SAFA FINANCIAL REPORTING STANDARD

FOR

SMALL AND MEDIUM ENTITIES (SMEs)

Foreword

In the Asian pacific region as whole SMEs represents over 97% of the total entities. Not only in Asian pacific region but also in European Union and United States, SMEs accounts for whooping 95.77% and 99.7% of total companies respectively. In South Asian Region also SMEs constitutes a large part of economy in value and overwhelmingly large part in numbers. Because of their sheer scale when taken as a whole and the dramatic effect that successful SMEs can have on national and international economies, SMEs should be given its due priorities while framing standards of accounting

Heightened regulations, together with increased and more complex standards have placed increased burden on SMEs, which may not have capability to implement full IFRSs, also cost of full implementation may not be commensurate with benefit. The standards should be relevant and understandable that eases the compliance burden on SMEs and ensures that benefit exceeds the cost.

Keeping all the requirement of SME Sector in mind, SAFA Centre of Excellence on Standards and Quality Control, in its meeting held in March 2004 at Jaipur, India decided to develop separate standard for SMEs on which the Assembly has given its consent at its 53rd Assembly meeting held on 11th March 2004.

I would like to express my deep gratitude to Mr. Nishan Fernando, Chairman of the Centre of Excellence on Standards & Quality control and the technical team of the Institute of Chartered Accountants of Sri Lanka, who put special efforts in finalizing this standard. My special thanks to the Institute of Chartered Accountants of Pakistan, because of their painstaking efforts that helped the Centre of Excellence in developing this standard. Finally, I wish to put on record my sincere appreciation to all member bodies, which provided valuable comments.

I am particularly happy as the instant publication is the first ever standard developed by SAFA since its inception in 1984. I have no doubt that this document would go long way and could be the basis for SAFA member bodies for developing SMEs Standard in their respective countries.

26th December 2006 Sunil Goyal
Jaipur President SAFA

Preamble

Standards help to promote sound financial systems and financial stability, locally as well as globally. They play an important role in strengthening financial development and in reducing vulnerability of financial statements to various creative accounting practices adopted in different industries. Standards vary in scope and range from broad principles to specific accounting and financial reporting methodologies. Their implementation should ideally be in line with each country's overall economic strategy, financial development and institutional capacity etc.

The SAFA Financial Reporting Standard for Small & Medium Entities (SMEs) has been introduced in keeping with the broad objectives of the SAFA Centre of Excellence for Standards & Quality, in promoting transparency and accountability and to develop, disseminate and promote implementation of better accounting standards and best practices among the countries in the SAFA region.

The specific objectives of developing this Financial Reporting Standard also include;

- development of a high quality, understandable and enforceable accounting standard suitable for SMEs in the SAFA region
- reduction of the financial reporting burden on SMEs
- meeting the needs of the various users of the SME financial statements

The following aspects have been considered in developing the Standard;

- ensuring that the Standard is inline with the Generally Accepted Accounting Principles
- treatment and recognition of transactions in a manner, that would be readily understood by a proprietor or manager of a business, corresponding to the understanding of the transaction
- provision of the least cumbersome method of achieving the desired accounting treatment or disclosure for a SME, that is not complex
- provision of guidance, that is expected to be widely relevant to the transactions of SMEs which are written in terms that can be understood by such businesses
- ensuring that the measurement methods prescribed in the Standard to be reasonably practical for SMEs

The project of developing this Standard was sphere-headed on behalf of SAFA Centre of Excellence for Standards and Quality by the Institute of Chartered Accountants of Pakistan. Several drafts of the Standard were reviewed and accepted by all other member bodies of the region; Sri Lanka, India, Bangladesh and Nepal. A Representative of Bhutan was also present at the 62nd SAFA General Assembly Meeting, which agreed to adopt the Standard as a SAFA Regional Standard.

I take this opportunity to thank the Institute of Chartered Accountants of Pakistan for the very valuable contribution made by them in developing this standard. I would also like to thank the Technical Unit of the Institute of Chartered Accountants of Sri Lanka for their valuable contribution in numerous ways in finalising this Standard. Finally, as the Chairman of the Centre of Excellence for Standards and Quality, I consider this, a step in the right direction to harmonise for financial reporting practices within the region.

Nishan Fernando FCA(SL)
Chairman
SAFA Centre of Excellence for Standards & Quality

CONTENTS

Application of International Accounting & Financial Reporting Standards

The following International Accounting and Financial reporting Standards have been identified as being relevant to Small and medium entities. The requirements of these Standards have been considered and amended, where necessary, to suit the operations and transactions of SMEs. The tale below indicates the summary of Standards used in preparing this document.

Name of Standard	**IAS/IFRS No**	**Section**
Presentation of Financial Statements	IAS 1	1
Inventories	IAS 2	6
Cash Flow Statements	IAS 7	2
Accounting Policies, Changes in Accounting Estimates and Errors	IAS 8	12
Events after the Balance Sheet Date	IAS 10	14
Income Taxes	IAS 12	11
Property, Plant & Equipment	IAS 16	3
Leases	IAS 17	4
Revenue	IAS 18	9
Employee Benefits	IAS 19	17
Accounting for Government Grants and Disclosures of Government Assistance	IAS 20	7
The Effects of Changes in Foreign Exchange Rates	IAS 21	13
Borrowing Costs	IAS 23	10
Related Party Disclosures	IAS 24	15
Financial Instruments : Presentation	IAS 32	16
Provisions, Contingent Liabilities and Contingent Assets	IAS 37	8
Intangible Assets	IAS 38	5
Financial Instruments : Recognition & Measurement	IAS 39	16
Financial Instruments : Disclosures	IFRS 7	16
Non-current Assets Held for Sale and Discontinued Operations	IFRS 2	

The Standards mentioned below are not considered to be relevant for entities operating as a SME. However, ion a situation, where, such a standard is required in preparation and presentation of financial statements of the SME, the full scope of the relevant IAS/IFRS should be taken into account, as discussed in Framework p 14 and Section 12 p1.

Name of Standard	**IAS/IFRS No**
Construction Contracts	IAS 11
Segment Reporting	IAS 14
Accounting and Reporting by Retirement Benefit Plans	IAS 26
Consolidated and Separate Financial Statements	IAS 27
Investments in Associates	IAS 28
Financial Reporting in Hyper Inflationary Economies	IAS 29
Interest in Joint Ventures	IAS 31
Earnings per Share	IAS 33
Interim Financial Reporting	IAS 34
Impairment of Assets	IAS 36
Investment Property	IAS 40
Agriculture	IAS 41
First Time adoption of International Financial Reporting Standards	IFRS 1
Share-based Payments	IFRS 2
Business Combinations	IFRS 3
Insurance Contracts	IFRS 4
Exploration for and Evaluation of Mineral Resources	IFRS 6

Framework

Scope

1. This Framework sets out the conceptual basis and qualifying criteria for the preparation of general purpose financial statements of Small and Medium Entities in accordance with the SAFA Financial Reporting Standard for Small and Medium Entities.

2. Entities which can be classified as a Small & Medium Entities are discussed in Annex 2 to the Standard.

Users

3. Users of financial statements generally include present and potential investors, employees, lenders, suppliers and other trade creditors, customers, governments and their agencies and, in some jurisdictions, the public. For SMEs, the most significant users are likely to be investors/owners and creditors, who may have the power to obtain information additional to that contained in the financial statements. Management is also interested in the information contained in the financial statements, even though it has access to additional management and financial information.

Objectives

4. The objective of financial statements is to provide information about the financial position, performance and changes in financial position of an entity that is useful to users of such information in making economic decisions. Financial statements prepared for this purpose meet the common needs of most economic decisions since they largely portray the financial effects of past events and do not necessarily provide non-financial information. Financial statements show the results of management's stewardship of and accountability for the resources entrusted to it.

Underlying assumptions

5. Financial statements are prepared on the accrual basis of accounting. Under this basis, the effects of transactions and other events are recognized when they occur (and not as cash or its equivalent are received or paid) and they are recorded in the accounting records and reported in the financial statements of the periods to which they relate. Financial statements prepared on the accrual basis inform users not only of past transactions involving the payment and receipt of cash but also of obligations to pay cash in the future and of resources that represent cash to be received in the future. Hence, they provide the type of information about past transactions and other events that is most useful to users in making economic decisions. They are normally prepared on the assumption that an entity is a going concern that will continue to operate for at least the foreseeable future.

   Hence, it is assumed that the entity has neither the intention nor the need to liquidate or curtail materially the scale of its operations; if such an intention or need exists, the financial statements may have to be prepared on a different basis and, if so, the basis used is disclosed.

Qualitative characteristics

6. Qualitative characteristics are the attributes that make the information provided in financial statements useful to users. The principal characteristics are:

   (a) Understandability: It is essential that information provided in financial statements be readily understandable by users.

   (b) Relevance: To be useful, information must be relevant to the decision-making needs of users. The relevance of information is affected by its nature and materiality.

(c) Materiality: The relevance of information is affected by its nature and materiality, information is material if its omission or misstatement could influence the economic decisions of users taken on the basis of the financial statements. Materiality depends on the size of the item or error judged in the particular circumstances of its omission or misstatement. Thus, materiality provides a threshold or cut-off point rather than being a primary qualitative characteristic which information must have if is to be useful.

(d) Reliability: Information is reliable when it is free from material error and bias and can be depended on by users to represent faithfully that which it is said to represent. In assessing reliability, substance over form, prudence, neutrality and completeness are also considered.

(e) Faithful Representation: To be reliable, information must represent faithfully the transactions and other events it either purports to represent or could reasonably be expected to represent.

