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- Illustrative IFRS consolidated financial statements for 2013 year ends

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Guide aimed at finance directors, financial controllers and deal-makers, providing background to the standard, impact on the financial statements and controls, and summary differences with US GAAP.

**IFRS disclosure checklist 2013**
Outlines the disclosures required for 31 December 2013 year ends.

**IFRS pocket guide 2013**
Summary of the IFRS recognition and measurement requirements. Including currencies, assets, liabilities, equity, income, expenses, business combinations and interim financial statements.

**Manual of accounting – Interim financial reporting 2013**
Guidance on preparing interim financial reports under IAS 34, including illustrative financial statements and disclosure checklist. Update due May 2014.

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**Illustrative consolidated financial statements**
- Investment property, 2013
- Private equity, 2013
- Investment funds, 2013

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Guidance includes:
- Questions and answers on impairment of nonfinancial assets in the current crisis.
- Top 10 tips for impairment testing.

**Preparing your first IFRS financial statements: Adopting IFRS**
Outlines how companies should address the process of selecting their new IFRS accounting policies and applying the guidance in IFRS 1. Provides specific considerations for US market.

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Introduction

A group of five new and revised standards were published in May 2011 and effective 1 January 2013 but endorsed for EU entities for annual periods starting on or after 1 January 2014. IFRS 10, ‘Consolidated financial statements’, changes the definition of control; IFRS 11, ‘Joint arrangements’, reduces the types of joint arrangement to joint operations and joint ventures, and prohibits the use of proportional consolidation. IFRS 12, ‘Disclosure of interests in other entities’, brings together in one standard the disclosure requirements that apply to investments in subsidiaries, associates, joint ventures, structured entities and unconsolidated structured entities. As part of this overhaul of the consolidation standards, IAS 27 (revised) now deals only with separate financial statements, and IAS 28 (revised) covers equity accounting for joint ventures as well as associates. These new standards have to be implemented together. A further amendment to these standards sets out the accounting for investment entities and this comes into effect from 1 January 2014.

IFRS 9, ‘Financial instruments’, was reissued in 2010 and includes guidance on the classification and measurement of financial assets and financial liabilities and the de-recognition of financial instruments. In November 2013 an amendment to IFRS 9 was issued on hedge accounting which includes a substantial overhaul of hedge accounting that will allow entities to better reflect their risk management activities in the financial statements and also removed the 1 January 2015 effective date. The effective date is yet to be determined and the standard will not be endorsed until the rest of IFRS 9 is released, although IFRS 9 can be adopted early by non EU entities.

IFRS 14 permits first-time adopters to continue to recognise amounts related to rate regulation in accordance with their previous GAAP requirements when they adopt IFRS.

A few narrow scope amendments to existing standards have also been issued and are effective for annual periods beginning on or after 1 January 2014. Firstly an amendment to IAS 32, ‘Financial instruments: Presentation’ regarding the offsetting of financial assets and financial liabilities. Secondly an amendment to IAS 36, ‘Impairment of assets’ regarding recoverable amount disclosures for non-financial assets and finally an amendment to IAS 39, ‘Financial instruments; Recognition and measurement’ regarding the novation of derivatives and continuation of hedge accounting.

In addition an amendment to IAS 19, ‘Employee benefits’, concerning defined benefit plans that require employers or third parties to contribute towards the costs of benefits, was issued in December 2013 and is effective annual periods on or after 1 July 2014 subject to EU endorsement for EU entities.

The 2012 improvements project containing seven amendments and the 2013 improvements project containing four amendments were issued in December 2013 and all the amendments are effective for annual periods beginning on or after 1 July 2014 subject to EU endorsement for EU entities.

One interpretation – IFRIC 21, ‘Levies’, was published in 2013 in relation to IAS 37, ‘Provisions, contingent liabilities and contingent assets’. IAS 37 sets out criteria for the recognition of a liability, one of which is the requirement for the entity to have a present obligation as a result of a past event (known as an obligating event). The interpretation clarifies that the obligating event that gives rise to a liability to pay a levy is the activity described in the relevant legislation that triggers the payment of the levy and is effective 1 January 2014 subject to EU endorsement for EU entities.

This publication is a practical guide to the new IFRS standards and interpretations that come into effect for 2014 year ends.
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Amended standards

Defined benefit plans

Amendments to IAS 19, ‘Employee contributions’

Effective date
Annual periods beginning on or after 1 July 2014. Early adoption is permitted.

EU adoption status
Not adopted at the time of going to print.

What is the issue?
This amendment clarifies the application of IAS 19, ‘Employee benefits’ (2011) – referred to as ‘IAS 19R’, to plans that require employees or third parties to contribute towards the cost of benefits. The amendment does not affect the accounting for voluntary contributions.

Some pension plans require employees or third parties to contribute to the plan. These contributions reduce the cost to the employer of providing the benefits. Common practice under the previous version of IAS 19 was to deduct the contributions from the cost of the benefits earned in the year in which the contributions were paid.

IAS 19R, which is applicable to periods commencing on or after 1 January 2013, was intended to clarify the treatment of contributions from employees or third parties. However, the revised guidance is open to a range of potentially complex interpretations, and could require most entities to change the way in which they account for these contributions.

The 2011 revisions to IAS 19 distinguished between employee contributions related to service and those not linked to service. The current amendment further distinguishes between contributions that are linked to service only in the period in which they arise and those linked to service in more than one period. In our view, a contribution that is payable out of current salary is linked to service.

The amendment allows contributions that are linked to service, and do not vary with the length of employee service, to be deducted from the cost of benefits earned in the period that the service is provided.

The amendment will allow (but not require) many entities to continue accounting for employee contributions using their existing accounting policy, rather than spreading them over the employees’ working lives.

Contributions that are linked to service, and vary according to the length of employee service, must be spread over the service period using the same attribution method that is applied to the benefits; that means either in accordance with the formula in the pension plan, or, where the plan provides a materially higher level of benefit for service in later years, on a straight line basis.

Example 1
A plan that requires employees to contribute 4% of salary if they are below age 40, and 7% of salary if they are 40 or above, is an example of a plan in which employee contributions are not linked to the length of service.

The contributions are linked to age and salary, but are not dependent on the length of service. So the contributions would be recognised as a reduction of pension expense in the year in which the related service is delivered.
Example 2
A plan that provides a lump sum benefit on retirement of 10% of final salary for the first ten years of service, plus 20% of final salary for each subsequent year of service, and requires employee contributions equal to 5% of salary for the first ten years of service and 8% thereafter, is a plan in which contributions are linked to the length of service.

The contributions vary with the length of service, as well as salary, and so they have to be recognised over the working life. The benefit earned and the employee contributions would be recognised on a straight line basis over the employee's working life in this example.

Example 3
A post-employment medical insurance plan, where the employee is required to meet the first CU20 per month of the insurance premium, is an arrangement in which the contributions are not linked to service. The expected future contributions from the employee, which would be payable after retirement, would be included in the measurement of the benefit obligation.

Am I affected?
The amendment to IAS 19R will affect any post-employment benefit plans where employees or third parties are required to meet some of the cost of the plan.

The amendment clarifies the accounting by entities with plans that require contributions linked only to service in each period.

Entities with plans that require contributions that vary with service will be required to recognise the benefit of those contributions over employees’ working lives. Management should consider how it will apply that model.
Offsetting financial assets and financial liabilities

Amendments to IAS 32, ‘Financial instruments: Presentation’

Effective date
Annual periods beginning on or after 1 January 2014. Early adoption is permitted.

