34J.4 The criteria set out in FRS 6 *Acquisitions and Mergers* have been adapted to make them more appropriate for public benefit entities. In particular, a criterion has been added to include consideration of the impact of the combination on beneficiaries and the benefits to which they are entitled.

B34J.5 One specific concern highlighted in relation to the requirements of FRS 6, is the need to restate comparatives by adding together the previous periods' reported figures of each of the combining entities. This does not reflect the substance of the transaction as the historical parties which formed the entity did not exist as a single entity in the previous accounting period and therefore FRS 102 requires comparatives to be marked as 'combined' to make it clear that they are a combination of previously reported figures for the combining entities.

B34J.6 In July 2015, as part of the implementation of the EU Accounting Directive, this section was amended to clarify that a public benefit entity may apply merger accounting to an entity combination that is a merger provided that it is permitted by the statutory framework under which it reports. Company Law only permits companies to apply merger accounting for group reconstructions and this amendment to FRS 102 was made to ensure merger accounting is not applied by public benefit entities that are companies when not permitted in law. Some respondents suggested that FRS 102 should continue to require the use of merger accounting by all public benefit entity combinations meeting the definition and criteria of a merger, through requiring the use of the true and fair override. It was noted that 'true mergers' (other than those that might be considered group reconstructions) are not likely to be common. However, Appendix III *Note on legal requirements* notes that an individual public benefit entity may apply the true and fair override if it considers it appropriate to its circumstances, and provides the corresponding disclosures.

(K) Public Benefit Entity Concessionary Loans

B34K.1 The two main accounting treatments to consider when determining the basis for the measurement of concessionary loans are the amount paid or received, and fair value.

B34K.2 Accounting for concessionary loans at the amount paid or received (rather than fair value) is not consistent with the accounting requirements set out in Section 11 *Basic Financial Instruments*, adopted IFRS or IPSAS 29 *Financial Instruments: Recognition and Measurement* which require that such arrangements are measured and recognised in the financial statements at their fair value.

B34K.3 Nevertheless, due to the difficulties that smaller PBEs may face with determining fair value, PBEs that make or receive concessionary loans have the option of measuring such loans at either the amount paid or received or at fair value. PBEs that make and receive concessionary loans must apply the same measurement method to both. Further, the same accounting may be applied by other wholly-owned entities in a public benefit entity group, to eliminate the need to restate concessionary loans made or received for the purposes of furthering the PBEs objectives on consolidation.

B34K.4 The disclosure requirements in FRS 102 provide sufficient information to understand and interpret the impact of these types of transaction on the financial statements.

B35 Section 35 *Transition to this FRS*

Goodwill on transition

B35.1 FRS 102 does not permit goodwill to have an indefinite useful life, unlike previous accounting standards. On transition to FRS 102 entities that previously determined that goodwill had an indefinite useful life would need to reassess goodwill to determine its remaining useful life, and subsequently amortise the goodwill over that period.

Table 1

Exposure drafts and consultation documents

Feedback from the following FRC exposure drafts and consultations has been considered in the development of FRS 102.

More detailed information on the early development of current UK and Republic of Ireland accounting standards can be found on the FRC website.

Exposure draft		**Date of issue**	**Finalised as**	**Date of issue**	**Mandatory effective date**
FRED 44	*Financial Reporting Standard for Medium-sized Entities*	Oct 2010	FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland*	Mar 2013	1 Jan 2015
FRED 45	*Financial Reporting Standard for Public Benefit Entities*	Mar 2011			
FRED 48	*Draft Financial Reporting Standard – The Financial Reporting Standard applicable in the UK and Republic of Ireland*	Jan 2012			
Amendment to FRED 48	*Draft FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Section 28 'Employee Benefits' and Section 34 'Specialised Activities'*	Oct 2012			
FRED 50	*Draft FRC Abstract 1 – Residential Management Companies' Financial Statements and Consequential Amendments to the FRSSE*	Aug 2013	*Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Small entities and other minor amendments*	Jul 2015	No amendments made in respect of FRED 50
FRED 51	*Draft amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Hedge accounting*	Nov 2013	*Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Basic financial instruments and Hedge accounting*	Jul 2014	1 Jan 2015
FRED 54	*Draft amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Basic financial instruments*	Feb 2014			
FRED 55	*Draft amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Pension obligations*	Aug 2014	*Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Pension obligations*	Feb 2015	1 Jan 2015