(f) Substance over form: information is to represent faithfully the transactions and other events that it purports to represent, it is necessary that they are accounted for and presented in accordance with their substance and economic reality and not merely their legal form.

(g) Neutrality: To be reliable, the information contained in financial statements must be neutral, that is, free from bias.

(h) Prudence: Prudence is the inclusion of a degree of caution in the exercise of the judgments needed in making the estimates required under conditions of uncertainty, such that assets or income are not overstated and liabilities or expenses are not understated.

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

(j) Comparability: Users must be able to compare the financial statements of an entity over time in order to identify trends in the entity's financial position and performance. Users must also be able to compare the financial statements of different entities in order to evaluate their relative financial position, performance and changes in financial position.

Constraints on relevant and reliable information

Timeliness

7 If there is undue delay in the reporting of information it may lose its relevance. Management may need to balance the relative merits of timely reporting and the provision of reliable information. To provide information on a timely basis it may often be necessary to report before all aspects of a transaction or other event are known, thus impairing reliability. Conversely, if reporting is delayed until all aspects are known, the information may be highly reliable but of little use to users who have had to make decisions in the interim. In achieving a balance between relevance and reliability, the overriding consideration is how best to satisfy the economic decision–making needs of users.

Balance between benefit and cost

8 The balance between benefit and cost is a pervasive constraint rather than a qualitative characteristic. The benefits derived from information should exceed the cost of providing it. The evaluation of benefits and costs is, however, substantially a judgmental process. The preparers and users of financial statements should be aware of this constraint. In achieving a balance between relevance and reliability, the overriding consideration is how best to satisfy the economic decision-making needs of users.

Balance between qualitative characteristics

9 In practice, trade-offs between qualitative characteristics are often necessary. Determining the relative importance of the characteristics in different cases is a matter of professional judgment.

Elements

10 The elements directly related to the measurement of financial position are assets, liabilities and equity. These are defined as follows:-

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

(b) A **"***liability***"** is a present obligation of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits.

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

11 Profit is frequently used as a measure of performance or as the basis for other measures, such as return on investment or earnings per share. The elements directly related to the measurement of profit are income and expenses.

The elements of income and expenses are defined as follows:

(a) Income is increase in economic benefits during the accounting period in the form of inflows or enhancements of *assets* as well as decreases of *liabilities* that result in increase in equity, other than those relating to contributions from equity participants.

(b) Expenses are decrease in economic benefits during the accounting period in the form of outflows or depletions of assets or incurrence of liabilities that results in decrease in equity, other than those relating to distributions to equity participants.

Recognition

12 An item that meets the definition of an element should be recognized if (a) it is probable that any future economic benefit associated with the item will flow to or from the entity, and (b) the item has a cost or value that can be measured with reliability.

Measurement

13 The measurement basis most commonly adopted by entities in preparing their financial statements is historical cost. This is usually combined with other measurement bases. For example, inventories are usually carried at the lower of cost and net realizable value, marketable securities may be carried at market value and pension liabilities are carried at their present value.

Transactions not covered by this standard

14 Where an entity has a transaction that falls outside these standards, it is suggested that the preparer look for guidance within the:

(a) full IAS/IFRS issued by IASB;

(b) interpretations issued by SIC and IFRIC;

(c) appendices to standards issued by IASB;

(d) implementation guidance issued by IASB;

(e) the definitions, recognition criteria and measurement concepts set out in the conceptual framework of IASB; and

(f) pronouncements of the Country and jurisdiction that use a similar conceptual framework to develop accounting standards; other accounting literature; and accepted industry practice, to the extent that these are consistent with items (a) to (e) above.

Effective Date

15 Small and Medium Entities shall apply this SAFA Financial Reporting Framework and Standard for annual periods beginning on or after a date specified in the respective country and jurisdiction.

Section 1. Presentation of Financial Statements

Components of financial statements

1.1 A complete set of financial statements includes the following components:

(a) a balance sheet;

(b) an income statement;

(c) a statement showing either:

(i) all changes in equity; or
(ii) changes in equity other than those arising from capital transactions with owners and distributions to owners;

(d) a cash flow statement; and

(e) accounting policies and explanatory notes.

Overall considerations

1.2 Financial statements shall present fairly the financial position, financial performance and *cash flows* of an entity. The appropriate application of the standard, with additional disclosure when necessary, results, in virtually all circumstances, in financial statements that achieve a fair presentation as appropriate for SMEs. In the event that a transaction undertaken by an entity, is not covered by the standard, the entity should look to the full set of International Accounting Standards (IAS) and International Financial Reporting Standards (IFRS) for authoritative guidance, as set out in paragraph 12.1.

1.3 An entity whose financial statements are drawn up in compliance with the standard and laws and regulations of the respective country, shall specify in its accounting policy note that these financial statements are in compliance with the SAFA Financial Reporting Framework for SMEs and the respective laws and regulations of that specific country.

1.4 Inappropriate accounting treatments are not rectified either by disclosure of the accounting policies used or by notes or explanatory material.

1.5 In the extremely rare circumstances when management concludes that compliance with a requirement in the standard would be misleading, and that therefore departure from a requirement is necessary in order to achieve a fair presentation, the entity shall depart from that requirement and shall disclose:

(a) that management has concluded that the financial statements fairly present the entity's financial position, financial performance and *cash flows*;

(b) that it has complied in all material respects with the Standard, except for departing from them in order to achieve a fair presentation; and

(c) the nature of the departure, including the treatment required by the standard, the reason why that treatment would be misleading in the circumstances, and the treatment adopted; and

(d) for each period presented, the financial impact of the departure on each item in the financial statements that would have been reported in complying with the requirement.

1.6 When preparing financial statements, management shall make an assessment of an entity's ability to continue as a going concern. Financial statements shall be prepared on a going-concern basis unless management either intends to liquidate the entity or cease trading, or has no realistic alternative but to do so. When management is aware, in making its assessment, of material uncertainties related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern, those uncertainties shall be disclosed. When the financial statements are not prepared on a going-concern basis, that fact shall be disclosed, together with the basis on which the financial statements are prepared and the reason why the entity is not considered to be a going concern.

In assessing whether the going concern assumption is appropriate, management takes into account all available information for the foreseeable future, which shall be, but is not limited to, twelve months or any other period as required by each country's jurisdiction, from the balance sheet date. The degree of consideration depends on the facts in each case. When an entity has a history of profitable operations and ready access to financial resources, a conclusion that the going concern basis of accounting is appropriate may be reached without detailed analysis. In other cases, management may need to consider a wide range of factors surrounding current and expected profitability, debt repayment schedules and potential sources of replacement financing before it can satisfy itself that the going concern basis is appropriate.

1.7 An entity shall prepare its financial statements, except for cash flow information, under the accrual basis of accounting.

1.8 The presentation and classification of items in the financial statements shall be retained from one period to the next unless

(a) a significant change in the nature of the operations of the entity or a review of its financial statement presentation demonstrates that the change will result in a more appropriate presentation of events or transactions; or

(b) a change in presentation is required by the standard.

1.9 Each material item shall be presented separately in the financial statements. Immaterial items shall be aggregated with amounts of a similar nature or function and need not be presented separately. Information is material if its omission or misstatement could influence the economic decisions of users taken on the basis of the financial statements. Materiality depends on the size and nature of the item judged in the particular circumstances where its presentation comes into question.

1.10 *Assets* and *liabilities* shall not normally be offset in the financial statements. However, some offsetting is required or permitted in exceptional circumstances, as mandated by the Standard (e.g. paragraph 2.6). Offsetting may also take place where gains, losses and related expenses arising from the same or similar transactions are not material.

1.11 Unless the standard permits or requires otherwise, comparative information with respect to the previous period shall be disclosed for all numerical information in the financial statements. Comparative information shall be included in narrative and descriptive information when it is relevant to an understanding of the current period's financial statements. When the presentation or classification of items in the financial statements is amended, comparative amounts shall be reclassified unless the reclassification is impracticable. When comparative amounts are reclassified, an entity shall disclose the nature, amount and reason of the reclassification. When it is impracticable to reclassify comparative amounts, an entity shall disclose the reason for not reclassifying the amounts and the nature of the adjustments.

Structure and content

1.12. Each component of the financial statements shall be clearly identified. In addition, the following information shall be prominently displayed and repeated when it is necessary for a proper understanding of the information presented:

(a) the name of the reporting entity or other means of identification;

(b) the balance sheet date or the period covered by the other financial statements, whichever is appropriate to the related component of the financial statements; and

(c) the *reporting currency*.

1.13. Financial statements shall be presented at least annually. When, in exceptional circumstances, an entity's balance sheet date changes and annual financial statements are presented for a period longer or shorter than one year, an entity shall disclose, in addition to the period covered by the financial statements:

(a) the reason why a period other than one year is being used; and

(b) the fact that comparative amounts for the income statement, changes in equity, cash flows and related notes are not comparable.

Balance sheet

1.14. Each entity shall determine, based on the nature of its operations, whether or not to present current and non-current assets and current and non-current liabilities as separate classifications on the face of the balance sheet. Paragraphs 1.16 to 1.20 of this Standard apply when this distinction is made. When an entity chooses not to make this classification, *assets* and *liabilities* shall be presented broadly in order of their liquidity.

1.15. Whichever method of presentation is adopted, an entity shall disclose, for each *asset* and *liability* item that combines amounts expected to be recovered or settled both before and after 12 months from the balance sheet date, the amount expected to be recovered or settled after more than 12 months.

1.16. An *asset* shall be classified as a current asset when it:

(a) is expected to be realized in, or is held for sale or consumption in, the normal course of the entity's operating cycle; or

(b) is held primarily for trading purposes or for the short term and is expected to be realized within 12 months of the balance sheet date; or

(c) is *cash* or a *cash-equivalent* asset that is not restricted in its use.

