IFRS Accounting Standards discussion fora: financial statement presentation

2023

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WORLD BANK GROUP

AABE

Accounting and Audit Board of Ethiopia

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Applicable version of IFRS Accounting Standards

Unless specified otherwise, the accounting requirements that are the subject matter of this discussion forum are IFRS Accounting Standards as issued by the International Accounting Standards Board that are applicable for annual period beginning on or after 1 January 2023 without early applying new and amended IFRS Accounting Standards that have a later mandatory application date.

Aims

» Develop a more cohesive understanding in Ethiopia of the presentation of IFRS financial statements.

» Enhance capacity in Ethiopia to apply IFRS Accounting Standards relating to the presentation of financial statements more consistently.

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Index of issues

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Materiality

Index of materiality issues

» Issue 1: determining whether an item is material

» Issue 2: over-riding a requirement of an IFRS Accounting Standard on the basis of immateriality

Issue 1: determining whether an item is material

Materiality judgements
What do you think?

Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users make on the basis of that reporting entity's IFRS financial information (Conceptual Framework 1.5).

In other words, materiality is an entity-specific aspect of relevance based on the nature or magnitude, or both, of the items to which the information relates in the context of the reporting entity's financial report.

How to determine whether an item is material?

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Materiality judgements
Summary of discussion

How to determine whether an item is material? Discussants' consensus view = judgement is used to determine whether particular information is material to primary users, on the basis of both nature and magnitude, and in the context of the reporting entity's financial report.

» Consequently, the IASB cannot specify a uniform quantitative threshold for materiality or predetermine what information is material in a particular situation.

- Nonetheless, *IFRS Practice Statement 2: Making Materiality Judgements* provides no-mandatory guidance on how to make materiality judgements when preparing IFRS financial statements. The guidance covers the following three main areas:
  - provides an overview of the characteristics of materiality;
  - presents a four-step process in making materiality judgements (see next slide); and
  - provides guidance on how to make materiality judgements in specific circumstances (see www.ifrs.org/issued-standards/list-of-standards/materiality-practice-statement/).

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Materiality judgements

The IFRS Foundation identifies the following steps "as a possible approach to the assessment of materiality in the preparation of the financial statements. In summary:

(a) Step 1—identify. Identify information that has the potential to be material.

(b) Step 2—assess. Assess whether the information identified in Step 1 is, in fact, material.

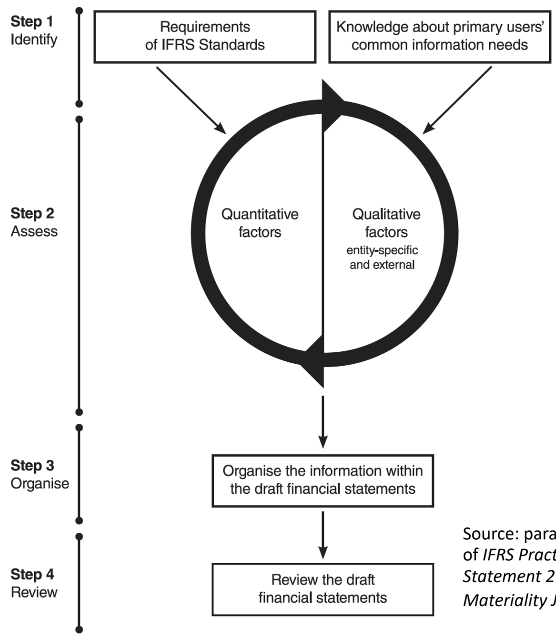
(c) Step 3—organise. Organise the information within the draft financial statements in a way that communicates the information clearly and concisely to primary users.

(d) Step 4—review. Review the draft financial statements to determine whether all material information has been identified and materiality considered from a wide perspective and in aggregate, on the basis of the complete set of financial statements."

(Source: paragraph 33 of *IFRS Practice Statement 2: Making Materiality Judgements)*

Note: Practice Statements are non-mandatory guidance. They do not change or introduce any requirements in IFRS Accounting Standards and entities are not required to comply with them to state compliance with IFRS Accounting Standards.

Diagram 1—the four-step materiality process



Source: paragraph 34 of *IFRS Practice Statement 2 Making Materiality Judgements*

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Issue 2: over-riding a requirement of an IFRS Accounting Standard on the basis of immateriality

Materiality judgements
What do you think?

Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users make on the basis of that reporting entity's IFRS financial information (Conceptual Framework 1.5).

In other words, materiality is an entity-specific aspect of relevance based on the nature or magnitude, or both, of the items to which the information relates in the context of the reporting entity's financial report.

Can management over-ride a requirement of an IFRS Accounting Standard on the basis of immateriality?

Materiality judgements
Summary of discussion

Can management over-ride a requirement of an IFRS Accounting Standard on the basis of immateriality? Discussants' consensus view =Yes, IFRS Accounting Standards explicitly state that an entity:

» **need not** apply its accounting policies to immaterial items; and

» **need not** disclose immaterial information.

Note too that an entity **must not** reduce the understandability of its financial statements by:

- obscuring material information with immaterial information; or
- aggregating material items that have different natures or functions.

Sources: paragraphs 17(c), 30A and 31 of IAS 1 and paragraph 8 of IAS 8

Nomenclature

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» Issue 1: using alternative terminology, for example, balance sheet instead of statement of financial position

Issue 1: using alternative terminology, for example, balance sheet instead of statement of financial position

Nomenclature

What do you think?

IFRS Accounting Standards use particular nomenclature for:

(i) specified line items in the financial statements; and

(ii) the specified components that comprise a complete set of IFRS financial statements.