EU adoption status
Adopted.

What is the issue?
This amendment clarifies some of the requirements for offsetting financial assets and financial liabilities on the statement of financial position.

Key provisions
The amendments do not change the current offsetting model in IAS 32, which requires an entity to offset a financial asset and financial liability in the statement of financial position only when the entity currently has a legally enforceable right of set-off and intends either to settle the asset and liability on a net basis or to realise the asset and settle the liability simultaneously.

The amendments clarify that the right of set-off must be available today – that is, it is not contingent on a future event. It also must be legally enforceable for all counterparties in the normal course of business, as well as in the event of default, insolvency or bankruptcy.

The amendments also clarify that gross settlement mechanisms (such as through a clearing house) with features that both (i) eliminate credit and liquidity risk and (ii) process receivables and payables in a single settlement process, are effectively equivalent to net settlement; they would therefore satisfy the IAS 32 criterion in these instances.

Master netting agreements where the legal right of offset is only enforceable on the occurrence of some future event, such as default of the counterparty, continue not to meet the offsetting requirements.

Disclosures
The amended disclosures will require more extensive disclosures than are currently required under IFRS and US GAAP. The disclosures focus on quantitative information about recognised financial instruments that are offset in the statement of financial position, as well as those recognised financial instruments that are subject to master netting or similar arrangements irrespective of whether they are offset.

Am I affected?
These amendments primarily affect financial institutions, as they will be required to provide additional disclosures described above. However, other entities that hold financial instruments that may be subject to offsetting rules will also be affected.

What do I need to do?
Management should begin gathering the information necessary to prepare the new disclosure requirements. Management will also need to investigate whether the clarifications of the offsetting principle in IAS 32 result in any changes to what they offset in the statement of financial position today. Management may need to work with the clearing houses they use to determine whether their settlement processes comply with the new requirements.
Recoverable amount disclosures for non-financial assets

Amendments to IAS 36, ‘Impairment of assets’

What is the issue?

This narrow scope amendment has made small changes to the disclosures required by IAS 36, Impairment of assets when recoverable amount is determined based on fair value less costs of disposal. The IASB made consequential amendments to the disclosure requirements of IAS 36 when it issued IFRS 13. One of the amendments was drafted more widely than intended. This limited scope amendment corrects this and introduces additional disclosures about fair value measurements when there has been impairment or a reversal of impairment.

Key amendments

The IASB has amended IAS 36 as follows:

• to remove the requirement to disclose recoverable amount when a cash generating unit (CGU) contains goodwill or indefinite lived intangible assets but there has been no impairment;
• to require disclosure of the recoverable amount of an asset or CGU when an impairment loss has been recognised or reversed; and
• to require detailed disclosure of how the fair value less costs of disposal has been measured when an impairment loss has been recognised or reversed.

The amendments will impact all preparers who recognise or reverse an impairment loss on non-financial assets.

Am I affected?

The amendments will impact all preparers who recognise or reverse an impairment loss on non-financial assets.

What do I need to do?

Read the proposed amendments in their entirety to determine the impact for you.

Effective date

Annual periods beginning on or after 1 January 2014.

EU adoption status

Adopted.
Novation of derivatives and continuation of hedge accounting

Amendments to IAS 39, ‘Financial instruments: Recognition and measurement’

What is the issue?

Widespread legislative changes have been introduced to improve transparency and regulatory oversight of over-the-counter (OTC) derivatives. As a result, entities are novating derivative contracts to central counterparties (CCPs) in an effort to reduce counterparty credit risk.

Under IAS 39, ‘Financial instruments: Recognition and measurement’, an entity is required to discontinue hedge accounting for a derivative that has been designated as a hedging instrument where the derivative is novated to a CCP; this is because the original derivative no longer exists. The new derivative with the CCP is recognised at the time of the novation.

The IASB, however, was concerned about the financial reporting effects that would arise from novations that are a consequence of laws or regulations. As a result, the IASB has amended IAS 39 to provide relief from discontinuing hedge accounting when novation of a hedging instrument to a CCP meets specified criteria. Similar relief will be included in IFRS 9, ‘Financial instruments’.

Key amendments

The amendments will not result in the expiration or termination of the hedging instrument if:

- as a consequence of laws or regulations, the parties to the hedging instrument agree that a CCP, or an entity (or entities) acting as a counterparty in order to effect clearing by a CCP (‘the clearing counterparty’), replaces their original counterparty; and
- other changes, if any, to the hedging instrument are limited to those that are necessary to effect such replacement of the counterparty. These changes include changes in the contractual collateral requirements, rights to offset receivables and payables balances, and charges levied.

The changes are broader than those proposed in the exposure draft published in February 2013, since the amendments refer to novations ‘as a consequence of’ laws or regulations, rather than those ‘required by’ laws or regulations. The changes also expand the scope to allow the use of clearing brokers.

The amendments will apply for annual periods beginning on or after 1 January 2014. Earlier application is permitted.

Am I affected?

These amendments are beneficial to all entities applying hedge accounting that are subject to novation of OTC derivatives, as described above.
New standards

Financial instruments

IFRS 9

Effective date
Annual periods beginning on or after 1 January 2018. Early adoption is permitted (see detail below).

EU adoption status
Not adopted at the time of going to print.


If an entity early adopts IFRS 9, it will not be required to early adopt subsequent stages in the IAS 39 replacement project – that is, impairment and hedging. This is to facilitate early adoption of IFRS 9. However, if an entity chooses to early adopt any of the subsequent stages, it will be required to early adopt all preceding stages from the same date.

What determines classification?

IFRS 9 introduces a two-step classification approach. First, an entity considers its business model – that is, whether it holds the financial asset to collect contractual cash flows rather than to sell it prior to maturity to realise fair value changes. If the latter, the instrument is measured at fair value through profit or loss (FVTPL). If the former, an entity further considers the contractual cash flow characteristics of the instrument.

What is a contractual cash flow characteristics test?

A financial asset within a qualifying business model will be eligible for amortised cost accounting if the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding. Interest is defined as consideration for the time value of money and for the credit risk associated with the principal amount outstanding during a particular period of time.

Any leverage feature increases the variability of the contractual cash flows with the result that they do not have the economic characteristics of interest. If a contractual cash flow characteristic is not genuine, it does not affect the classification of a financial asset. A cash flow characteristic is not genuine if it affects the instrument’s contractual cash flows only on the occurrence of an event that is extremely rare, highly abnormal and very unlikely to occur.

Classification and measurement of financial assets

How are financial assets to be measured?

IFRS 9 requires all financial assets to be measured at either amortised cost or full fair value. Amortised cost provides decision-useful information for financial assets that are held primarily to collect cash flows that represent the payment of principal and interest. For all other financial assets, including those held for trading, fair value is the most relevant measurement basis.
What are common features that would generally pass the cash flow characteristics test?

- unleveraged linkage to an inflation index in the currency in which the financial asset is denominated;
- multiple extension options (for example, a perpetual bond);
- call and put options if they are not contingent on future events, and the pre-payment amount substantially represents unpaid amounts of principal and interest on the principal amount outstanding, which may include reasonable additional compensation for the early termination of the contract;
- interest rate caps, floors and collars that effectively switch the interest rate from fixed to variable and vice versa; and
- in a variable rate financial asset, a borrower option to choose a rate at each interest rate reset day as long as the rate compensates the lender for the time value of money (for example, an option to pay three-month LIBOR for a three-month term or one-month LIBOR for a one-month term).

What are common features that would generally fail the cash flow characteristics test?