All other *assets* shall be classified as non-current assets.

1.17. A *liability* shall be classified as a current liability when it:

(a) is expected to be settled in the normal course of the entity's operating cycle; or

(b) is due to be settled within 12 months of the balance sheet date.

(c) it is held primarily for the purpose of being traded;

(d) the entity does not have an unconditional right to defer settlement of the liability for at least twelve months after the balance sheet date.

All other *liabilities* shall be classified as non-current liabilities.

1.18. An entity classifies its financial liabilities as current when they are due to be settled within twelve months after the balance sheet date, even if:

(a) the original term was for a period longer than twelve months; and

(b) an agreement to refinance, or to reschedule payments, on a long-term basis is completed after the balance sheet date and before the financial statements are authorised for issue.

1.19. At a minimum, the face of the balance sheet shall include line items presenting the following amounts:

(a) *property, plant and equipment;*

(b) *intangible assets;*

(c) Investments
(d) *inventories;*

(e) trade and other receivables;

(f) *cash* and *cash equivalents;*

(g) trade and other payables;

(h) tax liabilities and assets;

(i) *provisions;*

(j) non-current interest-bearing liabilities; and

(k) capital and reserves.

1.20. Additional line items, headings and subtotals shall be presented on the face of the balance sheet when such presentation is necessary to present fairly the entity's financial position.

1.21. An entity shall disclose the following, either on the face of the balance sheet or in the notes:

(a) for each class of share capital:

(i) the number of shares authorized;

(ii) the number of shares issued and fully paid, and issued but not fully paid;

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

(iv) a reconciliation of the number of shares outstanding at the beginning and at the end of the year;

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

(vi) shares in the entity held by the entity itself; and

(vii) shares reserved for issuance under options and sales contracts, including the terms and amounts;

(b) a description of the nature and purpose of each reserve within equity;

Income statement

1.22. At a minimum, the face of the income statement shall include line items that present the following amounts:

(a) *revenue;*

(b) the results of *operating activities;*

(c) finance costs;

(d) *tax expense;*

(e) net profit or loss for the period.

Additional line items, headings and subtotals shall be presented on the face of the income statement when such presentation is necessary to present fairly the entity's financial performance.

1.23. All items of income and expense recognized in a period shall be included in the determination of the net profit or loss for the period unless the standard requires or permits otherwise.

1.24. When items of income and expense within profit or loss from *ordinary activities* are of such size, nature or incidence that their disclosure is relevant to explain the performance of the entity for the period, the nature and amount of such items shall be disclosed separately.

1.25. Circumstances that may give rise to the separate disclosure of items of income and expense in accordance with paragraph 1.24 include the following:

(a) the write-down of *inventories* to *net realizable value* or *property, plant and equipment* to recoverable amount, as well as the reversal of such write-downs;

(b) a restructuring of the activities of an entity and the reversal of any *provisions* for the costs of restructuring;

(c) disposals of items of *property, plant and equipment*;

(d) disposals of long-term investments;

(e) discontinuing operations;

(f) litigation settlements; and

(g) other reversals of *provisions*.

1.26. An entity shall present, either on the face of the income statement or in the notes to the income statement, an analysis of expenses using a classification based on either the nature of expenses or their function within the entity.

1.27. Entities classifying expenses by function shall disclose additional information on the nature of expenses, including *depreciation* and amortization expense and staff costs.

1.28 An entity shall disclose**,** in the notes, the amount of dividends per share, declared, for the period covered by the financial statements.

1.29 An entity shall not present any items of income and expense as extraordinary items, either on the face of the income statement or in the notes.

Changes in equity

1.30. An entity shall present, as a separate component of its financial statements, a statement showing the following:

(a) the net profit or loss for the period;

(b) each item of income and expense, gain or loss that, as required by the Standard, is recognized directly in equity, and the total of these items; and

(c) the cumulative effect of changes in accounting policy and the correction of *errors*.

In addition, an entity shall present, either within this statement or in the notes, the following:

(d) capital transactions with owners and distributions to owners;

(e) the balance of accumulated profit or loss at the beginning of the period and at the balance sheet date, and the movements for the period; and

(f) a reconciliation between the carrying amount of each class of equity capital, share premium and each reserve at the beginning and the end of the period, separately disclosing each movement.

Notes to the financial statements

1.31. The notes to the financial statements of an entity shall:

(a) present information about the basis of preparation of the financial statements and the specific *accounting policies* selected and applied for significant transactions and events;

(b) disclose the information required by the standard that is not presented elsewhere in the financial statements; and

(c) provide additional information that is not presented on the face of the financial statements but that is necessary for a fair presentation.

(d) the amount of dividends that were declared after the balance sheet date but before the financial statements were authorized for issue; and

(e) the amount of any cumulative preference dividends not recognized.

1.32. Notes to the financial statements shall be presented in a systematic manner. Each item on the face of the balance sheet, the income statement and the cash flow statement shall be cross-referenced to any related information in the notes.

1.33. The *accounting policies* section of the notes to the financial statements shall describe the following:

(a) the measurement basis (or bases) used in preparing the financial statements; and

(b) each specific accounting policy that is necessary for a proper understanding of the financial statements.

1.34 An entity shall disclose in the notes information about the key assumptions concerning the future, and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year. In respect of those assets and liabilities, the notes shall include details of:

(a) their nature; and

(b) their carrying amount as at the balance sheet date.

1.35. Determining the carrying amounts of some assets and liabilities requires estimation of the effects of uncertain future events on those assets and liabilities at the balance sheet date. For example, in the absence of recently observed market prices used to measure the following assets and liabilities, future-oriented estimates are necessary to measure the recoverable amount of classes of property, plant and equipment, the effect of technological obsolescence on inventories, provisions subject to the future outcome of litigation in progress, and long-term employee benefit liabilities such as pension obligations. These estimates involve assumptions about such items as the risk adjustment to cash flows or discount rates used, future changes in salaries and future changes in prices affecting other costs.

1.36. An entity shall disclose the following, if the information is not disclosed elsewhere in information published with the financial statements:

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

(b) a description of the nature of the entity's operations and its principal activities.

(c) the name of the parent and the ultimate parent of the group, if any.

Section 2. Cash Flow Statements

2.1. The cash flow statement shall report *cash flows* during the period classified by operating, investing and *financing activities*.

Operating activities

2.2. *Cash flows* from *operating activities* are primarily derived from the principal *revenue* producing activities of the entity. Therefore, they generally result from the transactions and other events that enter into the determination of net profit or loss. Some transactions, such as the sale of an item of plant, may give rise to a gain or loss that is included in the determination of net profit or loss. However, the *cash flows* relating to such transactions are *cash flows* from *investing activities.*

Investing activities

2.3. The separate disclosure of *cash flows* arising from *investing activities* is important because the cash flows represent the extent to which expenditures have been made for resources intended to generate future income and *cash flows*.

Financing activities

2.4. The separate disclosure of *cash flows* arising from financing activities is important because it is useful in predicting claims on future *cash flows* by providers of capital to the entity.

2.5. An entity shall report *cash flows* from *operating activities* using either:

(a) the direct method, whereby major classes of gross cash receipts and gross cash payments are disclosed; or

(b) the indirect method, whereby net profit or loss is adjusted for the effects of transactions of a non-cash nature, any deferrals or accruals of past or future operating cash receipts or payments, and items of income or expense associated with investing or financing *cash flows*.

2.6. An entity shall report separately major classes of gross cash receipts and gross cash payments arising from financing and *investing activities*, except to the extent that *cash flows* described in paragraph 2.7 are reported on a net basis.

2.7. *Cash flows* arising from the following operating, investing or *financing activities* may be reported on a net basis:

(a) cash receipts and payments on behalf of customers when the *cash flows* reflect the activities of the customer rather than those of the entity; and

(b) cash receipts and payments for items in which the turnover is quick, the amounts are large, and the maturities are short.

2.8 Cash flows arising from transactions in a foreign currency shall be recorded in an entity's reporting currency by applying to the foreign currency amount the exchange rate between the reporting currency and the foreign currency at the date of the cash flow.

2.9 Investing and financing transactions that do not require the use of *cash* or *cash equivalents* shall be excluded from a cash flow statement. Such transactions shall be disclosed elsewhere in the financial statements in a way that provides all the relevant information about these investing and *financing activities*.

2.10 An entity shall disclose the components of *cash* and *cash equivalents* and shall present a reconciliation of the amounts in its cash flow statement with the equivalent items reported in the balance sheet.

2.11 Cash flows from interest and dividends received and paid shall each be disclosed separately. Each shall be classified in a consistent manner from period to period as either operating, investing or financing activities.

2.12 *Cash flows* arising from income taxes shall be separately disclosed within the *operating activities* section unless they can be specifically identified with financing and *investing activities*.

Cash and cash equivalents

2.13. *Cash equivalents* are held for the purpose of meeting short-term cash commitments rather than for investment or other purposes. To qualify as a *cash equivalent*, an investment must be readily convertible to a known amount of *cash* and be subject to an insignificant risk of changes in value. Therefore, an investment normally qualifies as a *cash equivalent* only when it has a short maturity of, say, three months or less from the date of acquisition. Equity investments are excluded from *cash equivalents* unless they are, in substance, *cash equivalents* – for example, in the case of preferred shares acquired within a short period of their maturity and with a specified redemption date.

2.14 Bank borrowings are generally considered to be *financing activities*. However, bank overdrafts that are repayable on demand form an integral part of an entity's cash management. In these circumstances, bank overdrafts are included as a component of *cash* and *cash equivalents*. A characteristic of such banking arrangements is that the bank balance often fluctuates between being positive and being overdrawn.