Can management elect to use alternative terminology, for example, 'balance sheet' instead of 'statement of financial position'?

Nomenclature
Summary of discussion

Can management elect to use alternative terminology, for example, 'balance sheet' instead of 'statement of financial position'? Discussants' consensus view = Yes, provided that the alternative terminology used is not misleading.

» Although IFRS Accounting Standards use particular nomenclature for the specified components that comprise a complete set of IFRS financial statements (and for specified line items in the financial statements), the IASB foresees circumstances in which an entity may need to amend the descriptions used for particular line items in the financial statements and for the financial statements themselves (IAS 1.5).

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Other comprehensive income (OCI)

Index of other comprehensive income (OCI) issues

» Issue 1: income and expenses presented in OCI that are recycled

» Issue 2: income and expenses presented in OCI that are not recycled

Issue 1: income and expenses presented in OCI that are recycled

Other comprehensive income (OCI)
What do you think?

IFRS Accounting Standards require (or permit) specified items of income and expense be presented in OCI (ie in comprehensive income but outside of profit or loss for the period).

Furthermore, particular items of OCI are reclassified from OCI to profit or loss in specified circumstance (recycling) whilst recycling of other items of OCI is not permitted.

Which items of OCI are recycled?

Other comprehensive income (OCI)
Summary of discussion

Which items of OCI are recycled? Discussants' consensus view: OCI items that are recycled include, amongst others:

» IFRS 9 *Financial Instruments*: (i) fair value gain or loss on a financial asset classified FVOCI debt instruments; (ii) specified fair value gains and losses on designated hedging instruments in cash flow hedge accounting; (iii) the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge of a net investment in a foreign operation.

» IAS 21 *The Effects of Changes in Foreign Exchange Rates*: (i) tax effects of underlying items included in OCI that are recycled; (ii) exchange differences resulting from translating a foreign operation into the reporting entity's presentation currency for consolidation purposes; (iii) exchange differences resulting from translating from using a presentation currency that is different from the functional currency.

» IAS 28 *Investments in Associates and Joint Ventures*: equity method accounting for share of the investees' OCI that are recycled.

Issue 2: income and expenses presented in OCI that are not recycled

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Other comprehensive income (OCI)
What do you think?

IFRS Accounting Standards require (or permit) specified items of income and expense be presented in OCI (ie in comprehensive income but outside of profit or loss for the period).

Furthermore, particular items of OCI are reclassified from OCI to profit or loss in specified circumstance (recycling) whilst recycling of other items of OCI is not permitted.

Which items of OCI are not recycled?

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Other comprehensive income (OCI)
Summary of discussion

Which items of OCI are not recycled? Discussants' consensus view: OCI items that are not recycled include, amongst others:

» IFRS 9: (i) fair value gain or loss on financial assets classified FVOCI equity instruments; (ii) fair value gain or loss on the hedging instrument in a fair value hedge when hedging a financial assets classified FVOCI equity instrument; (iii) effects of changes in the recognised fair value of financial liabilities that are attributed to changes in the entity's own credit risk.

» IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets*: specified revaluation gains and losses.

» IAS 19 *Employee Benefits*: gains and losses from specified remeasurements of defined benefit plans.

» IAS 21 *The Effects of Changes in Foreign Exchange Rates*: tax effects of underlying items included in OCI that are not recycled.

» IAS 28 *Investments in Associates and Joint Ventures*: equity method accounting for share of the investees' OCI.

» Adjustment when an owner-occupied property (IAS 16) becomes an investment property (IAS 40) carried at fair value.

Current non-current distinction

Index of current non-current distinction issues

» Issue 1: are inventories classified as current assets?

Issue 1: are inventories classified as current assets?

Current non-current distinction
What do you think?

IFRS Accounting Standards requires separate presentation of current and non-current assets/liabilities except when using order of liquidity basis of presentation (IAS 1.60).

Nonetheless, asset/liability line-items that combine amounts expected to be recovered/settled in both <12 and >12 months later, must disclose the amount expected to be recovered/settled after >12 months (IAS 1.61).

Are inventories classified as current assets?

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Current non-current distinction
Summary of discussion

Are inventories classified as current assets? Discussants' consensus view: it depends

» Yes, when the entity makes the current / non-current presentation distinction, and because it expects to consume raw materials and consumables and sell its work in process and finished goods in its normal operating cycle and because inventories are held primarily for the purpose of trading (IAS 1.66).

» However, if the entity expects to realise some of its inventory >12 months after the reporting period, it must disclose the carrying amount of the inventories expected to be recovered >12 months after the reporting period (IAS 1.61).

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Presentation currency

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» Issue 1: how to translate from ETB functional currency to USD reporting currency

Issue 1: how to translate from ETB functional currency to USD reporting currency

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Translating from ETB functional currency to USD reporting currency
What do you think?

IAS 21 *The Effects of Changes in Foreign Exchange Rates* specifies how to translate from functional currency to a presentation currency that is different from functional currency (IAS 21.38–.43).

How to translate from ETB functional currency to USD reporting currency?

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Translating from ETB functional currency to USD reporting currency
Summary of discussion

How to translate from ETB functional currency to USD reporting currency? Discussants' consensus view: to translate from ETB functional currency into USD presentation currency (IAS 21.39):

- translate assets and liabilities at the closing rate on reporting date;
- translate income and expenses at exchange rates at the dates of the transactions (can use average rate if difference is not material); and
- recognise resulting exchange differences in OCI.