- linkage to equity index, borrower’s net income or other variables;
- inverse floating rate;
- call option at an amount not reflective of outstanding principal and interest;
- issuer is required or can choose to defer interest payments and additional interest does not accrue on those deferred amounts;
- in a variable rate financial asset, a borrower option to choose a rate at each interest rate reset day such that the rate does not compensate the lender for the time value of money (for example, an option to pay one-month LIBOR for a three-month term and one-month LIBOR is not reset each month);
- a variable rate that is reset periodically but always reflects a five-year maturity in a five-year constant maturity bond (that is, the rate is disconnected with the term of the instrument except at origination); and
- an equity conversion option in a debt host (from a holder perspective).

Are reclassifications permitted?

Classification of financial assets is determined on initial recognition. Subsequent reclassification is permitted only in those rare circumstances when there is a change to the business model within which the financial asset is held. In such cases, all affected financial assets are reclassified.

IFRS 9 specifies that changes in business model are expected to be very infrequent, should be determined by the entity’s senior management as a result of external or internal changes, should be significant to the entity’s operations and demonstrable to external parties. For example, an entity has a portfolio of commercial loans that it holds to sell in the short term. The entity acquires a company that manages commercial loans and has a business model that holds the loans in order to collect the contractual cash flows. The portfolio of commercial loans is no longer for sale, and the portfolio is now managed together with the acquired commercial loans; all are held to collect the contractual cash flows.

Another example of a change in the business model is where an entity decides to shut down a line of service (for example, a retail mortgage business). The line of service does not accept new business, and the affected portfolio is being actively marketed for sale.

Changes in intentions with respect to individual instruments, temporary disappearance of a particular market or transfers of instrument between business models do not represent a change in business model.

What does this mean for equity investments?

Equity investments do not demonstrate contractual cash flow characteristics of principal and interest; they are therefore accounted for at fair value. However, IFRS 9 provides an option to designate a non-trading equity investment at FVTPL or at fair value through other comprehensive income. The designation is available on an instrument-by-instrument basis and only on initial recognition. Once made, the designation is irrevocable.

All realised and unrealised fair value gains and losses follow the initial designation, and there is no recycling of fair value gains and losses recognised in other comprehensive income to profit or loss. Dividends that represent a return on investment from equity investments continue to be recognised in profit or loss regardless of the designation.

Can an equity investment be measured at cost where no reliable fair value measure is available?

IFRS 9 removes the cost exemption for unquoted equities and derivatives on unquoted equities but stipulates that, in
certain circumstances, cost may be an appropriate estimate of fair value. This may be the case where insufficient recent information is available or where there is a wide range of possible fair value measurements. Cost will not be an appropriate estimate of fair value if there are changes in investee circumstances, markets or wider economy, or if there is evidence from external transactions or for investments in quoted equity instruments. To the extent factors exist that indicate cost might not be representative of fair value, the entity should estimate fair value.

**What does this mean for hybrid contracts?**

IFRS 9 requires financial assets to be classified in their entirety. Hybrid contracts are those instruments that contain a financial or non-financial host and an embedded derivative.

Hybrid contracts within the scope of IFRS 9 — that is, hybrid contracts with financial asset hosts — are assessed in their entirety against the two classification criteria. Hybrid contracts outside the scope of IFRS 9 are assessed for bifurcation under IAS 39. In many cases, hybrid contracts may fail the contractual cash flow characteristic test and should therefore be measured at FVTPL.

**Is a fair value option available?**

Two of the existing three fair value option criteria currently in IAS 39 become obsolete under IFRS 9, as a fair-value-driven business model requires fair value accounting, and hybrid contracts are classified in their entirety. The remaining fair value option condition in IAS 39 is carried forward to the new standard – that is, management may still designate a financial asset as at FVTPL on initial recognition if this significantly reduces recognition or measurement inconsistency, commonly referred to as ‘an accounting mismatch’. The designation at FVTPL continues to be irrevocable.

**Classification and measurement of financial liabilities**

**How are financial liabilities to be measured?**

Financial liabilities are measured at amortised cost unless they are required to be measured at fair value through profit or loss or an entity has chosen to measure a liability at fair value through profit or loss.

**What determines classification?**

The classification and measurement of financial liabilities under IFRS 9 remains unchanged from the guidance in IAS 39 except where an entity has chosen to measure a liability at fair value through profit or loss. There continue to be two measurement categories for financial liabilities: fair value and amortised cost. Certain liabilities are required to be at fair value through profit or loss, such as liabilities held for trading and derivatives. Other liabilities are measured at amortised cost unless the entity elects the fair value option; however, if the liability contains embedded derivatives, the embedded derivatives might be required to be separated and measured at fair value through profit or loss.

**What is the accounting for financial liabilities that are required to be at fair value through profit and loss?**

Financial liabilities that are required to be measured at fair value through profit or loss (as distinct from those that the entity has chosen to measure at fair value through profit or loss) continue to have all fair value movements recognised in profit or loss, with none of the fair value movement recognised in ‘other comprehensive income’ (OCI). This includes all derivatives (such as foreign currency forwards or interest rate swaps), or an entity’s own liabilities that are ‘held for trading’. Similarly, financial guarantees and loan commitments that entities choose to measure at fair value through profit or loss will have all fair value movements in profit or loss.

**What is the accounting for financial liabilities that an entity chooses to account for at fair value?**

IFRS 9 changes the accounting for financial liabilities that an entity chooses to account for at fair value through profit or loss, using the fair value option. For such liabilities, changes in fair value related to changes in own credit risk are recognised in OCI.

However, if presenting the changes in own credit of a financial liability in OCI would create an accounting mismatch in profit or loss, all fair value movements are recognised in profit or loss.

The accounting mismatch must arise due to an economic relationship between the financial liability and a financial asset that results in the liability’s credit risk being offset by a change in the fair value of the asset.

The accounting mismatch:

- is required to be determined when the liability is first recognised;
- is not reassessed subsequently; and
- must not be caused solely by the measurement method that an entity uses to determine the changes in a liability’s credit risk.
New standards

Use of this exemption from the requirement to present movements in the own credit risk of a liability in OCI is expected to be rare.

**What are the eligibility criteria for the fair value option?**

The eligibility criteria for the fair value option remain the same; they are based on whether:

- • the liability is managed on a fair value basis;
- • electing fair value will eliminate or reduce an accounting mismatch; or
- • the instrument is a hybrid contract (that is, it contains a host contract and an embedded derivative) for which separation of an embedded derivative would be required.

**Have there been any changes in the accounting for embedded derivatives?**

The existing guidance in IAS 39 for embedded derivatives has been retained in this new part of IFRS 9. Entities are still required to separate derivatives embedded in financial liabilities where they are not closely related to the host contract – for example, a structured note where the interest is linked to an equity index. The separated embedded derivative continues to be measured at fair value through profit or loss, and the residual debt host is measured at amortised cost. The accounting for embedded derivatives in non-financial host contracts also remains unchanged.

**Is the treatment of derivatives embedded in financial liabilities symmetrical to the treatment of derivatives embedded in financial assets?**

No. The existing embedded derivative guidance in IAS 39 is retained in IFRS 9 for financial liabilities and non-financial instruments. This results in some embedded derivatives still being separately accounted for at fair value through profit or loss. However, embedded derivatives are no longer separated from financial assets. Instead, they are part of the contractual terms that are considered in determining whether the entire financial asset meets the contractual cash flow test (that is, the instrument has solely payments of principal and interest) to be measured at amortised cost or whether it should be measured at fair value through profit or loss.