Other disclosures

2.15. An entity shall disclose, together with a commentary by management, the amount of significant *cash* and *cash equivalent* balances held by the entity that are not available for use by the entity.

Section 3. Property, Plant and Equipment

Recognition

3.1 An item of *property, plant and equipment* shall be recognized as an *asset* when:

(a) it is probable that future economic benefits associated with the *asset* will flow to the entity; and

(b) the *cost* of the *asset* to the entity can be measured reliably.

3.2 Spare parts and servicing equipment are usually carried as inventory and recognized in profit or loss as consumed. However, major spare parts and stand-by equipment qualify as property, plant and equipment when an entity expects to use them during more than one period. Similarly, if the spare parts and servicing equipment can be used only in connection with an item of property, plant and equipment, they are accounted for as property, plant and equipment.

Measurement at Initial Recognition

3.3 An item of *property, plant and equipment* that qualifies for recognition as an asset shall initially be measured at its *cost*.

(a) The *cost* of an item of *property, plant and equipment* comprises its purchase price, including import duties and non-refundable purchase taxes after deducting trade discounts and rebates;

(b) any directly attributable *costs* of bringing the *asset* to working condition for its intended use the initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located, the obligation for which an entity incurs either when the item is acquired or as a consequence of having used the item during a particular period for purposes other than to produce inventories during that period.

Examples of directly attributable *costs* include the following:

(a) costs of employee benefits (as defined in Section 17 *Employee Benefits*) arising directly from the construction or acquisition of the item of property, plant and equipment;

(b) costs of site preparation;

(c) initial delivery and handling costs;

(d) installation and assembly costs;

(e) costs of testing whether the asset is functioning properly, after deducting the net proceeds from selling any items produced while bringing the asset to that location and condition (such as samples produced when testing equipment); and

(f) professional fees .

3.4 Examples of costs that are not costs of an item of property, plant and equipment are:

(a) costs of opening a new facility;

(b) costs of introducing a new product or service (including costs of advertising and promotional activities);

(c) costs of conducting business in a new location or with a new class of customer (including costs of staff training); and

(d) administration and other general overhead costs.

3.5 Recognition of costs in the carrying amount of an item of property, plant and equipment ceases when the item is in the location and condition necessary for it to be capable of operating in the manner intended by management. Therefore, costs incurred in using or redeploying an item is not included in the carrying amount of that item. For example, the following costs are not included in the carrying amount of an item of property, plant and equipment:

(a) costs incurred while an item capable of operating in the manner intended by management has yet to be brought into use or is operated at less than full capacity;

(b) initial operating losses, such as those incurred while demand for the item's output builds up; and

(c) costs of relocating or re-organising part or all of an entity's operations.

3.6 The *cost* of a self-constructed *asset* is determined using the same principles as for an acquired asset.

3.7 An item of *property, plant and equipment* may be acquired in exchange or part exchange for a dissimilar item of *property, plant and equipment* or other *asset*. The fair value of an asset for which comparable market transactions do not exist is reliably measurable if (a) the variability in the range of reasonable fair value estimates is not significant for that asset or (b) the probabilities of the various estimates within the range can be reasonably assessed and used in estimating fair value. If an entity is able to determine reliably the fair value of either the asset received or the asset given up, then the fair value of the asset given up is used to measure the cost of the asset received unless the fair value of the asset received is more clearly evident.

3.8 Parts of some items of property, plant and equipment may require replacement at regular intervals. Items of property, plant and equipment may also be acquired to make a less frequently recurring replacement, such as replacing the interior walls of a building, or to make a nonrecurring replacement. Under the recognition principle in paragraph 3.1, an entity recognises in the carrying amount of an item of property, plant and equipment the cost of replacing part of such an item when that cost is incurred if the recognition criteria are met. The carrying amount of those parts that are replaced is derecognised in accordance with the derecognition provisions of this Section.

3.9 A condition of continuing to operate an item of property, plant and equipment (for example, an aircraft) may be performing regular major inspections for faults regardless of whether parts of the item are replaced. When each major inspection is performed, its cost is recognised in the carrying amount of the item of property, plant and equipment as a replacement if the recognition criteria are satisfied. Any remaining carrying amount of the cost of the previous inspection (as distinct from physical parts) is derecognised. This occurs regardless of whether the cost of the previous inspection was identified in the transaction in which the item was acquired or constructed. If necessary, the estimated cost of a future similar inspection may be used as an indication of what the cost of the existing inspection component was when the item was acquired or constructed.

3.10 An entity does not recognize in the carrying amount of an item of property, plant and equipment the costs of the day-to-day servicing of the item. Rather, these costs are recognised in profit or loss as incurred. Costs of day-to-day servicing are primarily the costs of labour and consumables, and may include the cost of small parts. The purpose of these expenditures is often described as for the 'repairs and maintenance' of the item of property, plant and equipment.

3.11. Major components of some items of *property, plant and equipment* may require replacement at regular intervals. For example, a furnace may require relining after a specified number of hours of usage. The components are accounted for as separate *assets* because they have useful lives different from those of the items of *property, plant and equipment* to which they relate. Therefore, provided the recognition criteria in paragraph 3.1 are satisfied, the expenditure incurred in replacing or renewing the component is accounted for as the acquisition of a separate *asset*, and the replaced *asset* is written off.

Measurement subsequent to initial recognition

3.12 An entity shall choose either the cost model or the revaluation model as its accounting policy and shall apply that policy to an entire class of property, plant and equipment.

Cost model

3.13 After recognition as an asset, an item of property, plant and equipment shall be carried at its cost less any accumulated depreciation and any accumulated impairment losses.

Revaluation model

3.14 After recognition as an asset, an item of property, plant and equipment whose fair value can be measured reliably shall be carried at a revalued amount, being its fair value at the date of the revaluation less any subsequent accumulated depreciation and subsequent accumulated impairment losses. Revaluations shall be made with sufficient regularity to ensure that the carrying amount does not differ materially from that which would be determined using fair value at the balance sheet date.

3.15 The *fair value* of land and buildings is usually the market value. This value is determined by appraisal, which is normally undertaken by professionally qualified valuers. The fair value of items of plant and equipment is usually their market value determined by appraisal.

3.16. When there is no evidence of market value because of the specialized nature of the plant and equipment and because these items are rarely sold, except as part of a continuing business, they are valued at their depreciated replacement cost.

3.17. When an item of *property, plant and equipment* is revalued, any accumulated depreciation at the date of the revaluation is either:

(a) Restated proportionately with the change in the gross carrying amount of the *asset* so that the *carrying amount* of the *asset* after revaluation equals its revalued amount (this method is often used when an *asset* is revalued by means of an index to its depreciated replacement cost); or

(b) Eliminated against the gross carrying amount of the *asset* and the net amount restated to the revalued amount of the *asset*. For example, this method is used for buildings that are revalued to their market value.

The amount of the adjustment arising on the restatement or elimination of accumulated depreciation forms part of the increase or decrease in *carrying amount*, in accordance with paragraph 3.18 and 3.20.

3.18 When an item of *property, plant and equipment* is revalued, the entire class of *property, plant and equipment* to which that *asset* belongs shall be revalued.

3.19. When an asset's carrying amount is increased as a result of revaluation, the increase shall be credited directly to the "Surplus on Revaluation of Fixed Assets Accounts" and disclosed in the balance-sheet of the entity after Capital and Reserves.

3.20 Except and to the extent actually realised on disposal of the assets which are revalued, the surplus on revaluation of fixed assets shall not be applied to set-off or reduce any deficit or loss, whether past, current or future, or in any manner applied, adjusted or treated so as to add to the income, profit or surplus of the entity, or utilised directly or indirectly by way of dividend or bonus:

3.21 When an asset's carrying amount is decreased as a result of a revaluation, the decrease shall be recognized as an expense. The surplus on revaluation of fixed assets may be applied by the entity in setting-off or in diminution of any deficit arising from the revaluation of any other fixed assets of the entity:

3.22 Depreciation on assets which are revalued shall be determined with reference to the value assigned to such assets on revaluation and depreciation charge for the period shall be taken to the Profit and Loss Account.

3.23 An amount equal to incremental depreciation for the period shall be transferred from "Surplus on Revaluation of Fixed Assets Account" to equity through Statement of Changes in Equity to record realization of surplus to the extent of the incremental depreciation.

Depreciation

3.24. 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 shall be depreciated separately. A significant part of an item of property, plant and equipment may have a useful life and a depreciation method that are the same as the useful life and the depreciation method of another significant part of that same item. Such parts may be grouped in determining the depreciation charge.

3.25 The *depreciable amount* of an item of *property, plant and equipment* shall be allocated on a systematic basis over its *useful life*. The depreciation method used shall reflect the pattern according to which the *asset's* economic benefits are consumed by the entity. The depreciation charge for each period shall be recognized as an expense unless it is included in the *carrying amount* of another *asset*.

3.26. The economic benefits embodied in an item of *property, plant and equipment* are consumed by the entity principally through the use of the *asset*. However, other factors such as technical obsolescence and wear and tear while an *asset* remains idle often result in the diminution of the economic benefits that might have been expected to be available from the *asset*. Consequently, all the following factors need to be considered in determining the *useful life* of an *asset*:

(a) the expected usage of the *asset* by the entity (usage is assessed by reference to the *asset's* expected capacity or physical output);

(b) the expected physical wear and tear, which depends on operational factors such as the number of shifts for which the *asset* is to be used, the repair and maintenance programme of the entity, and the care and maintenance of the *asset* while idle;

(c) technical obsolescence arising from changes or improvements in production, or from a change in the market demand for the product or the service output of the *asset*; and

(d) legal or similar limits on the use of the *asset*, such as the expiry dates of related *lease*s.