Exposure draft		**Date of issue**	**Finalised as**	**Date of issue**	**Mandatory effective date**
Consultation document	*Accounting standards for small entities – Implementation of the EU Accounting Directive*	Sep 2014	*Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Small entities and other minor amendments*	Jul 2015	All paragraphs except 26.15 to 26.15B: 1 Jan 2016 Paragraphs 26.15 to 26.15B: 1 Jan 2015
FRED 59	*Draft amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Small entities and other minor amendments*	Feb 2015			
FRED 61	*Draft amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Share-based payment transactions with cash alternatives*	Apr 2015			
FRED 62	*Draft amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Fair value hierarchy disclosures*	Nov 2015	*Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Fair value hierarchy disclosures*	Mar 2016	1 Jan 2017
FRED 65	*Draft amendments to FRS 101 Reduced Disclosure Framework – Notification of shareholders*	Jul 2016	*Amendments to FRS 101 Reduced Disclosure Framework and FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Notification of shareholders*	Dec 2016	1 Jan 2016
Request for information	*Request for comments on the implementation of FRS 102 in order to inform the future development of FRS 102*	Mar 2016	*Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Directors' loans – optional interim relief for small entities*	May 2017	8 May 2017
Consultation Document	*Triennial review of UK and Ireland accounting standards – Approach to changes in IFRS*	Sep 2016	*Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Triennial review 2017 – Incremental improvements and clarifications*	Dec 2017	1 Jan 2019
FRED 67	*Draft amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Triennial review 2017 – Incremental improvements and clarifications*	Mar 2017			

Exposure draft		Date of issue	Finalised as	Date of issue	Mandatory effective date
FRED 68	*Draft amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Payments by subsidiaries to their charitable parents that qualify for gift aid*	Sep 2017	(see above)		
FRED 70	*Draft Amendments to FRS 101 Reduced Disclosure Framework – 2018/19 cycle*	Jan 2019	*Amendments to FRS 101 Reduced Disclosure Framework – 2018/19 cycle*	Jul 2019	1 Jan 2023[84]
FRED 71	*Draft Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Multi-employer defined benefit plans*	Jan 2019	*Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Multi-employer defined benefit plans*	May 2019	1 Jan 2020
FRED 72	*Draft Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Interest rate benchmark reform*	Jul 2019	*Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Interest rate benchmark reform*	Dec 2019	1 Jan 2020
FRED 73	*Draft Amendments to FRS 101 Reduced Disclosure Framework – 2019/20 cycle*	Dec 2019	*Amendments to FRS 101 Reduced Disclosure Framework – 2019/20 cycle*	May 2020	Financial statements approved after 29 May 2020
FRED 74	*Draft amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Interest rate benchmark reform (Phase 2)*	May 2020	*Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland – Interest rate benchmark reform (Phase 2)*	Dec 2020	1 Jan 2021
N/A			*Amendment to FRS 101 Reduced Disclosure Framework – Effective date of IFRS 17*	Oct 2020	1 Jan 2023
FRED 76	*Draft Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland and FRS 105 The Financial Reporting Standard applicable to the Micro-entities Regime – COVID-19-related rent concessions*	Jul 2020	*Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland and FRS 105 The Financial Reporting Standard applicable to the Micro-entities Regime – COVID-19-related rent concessions*	Oct 2020	1 Jan 2020

[84] Originally, the amendments' effective date was for accounting periods beginning on or after 1 January 2021. This date aligned with the original effective date of IFRS 17 *Insurance Contracts*. In October 2020, the effective date was aligned with the revised effective date of IFRS 17.

Exposure draft		Date of issue	Finalised as	Date of issue	Mandatory effective date
N/A			*Amendments to UK and Republic of Ireland accounting standards – UK exit from the European Union*	Dec 2020	1 Jan 2021
FRED 78	*Draft Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland and FRS 105 The Financial Reporting Standard applicable to the Micro-entities Regime – COVID-19-related rent concessions beyond 30 June 2021*	Apr 2021	*Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland and FRS 105 The Financial Reporting Standard applicable to the Micro-entities Regime – COVID-19-related rent concessions beyond 30 June 2021*	Jun 2021	1 Jan 2021

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