AAT Webinar

- Hello and welcome to this IFRS Update CPD webinar
- We are due to start at 19:00. You should not have any sound at this stage. We will be doing a sound check at 18:55
- Please check your sound is working by selecting ‘Meeting’ in the top left corner and ‘Audio setup wizard’
- If you have any questions during the webinar please use the Q&A panel on the right hand side and direct your questions to ‘all panellists‘.

IFRS Update

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IFRS Update Overview

- IFRS 15 *Revenue from Contracts with Customers*
- Accounting policies
- Leasing
- Recognition of deferred tax assets

IFRS 15 *Revenue from Contracts with Customers*

- IFRS 15 was issued in May 2014
- Will replace:
  - IAS 11 *Construction Contracts*
  - IAS 18 *Revenue*
  - IFRIC 13 *Customer Loyalty Programmes*
  - IFRIC 15 *Agreements for the Construction of Real Estate*
  - IFRIC 18 *Transfers of Assets from Customers*
  - SIC-31 *Revenue – Barter Transactions Involving Advertising Services*

IFRS 15 *Revenue from Contracts with Customers*

- Mandatory application date for accounting periods starting on or after 1 January 2017 (earlier adoption permissible)
- Already problems emerging with the standard which may result in the implementation date being revised
- Joint project with the IASB/FASB
- Is ‘principles based’ but is more stringent than previous revenue standards and interpretations

IFRS 15 *Revenue from Contracts with Customers*

- Includes a five-step model to revenue recognition:
  1. Identify the contract(s) with a customer
  2. Identify the performance obligations in the contract
  3. Determine the transaction price
  4. Allocate the transaction price to the performance obligations in the contract
  5. Recognise revenue when (or as) the entity satisfies a performance obligation
- Application of the model is dependent on the facts/circumstances and will need professional judgement

IFRS 15 *Revenue from Contracts with Customers*

- Revenue is recognised when **control** passes which can be at a point in time or over time
- Control is defined as:

  The ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset.

- Benefits can include (among others):
  - Using the asset to produce goods/render services
  - Using the asset to enhance the value of other assets
  - Using the asset to settle liabilities or to reduce expenses
  - Selling or exchanging the asset
  - Pledging the asset to secure a loan
  - Holding the asset

IFRS 15 *Revenue from Contracts with Customers*

- Implementation issues have arisen which may result in a delay to the ‘effective from’ date
- Issues relate to entities having problems with:
  - Licence of intellectual property
  - Performance obligations
- Both IASB/FASB acknowledge a change to the standard is needed but support different Articulations
- FASB has decided to make two additional amendments to highlight additional considerations for licences and to clarify contractual restrictions but IASB is not proposing to change the standard in these areas.

Accounting policies

- Stakeholders are calling for clarity and conciseness in accounting policy disclosures
- Focus was on accounting policies, the format of financial statements and the linkage between financial results and management commentary
- 3 action points came out of the survey of 85 investment professionals:
    - Action 1: combine policies with notes
    - Action 2: be clear about changes to policies
    - Action 3: be specific

Leasing

- Extremely controversial issue!
- A new leasing standard is due to be published in the second half of 2015
- Attempts by IASB to reduce ‘off balance sheet finance’
- Joint project with the IASB and FASB
- All leases create assets and liabilities (even operating leases)

Leasing

- Problem is most leases are not reported on the balance sheet
- Existing methods of accounting for leases allegedly makes comparisons between entities difficult
- Proposals bring about a **substantial** change in how leases will be accounted for
- Tentative decision made to report all leases on balance sheet with some exceptions
- Risks and rewards approach essentially eradicated in the new model
- New model based on the fact that at the start of a lease, the lessee obtains a right to use the asset for a period of time, and the lessor has provided that right

Leasing

- Only leases for 12 months or less are not required on the balance sheet
- Lease assets and liabilities will be measured at the present value of future lease payments
- Lease assets will also include any costs directly related to entering into the lease
- Variable payments and most optional payments excluded from the measurement as a means of simplification
- In the statement of cash flows:
  - Cash payments for principal amounts = financing activity
  - Cash payments for the interest amounts = requirements relating to other interest paid

Leasing

- Impact of the new leasing standard must be considered as a matter of urgency
- As most operating leases will appear on balance sheet, assets and liabilities will increase affecting gearing, asset turnover, interest cover, EBIT, EBITDA or operating profit
- Leasing standard will have to be applied retrospectively and so impact is not limited to leases entered into in the future
- Keep an eye on developments in this area during this year as the standard is going to be issued in 2015

Deferred tax assets

- IAS 12 *Income Taxes* recognises a deferred tax asset (DTA) for:
  - Deductible temporary differences
  - Unused tax losses
  - Unused tax credits
- Exception is where the DRA arises from initial recognition of an asset/liability which does not affect accounting/taxable profit (other than in a business combination)
- IAS 12 determines a DTA on the basis of its nominal amount rather than fair value
- Stakeholders are concerned about DTA's as a long period of time can elapse before net operating losses are recovered

Deferred tax assets

- Assessing a DTA is heavily dependent on judgement especially where losses have been occurring for many years as greater subjectivity will be involved in assessing when profits are yielded
- For this reason, IAS 12 takes a ‘glass half empty’ approach
- DTA’s can only be recognised when there is convincing evidence of sufficient future taxable profit
- Assessing when suitable taxable profit can be done by way of reviewing forecasts
- Should form part of any impairment testing of DTA’s

Deferred tax assets

- Carrying value of DTA's should be reviewed at the end of each reporting period
- Where it is no longer probable that sufficient taxable profit will be available, the DTA is reduced accordingly
- Diversity in practice has been identified by the IFRS Interpretations Committee regarding debt instruments measured at fair value
- ED issued by the Interpretations Committee in August 2014
- In essence, an unrealised loss on a debt instrument does not fit the definition of a deductible temporary difference where such losses are not allowable for tax purposes

Deferred tax assets

- Unrealised losses on debt instruments at fair value and measured at cost for tax give rise to a deductible temporary difference
- IASB is also expected to clarify the extent to which an estimate of ‘future taxable profit’ includes amounts from recovering assets for more than carrying value
- Unlikely to affect entities where such assets are impaired
- May affect assets carried at depreciated cost where the entity is profitable
- What are ‘future taxable profits’?

Deferred tax assets

- Proposal to say that 'future taxable profits' are profits before the reversal of deductible temporary differences
- Deductible temporary differences should also be recognised on a combined basis
- Tax legislation might restrict the sources of taxable profit against which a deductible temporary difference can be used
- Where restrictions do exist, the entity must assess deductible temporary differences in combination with other deductible temporary differences of the appropriate type

Webinar close

- Thank you for attending
- Questions asked will be answered and posted up in the CPD Interactive Zone of the AAT website.