3.27. Land and buildings are separable *assets* and are dealt with separately for accounting purposes, even when they are acquired together. Land normally has an unlimited life and, therefore, is not depreciated. Buildings have a limited life and, therefore, are depreciable *assets*. An increase in the value of the land on which a building stands does not affect the determination of the *useful life* of the building.

3.28 A variety of depreciation methods can be used to allocate the *depreciable amount* of an *asset* on a systematic basis over its *useful life*. These methods include the straight-line method, the diminishing balance method and the sum-of-the-units method. Straight-line depreciation results in a constant charge over the *useful life* of the *asset*. The diminishing balance method results in a decreasing charge over the *useful life* of the *asset*. The sum-of-the-units method results in a charge based on the expected use or output of the *asset*. The method used for an *asset* is selected based on the expected pattern of economic benefits and is consistently applied from period to period unless there is a change in the expected pattern of economic benefits from that *asset*.

3.29. The residual value and the useful life of an asset shall be reviewed at least at each financial year-end and, if expectations differ from previous estimates, the change(s) shall be accounted for as a change in an accounting estimate in accordance with paragraphs 12.10 to 12.11.

3.30 The depreciable amount of an asset is determined after deducting its residual value. In practice, the residual value of an asset is often insignificant and therefore immaterial in the calculation of the depreciable amount.

3.31 The depreciation method applied to *property, plant and equipment* shall be reviewed periodically and, if there has been a significant change in the expected pattern of economic benefits from those *assets*, the method shall be changed to reflect the changed pattern. When such a change in depreciation method is necessary, the change shall be accounted for as a change in accounting estimate, and the depreciation charge for the current and future periods shall be adjusted.

3.32 Depreciation of an asset begins when it is available for use, i.e. when it is in the location and condition necessary for it to be capable of operating in the manner intended by management. Depreciation of an asset ceases the date when the asset is derecognized. Therefore, depreciation does not cease when the asset becomes idle or is retired from active use unless the asset is fully depreciated. However, under usage methods of depreciation the depreciation charge can be zero while there is no production.

Impairment

3.33. At each balance sheet date, the entity shall assess whether there is any indication that an *asset* may be impaired. If there is any such indication, the entity shall consider whether the continued use of the *asset*, or group of *assets* forming a *cash generating unit*, is likely to generate *cash flows* sufficient to absorb the *amortization* of the *cost* of the *asset*. In the event that the undiscounted future *cash flows* are expected to be insufficient, the carrying value shall be reduced.

Derecognition

3.34 The carrying amount of an item of property, plant and equipment shall be derecognized:

(a) on disposal; or

(b) when no future economic benefits are expected from its use or disposal.

3.35 The gain or loss arising from the derecognition of an item of property, plant and equipment shall be included in profit or loss when the item is derecognized. Gains shall not be classified as revenue.

3.36 The disposal of an item of property, plant and equipment may occur in a variety of ways. In determining the date of disposal of an item, an entity applies the criteria applicable for recognizing revenue from the sale of goods.

Disclosure

3.37. The financial statements shall disclose, for each class of *property, plant and equipment*:

(a) the measurement bases used for determining the gross carrying amount (when more than one basis has been used, the gross carrying amount for that basis in each category shall be disclosed);

(b) the depreciation methods used;

(c) the useful lives or the depreciation rates used;

(d) the gross carrying amount and the accumulated depreciation (aggregated with accumulated impairment losses) at the beginning and end of the period; and

(e) a reconciliation of the *carrying amount* at the beginning and end of the period showing:

(i) additions;

(ii) disposals;

(iii) increases or decreases during the period resulting from revaluations;

(iv) *impairment losses* recognized in the income statement during the period (if any);

(v) *impairment losses* reversed in the income statement during the period (if any);

(vi) *depreciation*; and

(vii) other movements.

Comparative information is not required for the reconciliation in (e) above.

3.38 The financial statements shall also disclose the existence and amounts of restrictions on title, as well as *property, plant and equipment* pledged as security for *liabilities*.

3.39. When items of *property, plant and equipment* are stated at revalued amounts, the following shall be disclosed:

(a) the basis used to revalue the *assets*;

(b) the effective date of the revaluation; and

(c) whether an independent valuer was involved.

Section 4. Leases

Classification of leases

4.1. The classification of *leases* is based on the extent to which risks and rewards incident to ownership of a leased asset lie with the lessor or the lessee. Risks include the possibility of losses from idle capacity or technological obsolescence and of variations in return caused by changing economic conditions. Rewards may be represented by the expectation of profitable operation over the asset's *economic life* and of gain from appreciation in value or realization of a *residual value*.

4.2. A lease is classified as a finance lease if it transfers substantially all the risks and rewards incidental to ownership. A lease is classified as an operating lease if it does not transfer substantially all the risks and rewards incidental to ownership.

4.3. Whether a *lease* is a *finance lease* or an *operating lease* depends on the substance of the transaction rather than the form of the contract. Following are examples of situations that would normally lead to a lease's being classified as a finance lease:

(a) the *lease* transfers ownership of the *asset* to the lessee by the end of the *lease term*.

(b) the lessee has the option to purchase the *asset* at a price that is expected to be sufficiently lower than the *fair value* at the date the option becomes exercisable such that, at the *inception* of the *lease*, it is reasonably certain that the option will be exercised.

(c) the *lease term* is for the major part of the *economic life* of the *asset*, even if title is not transferred.

(d) at the *inception* of the *lease*, the present value of the *minimum lease payments* amounts to at least substantially all of the *fair value* of the leased asset.

(e) the leased assets are of a specialized nature such that only the lessee can use them without major modifications.

4.4. Following are indicators of situations that, individually or in combination, could also lead to a *lease* being classified as a finance lease:

(a) If the lessee can cancel the *lease*, the lessor's losses associated with the cancellation are borne by the lessee.

(b) Gains or losses from the fluctuation in the *fair value* of the residual fall to the lessee (for example, in the form of a rent rebate equalling most of the sales proceeds at the end of the *lease*).

(c) The lessee has the ability to continue the *lease* for a secondary period at a rent substantially lower than market rent.

Finance leases

4.5. At the commencement of the lease term**,** lessees shall recognize finance leases as *assets* and *liabilities* in their balance sheets at amounts equal to the *fair value* of the leased property or, if lower, at the present value of the *minimum lease payments*. In calculating the present value of the *minimum lease payments,* the discount factor is the *interest rate implicit in the lease,* if this is practicable to determine; if not, the lessee's incremental borrowing rate shall be used. Any initial direct costs of the lessee are added to the amount recognized as an asset.

4.6. Minimum Lease payments shall be apportioned between the finance charge and the reduction of the outstanding *liability*. The finance charge shall be allocated to periods during the *lease term* so as to produce a constant periodic rate of interest on the remaining balance of the *liability* for each period. Contingent rents shall be charged as expenses in the periods in which they are incurred.

4.7 A *finance lease* gives rise to a depreciation expense for the depreciable *asset* as well as a finance expense for each accounting period. The depreciation policy for depreciable leased *assets* shall be consistent with that for depreciable *assets* that are owned, and the depreciation recognized shall be calculated in accordance with Section 3 *Property, Plant & Equipment* and Section 5 *Intangible Assets*.

4.8. If there is no reasonable certainty that the lessee will obtain ownership by the end of the *lease term*, the *asset* shall be fully depreciated over the *lease term* or its *useful life*, whichever is shorter.

4.9. Lessees shall make the following disclosures for finance leases:

a) for each class of *asset*, the net *carrying amount* at the balance sheet date

b) a reconciliation between the total of future minimum lease payments at the balance sheet date, and their present value. In addition, an entity shall disclose the total of future minimum lease payments at the balance sheet date, and their present value, for each of the following periods:

(i) not later than one year;

(ii) later than one year and not later than five years;

(iii) later than five years.

(c) contingent rent recognized as an expense in the period.

Operating leases

4.10. Lease payments under an *operating lease* shall be recognized as an expense in the income statement on a straight-line basis over the *lease term* unless another systematic basis is representative of the time pattern of the user's benefit.

4.11. All incentives for the agreement of a new or renewed *operating lease* shall be recognized as an integral part of the net consideration agreed for the use of the leased asset. The lessee shall recognize the aggregate benefit of incentives as a reduction of rental expense over the *lease term*.

4.12. Lessees shall disclose the total of future *minimum lease payments* under *non-cancellable operating leases* for each of the following periods:

(i) not later than one year;

(ii) later than one year and not later than five years; and

(iii) later than five years.

Sale and leaseback

4.13. A sale-and-leaseback transaction involves the sale of an *asset* by the vendor and the leasing of the same *asset* back to the vendor. The lease payment and the sale price are usually interdependent since they are negotiated as a package. The accounting treatment of a sale-and-leaseback transaction depends on the type of *lease* involved.

4.14. If a sale-and-leaseback transaction results in a finance lease, any excess of sales proceeds over the *carrying amount* shall not be immediately recognized as income in the financial statements of a seller-lessee. Instead, it shall be deferred and amortized over the *lease term*.

4.15. If a sale-and-leaseback transaction results in an *operating lease* and it is clear that the transaction is established at *fair value*, any profit or loss shall be recognized immediately. If the sale price is below *fair value*, any profit or loss shall be recognized immediately except that, if the loss is compensated by future lease payments at below market price, it shall be deferred and amortized in proportion to the lease payments over the period for which the *asset* is expected to be used. If the sale price is above *fair value*, the excess over *fair value* shall be deferred and amortized over the period for which the *asset* is expected to be used.

