



**White Paper**  
**The implications of the**  
**International Financial**  
**Reporting Standards**  
**(IFRS) on Finance**  
**Systems**

The requirements for the implementation of the  
International Financial Reporting Standards (IFRS)  
based on individual International Accounting Standards (IAS)  
in Business & Accounting Systems

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This specification is designed for business applications used for normal commercial purposes. If the software application is to be used for banking, insurance, finance or foreign currency dealing purposes, the requirements are outside the scope of this specification.

## **Acknowledgements**

BASDA formed an IFRS working party to specify the business application requirements for the introduction of IFRS, which will be required throughout the European Union for the consolidated financial statements of listed companies as of 2005.

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Note: These summaries cover International Financial Reporting Standards, International Accounting Standards, and Interpretations issued on or before 31 March 2004.

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## **Foreword from BASDA**

BASDA is the representative body for 250 of the largest software developers in the world. We have set out in this White Paper to provide the definitive reference for the implementation of the International Financial Reporting Standard (IFRS) in business systems. The International Accounting Standards Board (IASB) has issued a wide range of International Accounting Standards (IAS) over the past years that, along with recent improvements and additions, collectively make up the body of requirements for IFRS. In this White Paper we look at each individual standard and draw attention to any requirements relating to accounting software that will be required to satisfactorily meet the accounting and disclosure requirements stipulated.

We would like to thank our sponsors for their involvement in the development of this White Paper, IASB for its summaries and Deloitte, who provided us with the text from its 'IFRS in your pocket' publication as a reference point for the first edition of our White Paper. We would also like to thank Infocert, of France, who has permitted us to refer to its Accreditation Standard for Finance Systems.

We realise that there will be continuous changes to the International Accounting Standards especially as the intention is for the US FASB standards and IFRS to Converge. This is the second edition of our White Paper, and we expect to regularly provide updates to this document as the international accounting standards evolve.

This is version 2 of our White Paper, which contains the summaries of the International Accounting Standards Boards recommendations as at April 2004. We are also looking into an Accreditation Standard for the IFRS requirements for Business Software associated with the recommendations set out in this White Paper.

**Dennis Keeling,**  
**CEO, BASDA**

## **WHY IFRS? WHY NOW?**

"Developments over the past year and more have strongly reinforced the logic of achieving and implementing high-quality international accounting standards. In an age when capital flows freely across borders, it simply makes sense to account for economic transactions, whether they occur in the Americas, Asia, or Europe, in the same manner. Providing improved transparency and comparability will certainly help ensure that capital is allocated efficiently. Not so incidentally, generally accepted international standards will reduce the cost of compliance with multiple national standards.

"I do not think it reasonable today, if it ever was, to take the position that U.S. GAAP should, de facto, be the standards for the entire world. Rather, the International Accounting Standards Board, whose oversight Trustees I chair, is now working closely with national standard setters throughout the world to develop common solutions to the accounting challenges of the day. The aim is to find a consensus on clearly defined principles, and I am delighted that the American authorities appear sympathetic to that objective."

**Hon. Paul A. Volcker**

**Chairman, IASC Foundation Trustees**

**Speaking on "Accounting, Accountants, and Accountability in an Integrated World Economy" at the World Congress of Accountants, Hong Kong, 9 November 2002**

## **Adoption of IFRS in Europe**

### ***Accounting Regulation Adopted in Europe***

To implement a “financial reporting strategy” adopted by the European Commission in June 2000, the Parliament and Council of the European Union have approved an Accounting Regulation requiring all EU listed companies to follow IASB standards in their consolidated financial statements starting no later than 2005. Member States may extend the IFRS requirement to non-listed companies and parent company statements. Member States may exempt certain companies temporarily from the IFRS requirement – but only until 2007 – in two limited cases: (1) companies that are listed both in the EU and on a non-EU exchange and that currently use US GAAP as their primary accounting standards and (2) companies that have only publicly traded debt securities. The IFRS requirement applies not only in the 15 EU countries but also in the 3 European Economic Area countries and 10 additional countries approved for EU membership starting May 2004. Many large companies in Switzerland (not an EU or EEA member) already use IFRS.

### ***EFrag Recommends EC Endorsement of All Existing IFRS***

In response to a request from the European Commission, the private-sector European Financial Reporting Advisory Group (EFRAG) reviewed IAS 1-41 and related SICs and, in June 2002, concluded that (a) they are not contrary to the 4th and 7th Directives and (b) they meet the required criteria of understandability, relevance, reliability, and comparability. Accordingly, EFRAG recommended EU endorsement of the current standards ‘en bloc’.

Remaining steps before the IFRS regulation is effective are (a) translation of IFRS into the various EU languages and (b) endorsement of IFRS by a European Commission Accounting Regulatory Committee.

### ***Enforcement***

In March 2003, the Committee of European Securities Regulators published its Standard No. 1, Enforcement of Standards on Financial Information in Europe, aimed at developing and implementing a common approach to the enforcement of IFRS throughout the EU. The document sets out 21 high level principles that define enforcement and describe principles that EU member states should adopt in enforcing IFRS, including the structure of their enforcement authority; selection of financial information to be reviewed for enforcement purposes; actions available to enforcers (including, in particular, asking for public correction); cross-border coordination; and reporting by enforcement agencies.

### ***Use of IFRS in the United States***

A foreign company registered with the Securities and Exchange Commission may submit IFRS or local GAAP financial statements, but a reconciliation of earnings and net assets to US GAAP figures is required. In effect, this forces companies to “keep two sets of books”. In February 2000, the SEC issued a Concept Release, *International Accounting Standards*, inviting views on whether and how IFRS might be permitted for foreign registrants, and possibly domestic registrants as well. The matter continues to be under study by the SEC.

The movement to IFRS around the world will have a significant impact on the SEC, especially in relation to the requirements in the Sarbanes-Oxley Act for a review of all registrant filings at least once every three years. Roughly 1,400 foreign companies are listed with the SEC, from about 59 different countries. Approximately 40% are from Europe. Therefore, by 2005 there will be an additional 500 to 600 registrants filing IFRS statements with the SEC. Currently, only about 50 foreign companies file IFRS financial statements and reconcile to US GAAP.

In October 2002, IASB and FASB jointly issued a memorandum of understanding, formalising their commitment to the convergence of US and international accounting standards. The two boards presented the agreement to the chairs of leading national standard setters at a two-day meeting in London. The boards agreed, as a matter of high priority, to:

- undertake a short-term project aimed at removing a variety of individual differences between US GAAP and IFRS;

- remove other differences by undertaking new joint projects that both boards would address concurrently;
- continue progress on the joint projects that they are currently undertaking; and
- encourage their respective interpretative bodies (EITF and IFRIC) to coordinate their activities.

Shortly thereafter, both the FASB and the IASB added to their agendas a number of projects relating to the above agreement, including a short-term international convergence project with a target completion date of 31 December 2003 as well as several joint standards projects. The joint projects include application of the purchase method of accounting for business combinations and revenue recognition concepts.

### ***Use of IFRS in Canada***

There is no current plan to allow domestic companies to use IFRS in place of Canadian GAAP. The securities regulators are considering whether to allow foreign issuers to use IFRS or a number of foreign GAAPs rather than Canadian GAAP.

### ***Use of IFRS in Asia-Pacific countries***

Asia-Pacific countries are taking a variety of approaches toward convergence of GAAP for domestic companies with IFRS.

### ***Adoption of IFRS in Place of National GAAP***

New Zealand is taking this approach with respect to listed companies, compulsory in 2007, permitted starting 2005. Bangladesh also requires IFRS for domestic companies.

### ***New National Standards Are Generally Word-for-Word IFRS***

Australia, Hong Kong, Philippines, and Singapore are taking this approach, but none of those jurisdictions has adopted all IFRS and in some instances changes are made to IFRS.

### ***IFRS Are Looked to in Developing National GAAP***

This is done to varying degrees in most of the rest of Asia-Pacific.

### ***Some Domestic Listed Companies May Use IFRS***

This is true in China, Laos, and Myanmar.

### ***In Some Countries, Foreign Listed Companies May Use IFRS***

This is true for stock exchanges in Australia, Hong Kong, New Zealand, Pakistan, Singapore, and Thailand. Japan has also permitted foreign companies to use IFRS in several cases.

## **Transition to IFRS – Overall three-step strategy**

### ***1. Determine consequences of IFRS***

- Perform gap analysis between what information is currently available and what is required under IFRS
- Determine new IFRS accounting policies/treatment, considering harmonisation with old ones
- Consider the impact on your entity, not just the impact on your published financial report

### ***2. Analysis of ability to cope with transition***

- Assess system and process impacts on your financial reporting and consolidated systems
- Determine system requirements to provide additional data
- Consider the adequacy of resources you have available

### ***3. Practical Implementation***

- New reporting requirements must be understood by Audit Committees, Senior Executives and accountants involved in financial reporting, to avoid misinterpretation
- Re-align performance measures with IFRS
- Plan for adequate training of staff
- Implement major system modifications to enable sustainable IFRS reporting
- Communicate with external stakeholders

## **Software requirements during the transition to IFRS**

As pointed out in the preceding section, the approach to adopting IFRS will vary by region. In countries or economic areas with long standing accounting traditions firmly anchored in local practices, institutions and business law, adoption is likely to be progressive, whereas countries with short accounting track records may be able to make the transition much more rapidly.

In EU, for example, IFRS will initially only apply to the consolidated accounts of publicly listed companies, while tax and statutory books will continue to be governed by local fiscal rules and accounting principles. Although such differences are likely to diminish as IFRS gains broad acceptance, it is unlikely that the fair value approach to income measurement will replace tax authorities insistence on arm's length realisation altogether.

As a result, software must be capable of:

- Applying different accounting rules to a given economic event (e.g.: fiscal and economic depreciation for the same asset)
- Storing statutory, fiscal and consolidated results separately
- Insuring the integrity of each set of books
- Reconciling differences between different accounting perspectives

Producing reports required for each accounting objective

## Summary of BASDA software recommendations

| IFRS/IAS | Description  | BASDA Software recommendations   |
|----------|--|--|
| IFRS 1   | First-time Adoption of International Financial Reporting Standards | For first time adopters in the EU, 2004 is a pivotal year, as consolidated accounts must be produced according to both existing accounting norms at year's end and subsequently IFRS for the purpose of comparative history. Software must therefore be able to store, produce and reconcile information for both purposes.  |
| IFRS 2   | Share Based Payment  | Will generally be undertaken by specialized software beyond the scope of this document.  |
| IFRS 3   | Business Combinations  | <ul style="list-style-type: none"> <li>• Consolidation Software should comply with the purchase method of accounting for acquisitions.</li> <li>• All assets including goodwill should be associated to cash generating units for the purpose of testing goodwill for impairment.</li> </ul>   |
| IFRS 4   | Insurance Contracts  | Will generally be undertaken by specialized software beyond the scope of this document.  |
| IFRS 5   | Non-current Assets Held for Sale and Discontinued Operations       | <ul style="list-style-type: none"> <li>• Software requirements for discontinuing operations apply to relatively large components of a business that will only require additional disclosure under IFRS 5 should conditions sometimes uncertain at the outset of an accounting year be met</li> <li>• Information systems must therefore be capable of providing detailed and reliable financial information as required by IFRS 5 relating to current and prior periods for all key business areas on an ongoing basis.</li> <li>• Consolidation software must be capable of showing the results of the group both before and after the disposal to facilitate restatement of results and thus provide an audit trail.</li> <li>• In order to measure non-current assets or disposal groups at the lower of carrying amount or fair value less costs to sell, software must provide the ability to suspend ongoing depreciation calculation on related assets and support impairment.</li> </ul> |
| IAS 1    | Presentation of Financial Statements                               | <ul style="list-style-type: none"> <li>• Software must reinforce fundamental accounting principles underlying presentation of financial statements that lend themselves to automation (e.g. accruing expense for receipts not invoiced)</li> <li>• Reporting tools should be flexible to enable customers to define presentation modes and categories that accurately reflect their economic conditions.</li> </ul>  |

| IFRS/IAS | Description   | BASDA Software recommendations  |
|----------|---|---|
| IAS 2    | Inventories   | <ul style="list-style-type: none"> <li>• Software must be capable of costing inventory by one of the accepted alternatives (specific identification, FIFO or weighted average).</li> <li>• The standard cost inventory method may be used, provided that results after incorporation of variance reconcile back to an acceptable IFRS alternative.</li> </ul>   |
| IAS 7    | Cash Flow Statements  | <p>Software should be able to produce a cash-flow statement, in accordance with the direct or indirect method, or create an extract file for cash flow data to an external reporting tool.</p> <p>Finance Systems should be able to analyse cash flows by the following activities:</p> <ul style="list-style-type: none"> <li>• Operating</li> <li>• Investing <ul style="list-style-type: none"> <li>- Short term</li> <li>- Long term</li> </ul> </li> <li>• Financing</li> </ul>  |
| IAS 8    | Accounting Policies, Changes in Accounting Estimates and Errors | <p>If the Finance Software produces final accounts, then it should be able to handle adjustments to prior years – subject to the appropriate security permissions.</p>  |
| IAS 10   | Events After the Balance Sheet Date                             | <p>The General Ledger should be able to post to the prior reporting period between the balance sheet date and the date when financial statements are authorised for issue - subject to the appropriate security permissions.</p>  |
| IAS 11   | Construction Contracts  | <p>Software used to manage revenue generating projects should be capable of measuring and reporting income in accordance with the % of completion method of accounting.</p>   |
| IAS 12   | Income Taxes  | <ul style="list-style-type: none"> <li>• Surveys on the experience of early IAS adopters have shown deferred taxes, which are not mandatory in all EU states today, to be one of the biggest challenges for early adopters.</li> <li>• Accounting software should be able to produce results in accordance with both fiscal and economic rules and capture the temporary differences necessary for calculating deferred tax liabilities and assets.</li> <li>• Fixed Assets should be able to handle multiple books to value assets for both tax and statutory purposes.</li> </ul> |
| IAS 14   | Segment Reporting   | <ul style="list-style-type: none"> <li>• Provide the means to associate primary and secondary segment attributes with all accounting</li> </ul>   |

| IFRS/IAS | Description                   | BASDA Software recommendations  |
|----------|-------------------------------|---|
|          |                               | <p>information flows.</p> <ul style="list-style-type: none"> <li>• Store information in accordance with segment reporting classification requirements.</li> <li>• Capture all information necessary for reconciling segment level disclosure with totals shown in financial statements.</li> <li>• Enable full reporting of segment information required by IAS 14:</li> <li>• Primary Segment <ul style="list-style-type: none"> <li>○ Revenue (external and inter-segment shown separately);</li> <li>○ Operating result (before interest and taxes);</li> <li>○ Carrying amount of segment assets;</li> <li>○ Carrying amount of segment liabilities;</li> <li>○ Cost to acquire property, plant, equipment, and intangibles;</li> <li>○ Depreciation and amortisation;</li> <li>○ Non-cash expenses other than depreciation;</li> <li>○ Share of profit or loss of equity and joint venture investments;</li> <li>○ The basis of inter-segment pricing</li> </ul> </li> <li>• Secondary Segment <ul style="list-style-type: none"> <li>○ Revenue (external and inter-segment shown separately);</li> <li>○ Carrying amount of segment assets;</li> <li>○ Cost to acquire property, plant, equipment, and intangibles;</li> <li>○ The basis of inter-segment pricing.</li> </ul> </li> <li>• In an IFRS context, it is highly desirable that software provide features that assist in: <ul style="list-style-type: none"> <li>○ Insuring the integrity of segment results</li> <li>○ Distinguishing between external and inter-segment revenues</li> <li>○ Reconciling segment results with statement totals.</li> </ul> </li> <li>• Intra-segment balancing supports these three objectives.</li> </ul> |
| IAS 16   | Property, Plant and Equipment | <ul style="list-style-type: none"> <li>• Software must enable initial asset recognition as cost, and subsequent measurement at either cost less accumulated depreciation and impairment losses or revaluation on a systematic basis.</li> <li>• Depreciation methods must be open and customisable in order to reflect the expected consumption of economic benefits</li> </ul>   |