**How are financial liabilities at fair value to be measured?**

Entities will need to calculate the amount of the fair value movement that relates to the credit risk of the liability. IFRS 7 already requires disclosure of the amount of fair value changes that are attributable to own credit risk for liabilities designated at fair value through profit or loss. The existing guidance on how to calculate own credit risk in IFRS 7 is retained but has been relocated to IFRS 9, and some aspects have been clarified.

**How can own credit risk be determined?**

This can be determined as either:

- • the amount of fair value change not attributable to changes in market risk (for example, benchmark interest rates) – this is often referred to as the default method; or
- • an alternative method that the entity believes more faithfully represents the changes in fair value due to ‘own credit’ (for example, a method that calculates credit risk based on credit default swap rates).

IFRS 9 clarifies that if the changes in fair value arising from factors other than changes in the liability’s credit risk or changes in observed interest rates (that is, benchmark rates such as LIBOR) are significant, an entity is required to use an alternative method and may not use the default method. For example, changes in the fair value of a liability might arise due to changes in value of a derivative embedded in that liability rather than changes in benchmark interest rates. In that situation, changes in the value of the embedded derivative should be excluded in determining the amount of own credit risk that is presented in OCI.

The expanded guidance in IFRS 9 confirms that the credit risk of a liability with collateral is likely to be different from the credit risk of an equivalent liability without collateral issued by the same entity.

It also clarifies that unit-linking features usually give rise to asset performance risk rather than credit risk – that is, the value of the liability changes due to changes in value of the linked asset(s) and not because of changes in the own credit risk of the liability. This means that changes in the fair value of a unit-linked liability due to changes in the fair value of the linked asset will continue to be recognised in the income statement: they are not regarded as being part of the own credit risk of the liability that is recognised in OCI.

**What is the impact of the changes on the presentation of financial liabilities?**

Elements of the fair value movement of the liability are presented in different parts of the performance statement; changes in own credit risk are presented in OCI, and all other fair value changes are presented in profit or loss. This means that the amount of the overall fair value movement does not change, but it is presented in separate sections of the statement of comprehensive income.

Amounts in OCI relating to own credit are not recycled to the income statement even when the liability is derecognised and the amounts are realised. However, the standard does allow transfers within equity.
Financial instruments hedge accounting
Amendment to IFRS 9

What’s the issue?
This is the third phase of the IASB’s replacement of IAS 39. The new requirements align hedge accounting more closely with risk management, and so should result in more ‘decision-useful’ information to users of financial statements. The revised standard also establishes a more principles-based approach to hedge accounting and addresses inconsistencies and weaknesses in the current model in IAS 39.

What are the key changes?
Hedge effectiveness tests and eligibility for hedge accounting
IFRS 9 relaxes the requirements for hedge effectiveness and, consequently to apply hedge accounting. Under IAS 39, a hedge must be highly effective, both going forward and in the past (that is, a prospective and retrospective test, with results in the range of 80%-125%). IFRS 9 replaces this bright line with a requirement for an economic relationship between the hedged item and hedging instrument, and for the ‘hedged ratio’ to be the same as the one that the entity actually uses for risk management purposes. Hedge ineffectiveness will continue to be reported in profit or loss (P&L). An entity is still required to prepare contemporaneous documentation; however, the information to be documented under IFRS 9 will differ.

Hedged items
The new requirements change what qualifies as a hedged item, primarily removing restrictions that currently prevent some economically rational hedging strategies from qualifying for hedge accounting. For example:

- Risk components of non-financial items can be designated as hedged items, provided they are separately identifiable and reliably measurable. This is good news for entities that hedge for only a component of the overall price of non-financial items (such as the oil price component of jet fuel price exposure), because it is likely that more hedges will now qualify for hedge accounting.
- Aggregated exposures (that is, exposures that include derivatives) can be hedged items.
- IFRS 9 makes the hedging of groups of items more flexible, although it does not cover macro hedging (this will be the subject of a separate discussion paper in the future). Treasurers commonly group similar risk exposures and hedge only the net position (for example, the net of forecast purchases and sales in a foreign currency). Under IAS 39, such a net position cannot be designated as the hedged item; but IFRS 9 permits this if it is consistent with an entity’s risk management strategy. However, if the hedged net position consists of forecast transactions, hedge accounting on a net basis is only available for foreign currency hedges.
- IFRS 9 allows hedge accounting for equity instruments measured at fair value through other comprehensive income (OCI), even though there will be no impact on P&L from these investments.
Hedging instruments

IFRS 9 relaxes the rules on the use of some hedging instruments as follows:

- Under IAS 39, the time value of purchased options is recognised on a fair value basis in P&L, which can create significant volatility. IFRS 9 views a purchased option as similar to an insurance contract, such that the initial time value (that is, the premium generally paid for an at or out of the money option) must be recognised in P&L, either over the period of the hedge (if the hedge item is time related, such as a fair value hedge of inventory for six months), or when the hedged transaction affects P&L (if the hedge item is transaction related, such as a hedge of a forecast purchase transaction). Any changes in the option’s fair value associated with time value will be recognised in OCI.

- A similar accounting treatment to options can also be applied to the forward element of forward contracts and to foreign currency basis spreads of financial instruments. This should result in less volatility in P&L.

- Non-derivative financial items can be used as hedging instruments, provided they are accounted for at fair value through P&L, unless they are hedging foreign currency (FX) risk. Under IAS 39, non-derivative financial items were only allowed for hedges of FX risk.

Own credit risk in financial liabilities

Although not related to hedge accounting, the IASB has also amended IFRS 9 to allow entities to early adopt the requirement to recognise in OCI the changes in fair value attributable to changes in an entity’s own credit risk (from financial liabilities that are designated under the fair value option). This can be applied without having to adopt the remainder of IFRS 9.

Am I affected?

All entities that engage in risk management activities, regardless of whether they currently use hedge accounting, could potentially benefit from the changes to hedge accounting. However, entities should note that the European Union has not yet endorsed any aspect of IFRS 9.

Amendments to IFRS 9 have removed the previous mandatory effective date of 1 January 2015, but the standard is available for immediate application. The standard provides an accounting policy choice for an entity to continue to apply hedge accounting (and hedge accounting only) under IAS 39 instead of IFRS 9 until the IASB completes its separate macro hedging project.

Entities can elect to apply IFRS 9 for any of the following:

- The own credit risk requirements for financial liabilities.
- Classification and measurement (C&M) requirements for financial assets.
- C&M requirements for financial assets and financial liabilities.
- The full current version of IFRS 9 (that is, C&M requirements for financial assets and financial liabilities and hedge accounting).

The transitional provisions described above are likely to change once the IASB completes all phases of IFRS 9.

IFRS 9 applies prospectively; however, hedge accounting is to be applied prospectively (with some exceptions).
Consolidated financial statements

IFRS 10

Effective date
Annual periods beginning on or after 1 January 2013. Early adoption is permitted.

EU adoption status
Adopted for annual periods beginning on or after 1 January 2014.

The IASB has issued IFRS 10, ‘Consolidated financial statements’, as part of the group of five new standards that address the scope of the reporting entity. IFRS 10 replaces all of the guidance on control and consolidation in IAS 27, ‘Consolidated and separate financial statements’, and SIC-12, ‘Consolidation – special purpose entities’. IAS 27 is renamed ‘Separate financial statements’; it continues to be a standard dealing solely with separate financial statements. The existing guidance for separate financial statements is unchanged.