4.16. For *operating leases*, if the *fair value* at the time of a sale-and-leaseback transaction is less than the *carrying amount* of the *asset*, a loss equal to the amount of the difference between the *carrying amount* and *fair value* shall be recognized immediately.

Section 5. Intangible Assets

Recognition and initial measurement of an intangible asset

5.1. An *intangible asset* shall be recognized if, and only if, it meets the definition of an *asset*, and:

(a) it is probable that the future economic benefits that are attributable to the *asset* will flow to the entity; and

(b) the *cost* of the *asset* can be measured reliably.

An entity controls an *asset* if the entity has the power to obtain the future economic benefits flowing from the underlying resource and also can restrict the access of others to those benefits. The capacity of an entity to control the future economic benefits from an *intangible asset* would normally stem from legal rights that are enforceable in a court of law. In the absence of legal rights, it is more difficult to demonstrate control. However, legal enforceability of a right is not a necessary condition for control, since an entity may be able to control the future economic benefits in some other way.

5.2. An entity shall assess the probability of future economic benefits using reasonable and supportable assumptions that represent management's best estimate of the set of economic conditions that will exist over the *useful life* of the *asset*.

5.3. An *intangible asset* shall be measured initially at cost.

5.4. Internally generated goodwill shall not be recognized as an *asset*.

Internally generated intangible assets

Research phase

5.5. No *intangible asset* arising from *research* (or from the research phase of an internal project) shall be recognized. Expenditure on research (or on the research phase of an internal project) shall be recognized as an expense when it is incurred.

Development phase

5.6. An *intangible asset* arising from *development* (or from the development phase of an internal project) shall be recognized if, and only if, an entity can demonstrate all of the following:

(a) the technical feasibility of completing the *intangible asset* so that it will be available for use or sale;

(b) the entity's intention to complete the *intangible asset* and use or sell it;

(c) its ability to use or sell the *intangible asset*;

(d) how the *intangible asset* will generate probable future economic benefits (among other things, the entity shall demonstrate the existence of a market for the output of the *intangible asset* or the *intangible asset* itself or, if it is to be used internally, the usefulness of the *intangible asset*);

(e) the availability of adequate technical, financial and other resources to complete the *development* and to use or sell the *intangible asset*; and

(f) its ability to measure reliably the expenditure attributable to the *intangible asset* during its *development*.

5.7. Internally generated brands, mastheads, publishing titles, customer lists and items similar in substance shall not be recognized as *intangible assets*.

Recognition of an expense

5.8. Expenditure on an intangible item shall be recognized as an expense when it is incurred, unless it forms part of the *cost* of an *intangible asset* that meets the recognition criteria (see paragraphs 5.1 to 5.7).

5.9. Expenditure on an intangible item that was initially recognized as an expense by a reporting entity in previous annual financial statements or interim financial reports shall not be recognized as part of the *cost* of an *intangible asset* at a later date.

5.10. Subsequent expenditure on an *intangible asset* after its purchase or its completion shall be recognized as an expense when it is incurred unless:

(a) it is probable that this expenditure will enable the *asset* to generate future economic benefits in excess of its originally assessed standard of performance; and

(b) this expenditure can be reliably measured and attributed to the *asset*.

If these conditions are met, the subsequent expenditure shall be added to the *cost* of the *intangible asset*.

5.11 In some cases, expenditure is incurred to provide future economic benefits to an entity, but no intangible asset or other asset is acquired or created that can be recognised. In these cases, the expenditure is recognised as an expense when it is incurred. For example, except when it forms part of the cost of a business combination, expenditure on research is recognised as an expense when it is incurred. Other examples of expenditure that is recognised as an expense when it is incurred include:

(a) expenditure on start-up activities (i.e. start-up costs), unless this expenditure is included in the cost of an item of property, plant and equipment. Start-up costs may consist of establishment costs such as legal and secretarial costs incurred in establishing a legal entity, expenditure to open a new facility or business (i.e. pre-opening costs) or expenditures for starting new operations or launching new products or processes (i.e. pre-operating costs).

(b) expenditure on training activities.

(c) expenditure on advertising and promotional activities.

(d) expenditure on relocating or re-organising part or all of an entity.

Measurement after recognition

5.12 An entity shall choose either the cost model or the revaluation model as its accounting policy. If an intangible asset is accounted for using the revaluation model, all the other assets in its class shall also be accounted for using the same model, unless there is no active market for those assets.

Cost model

5.13 After initial recognition, an intangible asset shall be carried at its cost less any accumulated amortization and any accumulated impairment losses.

Revaluation model

5.14 After initial recognition, an intangible asset shall be carried at a revalued amount, being its fair value at the date of the revaluation less any subsequent accumulated amortization and any subsequent accumulated impairment losses. For the purpose of revaluations under this Section, fair value shall be determined by reference to an active market. Revaluations shall be made with such regularity that at the balance sheet date the carrying amount of the asset does not differ materially from its fair value.

Useful life

5.15 An entity shall assess whether the useful life of an intangible asset is finite or indefinite and, if finite, the length of, or number of production or similar units constituting, that useful life. An intangible asset shall be regarded by the entity as having an indefinite useful life when, based on an analysis of all of the relevant factors, there is no foreseeable limit to the period over which the asset is expected to generate net cash inflows for the entity.

5.16 The useful life of an intangible asset that arises from contractual or other legal rights shall not exceed the period of the contractual or other legal rights, but may be shorter depending on the period over which the entity expects to use the asset. If the contractual or other legal rights are conveyed for a limited term that can be renewed, the useful life of the intangible asset shall include the renewal period(s) only if there is evidence to support renewal by the entity without significant cost.

Amortization

Intangible assets with finite useful lives

Amortization period and amortization method

5.17 The depreciable amount of an intangible asset with a finite useful life shall be allocated on a systematic basis over its useful life. Amortisation shall begin when the asset is available for use, i.e. when it is in the location and condition necessary for it to be capable of operating in the manner intended by management. Amortisation shall cease at the earlier of the date that the asset is classified as held for sale and the date that the asset is derecognised. The amortisation method used shall reflect the pattern in which the asset's future economic benefits are expected to be consumed by the entity. If that pattern cannot be determined reliably, the straight-line method shall be used. The amortisation charge for each period shall be recognised in profit or loss unless this or another Section permits or requires it to be included in the carrying amount of another asset.

Residual value

5.18 The residual value of an intangible asset with a finite useful life shall be assumed to be zero unless:

(a) there is a commitment by a third party to purchase the asset at the end of its useful life; or

(b) there is an active market for the asset and:

(i) residual value can be determined by reference to that market; and

(ii) it is probable that such a market will exist at the end of the asset's useful life.

Review of amortisation period and amortisation method

5.19 The amortisation period and the amortisation method for an intangible asset with a finite useful life shall be reviewed at least at each financial year-end. If the expected useful life of the asset is different from previous estimates, the amortisation period shall be changed accordingly. If there has been a change in the expected pattern of consumption of the future economic benefits embodied in the asset, the amortisation method shall be changed to reflect the changed pattern. Such changes shall be accounted for as changes in accounting estimates in accordance with paragraphs 12.10 to 12.11.

Intangible assets with indefinite useful lives

5.20 An intangible asset with an indefinite useful life shall not be amortized.

5.21 An entity is required to test an intangible asset with an indefinite useful life for impairment by comparing its recoverable amount with its carrying amount

(a) annually, and

(b) whenever there is an indication that the intangible asset may be impaired.

Review of useful life assessment

5.22 The useful life of an intangible asset that is not being amortized shall be reviewed each period to determine whether events and circumstances continue to support an indefinite useful life assessment for that asset. If they do not, the change in the useful life assessment from indefinite to finite shall be accounted for as a change in an accounting estimate.

Recoverability of the carrying amount: Impairment losses

5.23. At each balance sheet date, the entity shall assess whether there is any indication that an asset may be impaired. If there is any such indication, the entity shall consider whether the continued use of the asset, or group of assets forming a cash-generating unit, is likely to generate cash flows sufficient to absorb the amortization of the cost of the asset. In the event that the undiscounted future cash flows are expected to be insufficient, the carrying value shall be reduced.

Retirements and disposals

5.24. An *intangible asset* shall be de-recognized (eliminated from the balance sheet) on disposal or when no future economic benefits are expected from its use and subsequent disposal.

5.25. Gains or losses arising from the retirement or disposal of an *intangible asset* shall be determined as the difference between the net disposal proceeds and the *carrying amount* of the *asset* and shall be recognized as income or expense in the income statement.

Disclosure

5.26. The financial statements shall disclose the following for each class of *intangible assets*, distinguishing between internally generated *intangible assets* and other *intangible assets:*

(a) Whether the useful lives are indefinite or finite and, if finite, the useful lives or the amortization rates used;

(b) the amortization methods used for intangible assets with finite useful lives;

(c) the gross carrying amount and the accumulated *amortization* (aggregated with accumulated impairment losses) at the beginning and end of the period;

(d) the line item(s) of the income statement in which the *amortization* of *intangible assets* is included; and

(e) a reconciliation of the *carrying amount* at the beginning and end of the period showing:

(i) retirements and disposals;

(ii) *impairment losses* recognized;

(iii) *impairment losses* reversed;

(iv) *amortization* recognized during the period; and

(v) additions and other changes in the *carrying amount* during the period.

Comparative information is not required.

5.27. The financial statements shall also disclose:

(a) for an intangible asset assessed as having an indefinite useful life, the carrying amount of that asset and the reasons supporting the assessment of an indefinite useful life. In giving these reasons, the entity shall describe the factor(s) that played a significant role in determining that the asset has an indefinite useful life.

(b) a description, the carrying amount and remaining amortisation period of any individual intangible asset that is material to the entity's financial statements.