| IFRS/IAS | Description | BASDA Software recommendations   |
|----------|-------------|--|
|          |             | <ul style="list-style-type: none"> <li>• Should subcomponents of an asset have different expected lives or depreciation treatments, each component must be identified and managed separately, e.g. an aircraft and its engines.</li> <li>• Software must be able manage different valuations and processing for a given asset in parallel.</li> <li>• When the revaluation measurement option is adopted, software must:               <ul style="list-style-type: none"> <li>○ Generate the required accounting entries:                   <ul style="list-style-type: none"> <li>▪ Revaluations should be credited to equity (revaluation surplus) unless reversing a previous charge to income.</li> <li>▪ Decreases in valuation should be charged to income unless reversing a previous credit to equity (revaluation surplus)</li> <li>▪ If the re-valued asset is sold or otherwise disposed of, any remaining revaluation surplus either remains as a separate component of equity or is transferred directly to retained earnings</li> <li>▪ Calculate depreciation subsequent to revaluation on the basis of the revalued asset amount</li> </ul> </li> <li>○ Store and maintain system level attributes and information necessary for performing revaluation:                   <ul style="list-style-type: none"> <li>▪ Current revaluation surplus</li> <li>▪ History of revaluations</li> <li>▪ Asset carrying amount at depreciated historical cost.</li> </ul> </li> <li>○ Provide a facility for revaluing all assets within a class of assets "en mass".</li> </ul> </li> <li>• Provide a complete audit trail of revaluations.</li> <li>• Enable the re-estimation of expected asset life and residual value</li> </ul> |
| IAS 17   | Leases      | <p>Finance Leases - Lessee's Accounting</p> <ul style="list-style-type: none"> <li>• Assets are capitalised and depreciated as a normal asset</li> <li>• Leases are brought in as a liability.</li> <li>• Payments are split between interest and reduction of liability – rule of 78 (the calculation for lease interest)</li> </ul> <p>Operating leases – Lessor's Accounting:</p> <ul style="list-style-type: none"> <li>• Assets held for operating leases should be presented in the lessor's balance sheet according</li> </ul>  |

| IFRS/IAS | Description  | BASDA Software recommendations   |
|----------|--|--|
|          |  | <p>to the nature of the asset.</p> <ul style="list-style-type: none"> <li>• Lease income should be recognised on a straight-line basis over the lease term, unless another systematic basis is more representative of the pattern of benefit.</li> </ul> <p>N.B. The specialised requirements of leasing companies are outside the scope of the BASDA IFRS recommendations.</p>  |
| IAS 18   | Revenue  | <ul style="list-style-type: none"> <li>• Software should respect the accrual principle when recognising revenue.</li> </ul>  |
| IAS 19   | Employee Benefits  | <p>Although accounting for post-employment benefit plans and share based payments will pose challenges, solutions are likely to require specialized software that is beyond the scope of this White Paper.</p>   |
| IAS 20   | Accounting for Government Grants and Disclosure of Government Assistance | <p>A means of matching revenue recognition from grants to periods in which related costs are incurred would provide value in vertical markets where grants are prevalent (government, education, etc.).</p>  |
| IAS 21   | The Effects of Changes in Foreign Exchange Rates                         | <p>When transactions are initially recorded, software must:</p> <ul style="list-style-type: none"> <li>• Convert amounts denominated in foreign currency to an entity’s functional currency using the rate effective on the date of transaction (spot rate) or a reasonable approximation thereof (e.g. an average weekly or monthly rate)</li> </ul> <p>At the end of an accounting period, software must:</p> <ul style="list-style-type: none"> <li>• Revalue open monetary amounts at the period close rate</li> <li>• Revalue non-monetary items measured at fair value in a foreign currency at the rate effective when the fair value was determined.</li> <li>• Post exchange differences between the historical and re-valued amounts as currency gains or losses for disclosure in the income statement.</li> </ul> <p>When foreign operation are translated into presentation currency for inclusion in a reporting entity’s consolidated financial statements software must:</p> <ul style="list-style-type: none"> <li>• Translate assets and liabilities using the period end rate except where a historical rates is more appropriate.</li> <li>• Translate income and expense using period average rates</li> <li>• Recognize resulting exchange differences as a separate component of equity.</li> </ul> <p>All foreign currency conversions, revaluations and</p> |

| IFRS/IAS | Description  | BASDA Software recommendations   |
|----------|--|--|
|          |  | adjustments should retain a clear audit trail with system level attributes (currencies, amounts, rates, rate types, rate dates, ...) in order to fully explain foreign currency processing, including scenarios where local and translated currencies differ from the group presentation currency  |
| IAS 23   | Borrowing Costs                                      | Software should enable adjustments to assets or long-term projects to enable capitalization of borrowing costs.  |
| IAS 24   | Related Party Disclosures                            | As arrangements between third parties and corporate entities vary considerably, there are no specific recommendations for business applications beyond a need for sound auditing trails and procedures to insure corporate governance.   |
| IAS 26   | Accounting and Reporting by Retirement Benefit Plans | Solutions are likely to require specialized software that is beyond the scope of this white paper  |
| IAS 27   | Consolidated and Separate Financial Statements       | <p>The system must provide a facility to collect information relating to ownership such that the system can determine if the entity is a subsidiary company as defined in IAS 27.</p> <p>Subsidiary company definition may be defined based on share ownership or effective management control, both methods must be facilitated.</p> <p>Provide facilities to automatically calculate any minority interest in the entity together with facilities to eliminate this on consolidation.</p> <p>The system must provide that the ownership calculation recognises that the share holding or effective control may vary over time.</p>   |
| IAS 28   | Investment in Associates                             | <p>The system must provide a facility to collect information relating to ownership such that the system can determine if the entity is an associated company as defined in IAS 28</p> <p>Associated company definition may be defined based on share ownership or effective management control, both methods must be facilitated.</p> <p>Provide facilities to automatically calculate the holding companies interest in profit and thereby provide for proper equity accounting entries.</p> <p>The system must provide that the ownership calculation recognises that the share holding or effective control may vary over time.</p> |
| IAS 29   | Financial Reporting in Hyperinflationary Economies   | Enable the restatement of financial statements in accordance with the provisions of IAS 29 in cases of economic hyperinflation.  |

| IFRS/IAS | Description   | BASDA Software recommendations   |
|----------|---|--|
|          |   | The local (hyperinflationary) currency is the measurement currency; the alternate currency is the presentation currency (usually the US Dollar or the Euro) at the spot rate on the balance sheet date   |
| IAS 30   | Disclosures in the Financial Statements of Banks and Similar Financial Institutions | The specialised requirements of banks and similar institutions are outside the scope of the BASDA IFRS Standard.   |
| IAS 31   | Interests in Joint Ventures   | <ul style="list-style-type: none"> <li>• Consolidation software should enable joint ventures to be consolidated under the benchmark treatment (proportionate consolidation) as well as the allowed alternative (equity method)</li> </ul>  |
| IAS 32   | Financial Instruments: Disclosure and Presentation                                  | <p>General business Software must provide flexible means of classifying financial instruments and related operations in statements of financial position, performance, and cash flows – however much of the underlying processing will be performed in specialized systems beyond the scope of this document.</p> <p>Software must be able to store information and disclose information according to ‘on and off balance sheet classification’</p>  |
| IAS 33   | Earnings per Share  | Will generally be undertaken by specialized software packages or manual calculations.  |
| IAS 34   | Interim Financial Reporting   | <ul style="list-style-type: none"> <li>• Reinforced emphasis on interim reporting and shortened report cycles heightens the need for responsive business intelligence tools in order to produce and audit results in an efficient manor.</li> <li>• Requirement to specify comparative periods.</li> </ul>   |
| IAS 36   | Impairment of Assets  | <ul style="list-style-type: none"> <li>• Software should be capable of being able to recognize impairment for individual assets or asset groupings associated with a Cash Generating Unit (CGU)</li> <li>• As impairment may well apply to a subset of assets, for example business sector or geography, software should offer flexible means for identifying subgroups of assets for impairment processing.</li> <li>• Software should enable parallel depreciation of assets, with and without impairment.</li> <li>• When the recoverable amount of an asset is less than its carrying amount, software should generate the required accounting entries: <ul style="list-style-type: none"> <li>○ An impairment loss should be recognised in the income statement for assets carried at cost and treated as a revaluation decrease</li> </ul> </li> </ul> |

| IFRS/IAS | Description  | BASDA Software recommendations   |
|----------|--|--|
|          |  | <p>for assets carried at revalued amount</p> <ul style="list-style-type: none"> <li>○ An impairment loss should be reversed (and income recognised) when there is a positive reassessment of an asset's recoverable amount subsequent to the recognition of impairment loss</li> <li>○ However, an impairment loss should only be reversed to the extent the reversal does not increase the carrying amount of the asset above the carrying amount that would have been determined for the asset (net of amortisation or depreciation) had no impairment loss been recognised.</li> </ul> <ul style="list-style-type: none"> <li>● Software should store and maintain system level attributes and necessary information for performing revaluation:</li> </ul> |
| IAS 37   | Provisions, Contingent Liabilities and Contingent Assets | Increased scrutiny and disclosure requirements for obligations under IAS 37 will create additional work load that is largely outside of the scope of automated software processes.   |
| IAS 38   | Intangible Assets  | Increased scrutiny and disclosure requirements for intangible assets will create additional work load that is largely outside of the scope of automated software processes.  |
| IAS 39   | Financial Instruments: Recognition and Measurement       | To be completed at a future date pending ongoing discussions between the EU and the IASB.  |
| IAS 40   | Investment Property                                      | Specialist software requirements outside the scope of business systems   |
| IAS 41   | Agriculture  | Specialist software requirements outside the scope of business systems   |

# Summaries of International Financial Reporting Standards

*As of 1 April 2004*

Note: These summaries cover International Financial Reporting Standards, International Accounting Standards, and Interpretations issued on or before 31 March 2004.

## ***Framework Summary***

IASB has a conceptual framework underlying its financial reporting standards and interpretations, the *Framework for the Preparation and Presentation of Financial Statements* (the Framework). The Framework sets out the concepts that underlie the preparation and presentation of financial statements for external users.

## ***IFRS and IAS Summaries***

IASB publishes its Standards in a series of pronouncements called International Financial Reporting Standards (IFRS). It has also adopted the body of Standards issued by the Board of the International Accounting Standards Committee (IASC). Those pronouncements continue to be designated "International Accounting Standards" (IAS). This section provides summaries of the Standards issued and in force.

## ***IFRIC and SIC Summaries***

IASB publishes a series of Interpretations of International Accounting Standards developed by the International Financial Reporting Interpretations Committee (IFRIC) and approved by the IASB. This section provides summaries of final Interpretations.

## Summary of the Framework

This page provides a brief summary of the Framework.

Note: The unofficial summaries are, by their nature, incomplete.

The official full text of the *Framework*, IFRSs and IASs and IFRIC and SIC interpretations is available through the IASCF Shop. The official full text is available through the Comprehensive Subscription Services, the CD-Rom Subscriptions Service and also in the printed Bound Volume of International Financial Reporting Standards.

### ***Framework for the Preparation and Presentation of Financial Statements***

The Framework is a conceptual accounting *Framework* that sets out the concepts that underlie the preparation and presentation of financial statements for external users. It was approved in 1989 by the IASB's predecessor, the board of IASC, and adopted by the IASB in April 2001. The *Framework* assists the IASB:

- in the development of future International Financial Reporting Standards and in its review of existing Standards; and
- in promoting the harmonisation of regulations, financial reporting standards and procedures relating to the presentation of financial statements by providing a basis for reducing the number of alternative accounting treatments permitted by International Financial Reporting Standards.
- In addition, the *Framework* may assist:
  - national standard-setting bodies in developing national standards;
  - preparers of financial statements in applying International Financial Reporting Standards and in dealing with topics that have yet to form the subject of an International Financial Reporting Standard;
  - auditors in forming an opinion as to whether financial statements conform with International Financial Reporting Standards;
  - users of financial statements in interpreting the information contained in financial statements prepared in conformity with International Financial Reporting Standards; and
  - those who are interested in the work of IASB, providing them with information about its approach to the formulation of International Financial Reporting Standards.

The *Framework* is not an International Financial Reporting Standard and does not define standards for any particular measurement or disclosure issue.

In a limited number of cases there may be a conflict between the Framework and a requirement within an International Financial Reporting Standard. In those cases where there is a conflict, the requirements of the International Financial Reporting Standard prevail over those of the *Framework*.

## **IFRS 1: First-time Adoption of International Financial Reporting Standards**

### ***Introduction***

IFRS 1 *First-time Adoption of International Financial Reporting Standards* was issued in June 2003 and applies to an entity whose first IFRS financial statements are for a period beginning on or after 1 January 2004. IFRS 1 also applies to each interim financial report, if any, that the entity presents under IAS 34 *Interim Financial Reporting* for part of the period covered by its first IFRS financial statements.

IFRS 1 applies when an entity adopts IFRSs for the first time by an explicit and unreserved statement of compliance with IFRSs.

### ***Summary of IFRS 1***

In general, IFRS 1 requires an entity to comply with each IFRS effective at the reporting date for its first IFRS financial statements. In particular, in its opening IFRS balance sheet an entity must:

- recognise all assets and liabilities whose recognition is required by IFRSs;
- not recognise items as assets or liabilities if IFRSs do not permit such recognition;
- reclassify items that it recognised under previous GAAP as one type of asset, liability or component of equity, that are a different type of asset, liability or component of equity under IFRSs; and
- apply IFRSs in measuring all recognised assets and liabilities.

The transition provisions in other IFRSs do not apply to a first-time adopter's transition to IFRSs.

IFRS 1 grants limited exemptions from these requirements in specified areas where the cost of complying would be likely to exceed the benefits to users of financial statements. Exemptions exist in the following areas:

- business combinations;
- fair value or revaluation as deemed cost for certain non-current assets;
- defined benefit employee benefit plans;
- cumulative translation differences;
- compound financial instruments;
- assets and liabilities of subsidiaries, associates and joint ventures;
- designation of previously recognised financial instruments;
- share-based payment transactions; and
- insurance contracts.

The IFRS also prohibits retrospective application of IFRSs in some cases, particularly where retrospective application would require judgements by management about past conditions after the outcome of a particular transaction is already known.

IFRS 1 requires disclosures that explain how the transition from previous GAAP to IFRSs affected the entity's reported financial position, financial performance and cash flows.

### ***Software requirements***

For first time adopters in Europe, 2004 is a pivotal year, as consolidated accounts must be produced according to both existing accounting norms at year's end and subsequently IFRS for the purpose of comparative history. Software must therefore be able to store, produce and reconcile information for both purposes.