The rest of the package includes IFRS 11, ‘Joint arrangements’; IFRS 12, ‘Disclosure of interests in other entities’; and consequential amendments to IAS 28, ‘Investments in associates’.

What are the key provisions?

IFRS 10 changes the definition of control so that the same criteria are applied to all entities to determine control. This definition is supported by extensive application guidance that addresses the different ways in which a reporting entity (investor) might control another entity (investee). The changed definition and application guidance is not expected to result in widespread change in the consolidation decisions made by IFRS reporting entities, although some entities could see significant changes.

All entities will need to consider the new guidance. The core principle that a consolidated entity presents a parent and its subsidiaries as if they are a single entity remains unchanged, as do the mechanics of consolidation.

IFRS 10 excludes guidance specifically for investment companies, as the IASB continues to work on a project on accounting by investment companies for controlled entities.

The revised definition of control focuses on the need to have both power and variable returns before control is present. Power is the current ability to direct the activities that significantly influence returns. Returns must vary and can be positive, negative or both.

The determination of power is based on current facts and circumstances and is continuously assessed. The fact that control is intended to be temporary does not obviate the requirement to consolidate any investee under the control of the investor. Voting rights or contractual rights may be evidence of power, or a combination of the two may give an investor power. Power does not have to be exercised. An investor with more than half the voting rights would meet the power criteria in the absence of restrictions or other circumstances.

The application guidance includes examples illustrating when an investor may have control with less than half of the voting rights. When assessing if it controls the investee, an investor should consider potential voting rights, economic dependency and the size of its shareholding in comparison to other holdings, together with voting patterns at shareholder meetings. This last consideration will bring the notion of ‘de facto’ control firmly within the consolidation standard.
IFRS 10 also includes guidance on participating and protective rights. Participating rights give an investor the ability to direct the activities of an investee that significantly affect the returns. Protective rights (often known as veto rights) will only give an investor the ability to block certain decisions outside the ordinary course of business.

The new standard includes guidance on agent/principal relationships. An investor (the agent) may be engaged to act on behalf of a single party or a group of parties (the ‘principals’). Certain power is delegated to the agent – for example, to manage investments. The investor may or may not have control over the pooled investment funds. IFRS 10 includes a number of factors to consider when determining whether the investor has control or is acting as an agent.

The revised definition of control and associated guidance replaces not only the definition and guidance in IAS 27 but also the four indicators of control in SIC 12.

**Who is affected?**

IFRS 10 has the potential to affect all reporting entities (investors) that control one or more investees under the revised definition of control. The determination of control and consolidation decisions may not change for many entities. However, the new guidance will need to be understood and considered in the context of each investor’s business.

**What do affected entities need to do?**

Management should consider whether IFRS 10 will affect their control decisions and consolidated financial statements.
The IASB has issued the long awaited IFRS 11, ‘Joint arrangements’, as part of a ‘package’ of five new standards that address the scope of the reporting.

Changes in the definitions have reduced the ‘types’ of joint arrangements to two: joint operations and joint ventures. The existing policy choice of proportionate consolidation for jointly controlled entities has been eliminated. Equity accounting is mandatory for participants in joint ventures. Entities that participate in joint operations will follow accounting much like that for joint assets or joint operations today.

What are the key provisions?

Underlying principles

A joint arrangement is defined as being an arrangement where two or more parties contractually agree to share control. Joint control exists only when the decisions about activities that significantly affect the returns of an arrangement require the unanimous consent of the parties sharing control.

All parties to a joint arrangement should recognise their rights and obligations arising from the arrangement. The focus is no longer on the legal structure of joint arrangements, but rather on how rights and obligations are shared by the parties to the joint arrangement.

The structure and form of the arrangement is only one of the factors to consider in assessing each party’s rights and obligations. The terms and conditions agreed by the parties (for example, agreements that may modify the legal structure or form of the arrangement) and other relevant facts and circumstances should also be considered.

If the facts and circumstances change, a venture needs to reassess:

• whether it has joint control; and/or
• the type of joint arrangement in which it is involved.

Types of joint arrangement and their measurement

IFRS 11 classifies joint arrangements as either joint operations or joint ventures. The ‘Jointly controlled assets’ classification in IAS 31, ‘Interests in joint ventures’, has been merged into joint operations, as both types of arrangements generally result in the same accounting outcome.

A joint operation is a joint arrangement that gives parties to the arrangement direct rights to the assets and obligations for the liabilities. A joint operator will recognise its interest based on its involvement in the joint operation (that is, based on its direct rights and obligations) rather than on the participation interest it has in the joint arrangement.

A joint operator in a joint operation will therefore recognise in its own financial statements:

• its assets, including its share of any assets held jointly;
• its liabilities, including its share of any liabilities incurred jointly;
• its revenue from the sale of its share of the output of the joint operation;
• its share of the revenue from the sale of the output by the joint operation; and
• its expenses, including its share of any expenses incurred jointly.
A joint venture, in contrast, gives the parties rights to the net assets or outcome of the arrangement. A joint venture does not have rights to individual assets or obligations for individual liabilities of the joint venture. Instead, joint venture’s share in the net assets and, in turn, the outcome (profit or loss) of the activity undertaken by the joint venture. Joint ventures are accounted for using the equity method in accordance with IAS 28, ‘Investments in associates’. Entities can no longer account for an interest in a joint venture using the proportionate consolidation method.

The standard also provides guidance for parties that participate in joint arrangements but do not have joint control.

**Who is affected?**

Entities with existing joint arrangements or that plan to enter into new joint arrangements will be affected by the new standard. These entities will need to assess their arrangements to determine whether they have invested in a joint operation or a joint venture upon adoption of the new standard or upon entering into the arrangement.

Entities that have been accounting for their interest in a joint venture using proportionate consolidation will no longer be allowed to use this method; instead they will account for the joint venture using the equity method or account for their share of assets and liabilities if it is assessed as a joint operation. In addition, there may be some entities that previously equity-accounted for investments that may need to account for their share of assets and liabilities now that there is less focus on the structure of the arrangement.

The transition provisions of IFRS 11 require entities to apply the new rules at the beginning of the earliest period presented upon adoption. When transitioning from the proportionate consolidation method to the equity method, entities should recognise their initial investment in the joint venture as the aggregate of the carrying amounts that were previously proportionately consolidated. In transitioning from the equity method to accounting for assets and liabilities, entities should recognise their share of each of the assets and liabilities in the joint operation, with specific rules detailing how to account for any difference from the previous carrying amount of the investment.

**What do affected entities need to do?**

Management of entities that are party to joint arrangements should evaluate how the requirements of the new standard will affect the way they account for their existing or new joint arrangements. The accounting may have a significant impact on entities’ financial results and financial position, which should be clearly communicated to stakeholders as soon as possible.

Management should also carefully consider the planned timing of their adoption. If they wish to retain the current accounting for existing arrangements, now is the time to consider how the terms of these arrangements can be reworked or restructured to achieve this.
Disclosure of interests in other entities

IFRS 12

Effective date
Annual periods beginning on or after 1 January 2013. Early adoption is permitted.

EU adoption status
Adopted for accounting periods on or after 1 January 2014.

The IASB has issued IFRS 12, ‘Disclosure of interests in other entities’, as part of the group of five new standards that address the scope of the reporting entity.

IFRS 12 sets out the required disclosures for entities reporting under the two new standards, IFRS 10, ‘Consolidated financial statements’, and IFRS 11, ‘Joint arrangements’; it replaces the disclosure requirements currently found in IAS 28, ‘Investments in associates’. IAS 27 is renamed ‘Separate financial statements’ and now deals solely with separate financial statements. The existing guidance and disclosure requirements for separate financial statements are unchanged.