(c) for intangible assets acquired by way of a government grant and initially recognised at fair value:

(i) the fair value initially recognised for these assets;
(ii) their carrying amount; and
(iii) whether they are measured after recognition under the cost model or the revaluation model.

(d) the existence and carrying amounts of intangible assets whose title is restricted and the carrying amounts of intangible assets pledged as security for liabilities.

(e) the amount of contractual commitments for the acquisition of intangible assets.

Section 6. Inventories

6.1 This Section does not apply to the measurement of inventories held by:

(a) producers of agricultural and forest products, agricultural produce after harvest, and minerals and mineral products, to the extent that they are measured at net realisable value in accordance with well established practices in those industries. When such inventories are measured at net realisable value, changes in that value are recognised in profit or loss in the period of the change.

(b) commodity broker-traders who measure their inventories at fair value less costs to sell. When such inventories are measured at fair value less costs to sell, changes in fair value less costs to sell are recognised in profit or loss in the period of the change.

6.2. *Inventories* shall be measured at the lower of cost and *net realizable value*.

6.3. The cost of *inventories* shall comprise all costs of purchase, costs of conversion and other costs incurred in bringing the *inventories* to their present location and condition.

6.4. The cost of *inventories* of items that are not ordinarily interchangeable and goods or services produced and segregated for specific projects shall be assigned by using specific identification of their individual costs.

6.5 The cost of *inventories*, other than those dealt with in paragraph 6.3, shall be assigned by using the first-in, first-out (FIFO) or weighted average cost formulas. *An entity shall use the same cost formula for all inventories having a similar nature and use to the entity. For inventories with a different nature or use, different cost formulas may be justified.*

Recognition as an expense

6.6. When *inventories* are sold, the carrying amount of those *inventories* shall be recognized as an expense in the period in which the related *revenue* is recognized. The amount of any write-down of *inventories* to *net realizable value* and all losses of *inventories* shall be recognized as an expense in the period in which the write-down or loss occurs. The amount of any reversal of any write-down of *inventories* arising from an increase in *net realizable value* shall be recognized as a reduction in the amount of *inventories* recognized as an expense in the period in which the reversal occurs.

Disclosure

6.7. The financial statements shall disclose:

(a) the *accounting policies* adopted in measuring *inventories*, including the cost formula used;

(b) the total carrying amount of *inventories* and the carrying amount in classifications appropriate to the entity; and

(c) the carrying amount of inventories carried at fair value less costs to sell.

(d) the amount of inventories recognized as an expense in the period.

(e) the amount of any write-down of inventories recognized as an expense in the period in accordance with paragraph 6.6.

(f) the amount of any reversal of any write-down that is recognized as a reduction in the amount of inventories recognized as expense in the period in accordance with paragraph 6.6.

(g) the circumstances or events that led to the reversal of a write-down of inventories in accordance with paragraph 6.6.

(h) the carrying amount of *inventories* pledged as security for *liabilities*.

Section 7. Accounting for Government Grants and Disclosure of Government Assistance

7.1. *Government grants* are assistance by government in the form of transfers of resources to an entity in return for past or future compliance with certain conditions relating to the operating activities of the entity. They exclude those forms of government assistance which cannot reasonably have a value placed upon them and transactions with government which cannot be distinguished from the normal trading transactions of the entity.

7.2. *Government grants*, including non-monetary grants at *fair value*, shall not be recognized until there is reasonable assurance that:

(a) the entity will comply with the conditions attaching to them; and
(b) the grants will be received.

7.3. *Government grants* shall be recognized as income over the periods necessary to match them with the related *costs* they are intended to compensate, on a systematic basis. They shall not be credited directly to shareholders' interests.

7.4. In most cases, the periods over which an entity recognizes the costs or expenses related to a government grant are readily ascertainable, and thus grants in recognition of specific expenses are recognized as income in the same period as the relevant expense. Similarly, grants related to depreciable *assets* are usually recognized as income over the periods and in the proportions in which *depreciation* on those *assets* is charged.

7.5. A government grant that becomes receivable as compensation for expenses or losses already incurred or for the purpose of giving immediate financial support to the entity, with no future related costs, shall be recognized as income of the period in which it becomes receivable,

7.6. Government *grants related to assets*, including non-monetary grants at *fair value*, shall be presented on the balance sheet either by setting up the grant as deferred income or by deducting the grant in arriving at the *carrying amount* of the *asset*.

7.7. *Grants related to income* are sometimes presented as a credit in the income statement, either separately or under a general heading such as "Other income"; alternatively, they are deducted in reporting the related expense.

7.8. A government grant that becomes repayable shall be accounted for as a revision to an accounting estimate. Repayment of a grant related to income shall be applied first against any unamortized deferred credit set up in respect of the grant. To the extent that the repayment exceeds any such deferred credit, or where no deferred credit exists, the repayment shall be recognized immediately as an expense. Repayment of a grant related to an *asset* shall be recorded by increasing the *carrying amount* of the *asset* or reducing the deferred income balance by the amount repayable. The cumulative additional *depreciation* that would have been recognized to date as an expense in the absence of the grant shall be recognized immediately as an expense.

Government assistance

7.9. Excluded from the definition of *government grants* in paragraph 7.1 are certain forms of *government assistance* that cannot reasonably have a value placed on them and transactions that cannot be distinguished from the normal trading transactions of the entity.

7.10. Examples of assistance that cannot reasonably have a value placed on them are free technical or marketing advice and the provision of guarantees. An example of assistance that cannot be distinguished from the normal trading transactions of the entity is a government procurement policy that is responsible for a portion of the entity's sales. The existence of the benefit might be unquestioned, but any attempt to segregate the trading activities from *government assistance* could well be arbitrary.

7.11. The significance of the benefit in the above examples may be such that disclosure of the nature, extent and duration of the assistance is necessary so that the financial statements will not be misleading.

7.12. Loans at nil or low interest rates are a form of *government assistance*, but the benefit is not quantified by the imputation of interest.

7.13. *Government assistance* to entities meets the definition of *government grants* even if there are no conditions specifically relating to the *operating activities* of the entity other than the requirement to operate in certain regions or industry sectors. Such grants shall therefore not be credited to equity.

Disclosure

7.14. The following matters shall be disclosed:

(a) the accounting policy adopted for *government grants*, including the methods of presentation adopted in the financial statements;

(b) the nature and extent of *government grants* recognized in the financial statements and an indication of other forms of *government assistance* from which the entity has directly benefited; and

(c) unfulfilled conditions and other contingencies attaching to *government assistance* that has been recognized.

Section 8. Provisions, Contingent Liabilities and Contingent Assets

8.1. A *provision* shall be recognized when:

(a) an entity has a present obligation (legal or constructive) as a result of a past event, excluding those arising from executory contracts, except where these are onerous;

(b) it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and

(c) a reliable estimate can be made of the amount of the obligation.

If these conditions are not met, no provision shall be recognized.

Probable outflow of resources embodying economic benefits

8.2. For a *liability* to qualify for recognition, there must be not only a present obligation but also the probability of an outflow of resources embodying economic benefits to settle that obligation. For the purpose of this Section, an outflow of resources or other event is regarded as probable if the event is more likely than not to occur (i.e. the probability that the event will occur is greater than the probability that it will not). Where it is not probable that a present obligation exists, an entity discloses a *contingent liability,* unless the possibility of an outflow of resources embodying economic benefits is remote (see paragraph 8.19).

Reliable estimate of the obligation

8.3. The use of estimates is an essential part of the preparation of financial statements and does not undermine their reliability. This is especially true in the case of *provisions*, which by their nature are more uncertain than most other balance sheet items. Except in extremely rare cases, an entity will be able to determine a range of possible outcomes and can therefore make an estimate of the obligation that is sufficiently reliable to use in recognizing a *provision*.

Contingent liabilities

8.4. An entity shall not recognize a *contingent liability.*

8.5. A *contingent liability* is disclosed, as required by paragraph 8.25, unless the possibility of an outflow of resources embodying economic benefits is remote.

Contingent assets

8.6. An entity shall not recognize a *contingent asset.*

8.7. *Contingent assets* are not recognized in financial statements, since this may result in the recognition of income that may never be realized. However, when the realization of income is virtually certain, then the related asset is not a *contingent asset* and its recognition is appropriate.

8.8. A *contingent asset* is disclosed, as required by paragraph 8.26, where an inflow of economic benefits is probable.

Measurement

8.9. The amount recognized as a *provision* shall be the best estimate of the expenditure required to settle the present obligation at the balance sheet date. The entity shall disclose whether the amount has been discounted

Risks and uncertainties

8.10. Risk describes variability of outcome. A risk adjustment may increase the amount at which a *liability* is measured. Caution is needed in making judgments under conditions of uncertainty, so that income or assets are not overstated and expenses or *liabilities* are not understated. However, uncertainty does not justify the creation of excessive *provisions* or a deliberate overstatement of *liabilities*. For example, if the projected costs of a particularly adverse outcome are estimated on a prudent basis, that outcome is not then deliberately treated as more probable than is realistically the case. Care is needed to avoid duplicating adjustments for risk and uncertainty with consequent overstatement of a *provision.*

8.11. The risks and uncertainties that inevitably surround many events and circumstances shall be taken into account in reaching the best estimate of a *provision*.

8.12. Where some or all of the expenditure required to settle a *provision* is expected to be reimbursed by another party, the reimbursement shall be recognized when, and only when, it is virtually certain that reimbursement will be received if the entity settles the obligation. The reimbursement shall be treated as a separate *asset*. The amount recognized for the reimbursement shall not exceed the amount of the *provision*. Gains from the expected disposal of *assets* shall not be taken into account when measuring a *provision*.