## **IFRS 2: Share Based Payment**

### ***Introduction***

IFRS 2 *Share-based Payment* was issued in February 2004 and applies to annual periods beginning on or after 1 January 2005.

IFRS 2 prescribes the financial reporting by an entity when it undertakes a share-based payment transaction. It applies to grants of shares, share options or other equity instruments made after 7 November 2002 that had not yet vested at the effective date of the IFRS. IFRS 2 applies retrospectively to liabilities arising from share-based payment transactions existing at the effective date.

### ***Summary of IFRS 2***

IFRS 2 requires an entity to reflect in its profit and loss and financial position the effects of share-based payment transactions, including expenses associated with share options granted to employees.

For equity-settled share-based payment transactions with employees (and others providing similar services), the measurement of the transaction amount is based on the fair value of the equity instruments granted. Fair value is measured at grant date. The valuation focuses on the specific terms and conditions of a grant of shares or share options to employees. In general, vesting conditions are not taken into account in the grant date valuation but the number of equity instruments included in the measurement of the transaction amount is adjusted so that, ultimately, the transaction amount is based on the number of equity instruments that vest.

The IFRS sets out requirements if the terms and conditions of an option or share grant are modified or if a grant is cancelled, repurchased or replaced with another grant of equity instruments. IFRS 2 also contains requirements for equity-settled transactions with other parties (ie other than employees and those providing similar services).

For cash-settled transactions, the good or services received and the liability incurred are measured at the fair value of the liability. The liability is remeasured to fair value at each reporting date and at the date of settlement, with changes in fair value recognised in profit or loss.

IFRS 2 also specifies requirements for transactions in which the terms of the arrangement provide either the entity or the supplier of goods or services with a choice of whether the entity settles the transaction in cash (or other assets) or by issuing equity instruments.

IFRS 2 specifies disclosures about share-based payment transactions.

### ***Software requirements***

Will generally be undertaken by specialized software beyond the scope of this document.

## **IFRS 3: Business Combinations**

### ***Introduction***

IFRS 3 *Business Combinations* was issued in March 2004 and is applicable for business combinations for which the agreement date is on or after 31 March 2004.

IFRS 3 prescribes the financial reporting by an entity when it undertakes a business combination. A business combination is the bringing together of separate entities or businesses into one reporting entity. IFRS 3 does not apply to:

- business combinations in which separate entities or businesses are brought together to form a joint venture;
- business combinations involving entities or businesses under common control;
- business combinations involving two or more mutual entities; and
- business combinations in which separate entities or businesses are brought together to form a reporting entity by contract alone without the obtaining of an ownership interest.

### ***Summary of IFRS 3***

All business combinations are accounted for by applying the purchase method, which views the business combination from the perspective of the acquirer. The acquirer is the combining entity that obtains control of the other combining entities or businesses (the acquiree).

The acquirer measures the cost of a business combination as the aggregate of:

- the fair values, at the date of exchange, of assets given, liabilities incurred or assumed, and equity instruments issued by the acquirer, in exchange for control of the acquiree; plus
- any costs directly attributable to the business combination.

Any adjustment to the cost of the combination, that is contingent on future events, is included in the cost of the combination at the acquisition date if the adjustment is probable and can be measured reliably.

The acquirer allocates the cost of the business combination by recognising the acquiree's identifiable assets, liabilities and contingent liabilities at their fair value at the date of acquisition, except for non-current assets that are classified as held for sale in accordance with IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*. Such assets held for sale are recognised at fair value less costs to sell.

Goodwill, being the excess of the cost over the acquirer's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities, is recognised as an asset. Goodwill is subsequently carried at cost less any accumulated impairment losses in accordance with IAS 36 *Impairment of Assets*. If the acquirer's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities exceeds the cost of the combination, the acquirer:

- reassesses the identification and measurement of the acquiree's identifiable assets, liabilities and contingent liabilities and the measurement of the cost of the combination; and
- recognises immediately in profit or loss any excess remaining after that reassessment.

IFRS 3 specifies the accounting treatment:

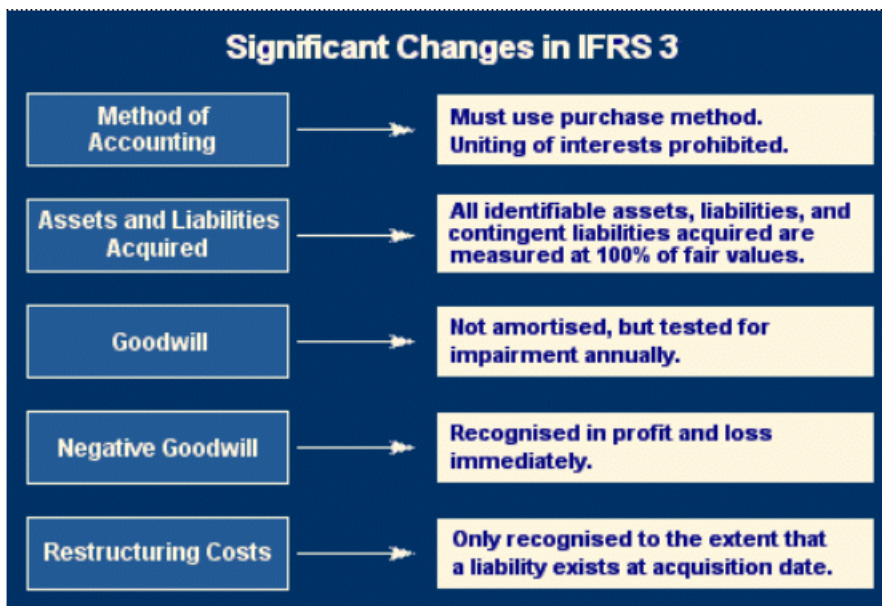
- for business combinations that are achieved in stages;

IFRS 3: Business Combinations

- where fair values can only be determined provisionally in the period of acquisition;
- where deferred tax assets are recognised after the accounting for the acquisition is complete; and

- for previously recognised goodwill, negative goodwill and intangible assets.

IFRS 3 also specifies disclosures about business combinations and any related goodwill.



### ***Recommendations for Software***

- Consolidation Software should comply with the purchase method of accounting for acquisitions.
- All assets including goodwill should be associated to cash generating units for the purpose of testing goodwill for impairment.

## **IFRS 4: Insurance Contracts**

### ***Introduction***

IFRS 4 *Insurance Contracts* was issued in March 2004 and is applicable for annual periods beginning on or after 1 January 2005.

IFRS 4 prescribes the financial reporting for insurance contracts by any entity that issues such contracts. It applies to insurance contracts issued, reinsurance contracts held and financial instruments issued with a discretionary participation feature. It does not apply to:

- product warranties issued directly by a manufacturer, dealer or retailer (IAS 18 *Revenue* and IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*);
- employers' assets and liabilities under employee benefit plans (IAS 19 *Employee Benefits*) and retirement benefit obligations reported by defined benefit retirement plans (IAS 26 *Accounting and Reporting by Retirement Benefit Plans*);
- contractual rights or obligations that are contingent on the future use of or right to use a non-financial item, as well as lessee's residual value guarantees on finance leases (IAS 17 *Leases*; IAS 18 *Revenue* and IAS 38 *Intangible Assets*);
- financial guarantees entered into or retained on transferring financial assets or financial liabilities within the scope of IAS 39;
- contingent consideration payable or receivable in a business combination (IFRS 3 *Business Combinations*);
- direct insurance contracts that an entity holds as a policyholder.

An entity need not apply some aspects of IFRS 4 to comparative information that relates to annual periods beginning before 1 January 2005.

### ***Summary of IFRS 4***

IFRS 4 is phase I of the IASB's project on insurance contracts. An entity is temporarily exempt from some requirements of other IFRSs, including the requirement in IAS 8 to consider the Framework in selecting accounting policies for insurance contracts. However, IFRS 4:

- prohibits recognition as a liability of provisions for possible future claims under insurance contracts that are not in existence at the reporting date (such as catastrophe provisions and equalisation provisions);
- requires assessment of the adequacy of recognised insurance liabilities and recognition of any impairment of reinsurance assets;
- requires an entity to keep insurance liabilities in its balance sheet until they are discharged or cancelled, or expire, and to present insurance liabilities without offsetting them against related reinsurance assets.

An entity may change its accounting policies for insurance contracts only if, as a result, its financial statements are more relevant and no less reliable, or more reliable and no less relevant. In particular, an entity must not introduce any of the following practices, although it may continue using accounting policies that involve them:

- measuring insurance liabilities on an undiscounted basis;
- measuring contractual rights to future investment management fees at an amount that exceeds their fair value as implied by a comparison with current fees charged by other market participants for similar services;
- using non-uniform accounting policies for the insurance contracts of subsidiaries;
- measuring insurance liabilities with excessive prudence.

There is a rebuttable presumption that an insurer's financial statements will become less relevant and reliable if it introduces an accounting policy that reflects future investment margins in the measurement of insurance contracts. When an insurer changes its accounting

policies for insurance liabilities, it may reclassify some or all financial assets as 'at fair value through profit or loss'.

IFRS 4 specifies the following:

- An entity need not account for an embedded derivative separately at fair value if the embedded derivative meets the definition of an insurance contract.
- An entity is required to unbundle (i.e. account separately for) deposit components of some insurance contracts.
- An entity may apply 'shadow accounting' (that is, account for both realised and unrealised gains or losses on assets in the same way relative to measurement of insurance liabilities).
- Discretionary participation features contained in insurance contracts or financial instruments may be recognised separately from the guaranteed element and classified as a liability or as a separate component of equity.

***IFRS 4 also specifies disclosures about:***

- The amounts in the entity's financial statements that arise from insurance contracts; and
- The amount, timing and uncertainty of future cash flows from insurance contracts.

***Software requirements***

Will generally be undertaken by specialized software beyond the scope of this document.

## **IFRS 5: Non-current Assets Held for Sale and Discontinued Operations**

### ***Introduction***

IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations* was issued in March 2004 and is applicable for annual periods beginning on or after 1 January 2005.

IFRS 5 prescribes the accounting for assets held for sale, and the presentation and disclosure of discontinued operations. The measurement provisions of IFRS 5 apply to all non-current assets and disposal groups, except for:

- deferred tax assets (IAS 12 *Income Taxes*);
- assets arising from employee benefits (IAS 19 *Employee Benefits*);
- financial assets within the scope of IAS 39 *Financial Instruments: Recognition and Measurement*;
- non-current assets that are accounted for in accordance with the fair value model in IAS 40 *Investment Property*;
- non-current assets that are measured at fair value less estimated point-of-sale costs
- in accordance with IAS 41 *Agriculture*; and
- contractual rights under insurance contracts as defined in IFRS 4 *Insurance Contracts*.

### ***Summary of IFRS 5***

#### **Assets held for sale**

A non-current asset (or disposal group) is classified as held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use. That is, the asset (or disposal group) is available for immediate sale and its sale is highly probable.

A non-current asset (or disposal group) classified as held for sale is measured at the lower of fair value less costs to sell and its carrying amount.

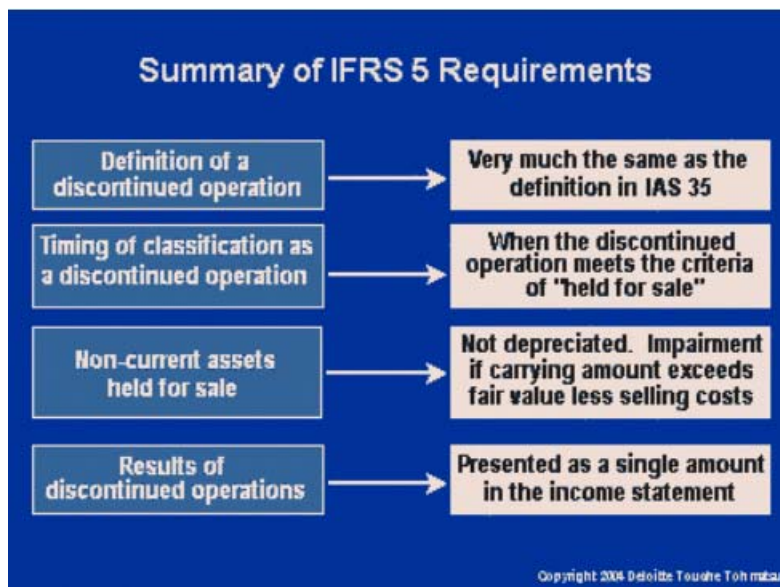
Any impairment loss on write-down of the asset (or disposal group) to fair value less costs to sell is recognised in profit or loss. Any gain on subsequent increase in fair value less costs to sell is also recognised in profit or loss, but not in excess of the cumulative impairment loss already recognised on the asset either in accordance with IFRS 5 or IAS 36 *Impairment of Assets*.

#### **Discontinued Operations**

A discontinued operation is a component of an entity that either has been disposed of or is held for sale. It may be a subsidiary, or a major line of business or geographical area. It will have been a cash-generating unit (or group of cash-generating units) as defined in IAS 36 *Impairment of Assets*.

Disclosures of discontinued operations include:

- analysis of the post-tax profit or loss into revenue, expenses, pre-tax profit or loss, and the related income tax expense;
- the gain or loss recognised on measurement to fair value less costs to sell or on disposal, and the related income tax expense;
- net cash flows attributable to operating, investing and financing activities;
- assets held for sale separately from all other assets; and
- liabilities of a disposal group held for sale separately from all other liabilities.



### ***Recommendations for Software***

- Software requirements for discontinuing operations apply to relatively large components of a business that will only require additional disclosure under IFRS 5 should conditions sometimes uncertain at the outset of an accounting year be met.
- Information systems must therefore be capable of providing detailed and reliable financial information as required by IFRS 5 relating to current and prior periods for all key business areas on an ongoing basis.
- Consolidation software must be capable of showing the results of the group both before and after the disposal to facilitate restatement of results and thus provide an audit trail.
- In order to measure non-current assets or disposal groups at the lower of carrying amount or fair value less costs to sell, software must provide the ability to suspend ongoing depreciation calculation on related assets and support impairment.

## **IAS 1: Presentation of Financial Statements**

### ***Introduction***

IAS 1 *Presentation of Financial Statements* was issued in December 2003 and is applicable for annual periods beginning on or after 1 January 2005.

IAS 1 prescribes the basis for presentation of general purpose financial statements, to ensure comparability both with the entity's financial statements of previous periods and with the financial statements of other entities.

IAS 1 does not apply to interim financial statements prepared in accordance with IAS 34 *Interim Financial Reporting*.

### ***Summary of IAS 1***

A complete set of financial statements comprises a balance sheet; an income statement; a statement of changes in equity; a cash flow statement; and notes, comprising a summary of significant accounting policies and other explanatory notes.

Financial statements present fairly the financial position, financial performance and cash flows of an entity. Fair presentation requires faithful representation of the effects of transactions, events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the *Framework for the Preparation and Presentation of Financial Statements*. The application of IFRSs (ie Standards and Interpretations), with additional disclosure when necessary, is presumed to result in financial statements that achieve a fair presentation. An entity makes an explicit and unreserved statement of compliance with IFRSs in the notes to the financial statements. Such a statement is only made on compliance with all the requirements of IFRSs. A departure from IFRSs is acceptable only in the extremely rare circumstances in which compliance with IFRSs conflicts with providing information useful to users in making economic decisions. IAS 1 specifies the disclosures required when an entity departs from a requirement of an IFRS.