What are the key provisions?
IFRS 12 requires entities to disclose information that helps financial statement readers to evaluate the nature, risks and financial effects associated with the entity’s interests in subsidiaries, associates, joint arrangements and unconsolidated structured entities.

To meet this objective, disclosures are required in the following areas.

Significant judgements and assumptions
Significant judgements and assumptions made in determining whether the entity controls, jointly controls, significantly influences or has some other interests in other entities include:

• an assessment of principal-agent relationships in consolidation;
• determination of the type of joint arrangement; and
• any override of presumptions of significant influence and control when voting rights range from 20% to 50%, and exceed 50%, respectively.

Interests in subsidiaries
This includes information about:

• group composition;
• interests of non-controlling interests (NCI) in group activities and cash flows, and information about each subsidiary that has material NCI, such as name, principal place of business and summarised financial information;
• significant restrictions on access to assets and obligations to settle liabilities;
• risks associated with consolidated structured entities, such as arrangements that could require the group to provide financial support;
• accounting for changes in the ownership interest in a subsidiary without a loss of control? a schedule of the impact on parent equity is required;
• accounting for the loss of control – detail of any gain/loss recognised and the line item in the statement of comprehensive income in which it is recognised; and
• subsidiaries that are consolidated using different year ends.
**Interests in joint arrangements and associates**

Detailed disclosures include:
- the name, country of incorporation and principal place of business;
- proportion of ownership interest and measurement method;
- summarised financial information;
- fair value (if published quotations are available);
- significant restrictions on the ability to transfer funds or repay loans;
- year-ends of joint arrangements or associates if different from the parent’s; and
- unrecognised share of losses, commitments and contingent liabilities.

**Interests in unconsolidated structured entities**

Detailed disclosures include:
- the nature, purpose, size, activities and financing of the structured entity;
- the policy for determining structured entities that are sponsored;
- a summary of income from structured entities;
- the carrying amount of assets transferred to structured entities;
- the recognised assets;
- liabilities relating to structured entities and line items in which they are recognised;
- the maximum loss arising from such involvement; and
- information on financial or other support provided to such entities, or current intentions to provide such support.

**Who is affected?**

All entities that have interests in subsidiaries, associates, joint ventures or unconsolidated structured entities are likely to face increased disclosure requirements.

**What do affected entities need to do?**

Management should consider whether it needs to implement additional processes to be able to compile the required information.
Transition guidance for IFRSs 10, 11 and 12

Amendments to IFRS 10, 11 and 12

**What’s the issue?**

This amendment clarifies that the date of initial application is the first day of the annual period in which IFRS 10 is adopted — for example, 1 January 2013 for a calendar-year entity that adopts IFRS 10 in 2013. Entities adopting IFRS 10 should assess control at the date of initial application; the treatment of comparative figures depends on this assessment.

The amendment also requires certain comparative disclosures under IFRS 12 upon transition.

The key changes in the amendment are:

- If the consolidation conclusion under IFRS 10 differs from IAS 27/SIC 12 as at the date of initial application, the immediately preceding comparative period (that is, 2012 for a calendar-year entity that adopts IFRS 10 in 2013) is restated to be consistent with the accounting conclusion under IFRS 10, unless impracticable;
- Any difference between IFRS 10 carrying amounts and previous carrying amounts at the beginning of the immediately preceding annual period is adjusted to equity;
- Adjustments to previous accounting are not required for investees that will be consolidated under both IFRS 10 and the previous guidance in IAS 27/SIC 12 as at the date of initial application, or investees that will be unconsolidated under both sets of guidance as at the date of initial application; and
- Comparative disclosures will be required for IFRS 12 disclosures in relation to subsidiaries, associates, and joint arrangements. However, this is limited only to the period that immediately precedes the first annual period of IFRS 12 application. Comparative disclosures are not required for interests in unconsolidated structured entities.

The amendment is effective for annual periods beginning on or after 1 January 2013, consistent with IFRS 10, 11 and 12.

**Am I affected?**

The amendment will affect all reporting entities (investors) who need to adopt IFRSs 10, 11 or 12.

**What do I need to do?**

IFRS preparers should start considering the transition amendment, and how they can use the exemptions granted to minimise implementation costs of IFRSs 10, 11 and 12.

IFRS preparers should also start collating the comparative disclosure information required by the amendment.

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**Effective date**

IFRS 10, 11 and 12: annual periods beginning on or after 1 January 2013, retrospectively applied. Early adoption is permitted.

**EU adoption status**

Adopted for annual periods beginning on or after 1 January 2014.
Exception from consolidation for ‘investment entities’

Amendments to IFRS 10, IFRS 12 and IAS 27

**What’s the issue?**

This amendment applies to an ‘investment entity’. The amendment to IFRS 10 defines an investment entity and introduces an exception from consolidation. The amendments to IFRS 12 also introduce disclosures that an investment entity needs to make.

The amendments apply for annual periods beginning on or after 1 January 2014; earlier application is permitted.

**Definition of an investment entity**

You will need to make an assessment of whether your business meets the investment entity definition.

An investment entity is an entity that:

- obtains funds from one or more investors for the purpose of providing those investor(s) with investment management services;
- commits to its investor(s) that its business purpose is to invest funds solely for returns from capital appreciation, investment income or both; and
- measures and evaluates the performance of substantially all of its investments on a fair value basis.

You will also need to consider a set of typical characteristics. These, combined with the definition, are intended to allow for an appropriate balance between creating a clear scope and allowing judgement in assessing whether you are an investment entity.

The characteristics are:
- holding more than one investment, having more than one investor, having investors that are not related parties of the entity, and having ownership interests in the form of equity or similar interests.
- The absence of one or more of these characteristics does not prevent the entity from qualifying as an investment entity.

You will not be disqualified from being an investment entity where you carry out any of the following activities:

- provision of investment-related services to third parties and to your investors, even when substantial; and
- providing management services and financial support to your investees, but only when these do not represent separate substantial business activity and are carried out with the objective of maximising the investment return from your investees.

**Exception from consolidation and measurement of investees**

You are required to account for your subsidiaries at fair value through profit or loss in accordance with IFRS 9, ‘Financial instruments’ (or IAS 39, ‘Financial instruments: Recognition and measurement’, where applicable), where you qualify as an investment entity. The only exception is for subsidiaries that provide services to you that are related to your investment activities, which are consolidated.

**Accounting by a non-investment entity parent for the controlled investments of an investment entity subsidiary**

You may be an investment entity but your parent is not. For example, your investment entity fund is controlled by an insurance company. Your non-investment entity parent is required to consolidate all entities it controls including those controlled...
through an investment entity. The insurance group will have to consolidate the subsidiaries of your fund in the insurance group’s financial statements, even though in your fund’s own financial statements you will fair value your subsidiaries. Therefore, what is known as the fair value ‘roll-up’ is not permitted to a non-investment parent entity.

**Disclosure**

Required disclosures, where you qualify as an investment entity, include the following:

- significant judgements and assumptions made in determining that you have met the definition of an investment entity;
- reasons for concluding that you are an investment entity even though you don’t have one or more of the typical characteristics;
- information on each unconsolidated subsidiary (name, country of incorporation, proportion of ownership interest held);
- restrictions on unconsolidated subsidiaries transferring funds to the investment entity;
- financial or other support provided to unconsolidated subsidiaries during the year, where there wasn’t any contractual obligation to do so; and
- information about any ‘structured entities’ you control (for example, any contractual arrangements to provide any financial or other support).