IAS 1 specifies the following about the preparation and presentation of financial statements:

- Financial statements are prepared on a going concern basis unless management either intends to liquidate the entity or to cease trading, or has no realistic alternative but to do so.
- Financial statements, except for cash flow information, are prepared using the accrual basis of accounting.
- The presentation and classification of items in the financial statements are usually retained from one period to the next.
- Each material class of similar items is presented separately. Dissimilar items are presented separately unless they are immaterial. 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.
- Assets and liabilities, and income and expenses, are not offset unless required or permitted by an IFRS.
- Comparative information is disclosed for all amounts reported in the financial statements, unless an IFRS requires or permits otherwise.
- Financial statements are presented at least annually.

IAS 1 specifies the minimum line item disclosures on the face of, or in the notes to, the balance sheet, the income statement, and the statement of changes in equity. Current and non-current assets, and current and non-current liabilities are presented as separate classifications on the face of the balance sheet.

IAS 1 specifies disclosures about information to be presented in the financial statements, including judgements, key sources of estimation uncertainty, and accounting policies.

***Recommendations for Software:***

- Software must reinforce fundamental accounting principles underlying presentation of financial statements that lend themselves to automation(e.g. accruing expense for receipts not invoiced)
- Reporting tools should be flexible to enable customers to define presentation modes and categories that accurately reflect their economic conditions.

## **IAS 2: Inventories**

### ***Introduction***

IAS 2 *Inventories* was issued in December 2003 and is applicable to annual periods beginning on or after 1 January 2005.

IAS 2 prescribes the accounting treatment for inventories, except:

- a) Work in progress arising under construction contracts (IAS 11 *Construction Contracts*);
- b) Financial instruments (IAS 39 *Financial Instruments*); and
- c) Biological assets related to agricultural activity and agricultural produce at the point of harvest (IAS 41 *Agriculture*).

### ***Summary of IAS 2***

Inventories are measured at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale. Cost includes all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition. The cost of inventories, other than those for which specific identification of costs are appropriate, is assigned by using the first-in, first-out (FIFO) or weighted average cost formula.

When inventories are sold, the carrying amount of those inventories is recognised as an expense in the same period as the revenue.

The amount of any write-down of inventories to net realisable value is recognised as an expense in the period the write-down or loss occurs. The amount of any reversal of a write-down of inventories is recognised as a reduction in the amount of inventories recognised as an expense in the period in which the reversal occurs.

IAS 2 specifies disclosures about inventories.

### ***Recommendations for Software:***

- Software must be capable of costing inventory by one of the accepted alternatives (specific identification, FIFO or weighted average).
- The standard cost inventory method may be used, provided that results after incorporation of variance reconcile back to an acceptable IFRS alternative.

## **IAS 7: Cash Flow Statements**

### ***Introduction***

IAS 7 *Cash Flow Statements* is applicable for periods beginning on or after 1 January 1994.

IAS 7 prescribes the principles in preparing a cash flow statement, which is presented as an integral part of the financial statements.

### ***Summary of IAS 7***

A cash flow statement provides information on changes in cash and cash equivalents during a reporting period. Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and subject to an insignificant risk of changes in value.

A cash flow statement reports cash flows during the period classified by operating, investing and financing activities.

Operating activities are the principal revenue-producing activities of the entity. They also include activities that are not investing or financing activities. Cash flows from operating activities are reported using either:

- the direct method, whereby major classes of gross cash receipts and gross cash payments are disclosed; or
- the indirect method, whereby profit or loss for the period is adjusted for non-cash items, and items of income or expense related to investing and financing activities.

IAS 7 encourages the use of the direct method.

Investing activities are the acquisition and disposal of long-term assets and other investments not included in cash equivalents (eg cash payments and receipts to acquire and dispose of property, plant and equipment; cash payments and receipts to acquire and dispose of equity and debt investments (including subsidiaries and other business units); cash advances and loans given to other parties).

Financing activities are activities that result in changes in the size and composition of the contributed equity and borrowings of the entity (eg cash proceeds from issuing shares; cash proceeds from issuing debt instruments; cash payments to repay amounts borrowed).

Cash flows are usually reported gross. Cash flows from interest and dividends are disclosed separately as either operating, investing or financing activities. Cash flows from taxes on income are also disclosed separately within operating activities.

IAS 7 specifies disclosures about cash and cash equivalents and certain non-cash transactions.

### ***Recommendations for Software:***

Software should be able to produce a cash-flow statement, in accordance with the direct or indirect method, or create an extract file for cash flow data to an external reporting tool.

Finance Systems should be able to analyse cash flows by the following activities:

- Operating
- Investing
  - Short term
  - Long term
- Financing

## **IAS 8: Accounting Policies, Changes in Accounting Estimates and Errors**

### ***Introduction***

IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* was issued in December 2003 and is applicable for annual periods beginning on or after 1 January 2005.

IAS 8 prescribes the criteria for selecting and applying accounting policies, and accounting for changes in accounting policies, changes in accounting estimates and corrections of prior period errors.

### ***Summary of IAS 8***

When a Standard or an Interpretation (hereafter "IFRS") specifically applies to a transaction, event or condition, the accounting policy applied to that item is determined by applying the IFRS and considering any relevant Implementation Guidance for the IFRS.

Accounting policies need not be applied when the effect of applying them is immaterial, as defined in IAS 1 *Presentation of Financial Statement*.

In the absence of an IFRS that specifically applies to a transaction, event or condition, management uses its judgement in selecting and applying an accounting policy that results in relevant and reliable financial information. IAS 8 specifies the following hierarchy of guidance which management uses when selecting accounting policies in such circumstances:

- requirements of Standards and Interpretations dealing with similar matters; the definitions, recognition criteria and measurement concepts for assets, liabilities, income and expenses in the *Framework for the Preparation and Presentation of Financial Statements*;
- the most recent pronouncements of other standard-setting bodies that use a similar conceptual framework, other accounting literature and accepted industry practices, to the extent that these do not conflict with IFRSs and the Framework. .

An entity applies its accounting policies consistently for similar transactions, other events and conditions, unless an IFRS specifically requires or permits categorisation of items for which different policies may be appropriate.

An entity changes an accounting policy only if the change is required by an IFRS, or results in the financial statements providing more relevant and reliable information about the entity's financial position, financial performance or cash flows. A change in accounting policy, resulting from the initial application of an IFRS, is accounted for in accordance with any specific transitional provisions of that IFRS. Otherwise a change in accounting policy is applied retrospectively to all periods presented in the financial statements as if the new accounting policy has always been applied.

The effect of a change in an accounting estimate is recognised prospectively in profit or loss in the period of the change, and also in profit or loss in future periods if the change affects both periods. Any corresponding changes in assets and liabilities, or to an item of equity, are recognised by adjusting the carrying amount of the asset, liability or equity item in the period of the change.

A material prior period error is corrected retrospectively in the first set of financial statements authorised for issue after its discovery. The comparative amounts for the prior period(s) presented in which the error occurred are restated; or if the error occurred before the earliest period presented, the opening balances of assets, liabilities and equity for the earliest prior period presented are restated.

IAS 8 specifies the accounting treatment when it is impracticable to account for a change in accounting policy or a correction of a prior period error using retrospective restatement in accordance with the Standard.

IAS 8 also specifies disclosures about accounting policies, changes in accounting estimates and errors.

***Recommendations for Software:***

If the Finance Software produces final accounts, then it should be able to handle adjustments to prior years – subject to the appropriate security permissions.

## **IAS 10: Events after the Balance Sheet Date**

### ***Introduction***

IAS 10 *Events After the Balance Sheet Date* was issued in December 2003 and is applicable for annual periods beginning on or after 1 January 2005.

IAS 10 prescribes the accounting for, and disclosure of, events after the balance sheet date. Events after the balance sheet date are those events that occur between the balance sheet date and the date when the financial statements are authorised for issue.

### ***Summary of IAS 10***

An entity adjusts the amounts recognised in the financial statements to reflect adjusting events after the balance sheet date. Adjusting events are those that provide evidence of conditions that existed at the balance sheet date (e.g. the settlement of a court case after the balance sheet date that confirms that the entity had a present obligation at the balance sheet date; the bankruptcy of a customer that occurs after the balance sheet date usually confirms that a loss existed at the balance sheet date on a receivable).

An entity does not adjust the amounts recognised in the financial statements to reflect non-adjusting events after the balance sheet date. Non-adjusting events are those that are indicative of conditions that arose after the balance sheet date (e.g. a decline in the market value of investments between the balance sheet date and the date when the financial statements are authorised for issue). For each material category of non-adjusting event after the balance sheet date, an entity discloses the nature of the event and an estimate of its financial effect.

Dividends declared after the balance sheet date are not recognised as a liability at the balance sheet date.

Financial statements are not prepared on a going concern basis if management determines after the balance sheet date either that it intends to liquidate the entity or to cease trading, or that it has no realistic alternative but to do so.

The financial statements disclose the date when the financial statements were authorised for issue, and who gave that authorisation.

### ***Recommendations for Software:***

The General Ledger should be able to post to the prior reporting period between the balance sheet date and the date when financial statements are authorised for issue - subject to the appropriate security permissions.

## **IAS 11: Construction Contracts**

### ***Introduction***

IAS 11 *Construction Contracts* is applicable for periods beginning on or after 1 January 1995.

IAS 11 prescribes the accounting treatment of revenue and costs associated with construction contracts.

### ***Summary of IAS 11***

When the outcome of a construction contract can be estimated reliably, contract revenue and contract costs are recognised as revenue and expenses respectively by reference to the stage of completion of the contract activity ("percentage of completion method"). The outcome can be estimated reliably when the contract revenue, contract costs to date and to completion, and the stage of completion can be measured reliably.

When the outcome of a construction contract cannot be estimated reliably, revenue is recognised only to the extent of contract costs incurred, that it is probable are recoverable. Contract costs are recognised as expenses when incurred. If the outcome of the contract subsequently can be estimated reliably, the percentage of completion method is used for recognition of revenue and expenses.

Any expected loss on a construction contract is recognised as an expense immediately.

IAS 11 specifies disclosures about construction contracts.

### ***Recommendations for Software:***

Software used to manage revenue generating projects should be capable of measuring and reporting income in accordance with the % of completion method of accounting.

## **IAS 12: Income Taxes**

### ***Introduction***

IAS 12 *Income Taxes* is applicable for periods beginning on or after 1 January 1998.

IAS 12 prescribes the accounting treatment for income taxes.

### ***Summary of IAS 12***

Current tax is the amount of income taxes payable (recoverable) in respect of taxable profit (tax loss) for the period. Income taxes payable for current and prior periods are recognised as a liability. Income tax recoverable or overpaid is recognised as an asset.

Deferred tax relates to differences between the carrying amount of assets and liabilities in the balance sheet, and the tax base of assets and liabilities. A deferred tax asset or liability arises if recovery (settlement) of assets (liabilities) affects the amount of future tax payments.

IAS 12 requires the entity to recognise a deferred tax liability in full. Exceptions:

- A deferred tax liability (asset) is not recognised for a taxable (deductible) temporary difference arising from the initial recognition of an asset or liability in a transaction which:
  - is not a business combination, and
  - at the time of the transaction, affects neither accounting profit nor
- taxable profit (e.g. an asset whose depreciation is not deductible for tax purposes; the entity intends to use the asset throughout its useful life).
- A deferred tax liability is not recognised for any taxable temporary difference arising from the initial recognition of goodwill, or from goodwill for which amortisation is not deductible for tax purposes.
- Deferred taxes are not recognised on temporary differences arising on investments in subsidiaries, branches, associates and joint ventures if the entity is able to control the timing of the reversal of the difference, and it is probable that the temporary difference will not reverse in the future.

A deferred tax asset is recognised only to the extent that it is probable that a tax benefit will be realised in the future. If it is probable that a tax benefit will be realised, a deferred tax asset is recognised on unused tax losses and unused tax credits.

Deferred tax is measured at tax rates expected to apply when the deferred tax asset (liability) is realised (settled). The tax rates used must have been enacted or substantially enacted by the balance sheet date. A deferred tax asset or liability is not discounted.

The tax consequences of transactions and events are recognised in the same financial statement as the transaction or event – that is, current and deferred taxes are:

- recognised in equity, if the items to which they relate are credited or charged directly to equity;
- recognised as identifiable assets or liabilities at the acquisition date, if they arise as part of a business combination in accordance with IFRS 3 Business Combinations;
- otherwise, recognised as tax income or expense.

IAS 12 specifies disclosures about income taxes.

### ***Recommendations for Software:***

- Surveys on the experience of early IAS adopters have shown deferred taxes, which are not mandatory in all EU states today, to be one of the biggest challenges for early adopters.
- Accounting software should be able to produce results in accordance with both fiscal and economic rules and capture the temporary differences necessary for calculating deferred tax liabilities and assets.

- Fixed Assets should be able to handle multiple books to value assets for both tax and statutory purposes.

## **IAS 14: Segment Reporting**

### ***Introduction***

IAS 14 *Segment Reporting* is applicable for periods beginning on or after 1 July 1998.

IAS 14 prescribes principles for reporting financial information by segment to help users of financial statements:

- better understand the entity's past performance;
- better assess the entity's risks and returns; and
- make more informed judgements about the entity as a whole.

IAS 14 is applied by entities whose equity or debt securities are publicly traded and by entities that are in the process of issuing equity or debt securities in public securities markets. If another entity chooses to disclose segment information in financial statements that comply with international financial reporting standards, it must comply fully with the requirements of IAS 14.

### ***Summary of IAS 14***

An entity reports information for business segments and for geographical segments, indicating the types of products and services included in each reported business segment and the composition of each reported geographical segment.

One basis of segmentation is primary (either business or geographical); the other is secondary. The source and nature of the entity's risks and rates of return determine whether the primary reporting format is business segments or geographical segments. This is usually identified by the entity's internal organisational and management structure and its system of internal financial reporting to senior management.

A business or geographical segment is identified as reportable if a majority of its revenue is earned from sales to external customers and:

- its revenue is 10 per cent or more of total revenue, external and internal, of all segments; or
- its result (either profit or loss) is 10 per cent or more of the combined result of all segments in profit or the combined result of all segments in loss, whichever is the greater in absolute amount; or
- its assets are 10 per cent or more of the total assets of all segments.

Any other segment can be designated as a reportable segment. If total external revenue attributable to reportable segments is less than 75 per cent of the total consolidated revenue, additional segments are identified as reportable segments until at least 75 per cent of total revenue is included in reportable segments.

The following is disclosed for each primary reportable segment:

- Revenue, separately disclosing sales to external customers and inter-segment revenue. The basis of inter-segment pricing is also disclosed;
- Result (before interest and taxes) from continuing operations and separately the result from discontinued operations;
- Carrying amount of segment assets;
- Segment liabilities;
- Cost incurred in the period to acquire property, plant and equipment, and intangibles;
- Depreciation and amortisation charges, and other significant non-cash expenses; or cash flows from operating, investing and financing activities in accordance with IAS 7 *Cash Flow Statements*;
- Aggregate share of the profit or loss of associates, joint ventures, or other investments accounted for under the equity method.

The following is disclosed for each secondary reportable segment:

- Revenue, separately disclosing sales to external customers and inter-segment revenue;
- Carrying amount of segment assets; and
- Cost incurred in the period to acquire property, plant and equipment, and intangibles.

Segment information is prepared in conformity with accounting policies used in preparing and presenting the consolidated financial statements, and is reconciled to these financial statements. There is symmetry between the inclusion of items in segment result and in segment assets.

***Recommendations for Software:***

- Provide the means to associate primary and secondary segment attributes with all accounting information flows.
- Store information in accordance with segment reporting classification requirements.
- Capture all information necessary for reconciling segment level disclosure with totals shown in financial statements.
- Enable full reporting of segment information required by IAS 14:
  - Primary Segment
    - Revenue (external and inter-segment shown separately);
    - Operating result (before interest and taxes);
    - Carrying amount of segment assets;
    - Carrying amount of segment liabilities;
    - Cost to acquire property, plant, equipment, and intangibles;
    - Depreciation and amortisation;
    - Non-cash expenses other than depreciation;
    - Share of profit or loss of equity and joint venture investments;
    - The basis of inter-segment pricing
  - Secondary Segment
    - Revenue (external and inter-segment shown separately);
    - Carrying amount of segment assets;
    - Cost to acquire property, plant, equipment, and intangibles;
    - The basis of inter-segment pricing.
- In an IFRS context, it is highly desirable that software provide features that assist in:
  - Insuring the integrity of segment results
  - Distinguishing between external and inter-segment revenues
  - Reconciling segment results with statement totals.

Intra-segment balancing supports these three objectives

## **IAS 16: Property, Plant and Equipment**

### ***Introduction***

IAS 16 *Property, Plant and Equipment* was issued in December 2003 and is applicable to annual periods beginning on or after 1 January 2005.

IAS 16 prescribes the accounting treatment for property, plant and equipment, unless another standard requires or permits a different accounting treatment. For example,

IFRS 5 *Non-current assets Held for Sale and Discontinued Operations* applies to property, plant and equipment classified as held for sale.

### ***Summary of IAS 16***

Property, plant and equipment is initially recognised at cost. Subsequent to initial recognition, property, plant and equipment is carried either at:

- Cost, less accumulated depreciation and any accumulated impairment losses, or
- Revalued amount, less subsequent accumulated depreciation and any accumulated
- impairment losses. The revalued amount is fair value at the date of revaluation.

The choice of measurement is applied consistency to an entire class of property, plant and equipment. Any revaluation increase is credited directly to the revaluation surplus in equity, unless it reverses a revaluation decrease previously recognised in profit or loss. Any revaluation decrease is recognised in profit or loss. However, the decrease is debited directly to the revaluation surplus in equity to the extent of the credit balance in revaluation surplus in respect of that asset.

Depreciation is applied on a component basis. That is to say, each part of an item of property, plant and equipment with a cost that is significant in relation to the total cost of the item is depreciated separately. The depreciable amount of an asset is allocated on a systematic basis over the useful life of the asset. Impairment is recognised in accordance with IAS 36 *Impairment of Assets*.

The gain or loss on derecognition of an item of property, plant and equipment is the difference between the net disposal proceeds, if any, and the carrying amount of the item. It is included in profit or loss.

IAS 16 specifies disclosures about property, plant and equipment.

### ***Recommendations for Software:***

- Software must enable initial asset recognition as cost, and subsequent measurement at either cost less accumulated depreciation and impairment losses or revaluation on a systematic basis.
- Depreciation methods must be open and customisable in order to reflect the expected consumption of economic benefits
- Should subcomponents of an asset have different expected lives or depreciation treatments, each component must be identified and managed separately, e.g. an aircraft and its engines.
- Software must be able manage different valuations and processing for a given asset in parallel.
- When the revaluation measurement option is adopted, software must:
  - Generate the required accounting entries:
    - Revaluations should be credited to equity (revaluation surplus) unless reversing a previous charge to income.
    - Decreases in valuation should be charged to income unless reversing a previous credit to equity (revaluation surplus)

- If the re-valued asset is sold or otherwise disposed of, any remaining revaluation surplus either remains as a separate component of equity or is transferred directly to retained earnings
- Calculate depreciation subsequent to revaluation on the basis of the revalued asset amount
- Store and maintain system level attributes and information necessary for performing revaluation:
  - Current revaluation surplus
  - History of revaluations
  - Asset carrying amount at depreciated historical cost.
- Provide a facility for revaluing all assets within a class of assets "en mass".
- Provide a complete audit trail of revaluations.
- Enable the re-estimation of expected asset life and residual value

## **IAS 17: Leases**

### ***Introduction***

IAS 17 *Leases* was issued in December 2003 and is applicable to annual periods beginning on or after 1 January 2005.

IAS 17 prescribes, for lessees and lessors, the accounting policies and disclosure to apply to leases.

### ***Summary of IAS 17***

A lease is classified as a finance lease or an operating lease at its inception (i.e. when the agreement or commitment is made). Finance leases are those that transfer substantially all the risks and rewards incident to ownership to the lessee. All other leases are operating leases.

#### **Accounting by lessees**

At inception of the lease, a finance lease is recognised as an asset and a liability in the lessee's balance sheet at the lower of:

- The fair value of the leased asset, and
- The present value of the minimum lease payments.

Any initial direct costs of the lessee are added to the amount recognised as an asset. The minimum lease payments are apportioned between the finance charge and reduction of the outstanding liability. The finance charge represents a constant periodic rate of interest on the outstanding liability. The leased asset is depreciated in accordance with IAS 16 *Property, Plant and Equipment*. If there is no reasonable certainty of eventual ownership, the asset is fully depreciated over the shorter of the lease term and the asset's useful life.

Operating lease payments are recognised as an expense on a straight-line basis over the lease term.

#### **Accounting by lessors**

At inception of the lease, a finance lease is recorded as a receivable at an amount equal to the net investment in the lease. The net investment in the lease is the present value of:

- The minimum lease payments, and
- Any unguaranteed residual value accruing to the lessor. Any initial direct costs incurred by lessors other than manufacturer or dealer lessors are included in the finance lease receivable. Finance income is recognised so as to produce a constant periodic rate of return on the lessor's net investment in the lease. Manufacturer or dealer lessors recognise selling profit or loss in accordance with their policy for outright sales.

Operating lease income is recognised on a straight-line basis over the lease term.

IAS 17 specifies the accounting treatment for sale and leaseback transactions, which is dependent upon the classification of the leaseback as either finance or operating.

IAS 17 specifies disclosures about leases, which are in addition to disclosure required by other standards.

### ***Recommendations for Software:***

#### **Finance Leases - Lessee's Accounting**

- Assets are capitalised and depreciated as a normal asset
- Leases are brought in as a liability.
- Payments are split between interest and reduction of liability – rule of 78 (the calculation for lease interest)

#### **Operating leases – Lessor's Accounting:**

- Assets held for operating leases should be presented in the lessor's balance sheet according to the nature of the asset.

- Lease income should be recognised on a straight-line basis over the lease term, unless another systematic basis is more representative of the pattern of benefit.

N.B. The specialised requirements of leasing companies are outside the scope of the BASDA IFRS recommendations.

## **IAS 18: Revenue**

### ***Introduction***

IAS 18 *Revenue* is applicable for periods beginning on or after 1 January 1995.

IAS 18 prescribes the accounting treatment for revenue arising from:

- the sale of goods;
- the rendering of services; and
- the use by others of entity assets yielding interest, royalties and dividends.
- It does not deal with revenue arising from transactions covered by other Standards (e.g. revenue arising from lease agreements dealt with in IAS 17 *Leases*).

### ***Summary of IAS 18***

Revenue is measured at the fair value of the consideration received or receivable. The consideration is usually cash. If the inflow of cash is significantly deferred, and there is no interest or a below-market rate of interest, the fair value of the consideration is determined by discounting expected future receipts. If dissimilar goods or services are exchanged (as in barter transactions), revenue is the fair value of the goods or services received or, if this is not reliably measurable, the fair value of the goods or services given up.

Revenue from the sale of goods is recognised when:

- significant risks and rewards of ownership are transferred to the buyer;
- the seller has no continuing managerial involvement or control over the goods;
- the amount of revenue can be measured reliably;
- it is probable that economic benefits will flow to the seller; and
- the costs of the transaction (including future costs) can be measured reliably.

Revenue from rendering services is recognised by reference to the stage of completion if the following conditions are satisfied:

- the amount of revenue can be measured reliably;
- it is probable that economic benefits will flow to the service provider;
- the stage of completion of the transaction can be measured reliably; and
- the costs of the transaction (including future costs) can be measured reliably.

If the outcome cannot be measured reliably, revenue is recognised only to the extent of the expenses recognised that are recoverable.

Interest revenue is recognised on a time-proportion basis using the effective interest method.

Royalties are recognised on an accruals basis in accordance with the substance of the relevant agreement.

Dividend revenue is recognised when the shareholder's right to receive the dividend is established.

IAS 18 specifies disclosures about revenue.

### ***Recommendations for Software:***

- Software should respect the accrual principle when recognising revenue.

## **IAS 19: Employee Benefits**

### ***Introduction***

IAS 19 *Employee Benefits* is applicable for periods beginning on or after 1 January 1999.

IAS 19 prescribes the accounting for, and disclosure of employee benefits by employers, except those to which IFRS 2 Share-based Payment applies. IAS 19 does not deal with reporting by employee benefit plans (IAS 26 *Accounting and Reporting by Retirement Benefit Plans*).

### ***Summary of IAS 19***

Employee benefits are all forms of consideration given by an entity in exchange for service rendered by employees. These include:

- short-term benefits: falling due within twelve months of the rendering of service (eg salaries, bonuses, holiday pay, sick pay);
- post-employment benefits: payable after completion of employment (eg pensions, life insurance, medical care);
- other long-term benefits such as long-service leave, and other benefits not payable within twelve months; and
- termination benefits: payable when an employee's contract is terminated either voluntarily or involuntarily (e.g. early retirement, redundancy pay).

#### **Short-term benefits**

Short-term benefits are recognised as an expense in the period when an employee has rendered service to the entity. The expected cost of compensated absences is recognised:

- when the absences occur for non-accumulating compensated absences, and
- when the service is rendered increasing the employee's entitlement to benefits for accumulating compensated absences.

Profit-sharing and bonus payments are recognised when the entity has a present legal or constructive obligation as a result of past events and a reliable estimate can be made of the obligation. A liability is recognised for unpaid short-term benefits.

#### **Post-employment benefits**

Post-employment benefits are classified as either defined contribution or defined benefit plans. Defined contribution plans are those where an employer pays fixed contributions into a separate entity and will have no legal or constructive obligation to pay further contributions. All other post-employment benefits are defined benefit plans.

Contributions payable to a defined contribution plan are recognised as an expense as the employee renders service to the entity.

For a defined benefit plan, an entity recognises a net defined benefit asset or liability comprising the present value of the defined benefit obligations at the balance sheet date, based on actuarial assumptions, net of the fair value of any plan assets at the balance sheet date. IAS 19 encourages the involvement of a qualified actuary in measuring defined benefit obligations, which are valued using the projected unit credit method. There is a limit on the recognition of a net defined benefit asset.

Actuarial gains and losses (comprising experience adjustments and the effects of changes in actuarial assumptions) are recognised immediately as income or expense to the extent that they exceed 10 per cent of the defined benefit obligation or 10 per cent of the fair value of plan assets. An entity can elect to recognise all actuarial gains and losses immediately. Any unrecognised actuarial gains and losses are included as part of the net defined benefit asset or liability.

Past service cost is recognised as an expense on a straight-line basis over the average period until the benefits become vested; any unvested past service cost not recognised is included as part of the net defined benefit asset or liability. Past service cost is the increase in the

defined benefit obligation for employee service in prior periods, resulting in the current period from the introduction of, or change to, a defined benefit plan.

Movements in the amount of the net defined benefit asset or liability is recognised in profit or loss as a net pension expense or income. The effects of a curtailment or settlement of a plan on the defined benefit obligation and plan assets are recognised when the curtailment or settlement occurs.

#### **Other long-term benefits**

An entity recognises a liability for other long-term benefits equal to the present value of the defined benefit obligation, minus the fair value of any plan assets at the balance sheet date. Any actuarial gains and losses, or past service costs are recognised as income or expense immediately.

#### **Termination benefits**

An entity recognises a liability and an expense for termination benefits when it is demonstrably committed to either:

- terminate the employment of employee(s) before the normal retirement date; or
- provide termination benefits as a result of an offer made in order to encourage voluntary redundancy.

An entity is demonstrably committed when it has a detailed formal plan for the termination and is without realistic possibility of withdrawal.

IAS 19 specifies disclosures about employee benefits.

#### ***Recommendations for Software:***

Although accounting for post-employment benefit plans and share based payments will pose challenges, solutions are likely to require specialized software that is beyond the scope of this White Paper

## **IAS 20: Accounting for Government Grants and Disclosure of Government Assistance**

### ***Introduction***

IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance* is applicable for periods beginning on or after 1 January 1984.

IAS 20 prescribes the accounting for, and disclosure of, government grants and the disclosure of other forms of government assistance.

IAS 20 does not deal with:

- Government assistance that is provided in the form of benefits that are available in determining taxable income
- Government participation in the ownership of an entity;
- Government grants covered by IAS 41 *Agriculture*.

### ***Summary of IAS 20***

A government grant is not recognised until there is reasonable assurance that:

- the entity will comply with the conditions attached to it; and
- the grant will be received.

A government grant is recognised as income on a systematic basis over the periods necessary to match the grant income with the related costs that it is intended to compensate. If the related costs have already been incurred, the grant is recognised as income in the period in which it becomes receivable. A government grant is not credited directly to equity.

Government grants related to assets are presented in the balance sheet either as deferred income or as a deduction in determining the carrying amount of the asset.

A government grant that becomes repayable is accounted for as a revision to an accounting estimate (IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*).

IAS 20 specifies disclosures about government grants and other forms of government assistance.

### ***Recommendations for Software:***

A means of matching revenue recognition from grants to periods in which related costs are incurred would provide value in vertical markets where grants are prevalent (government, education, etc.)

## **IAS 21: The Effects of Changes in Foreign Exchange Rates**

### ***Introduction***

IAS 21 *The Effects of Changes in Foreign Exchange Rates* was issued in December 2003 and is applicable for annual periods beginning on or after 1 January 2005.

IAS 21 prescribes how to include foreign currency transactions and foreign operations in the financial statements of an entity and how to translate financial statements into a presentation currency. IAS 21 does not apply to foreign currency derivatives and hedge accounting of foreign currency items covered by IAS 39 *Financial Instruments: Recognition and Measurement*.

### ***Summary of IAS 21***

#### **Foreign Currency Transactions**

A foreign currency transaction is recorded initially 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. For practical reasons, a rate that approximates the actual rate at the date of the transaction is often used (eg an average weekly or monthly rate). Functional currency is the currency of the primary economic environment in which the entity operates.

At each balance sheet date:

- Foreign currency monetary items are translated using the closing rate;
- Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction; and
- Non-monetary items that are measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

Exchange differences arising on the settlement of monetary items or on translating monetary items at rates different from those at initial recognition are recognised in profit or loss with one exception. Exchange differences arising on a monetary item that forms part of an entity's net investment in a foreign operation are recognised as a separate component of equity in the financial statements that include the foreign operation and the reporting entity (eg financial statements in which the foreign operation is consolidated, proportionately consolidated or accounted for using the equity method). Such exchange differences are recognised in profit or loss on disposal of the net investment.

#### **Foreign Operations**

When translating a foreign operation for inclusion in the reporting entity's financial statements (i.e. translation to a presentation currency), assets and liabilities are translated at the closing rate, and income and expenses are translated at exchange rates at the dates of the transactions. All resulting exchange differences are recognised as a separate component of equity.