**Am I affected?**

You will be affected if you are a fund or a similar entity. Some may qualify as investment entities, and some may not.

**What do I need to do?**

You should look closely at the guidance to determine whether or not you are an investment entity. If you are, for example, a property fund that actively develops properties, you are unlikely to qualify, as your objective is not solely capital appreciation or investment income. On the other hand, if you are a limited life fund set up to buy and sell or list a range of infrastructure subsidiaries, you might qualify as an investment entity.

You should start collating comparative information where you qualify as an investment entity, as the change in accounting has to be applied retrospectively in most cases.
Regulatory deferral accounts

IFRS 14

Effective date
Annual periods beginning on or after 1 January 2016. Early adoption is permitted.

EU adoption status
Not adopted at the time of going to print.

The IASB has issued IFRS 14, ‘Regulatory deferral accounts’ (‘IFRS 14’), an interim standard on the accounting for certain balances that arise from rate–regulated activities (‘regulatory deferral accounts’).

IFRS 14 is only applicable to entities that apply IFRS 1 as first-time adopters of IFRS. It permits such entities, on adoption of IFRS, to continue to apply their previous GAAP accounting policies for the recognition, measurement, impairment and de-recognition of regulatory deferral accounts. The interim standard also provides guidance on selecting and changing accounting policies (on first–time adoption or subsequently) and on presentation and disclosure.

There is currently no standard that specifically addresses rate–regulated activities. The objective of the interim standard is to allow entities adopting IFRS to avoid major changes in accounting policy before completion of the broader IASB project to develop an IFRS on rate–regulated activities. A discussion paper on the project is expected later in 2014.

What are the key provisions?

Scope
IFRS 14 only applies to first-time adopters of IFRS that apply IFRS 1 and conduct rate–regulated activities. Rate regulation is a framework where the price that an entity charges to its customers for goods and services is subject to oversight and/or approval by an authorised body. IFRS 14 excludes entities that are self–regulated (for example, if prices are regulated solely by the entity’s own governing body).

Entities in the scope of IFRS 14 are permitted to continue applying previous GAAP accounting policies for regulatory deferral accounts. Changes to existing policies are restricted. Any change must make the financial statements more relevant and no less reliable, as described by IAS 8.

Entities are not permitted to change accounting policies to start recognising regulatory deferral account balances that were not recognised under previous GAAP. Entities can, however, recognise new balances that arise as a result of a change in accounting policy (such as on the first–time adoption of IFRS or for changes to IFRS). For example, if a new deferral account arises from the adoption of new IFRS employee benefits guidance, the new account is accounted for consistently with the entity’s previous GAAP accounting policies.

Recognition, measurement, impairment and de-recognition
An entity is permitted to continue applying its previous GAAP accounting policies for the recognition and measurement of regulatory deferral accounts on first–time adoption. The interim standard does not include any further guidance on recognition, measurement, impairment and de-recognition.

Previous GAAP accounting policies are only applied to balances that are not otherwise covered by specific IFRSs. That is, other specific IFRSs should be applied first, and only any residual balance is accounted for under IFRS 14.

Other standards might also need to be applied to regulatory deferral accounts to reflect them appropriately in the financial statements. For example, the entity would apply its previous GAAP accounting policy to the impairment of regulatory deferral account balances, but it would apply the IFRS impairment guidance to cash generating units that contain such balances.
Judgement will be required to determine what other standards might be applicable and how they might interact with previous GAAP accounting policies.

**Presentation**

Balances arising from the application of IFRS 14 are presented separately in the balance sheet and the statement of comprehensive income.

A separate line item is presented in the balance sheet for total regulatory deferral debit balances and total regulatory deferral credit balances, following a sub-total of all other assets and liabilities. The distinction between current and non-current balances is not presented on the balance sheet, and offsetting is not permitted, although this information might be disclosed elsewhere.

The total movement in all regulatory deferral accounts is split between other comprehensive income (OCI) and profit and loss. The amount recorded in profit and loss is separately presented as a single line item after a sub-total for profit and loss. The amount recorded in OCI is presented in two line items, based on whether the amount relates to items that will or will not be subsequently reclassified to profit and loss. Movements are classified in OCI where the balances relate to items recognised in OCI. An entity that presents earnings per share (EPS) should present, in the income statement, EPS excluding and including the movement in the regulatory deferral accounts.

**Disclosures**

The disclosure requirements address information about the nature and risk of the regulation and the effect on the financial statements, including:

- a description of the nature and extent of rate regulation;
- how the future recovery or reversal of each balance is affected by risks and uncertainties;
- the basis on which the regulatory deferral account balances are recognised and measured; and
- a reconciliation of the balances from the beginning to the end of the period.

**Am I affected?**

IFRS 14 will affect first-time adopters of IFRS that currently recognise balances arising from rate regulation under previous GAAP accounting policies. This is common in the utilities industry, but the interim standard might affect other industries where prices are regulated.

**What is next?**

IFRS 14 is effective from 1 January 2016. Early adoption is permitted. Application is not compulsory, but entities that will apply the guidance should begin to consider the implications in connection with the adoption of IFRS.

The broader project on rate-regulated activities is ongoing. The IASB is expected to issue a discussion paper on the project later in 2014 to seek initial views on the accounting for rate-regulated activities.
IFRIC 21, ‘Levies’, sets out the accounting for an obligation to pay a levy that is not income tax. The interpretation could result in recognition of a liability later than today, particularly in connection with levies that are triggered by circumstances on a specific date.

**What is the issue?**

**Scope and objective**

Levies are imposed by governments in accordance with legislation and are often measured by reference to an entity’s revenues, assets or liabilities (for example, 1% of revenue).

The interpretation addresses diversity in practice around when the liability to pay a levy is recognised. Practice differs particularly when a levy is measured based on financial data relating to a period before the date on which the obligation to pay the levy arises.

IFRIC 21 addresses the accounting for a liability to pay a levy recognised in accordance with IAS 37, ‘Provisions’, and the liability to pay a levy whose timing and amount is certain. It excludes income taxes within the scope of IAS 12, ‘Income taxes’. Its application to liabilities arising from emissions trading schemes is optional.

The interpretation does not address whether the liability to pay a levy gives rise to an asset or an expense. Entities will need to apply other standards to determine the accounting for the expense.

**Key provisions**

IFRIC 21 addresses the following issues:

**What is the obligating event that gives rise to a liability to pay a levy?**

The obligating event that gives rise to a liability to pay a levy is the event identified by the legislation that triggers the obligation to pay the levy.

The fact that an entity is economically compelled to continue operating in a future period, or prepares its financial statements under the going concern principle, does not create an obligation to pay a levy that will arise from operating in the future.

**When is a liability to pay a levy recognised?**

A liability to pay a levy is recognised when the obligating event occurs. This might arise at a point in time or progressively over time.

The interpretation also requires that an obligation to pay a levy triggered by a minimum threshold is recognised when the threshold is reached.
**Example 1**

**Levy A** – 1% of current year revenues is due if the entity is operating on 1 January.

A liability equal to 1% of the current year revenues is recognised progressively as revenue is generated.

**Levy B** – 1% of prior year revenues is due if the entity is operating on 1 January.

A liability equal to 1% of the prior year revenues is recognised in full on 1 January.

**Levy C** – 1% of current year revenues is due if the entity is operating on 31 December.

A liability equal to 1% of the current year revenues is recognised in full on 31 December.

**Example 2**

**Levy D** – 1% of current year revenues is due if the entity is operating on 1 January (same as Levy A) and if current year revenue exceeds CU20m.