On disposal of the foreign operation, all exchange differences deferred in the separate component of equity relating to that operation, are recognised in profit or loss.

IAS 21 specifies disclosures about the functional currency of an entity, and exchange differences arising during the period.

### ***Recommendations for Software:***

When transactions are initially recorded, software must:

- Convert amounts denominated in foreign currency to an entity's functional currency using the rate effective on the date of transaction (spot rate) or a reasonable approximation thereof (e.g. an average weekly or monthly rate)
- At the end of an accounting period, software must:
- Revalue open monetary amounts at the period close rate

- Revalue non-monetary items measured at fair value in a foreign currency at the rate effective when the fair value was determined.
- Post exchange differences between the historical and re-valued amounts as currency gains or losses for disclosure in the income statement.

When foreign operations are translated into presentation currency for inclusion in a reporting entity's consolidated financial statements software must:

- Translate assets and liabilities using the period end rate except where a historical rates is more appropriate.
- Translate income and expense using period average rates
- Recognize resulting exchange differences as a separate component of equity.

All foreign currency conversions, revaluations and adjustments should retain a clear audit trail with system level attributes (currencies, amounts, rates, rate types, rate dates, ...) in order to fully explain foreign currency processing, including scenarios where local and translated currencies differ from the group presentation currency.

## **IAS 23: Borrowing Costs**

### ***Introduction***

IAS 23 *Borrowing Costs* is applicable for periods beginning on or after 1 January 1995.

IAS 23 prescribes the accounting treatment for borrowing costs. Borrowing costs are interest and other costs incurred by an entity in connection with the borrowing of funds.

### ***Summary of IAS 23***

Borrowings costs are recognised as an expense when incurred.

As an alternative, borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset (i.e. an asset that takes a substantial period of time to get ready for its intended use or sale) are capitalised as part of the cost of that asset.

Capitalisation of borrowing costs as part of the cost of an asset commences when:

- expenditures for the asset are being incurred;
- borrowing costs are being incurred; and
- activities to prepare the asset for its intended use or sale are in progress.

Capitalisation of borrowing costs ceases when substantially all the activities necessary to prepare the asset for its intended use or sale are complete.

IAS 23 specifies disclosures about borrowing costs.

### ***Recommendations for Software:***

Software should enable adjustments to assets or long-term projects to enable capitalization of borrowing costs.

## **IAS 24: Related Party Disclosures**

### ***Introduction***

IAS 24 *Related Party Disclosures* was issued in December 2003 and is applicable for annual periods beginning on or after 1 January 2005.

IAS 24 prescribes the disclosures necessary to draw attention to the possibility that the financial position and profit or loss of an entity may have been affected by the existence of related parties and by transactions and outstanding balances with such parties.

### ***Summary of IAS 24***

A party is related to an entity if it:

- directly or indirectly, controls, is controlled by, or is under common control with, the entity;
- has significant influence over the entity;
- has joint control over the entity;
- is a close member of the family of any individual who controls, or has significant influence or joint control over, the entity;
- is an associate of the entity;
- is a joint venture in which the entity is a venturer;
- is a member of the key management personnel of the entity or its parent;
- is a close member of the family of any of the aforementioned key management personnel;
- is an entity that is controlled, jointly controlled or significantly influenced by, or for which significant voting power in such entity resides with, any of the key management personnel or their close family members;
- is a post-employment benefit plan for the benefit of employees of the entity, or of any of its related parties.

IAS 24 requires the following related party disclosures:

- Nature of relationships between parents and subsidiaries, even if there were no transactions between those related parties;
- The name of the entity's parent and, if different, the ultimate controlling party;
- Compensation of key management personnel;
- If there have been transactions between related parties, the nature of the relationship and information about the transactions and outstanding balances with related parties. Such disclosures are made separately for each of the following categories: the parent; entities with joint control or significant influence over the entity; subsidiaries; associates; joint ventures in which the entity is a venturer; management personnel; and other related parties.

### ***Recommendations for Software:***

As arrangements between third parties and corporate entities vary considerably, there are no specific recommendations for business applications beyond a need for sound auditing trails and procedures to insure corporate governance.

## **IAS 26: Accounting and Reporting by Retirement Benefit Plans**

### ***Introduction***

IAS 26 *Accounting and Reporting by Retirement Benefit Plans* is applicable for periods beginning on or after 1 January 1988.

IAS 26 applies to the financial statements of retirement benefit plans. Retirement benefit plans are arrangements whereby an entity provides benefits for employees on or after termination of service 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 practices.

### ***Summary of IAS 26***

The financial statements of a defined contribution plan contain a statement of net assets available for benefits and a description of the funding policy. The financial statements of a defined benefit plan contain either:

- a statement that shows:
  - the net assets available for benefits;
  - the actuarial present value of promised retirement benefits, distinguishing
    - between vested and non-vested benefits; and
    - the resulting excess or deficit; or
- a statement of net assets available for benefits including either:
  - a note disclosing the actuarial present value of promised retirement benefits, distinguishing between vested and non-vested benefits; or
  - a reference to this information in an accompanying actuarial report.

The actuarial present value of promised retirement benefits is based on the benefits promised under the terms of the plan on service rendered to date using either current salary levels or projected salary levels. Retirement benefit plan investments are carried at fair value.

IAS 26 specifies disclosures in the financial statements of retirement benefit plans.

### ***Recommendations for Software:***

Solutions are likely to require specialized software that is beyond the scope of this white paper

## **IAS 27: Consolidated and Separate Financial Statements**

### ***Introduction***

IAS 27 *Consolidated and Separate Financial Statements* was issued in December 2003 and is applicable to annual periods beginning on or after 1 January 2005.

IAS 27 applies to the preparation and presentation of consolidated financial statements for a group of entities under the control of a parent. It also applies to accounting for investments in subsidiaries, jointly controlled entities and associates in the separate financial statements of a parent.

### ***Summary of IAS 27***

A parent presents consolidated financial statements in which it consolidates its investment in subsidiaries (those entities that it controls), unless certain conditions are met allowing it not to prepare consolidated financial statements. The consolidated financial statements are prepared using uniform accounting policies. The reporting date of the parent and its subsidiaries shall not be more than 3 months apart.

When separate financial statements are prepared, investment in subsidiaries, jointly controlled entities and associates should be accounted for either at cost or in accordance with IAS 39. The same accounting should be applied for each category of investments.

IAS 27 specifies disclosures to be made in consolidated and separate financial statements.

### ***Recommendations for Software:***

The system must provide a facility to collect information relating to ownership such that the system can determine if the entity is a subsidiary company as defined in IAS 27.

Subsidiary company definition may be defined based on share ownership or effective management control, both methods must be facilitated.

Provide facilities to automatically calculate any minority interest in the entity together with facilities to eliminate this on consolidation.

The system must provide that the ownership calculation recognises that the share holding or effective control may vary over time.

## **IAS 28: Investment in Associates**

### ***Introduction***

IAS 28 *Investment in Associates* was issued in December 2003 and is applicable to annual periods beginning on or after 1 January 2005.

IAS 28 applies in accounting for investments in associates, except those held by:

- Venture capital organisations, or
- Mutual funds, unit trusts and similar entities including investment-linked insurance funds

that upon initial recognition are designated as at fair value through profit or loss or are classified as held for trading and accounted for in accordance with IAS 39 *Financial Instruments: Recognition and Measurement*.

### ***Summary of IAS 28***

An associate is an entity over which the investor has significant influence and that is neither a subsidiary nor an interest in a joint venture. Significant influence is the power to participate in financial and operating policy decisions of the investee but is not control or joint control over those policies. Such influence is presumed to exist if the investor owns 20 per cent or more of the voting power of the investee.

An investment in an associate is accounted for using the equity method. The equity method is not used when:

- The investment is classified as held for sale in accordance with IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*; or
- The investor is itself a subsidiary, its owners do not object to the equity method not being applied, and its debt and equity securities are not publicly traded. In this case the investor's parent must present consolidated financial statements that comply with IFRSs.

The investor's financial statements are prepared using uniform accounting policies for like transactions and events in similar circumstances. Any difference between the reporting date of the investor and its associate must not be more than 3 months.

An investor discontinues the equity method from the date that it ceases to have significant influence over the associate. From that date it accounts for the investment in accordance with IAS 39, provided the associate does not become a subsidiary or a joint venture as defined in IAS 31.

IAS 28 specifies disclosures to be made in the investor's financial statements about associates.

### ***Recommendations for Software:***

The system must provide a facility to collect information relating to ownership such that the system can determine if the entity is an associated company as defined in IAS 28

Associated company definition may be defined based on share ownership or effective management control, both methods must be facilitated.

Provide facilities to automatically calculate the holding companies interest in profit and thereby provide for proper equity accounting entries.

The system must provide that the ownership calculation recognises that the share holding or effective control may vary over time.

## **IAS 29: Financial Reporting in Hyperinflationary Economies**

### ***Introduction***

IAS 29 *Financial Reporting in Hyperinflationary Economies* is applicable for periods beginning on or after 1 January 1990.

IAS 29 applies to the financial statements, including the consolidated financial statements, of any entity whose functional currency is the currency of a hyperinflationary economy. Hyperinflation is indicated by characteristics of the economic environment of a country, which include, amongst others, the cumulative inflation rate over three years is approaching, or exceeds, 100 per cent.

### ***Summary of IAS 29***

When an entity's functional currency is the currency of a hyperinflationary economy, the financial statements are stated in terms of the measuring unit current at the balance sheet date. Comparative amounts for prior periods should also be stated in the measuring unit current at the balance sheet date. The gain or loss on the net monetary position is included in profit or loss.

When an economy ceases to be hyperinflationary, an entity discontinues the preparation and presentation of financial statements in accordance with IAS 29. The amounts expressed in the measuring unit current at the end of the previous reporting period are treated as the basis for the carrying amounts in its subsequent financial statements.

IAS 29 specifies disclosures about the effects of a hyperinflationary economy on an entity's financial statements.

### ***Recommendations for Software:***

- Enable the restatement of financial statements in accordance with the provisions of IAS 29 in cases of economic hyperinflation.

The local (hyperinflationary) currency is the measurement currency; the alternate currency is the presentation currency (usually the US Dollar or the Euro) at the spot rate on the balance sheet date

## **IAS 30: Disclosures in the financial statements of Banks and similar financial institutions**

### ***Introduction***

IAS 30 *Disclosures in the Financial Statements of Banks and Similar Financial Institutions* is applicable in the financial statements of banks and similar financial institutions for periods beginning on or after 1 January 1991.

### ***Summary of IAS 30***

A bank presents an income statement that groups income and expenses by nature and discloses the amounts of the principal types of income and expenses. Disclosures of specific items of income and expenses are prescribed. Income and expense items are not offset except:

- those relating to hedges; and
- assets and liabilities that have been offset in accordance with IAS 32 *Financial Instruments: Disclosure and Presentation*.

A bank presents a balance sheet that groups assets and liabilities by nature and lists them in an order that reflects their relative liquidity. Disclosures of specific assets and liabilities are prescribed.

Disclosure is required of various kinds of contingencies and commitments, including off-balance-sheet items. Disclosure is required of information relating to losses on loans and advances. Other disclosure requirements include:

- The fair value of each class of financial assets and financial liabilities;
- Maturities of assets and liabilities based on the remaining period at the balance sheet date to the contractual maturity date;
- Concentrations of assets, liabilities, and off-balance-sheet items (by geographical area, customer or industry groups, or other aspects of risk);
- Amounts set aside for general banking risks, including future losses and other unforeseeable risks or contingencies disclosed separately as appropriations of retained earnings;
- Secured liabilities and nature and amount of assets pledged as security.

### ***Recommendations for Software:***

The specialised requirements of banks and similar institutions are outside the scope of the BASDA IFRS Standard.

## **IAS 31: Interests in Joint Ventures**

### ***Introduction***

IAS 31 *Interests in Joint Ventures* was issued in December 2003 and is applicable to annual periods beginning on or after 1 January 2005.

IAS 31 applies in accounting for interests in joint ventures and the reporting of joint venture assets, liabilities, income and expenses in the financial statements of venturers, regardless of the structures or forms under which the joint venture activities take place.

IAS 31 does not apply to interests in jointly controlled entities held by:

- Venture capital organisations, or
- Mutual funds, unit trusts and similar entities including investment-linked insurance funds

that upon initial recognition are designated as at fair value through profit or loss or are classified as held for trading and accounted for in accordance with IAS 39 *Financial Instruments: Recognition and Measurement*.

### ***Summary of IAS 31***

A joint venture is a contractual arrangement whereby two or more parties undertake an economic activity that is subject to joint control. These are of three types:

- Jointly controlled operations
- Jointly controlled assets
- Jointly controlled entities.

Joint control exists only when the strategic financial and operating decisions relating to the economic activity require the unanimous consent of the parties sharing control.

A venturer recognises its interest in a jointly controlled operation by recognising in its financial statements the assets that it controls, the liabilities and expenses that it incurs, and its share of the income that it earns from the sale of goods or services by the joint venture.

A venturer recognises its interest in jointly controlled assets on a proportional basis. It also recognises any liabilities or expenses it incurs, its share of liabilities or expenses incurred jointly, and any income from the sale or use of its share of the output of the joint venture.

A venturer recognises its interest in a jointly controlled entity using either proportionate consolidation or the equity method in accordance with IAS 28 *Investment in Associates*. Proportionate consolidation or the equity method is not used when:

- The investment is classified as held for sale in accordance with IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*; or
- The venturer is itself a subsidiary, its owners do not object to proportionate consolidation or the equity method not being applied, and its debt and equity securities are not publicly traded. In this case the venturer's parent must present consolidated financial statements that comply with IFRSs.

A venturer discontinues proportionate consolidation from the date that it ceases to have joint control over a jointly controlled entity. A venturer discontinues the equity method, from the date that it ceases to have joint control over, or significant influence in, a jointly controlled entity.

When a venturer transfers assets to a joint venture, the venturer recognises only the portion of the profit or loss that is attributable to the interests of the other venturers. When a venturer purchases assets from a joint venture, the venturer does not recognise its share of the joint venture's profit or loss from the transaction until it resells the assets to an independent third party. A loss on transactions between a venturer and a joint venture may provide evidence of a reduction in the net realisable value of current assets or an impairment loss. In such cases the loss is recognised immediately.

IAS 31 specifies disclosures to be made in venturer's financial statements about joint ventures.

***Recommendations for Software:***

- Consolidation software should enable joint ventures to be consolidated under the benchmark treatment (proportionate consolidation) as well as the allowed alternative (equity method)

## **IAS 32: Financial Instruments: Disclosure and Presentation**

### ***Introduction***

IAS 32 *Financial Instruments: Disclosure and Presentation* was issued in December 2003 and is applicable for annual periods beginning on or after 1 January 2005.

IAS 32 is intended to enhance financial statement users' understanding of the significance of financial instruments to an entity's financial position, performance and cash flows. It prescribes requirements for the presentation of financial instruments and identifies information that should be disclosed about them.

IAS 32 applies to all types of financial instruments except:

- those interests in subsidiaries, associates and joint ventures that are consolidated, or are accounted for using the equity method or proportionate consolidation in accordance with IAS 27 *Consolidated and Separate Financial Statements*, IAS 28 *Investment in Associates* or IAS 31 *Interests in Joint Ventures*;
- employers' rights and obligations under employee benefit plans (IAS 19 *Employee Benefits*);
- contracts for contingent consideration in a business combination (IFRS 3 *Business Combinations*);
- insurance contract as defined by IFRS 4 *Insurance Contracts*;
- financial instruments that are within the scope of IFRS 4 *Insurance Contracts* because they contain a discretionary participation feature; and
- financial instruments, contracts and obligations under share-based payment transactions (IFRS 2 *Share Based Payment*).

### ***Summary of IAS 32***

Financial instruments are classified, from the perspective of the issuer, as financial assets, financial liabilities and equity instruments. Compound financial instruments may contain both a liability and an equity component.

Interest, dividends, losses and gains relating to financial liabilities are recognised as income or expense in profit or loss. Distributions to holders of equity instruments are debited directly to equity, net of any related income tax benefit.

Financial assets and financial liabilities are offset when and only when there is a legally enforceable right to set off and the entity intends to settle on a net basis.

IAS 32 requires disclosure about factors that affect the amount, timing and certainty of an entity's future cash flows relating to financial instruments and the accounting policies applied to those instruments. It also requires disclosure about the nature and extent of an entity's use of financial instruments, the business purposes they serve, the risks associated with them, and management's policies for controlling those risks.

The principles in IAS 32 complement the principles for recognising and measuring financial assets and financial liabilities in IAS 39 *Financial Instruments: Recognition and Measurement*.

### ***Recommendations for Software:***

General business Software must provide flexible means of classifying financial instruments and related operations in statements of financial position, performance, and cash flows – however much of the underlying processing will be performed in specialized systems beyond the scope of this document.

Software must be able to store information and disclose information according to 'on and off balance sheet classification'

## **IAS 33: Earnings per Share**

### ***Introduction***

IAS 33 *Earnings per Share* was issued in December 2003 and is applicable for annual periods beginning on or after 1 January 2005.

IAS 33 prescribes principles for the determination and presentation of earnings per share, so as to improve performance comparisons between different reporting entities in the same reporting period and between different reporting periods for the same entity.

IAS 33 is applied by entities whose ordinary shares or potential ordinary shares are publicly traded and by entities that are in the process of issuing ordinary shares or potential ordinary shares in public markets. If another entity chooses to disclose earnings per share information, such information is calculated and disclosed in accordance with IAS 33.

### ***Summary of IAS 33***

An entity presents on the face of the income statement basic and diluted earnings per share for each class of ordinary shares that has a different right to share in profit for the period. An entity calculates basic and diluted earnings per share for profit or loss from continuing operations attributable to the ordinary equity holders of the parent entity. If an entity reports a discontinued operation, it also discloses basic and diluted earnings per share for the discontinued operation.

#### **Basic Earnings per Share**

Basic earnings per share is calculated by dividing profit or loss attributable to ordinary equity holders of the parent entity (the numerator) by the weighted average number of ordinary shares outstanding (the denominator) during the period.

The profit or loss attributable to the parent entity is adjusted for the after-tax amounts of preference dividends, differences arising on the settlement of preference shares, and other similar effects of preference shares classified as equity.

The weighted average number of ordinary shares outstanding during the period and for all periods presented is adjusted for events, other than the conversion of potential ordinary shares, that have changed the number of ordinary shares outstanding without a corresponding change in resources (e.g. a bonus issue, a share split).

#### **Diluted Earnings per Share**

Diluted earnings per share is calculated by adjusting the profit or loss attributable to ordinary equity holders of the parent entity, and the weighted average number of ordinary shares outstanding, for the effects of all dilutive potential ordinary shares.

The profit or loss attributable to ordinary equity holders of the parent entity, as calculated for basic earnings per share, is adjusted for the after-tax effects of:

- any dividends or other items related to dilutive potential ordinary shares deducted in arriving at profit or loss attributable to ordinary equity holders;
- any interest recognised in the period related to dilutive potential ordinary shares; and
- any other changes in income or expense that would result from the conversion of the dilutive potential ordinary shares.

The number of ordinary shares is the weighted average number of ordinary shares outstanding, as calculated for basic earnings per share, plus the weighted average number of ordinary shares that would be issued on the conversion of all the dilutive potential ordinary shares into ordinary shares. Potential ordinary shares are treated as dilutive when their conversion to ordinary shares would decrease earnings per share or increase loss per share from continuing operations (e.g. options and warrants, convertible instruments, contingently issuable shares).

IAS 33 specifies disclosures about earnings per share information.

***Recommendations for Software:***

Will generally be undertaken by specialized software packages or manual calculations.

## **IAS 34: Interim Financial Reporting**

### ***Introduction***

IAS 34 *Interim Financial Reporting* is applicable for periods beginning on or after 1 January 1999.

IAS 34 prescribes the minimum content of an interim financial report and the principles for recognition and measurement in any interim financial statements.

IAS 34 does not specify which entities must publish interim financial reports, how frequently, or how soon after the end of an interim period. Those are matters that are usually specified by law or regulation. IAS 34 applies if an entity is required or elects to publish an interim financial report in accordance with International Financial Reporting Standards.

### ***Summary of IAS 34***

IAS 34 defines the minimum content of an interim financial report as a condensed balance sheet, condensed income statement, condensed statement showing changes in equity, condensed cash flow statement, and selected explanatory notes.

Interim financial statements covers the following periods:

- A balance sheet at the end of the current interim period, and a comparative balance sheet as of the end of the most recent full financial year;
- Income statements for the current interim period and cumulatively for the current financial year to date, with comparative income statements for the comparable interim periods of the immediately preceding financial year;
- A statement of changes in equity cumulatively for the current financial year to date, and a comparative statement for the comparable year-to-date period of the prior year; and
- A cash flow statement cumulatively for the current financial year to date, and a comparative statement for the comparable year-to-date period of the prior financial year.

The notes to the interim financial statements are viewed primarily as an update since the last annual report. The notes required include disclosures about changes in accounting policies, seasonality or cyclicity, changes in estimates, changes in outstanding debt or equity, dividends, segment revenue and result, events occurring after balance sheet date, acquisition or disposal of subsidiaries and long-term investments, restructurings, discontinuing operations, and changes in contingent liabilities or contingent assets.

An entity applies the same accounting policies in its interim financial statements as in its latest annual financial statements. Measurements for interim reporting purposes are made on a year-to-date basis. The interim financial report includes a statement of compliance with IAS 34.

IAS 34 specifies disclosures required in interim financial statements.

### ***Recommendations for Software:***

- Reinforced emphasis on interim reporting and shortened report cycles heightens the need for responsive business intelligence tools in order to produce and audit results in an efficient manor.
- Requirement to specify comparative periods.

## **IAS 36: Impairment of Assets**

### ***Introduction***

IAS 36 *Impairment of Assets* was issued in March 2004. It is applied to goodwill and intangible assets acquired in business combinations after 31 March 2004, and to all other assets for annual periods beginning on or after 31 March 2004.

IAS 36 prescribes the procedures that an entity applies to ensure that its assets are carried at no more than their recoverable amount. IAS 36 applies in accounting for impairment of all assets other than:

- inventories (IAS 2 *Inventories*);
- assets arising from construction contracts (IAS 11 *Construction Contracts*);
- deferred tax assets (IAS 12 *Income Taxes*);
- assets arising from employee benefits (IAS 19 *Employee Benefits*);
- financial assets within the scope of IAS 39 *Financial Instruments: Recognition and Measurement*;
- investment property measured at fair value (IAS 40 *Investment Property*);
- biological assets related to agricultural activity that are measured at fair value less estimated point-of-sale costs (IAS 41 *Agriculture*);
- deferred acquisition costs and intangible assets, arising from insurance contracts within the scope of IFRS 4 *Insurance Contracts*; and
- non-current assets (or disposal groups) classified as held for sale in accordance with IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*.

### ***Summary of IAS 36***

The recoverable amount of an asset is measured whenever there is an indication that the asset may be impaired. At each reporting date, an entity assesses whether there is any indication that an asset may be impaired. In addition, the recoverable amount of the following assets is measured annually:

- an intangible asset with an indefinite useful life;
- an intangible asset not yet available for use; and
- goodwill.

The recoverable amount of an asset is the higher of its fair value less costs to sell and its value in use. 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. Value in use is the present value of the future cash flows expected to be derived from an asset.

Recoverable amount is determined for an individual asset. However, if the asset does not generate cash inflows that are largely independent of those from other assets, the recoverable amount is determined for the cash-generating unit to which the asset belongs. A cash-generating unit is 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.

For the purpose of impairment testing, goodwill acquired in a business combination is allocated to each of the cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the combination.

An impairment loss, being the carrying amount of an asset less its recoverable amount, is recognised immediately in profit or loss. If the asset is revalued in accordance with another Standard (e.g. an item of property, plant and equipment in accordance with IAS 16 *Property, Plant and Equipment*), the impairment loss is treated as a revaluation decrease in accordance with that other standard. An impairment loss for a cash-generating unit is allocated to reduce the carrying amount of the assets of the unit in the following order:

1. reduce the carrying amount of any goodwill allocated to the cash-generating unit, and then,
2. reduce the other assets of the unit pro rata on the basis of the carrying amount of each asset.

An impairment loss recognised in prior periods is reversed if there is a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised. In this case, the carrying amount of the asset is increased to its recoverable amount, but not exceeding the carrying amount of the asset that would have been determined had no impairment loss been recognised in prior years. Goodwill impairment must not be reversed.

IAS 36 specifies disclosures about impairment of assets and cash-generating units, and the allocation of goodwill acquired in a business combination to cash-generating units.

***Recommendations for Software:***

- Software should be capable of being able to recognize impairment for individual assets or asset groupings associated with a Cash Generating Unit (CGU)
- As impairment may well apply to a subset of assets, for example business sector or geography, software should offer flexible means for identifying subgroups of assets for impairment processing.
- Software should enable parallel depreciation of assets, with and without impairment.
- When the recoverable amount of an asset is less than its carrying amount, software should generate the required accounting entries:
  - An impairment loss should be recognised in the income statement for assets carried at cost and treated as a revaluation decrease for assets carried at revalued amount
  - An impairment loss should be reversed (and income recognised) when there is a positive reassessment of an asset's recoverable amount subsequent to the recognition of impairment loss
  - However, an impairment loss should only be reversed to the extent the reversal does not increase the carrying amount of the asset above the carrying amount that would have been determined for the asset (net of amortisation or depreciation) had no impairment loss been recognised.
- Software should store and maintain system level attributes and necessary information for performing revaluation:

## **IAS 37: Provisions, Contingent Liabilities and Contingent Assets**

### ***Introduction***

IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* was issued in July 1998 and is applicable for periods beginning on or after 1 July 1999.

IAS 37 prescribes the accounting and disclosure for provisions, contingent liabilities and contingent assets, other than:

- those resulting from executory contracts, except where the contract is onerous; and
- those covered by another Standard, including:
  - contingent liabilities assumed in a business combinations (IFRS 3 *Business Combinations*);
  - provisions with regard to
    - construction contracts (IAS 11 *Construction Contracts*);
    - income taxes (IAS 12 *Income Taxes*);
    - leases (IAS 17 *Leases*);
    - employee benefits (IAS 19 *Employee Benefits*); and
    - insurance contracts (IFRS 4 *Insurance Contracts*).

IAS 37 does not apply to financial instruments (including guarantees) within the scope of IAS 39 *Financial instruments: Recognition and Measurement*.

### ***Summary of IAS 37***

A provision is a liability of uncertain timing or amount. Examples of provisions are: warranty obligations; legal or constructive obligations to clean up contaminated land or restore facilities; and a retailer's policy to refund customers.

A provision is recognised when:

- an entity has a present obligation (legal or constructive) as a result of a past event;
- it is probable that an outflow of economic benefits will be required to settle the obligation; and
- a reliable estimate can be made of the amount of the obligation. A constructive obligation arises from the entity's actions, through which it has indicated to others that it will accept certain responsibilities, and as a result has created an expectation that it will discharge those responsibilities.

The amount recognised as a provision is the best estimate of the expenditure required to settle the obligation at the balance sheet date. Provisions are reviewed at each balance sheet date and adjusted to the current best estimate. A provision is used only for expenditures for which the provision was originally recognised.

Provisions are not recognised for future operating losses. If the entity has a contract that is onerous, the present obligation under the contract is recognised as a provision.

A constructive obligation to restructure arises only when an entity:

- has a detailed formal plan for the restructuring; and
- 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.

A contingent liability is not recognised, but is disclosed unless the possibility of an outflow of resources is remote.

A contingent asset is not recognised, but is disclosed when an inflow of economic benefits is probable.

IAS 37 specifies disclosures about provisions, contingent liabilities and contingent assets.

***Recommendations for Software:***

Increased scrutiny and disclosure requirements for obligations under IAS 37 will create additional work load that is largely outside of the scope of automated software processes.

## **IAS 38: Intangible Assets**

### ***Introduction***

IAS 38 *Intangible Assets* was issued in March 2004 and is applied to the accounting for intangible assets acquired in business combinations after 31 March 2004, and to all other intangible assets for annual periods beginning on or after 31 March 2004.

IAS 38 prescribes the accounting treatment for intangible assets, except:

- intangible assets that are within the scope of another Standard. For example, IAS 2 *Inventories* applies to intangible assets held for sale in the ordinary course of business;
- mineral rights and expenditure on exploration for, or development and extraction of non-regenerative resources.

### ***Summary of IAS 38***

An intangible asset is initially recognised at cost if all of the following criteria are met:

- the asset meets the definition of an intangible asset i.e. it is identifiable and controlled by the entity;
- it is probable that future economic benefits that are attributable to the asset will flow to the entity; and
- the cost of the asset can be measured reliably.

Internally generated goodwill, brands, mastheads, publishing titles, customer lists and similar items are not recognised as assets. Expenditure on research is recognised as an expense. There is no recognition of an intangible asset arising from research. An intangible asset arising from development is recognised only if specified criteria are met.

If an intangible item does not meet the criteria for recognition as an asset, the expenditure is recognised as an expense when incurred. Expenditure that was initially recognised as an expense is not included in the cost of an intangible asset at a later date.

Subsequent to initial recognition, an intangible asset is carried at:

- cost, less any accumulated amortisation and any accumulated impairment losses; or
- revalued amount, less any subsequent accumulated amortisation and any accumulated impairment losses. The revalued amount is fair value at the date of revaluation and is determined by reference to an active market.

An intangible asset can only be carried at revalued amount if there is an active market for the asset. Any revaluation increase is credited directly to equity as revaluation surplus, unless it reverses a revaluation decrease of the same asset previously recognised in profit or loss. Any revaluation decrease is recognised in profit or loss. However, the decrease is debited directly to the revaluation surplus in equity to the extent of any credit balance in revaluation surplus in respect of that asset.

An entity assesses whether the useful life of an intangible asset is finite or indefinite; the useful life is indefinite if there is no foreseeable limit to the period over which the asset is expected to generate net cash flows. The depreciable amount of an intangible asset with a finite life is amortised on a systematic basis over its useful life. An intangible asset with an indefinite useful life is not amortised, but is tested for impairment at least annually. Impairment of intangible assets is recognised in accordance with IAS 36 *Impairment of Assets*.

The gain or loss on derecognition of an intangible asset is the difference between the net disposal proceeds, if any, and the carrying amount of the item. The gain or loss is recognised in profit or loss.

IAS 38 specifies disclosures about intangible assets.