A liability equal to 1% of CU20m is recognised in full when the threshold is reached. The liability is then increased progressively as revenue over CU20m is generated.

**Is the accounting at an interim reporting date the same as at year end?**

The same recognition principles apply in interim and annual financial statements. The obligation should not be anticipated or deferred in the interim financial report if it would not be anticipated or deferred in annual financial statements.

The interpretation provides examples that illustrate the accounting for the liability to pay a levy.

**Am I affected?**

IFRIC 21 will affect entities that are subject to levies that are not income taxes within the scope of IAS 12. These are common in many countries and in many industries – banking, retail and transportation, to name a few.
The table below identifies the more significant changes to the standards arising from the 2010 to 2012 annual improvements project and the implications for management.

<table>
<thead>
<tr>
<th>Standard/Interpretation</th>
<th>Amendment</th>
<th>Effective date</th>
</tr>
</thead>
<tbody>
<tr>
<td>Amendment to IFRS 2, ‘Share based payment’</td>
<td>The amendment clarifies the definition of a ‘vesting condition’ and separately defines ‘performance condition’ and ‘service condition’. For share-based payment transactions for which the grant date is on or after 1 July 2014.</td>
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<tr>
<td>IFRS 3, ‘Business combinations’</td>
<td>The standard is amended to clarify that an obligation to pay contingent consideration which meets the definition of a financial instrument is classified as a financial liability or as equity, on the basis of the definitions in IAS 32, ‘Financial instruments: Presentation’. The standard is further amended to clarify that all non-equity contingent consideration, both financial and non-financial, is measured at fair value at each reporting date, with changes in fair value recognised in profit and loss. Consequential changes are also made to IFRS 9, IAS 37 and IAS 39. For business combinations where the acquisition date is on or after 1 July 2014.</td>
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<tr>
<td>IFRS 8, ‘Operating segments’</td>
<td>The standard is amended to require disclosure of the judgements made by management in aggregating operating segments. This includes a description of the segments which have been aggregated and the economic indicators which have been assessed in determining that the aggregated segments share similar economic characteristics. The standard is further amended to require a reconciliation of segment assets to the entity’s assets when segment assets are reported. Annual period beginning on or after 1 July 2014.</td>
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<td>Standard/Interpretation</td>
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<td>IFRS 13, ‘Fair value measurement’</td>
<td>When IFRS 13 was published, paragraphs B5.4.12 of IFRS 9 and AG79 of IAS 39 were deleted as consequential amendments. This led to a concern that entities no longer had the ability to measure short-term receivables and payables at invoice amounts where the impact of not discounting is immaterial. The IASB has amended the basis for conclusions of IFRS 13 to clarify that it did not intend to remove the ability to measure short-term receivables and payables at invoice amounts in such cases.</td>
<td>Amendment to the basis for conclusions only.</td>
</tr>
</tbody>
</table>
| IAS 16, ‘Property, plant and equipment’, and IAS 38, ‘Intangible assets’ | Both standards are amended to clarify how the gross carrying amount and the accumulated depreciation are treated where an entity uses the revaluation model.  

The carrying amount of the asset is restated to the revalued amount.  

The split between gross carrying amount and accumulated depreciation is treated in one of the following ways:  

- either the gross carrying amount is restated in a manner consistent with the revaluation of the carrying amount, and the accumulated depreciation is adjusted to equal the difference between the gross carrying amount and the carrying amount after taking into account accumulated impairment losses; or  

- the accumulated depreciation is eliminated against the gross carrying amount of the asset. | Annual periods beginning on or after 1 July 2014. |
| IAS 24, ‘Related party disclosures’ | The standard is amended to include, as a related party, an entity that provides key management personnel services to the reporting entity or to the parent of the reporting entity (‘the management entity’).  

The reporting entity is not required to disclose the compensation paid by the management entity to the management entity’s employees or directors, but it is required to disclose the amounts charged to the reporting entity by the management entity for services provided. | Annual periods beginning on or after 1 July 2014. |
The table below identifies the more significant changes to the standards arising from the 2011 to 2013 annual improvements project and the implications for management.

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<td>IFRS 1, ‘First-time adoption of International Financial Reporting Standards’</td>
<td>The basis for conclusions on IFRS 1 is amended to clarify that, where a new version of a standard is not yet mandatory but is available for early adoption; a first-time adopter can use either the old or the new version, provided the same standard is applied in all periods presented.</td>
<td>Amendment to basis of conclusion only.</td>
</tr>
<tr>
<td>IFRS 3, ‘Business combinations’</td>
<td>The standard is amended to clarify that IFRS 3 does not apply to the accounting for the formation of any joint arrangement under IFRS 11. The amendment also clarifies that the scope exemption only applies in the financial statements of the joint arrangement itself.</td>
<td>Annual periods beginning on or after 1 July 2014.</td>
</tr>
<tr>
<td>IFRS 13, ‘Fair value measurement’</td>
<td>The amendment clarifies that the portfolio exception in IFRS 13, which allows an entity to measure the fair value of a group of financial assets and financial liabilities on a net basis, applies to all contracts (including non-financial contracts) within the scope of IAS 39 or IFRS 9.</td>
<td>Annual periods beginning on or after 1 July 2014. An entity shall apply the amendment prospectively from the beginning of the first annual period in which IFRS 13 is applied.</td>
</tr>
<tr>
<td>IAS 40, ‘Investment property’</td>
<td>The standard is amended to clarify that IAS 40 and IFRS 3 are not mutually exclusive. The guidance in IAS 40 assists preparers to distinguish between investment property and owner-occupied property. Preparers also need to refer to the guidance in IFRS 3 to determine whether the acquisition of an investment property is a business combination.</td>
<td>Annual periods beginning on or after 1 July 2014, but can be applied to individual acquisitions of investment property before that date if, and only if, the information necessary to apply the amendment is available.</td>
</tr>
</tbody>
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IFRS for SMEs publications

- IFRS for SMEs – pocket guide
  Summary of the recognition and measurement requirements in the ‘IFRS for small and medium-sized entities’ published by the International Accounting Standards Board in July 2009.

- Similarities and differences – a comparison of ‘full IFRS’ and IFRS for SMEs
  60-page publication comparing the requirements of the IFRS for small and medium-sized entities with ‘full IFRS’ issued up to July 2009. An executive summary outlines some key differences that have implications beyond the entity’s reporting function.

- IFRS for SMEs – Illustrative consolidated financial statements
  Realistic set of financial statements prepared under IFRS for small and medium-sized entities, illustrating the required disclosure and presentation based on the requirements of the IFRS for SMEs published in July 2009.

Corporate reporting surveys and issues

- Assurance today and tomorrow
  Views of investment professionals on how well audit currently serves their needs and how it might evolve in the future.

- Corporate reporting: is it what investment professionals expect?
  Survey looking at the information that companies provide, and whether investors and analysts have the information they need to assess corporate performance.

- IFRS: The European investors’ view
  Impact of IFRS reporting on fund managers’ perceptions of value and their investment decisions.

- Measuring assets and liabilities
  Survey of investment professionals, looking at their use of the balance sheet in analysing performance and the measurement bases for assets and liabilities that best suit their needs.

- Performance statement: coming together to shape the future
  Survey of what investment professionals and corporate management require to assess performance.

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  Survey of investors’ and analysts’ perspectives on accounting for and reporting of financial instruments. See the full list at pwc.com/corporate reporting.

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  Survey of oil and gas investors and analysts on reporting and assurance issues.

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