### ***Recommendations for Software:***

Increased scrutiny and disclosure requirements for intangible assets will create additional work load that is largely outside of the scope of automated software processes.

## **IAS 39: Financial Instruments: Recognition and Measurement**

### ***Introduction***

IAS 39 *Financial Instruments: Recognition and Measurement* was issued in December 2003 and is applicable for annual periods beginning on or after 1 January 2005.

IAS 39 prescribes principles for recognising and measuring all types of financial instruments except:

- those interests in subsidiaries, associates and joint ventures that are consolidated, or are accounted for using the equity method or proportionate consolidation in accordance with IAS 27 *Consolidated and Separate Financial Statements*, IAS 28 *Investment in Associates* or IAS 31 *Interests in Joint Ventures*;
- rights and obligations under leases (IAS 17 *Leases*). However:
  - lease receivables recognised by a lessor are subject to the derecognition And
  - impairment provisions of IAS 39;
  - finance lease payables recognised by a lessee are subject to the
  - derecognition provisions of IAS 39; and
  - derivatives that are embedded in leases are subject to the embedded
  - derivatives provisions of IAS 39.
- employers' rights and obligations under employee benefit plans (IAS 19 *Employee Benefits*);
- financial instruments issued by the entity that meet the definition of an equity instrument in IAS 32 (including options and warrants).
- rights and obligations under an insurance contracts as defined by IFRS 4 *Insurance Contracts*, and under a contract that is within IFRS 4 because it contains a discretionary participation feature. However, IAS 39 applies to derivatives embedded in such a contract;
- contracts for contingent consideration in a business combination (IFRS 3 *Business Combinations*);
- contracts between an acquirer and a vendor in a business combination to buy or sell an acquiree at a future date;
- loan commitments that cannot be settled net in cash or another financial instrument (except those that are designated as financial liabilities at fair value through profit or loss); and
- financial instruments, contracts and obligations under share-based payment transactions (IFRS 2 *Share Based Payment*), except certain contracts to buy or sell a non-financial item as noted below.

IAS 39 applies to those contracts to buy or sell a non-financial item that can be settled net in cash or another financial instrument, or by exchanging financial instruments, as if the contracts were financial instruments. However, IAS 39 does not apply to any such 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.

### ***Summary of IAS 39***

#### **Recognition and derecognition**

A financial asset or liability is recognised when the entity becomes a party to the instrument contract. A financial liability is derecognised when the liability is extinguished. A financial asset is derecognised when, and only when:

- the contractual rights to the cash flows from the asset expire; or

- the entity transfers substantially all the risks and rewards of ownership of the asset; or
- the entity transfers the asset, while retaining some of the risks and rewards of ownership, but no longer has control of the asset (ie the transferee has the ability to sell the asset). The risks and rewards retained are recognised as an asset.

### **Measurement**

Financial assets and liabilities are initially recognised at fair value. Subsequent measurement depends on how the financial instrument is categorised:

At amortised cost using the effective interest method

- Held-to-maturity investments: non-derivative financial assets with fixed or determinable payments and maturity that the entity has the positive intention and ability to hold to maturity.
- Loans and receivables: non-derivative financial assets with fixed or determinable payments that are not quoted in an active market.
- Financial liabilities that are not held for trading and not designated at fair value through profit or loss.

### **At fair value**

- At fair value through profit or loss: Financial asset or liability that is classified as held for trading, is a derivative or has been designated by the entity at inception as at fair value through profit or loss.
- Available-for-sale financial assets: Non-derivative financial assets that do not fall within any of the other categories. The unrealised movements in fair value are recognised in equity until disposal or sale, at which time, those unrealised movements from prior periods are recognised in profit or loss.

If there is objective evidence that a financial asset is impaired, the carrying amount of the asset is reduced and an impairment loss is recognised. A financial asset carried at amortised cost is not carried at more than the present value of estimated future cash flows. An impairment loss on an available-for-sale asset that reduces the carrying amount below acquisition cost is recognised in profit or loss.

### **Hedge accounting**

IAS 39 provides for two kinds of hedge accounting, recognising that entities commonly hedge both the possibility of changes in cash flows (i.e. a cash flow hedge) and the possibility of changes in fair value (i.e. a fair value hedge). Strict conditions must be met before hedge accounting is applied:

- There is formal designation and documentation of a hedge at inception.
- The hedge is expected to be highly effective (i.e. the hedging instrument is expected to almost fully offset changes in fair value or cash flows of the hedged item that are attributable to the hedged risk).
- Any forecast transaction being hedged is highly probable.
- Hedge effectiveness is reliably measurable (i.e. the fair value or cash flows of the hedged item and the fair value of the hedging instrument can be reliably measured).
- The hedge must be assessed on an ongoing basis and be highly effective.

When a fair value hedge exists, the fair value movements on the hedging instrument and the corresponding fair value movements on the hedged item are recognised in profit or loss. When a cash flow hedge exists, the fair value movements, on the part of the hedging instrument that is effective, are recognised in equity until such time as the hedged item affects profit or loss. Any ineffective portion of the fair value movement on the hedging instrument is recognised in profit or loss.

### **Embedded derivatives**

IAS 39 requires derivatives that are embedded in non-derivative contracts to be accounted for separately at fair value through profit or loss.

***Recommendations for Software:***

To be completed at a future date pending ongoing discussions between the EU and the IASB.

## **IAS 40: Investment Property**

### ***Introduction***

IAS 40 *Investment Property* was issued in December 2003 and is applicable to annual periods beginning on or after 1 January 2005. IAS 40 prescribes the accounting treatment for investment property and related disclosure requirements. Investment property is land and/or buildings held to earn rentals or for capital appreciation or both.

### ***Summary of IAS 40***

Investment property is initially recognised at cost. Subsequent to initial recognition, investment property is carried either at:

- Cost, less accumulated depreciation and any accumulated impairment losses, as prescribed by IAS 16 *Property, Plant and Equipment*, or
- Fair value. Fair value is the price at which the property could be exchanged between knowledgeable, willing parties in an arm's length transaction.
- Movements in fair value are recognised immediately in profit or loss.

The measurement model is applied consistently to all investment property. However, an entity may choose either the fair value model or the cost model for investment property backing liabilities that pay a return linked directly to the fair value of specified assets including that investment property, regardless of the model chosen for all other investment property.

Transfers to, or from, the investment property classification are made only when there is evidence of a change in use.

The gain or loss on derecognition of an item of investment property is the difference between the net disposal proceeds, if any, and the carrying amount of the item. The gain or loss is included in profit or loss.

IAS 40 specifies disclosures about investment property.

### ***Recommendations for Software:***

Specialist software requirements outside the scope of business systems

## **IAS 41: Agriculture**

### ***Introduction***

IAS 41 *Agriculture* is applicable for periods beginning on or after 1 January 2003.

IAS 41 prescribes the accounting treatment, financial statement presentation, and disclosures related to agricultural activity. It applies to biological assets, agricultural produce at the point of harvest, and government grants related to biological assets. A biological asset is a living animal or plant.

IAS 41 does not apply to:

- Land related to agricultural activity (IAS 16 *Property, Plant and Equipment*);
- Intangible assets related to agricultural activity (IAS 38 *Intangible Assets*); and
- The processing of agricultural produce after harvest (IAS 2 *Inventories* or another applicable Standard).

### ***Summary of IAS 41***

A biological asset is measured on initial recognition and at each balance sheet date at its fair value less estimated point-of-sale costs. Agricultural produce harvested from an entity's biological assets is measured at its fair value less estimated point-of-sale costs at the point of harvest. Point-of-sales costs include commissions, levies, and transfer duties and taxes.

A gain or loss arising on initial recognition at fair value less point-of-sale costs and from a change in fair value less point-of-sale costs is included in profit or loss.

An unconditional government grant related to a biological asset is recognised as income when the grant becomes receivable; a conditional government grant is recognised when the conditions attaching to the grant are met.

IAS 41 specifies disclosures related to agricultural activity.

### ***Recommendations for Software:***

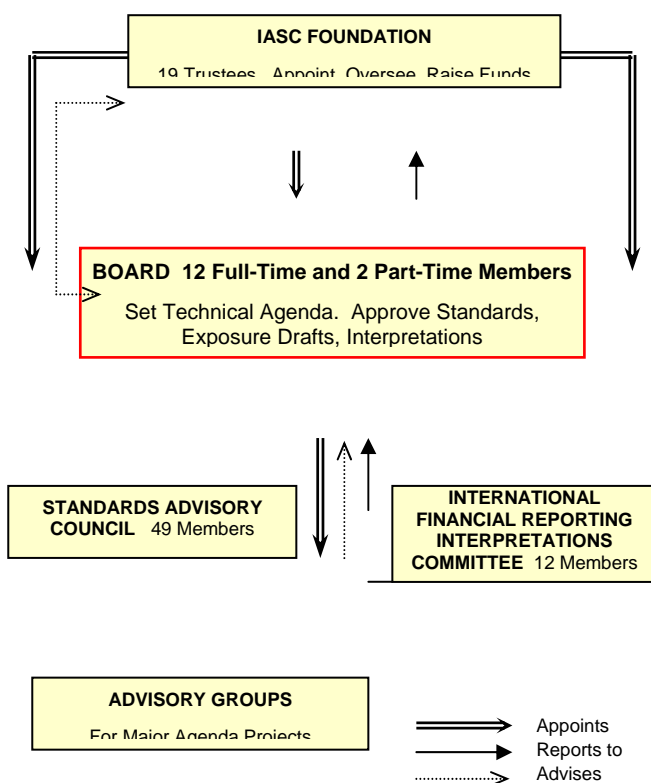
Specialist software requirements outside the scope of business systems.

## Glossary

The following abbreviations are used in this publication:

|       |  |
|-------|--|
| EEA   | European Economic Area   |
| EC    | European Commission  |
| EFRAG | European Financial Reporting Advisory Group                                    |
| EU    | European Union   |
| FASB  | Financial Accounting Standards Board (US)                                      |
| GAAP  | Generally Accepted Accounting Principle(s)                                     |
| IAS   | International Accounting Standard(s)   |
| IASC  | International Accounting Standards Committee                                   |
| IASB  | International Accounting Standards Board                                       |
| IFAC  | International Federation of Accountants  |
| IFRS  | International Financial Reporting Standard(s)                                  |
| IFRIC | International Financial Reporting Interpretations Committee of the IASB        |
| IOSCO | International Organization of Securities Commissions                           |
| SEC   | Securities and Exchange Commission (US)  |
| SIC   | Interpretation(s) issued by the Standing Interpretations Committee of the IASB |

## Current IASB Structure



## IASB Contact Information

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|      |  |
|------|--|
| 1973 | Agreement to establish IASC signed by representatives of the professional accountancy bodies in Australia, Canada, France, Germany, Japan, Mexico, Netherlands, United Kingdom/Ireland, and United States.<br>Steering committees appointed for IASC's first three projects.   |
| 1975 | First final IAS published: IAS 1 (1975), <i>Disclosure of Accounting Policies</i> , and IAS 2 (1975), <i>Valuation and Presentation of Inventories in the Context of the Historical Cost System</i> .  |
| 1982 | The IASC Board is expanded to up to 17 members, including 13 country members appointed by the Council of the International Federation of Accountants (IFAC) and up to 4 representatives of organisations with an interest in financial reporting. All members of IFAC are members of IASC. IFAC recognises and will look to IASC as the global accounting standard setter.   |
| 1989 | European Accounting Federation (FEE) supports international harmonisation and greater European involvement in IASC. IFAC adopts a public sector guideline to require government business enterprises to follow IAS.  |
| 1994 | Establishment of IASC Advisory Council approved, with responsibilities for oversight and finances.   |
| 1995 | European Commission supports the agreement between IASC and International Organization of Securities Commissions (IOSCO) to complete core standards and concludes that IAS should be followed by European Union multinationals.  |
| 1996 | US SEC announces its support of the IASC's objective to develop, as expeditiously as possible, accounting standards that could be used for preparing financial statements used in cross-border offerings.  |
| 1997 | Standing Interpretations Committee (SIC) is formed. 12 voting members. Mission to develop interpretations of IAS for final approval by the IASC.<br>Strategy Working Party is formed to make recommendations regarding the future structure and operation of IASC following completion of the core standards.  |
| 1998 | IFAC/IASC membership expands to 140 accountancy bodies in 101 countries.<br>IASC completes the core standards with approval of IAS 39.   |
| 1999 | G7 Finance Ministers and IMF urge support for IAS to "strengthen the international financial architecture".<br>IASC Board unanimously approves restructuring into 14-member board (12 full-time) under an independent board of trustees.   |
| 2000 | IOSCO recommends that its members allow multinational issuers to use IASC standards in cross-border offerings and listings.<br>Ad hoc nominating committee is formed, chaired by US SEC Chairman Arthur Levitt, to nominate the Trustees who will oversee the new IASB structure.<br>IASC member bodies approve IASC's restructuring and a new IASC Constitution.<br>Nominating Committee announces initial Trustees.<br>Trustees name Sir David Tweedie (chairman of the UK Accounting Standards Board) as the first Chairman of the restructured International Accounting Standards Board. |
| 2001 | Members and new name of IASB announced. IASC Foundation formed. On 1 April 2001, the new IASB assumes its standard-setting responsibilities from the IASC. Existing IAS and SIC adopted by IASB.<br>IASB moves into its new offices at 30 Cannon St., London.<br>IASB meets with chairs of its eight liaison national accounting standard-setting bodies to begin coordinating agendas and setting out convergence goals.  |
| 2002 | SIC is renamed as the International Financial Reporting Interpretations Committee (IFRIC) with a mandate not only to interpret existing IAS and IFRS but also to provide timely guidance on matters not addressed in an IAS or IFRS.<br>Europe requires IFRS for listed companies starting 2005.<br>IASB and FASB issue joint memorandum of understanding on convergence.  |
| 2003 | IASB holds public roundtable discussions on financial instruments. Representatives of 108 organisations participate.   |

## Website Links:

□ **BASDA – Business Application Software Developers’ Association**

www.basda.org

□ **IASB**

www.iasb.org.uk

□ **IASB’s Liaison Standard Setting Bodies**

|  |  |
|--|--|
| Australian Accounting Standards Board                                | <a href="http://www.aasb.com.au">www.aasb.com.au</a>                             |
| Canadian Accounting Standards Board                                  | <a href="http://www.cica.ca">www.cica.ca</a>                                     |
| France Conseil National de la Comptabilité                           | <a href="http://www.finances.gouv.fr/CNCompta">www.finances.gouv.fr/CNCompta</a> |
| German Accounting Standards Board                                    | <a href="http://www.drsc.de">www.drsc.de</a>                                     |
| Japan Accounting Standards Board                                     | <a href="http://www.asb.or.jp/index_e.html">www.asb.or.jp/index_e.html</a>       |
| New Zealand Financial Reporting Standards Board                      | <a href="http://www.icanz.co.nz">www.icanz.co.nz</a>                             |
| United Kingdom Accounting Standards Board (ASB)                      | <a href="http://www.asb.org.uk">www.asb.org.uk</a>                               |
| United States of America Financial Accounting Standards Board (FASB) | <a href="http://www.fasb.org">www.fasb.org</a>                                   |

□ **International Auditing and Assurance Standards Board**

www.ifac.org/iaasb

□ **International Federation of Accountants**

www.ifac.org

□ **International Organization of Securities Commissions**

www.iosco.org