8.13. In the income statement, the expense relating to a *provision* may be presented net of the amount recognized for a reimbursement.

8.14. *Provisions* shall be reviewed at each balance sheet date and adjusted to reflect the current best estimate. If it is no longer probable that an outflow of resources embodying economic benefits will be required to settle the obligation, the *provision* shall be reversed.

8.15. A *provision* shall be used only for expenditures for which the *provision* was originally recognized.

8.16 *Provisions* shall not be recognized for future operating losses.

8.17 If an entity has a contract that is onerous, the present obligation under the contract shall be recognized and measured as a *provision*.

Present Value

8.18 Where the effect of the time value of money is material, the amount of a provision shall be the present value of the expenditures expected to be required to settle the obligation.

8.19 The discount rate (or rates) shall be a pre-tax rate (or rates) that reflect(s) current market assessments of the time value of money and the risks specific to the liability. The discount rate(s) shall not reflect risks for which future cash flow estimates have been adjusted.

Future events and Expected disposal of assets

8.20 Future events that may affect the amount required to settle an obligation shall be reflected in the amount of a provision where there is sufficient objective evidence that they will occur. Gains from the expected disposal of assets shall not be taken into account in measuring a provision.

Restructuring

8.21 A provision for restructuring costs is recognised only when the general recognition criteria for provisions are met.

8.22 Constructive obligation to restructure arises only when an entity:

(a) has a detailed formal plan for the restructuring identifying at least:

(i) the business or part of a business concerned;

(ii) the principal locations affected;

(iii) the location, function, and approximate number of employees who will be compensated for terminating their services;

(iv) the expenditures that will be undertaken; and

(v) when the plan will be implemented; and

(b) has raised a valid expectation in those affected that it will carry out the restructuring by starting to implement that plan or announcing its main features to those affected by it.

8.23 No obligation arises for the sale of an operation until the entity is committed to the sale, i.e. there is a binding sale agreement. Even when an entity has taken a decision to sell an operation and announced that decision publicly, it cannot be committed to the sale until a purchaser has been identified and there is a binding sale agreement. Until there is a binding sale agreement, the entity will be able to change its mind and indeed will have to take another course of action if a purchaser cannot be found on acceptable terms.

8.24 A restructuring provision shall include only the direct expenditures arising from the restructuring, which are those that are both:

(a) necessarily entailed by the restructuring; and

(b) not associated with the ongoing activities of the entity.

Disclosure

8.25 For each class of *provision*, an entity shall disclose:

(a) the *carrying amount* at the beginning and end of the period;

(b) a brief description of the nature of the obligation and the expected timing of any resulting outflows of economic benefits;

(c) additional provisions made in the period, including increases to existing provisions;

(d) amounts used (i.e. incurred and charged against the provision) during the period;

(e) unused amounts reversed during the period;

(f) the increase during the period in the discounted amount arising from the passage of time and the effect of any change in the discount rate; and

(g) a brief description of the nature of the obligation and the expected timing of any resulting outflows of economic benefits including an indication of the uncertainties about the amount or timing of those outflows. Where necessary to provide adequate information, an entity shall disclose the major assumptions made concerning future events.

8.26 Unless the possibility of any outflow in settlement is remote, an entity shall disclose for each class of *contingent liability* at the balance sheet date a brief description of the nature of the *contingent liability* and, where practicable, an estimate of its financial effect, measured under paragraphs 8.9 and 8.10. An indication of the uncertainties relating to the amount or timing of any outflow; and the possibility of any reimbursement shall also be disclosed.

8.27 Where an inflow of economic benefits is probable, an entity shall disclose a brief description of the nature of the *contingent assets* at the balance sheet date and, where practicable, an estimate of their financial effect, measured using the principles set out for *provisions* in paragraphs 8.9 and 8.10.

8.28 Where any of the information required by paragraphs **8.26 and 8.27** is not disclosed because it is not practicable to do so, that fact shall be stated.

8.29 In extremely rare cases, disclosure of some or all of the information required by paragraphs **8.25 to 8.27** can be expected to prejudice seriously the position of the entity in a dispute with other parties on the subject matter of the *provision*, *contingent liability* or *contingent asset*. In such cases, an entity need not disclose the information but shall disclose the general nature of the dispute, together with the fact that, and the reason why, the information has not been disclosed.

8.30 Examples of accounting for *provisions* are given in Annex 3, part A.

Section 9. Revenue

Measurement of revenue

9.1. *Revenue* shall be measured at the *fair value* of the consideration received or receivable.

*9.*2 *Revenue* includes only the gross inflows of economic benefits received and receivable by the entity on its own account. Amounts collected on behalf of third parties, such as sales taxes, goods and services taxes and value-added taxes, are not economic benefits flowing to the entity and hence does not result in increases in equity. Therefore, they are excluded from *revenue*. Similarly, in an agency relationship, the gross inflows of economic benefits include amounts collected on behalf of the principal and which does not result in increases in equity for the entity. The amounts collected on behalf of the principal are not *revenue*. Instead, *revenue* is the amount of commission.

Sale of goods

9.3. *Revenue* from the sale of goods shall be recognized when all the following conditions have been satisfied:

(a) the entity has transferred to the buyer the significant risks and rewards of ownership of the goods;

(b) the entity retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold;

(c) the amount of *revenue* can be measured reliably;

(d) it is probable that the economic benefits associated with the transaction will flow to the entity; and

(e) the costs incurred or to be incurred in respect of the transaction can be measured reliably.

9.4 "Goods" include goods produced by the entity for the purpose of sale and goods purchased for resale, such as merchandise purchased by a retailer or land and other property held for resale

Rendering of services

9.5 The rendering of services typically involves the performance by the entity of a contractually agreed task over an agreed period of time. The services may be rendered within a single period or over more than one period. Some contracts for the rendering of services are directly related to *construction contract*s – for example, those for the services of project managers and architects.

9.6. When the outcome of a transaction involving the rendering of services can be estimated reliably, *revenue* associated with the transaction shall be recognized by reference to the stage of completion of the transaction at the balance sheet date. The outcome of a transaction can be estimated reliably when all the following conditions are satisfied:

(a) the amount of *revenue* can be measured reliably;

(b) it is probable that the economic benefits associated with the transaction will flow to the entity;

(c) the stage of completion of the transaction at the balance sheet date can be measured reliably; and

(d) the costs incurred for the transaction and the costs to complete the transaction can be measured reliably.

9.7. When the outcome of the transaction involving the rendering of services cannot be estimated reliably, *revenue* shall be recognized only to the extent of the expenses recognized that are recoverable.

Interest, royalties and dividends

9.8. *Revenue* arising from the use by others of entity *assets* yielding interest, royalties and dividends shall be recognized on the bases set out in paragraph 9.9 when:

(a) it is probable that the economic benefits associated with the transaction will flow to the entity; and

(b) the amount of the *revenue* can be measured reliably.

9.9. *Revenue* shall be recognized on the following bases:

(a) interest shall be recognized using the effective interest method taking into account the effective interest rate that exactly discounts the estimated future cash receipts to the net carrying amount of the related asset.

(b) royalties shall be recognized on an accrual basis in accordance with the substance of the relevant agreement; and

(c) dividends shall be recognized when the shareholder's right to receive payment is established.

9.10. *Revenue* is recognized only when it is probable that the economic benefits associated with the transaction will flow to the entity. However, when uncertainty arises about the collectibility of an amount already included in *revenue,* the uncollectible amount, or the amount in respect of which recovery has ceased to be probable, is recognized as an expense rather than as an adjustment of the amount of *revenue* originally recognized. Some examples of *revenue* recognition issues are given in Annex 3, part B.

Disclosure

9.11. An entity shall disclose:

(a) the *accounting policies* adopted for the recognition of *revenue*, including the methods adopted to determine the stage of completion of transactions involving the rendering of services;

(b) the amount of each significant category of *revenue* recognized during the period, including *revenue* arising from:

(i) the sale of goods;

(ii) the rendering of services;

(iii) interest;

(iv) royalties;

(v) dividends; and

(c) the amount of *revenue* arising from exchanges of goods or services included in each significant category of *revenue*.

Section 10. Borrowing Costs

10.1. *Borrowing costs* may include:

(a) interest on bank overdrafts and short-term and long-term borrowings;

(b) amortization of ancillary costs incurred in connection with the arrangement of borrowings;

(c) finance charges in respect of finance leases; and

(d) *exchange differences* arising from *foreign currency* borrowings to the extent that they are regarded as an adjustment to interest costs.

Recognition

Borrowing costs: benchmark treatment

10.2. *Borrowing costs* shall be recognized as an expense in the period in which they are incurred.

10.3. *Borrowing costs* shall be recognized as an expense in the period in which they are incurred, except to the extent that they are capitalized in accordance with paragraph 10.4.

10.4. *Borrowing costs* that are directly attributable to the acquisition, construction or production of a *qualifying asset* shall be capitalized as part of the cost of that *asset*. The amount of *borrowing costs* eligible for capitalization shall be determined in accordance with this Section.

10.5. Examples of *qualifying assets* are *inventories* that require a substantial period of time to bring them to a saleable condition, manufacturing plants, power generation facilities and investment properties. Other investments, and those *inventories* that are routinely manufactured or otherwise produced in large quantities on a repetitive basis over a short period of time, are not *qualifying assets*. *Assets* that are ready for their intended use or sale when acquired also are not *qualifying assets*.

Borrowing costs eligible for capitalization

10.6. To the extent that funds are borrowed specifically for the purpose of obtaining a *qualifying asset*, the amount of *borrowing costs* eligible for capitalization on that asset shall be determined as the actual *borrowing costs* incurred on that borrowing during the period less any investment income on the temporary investment of those borrowings.

10.7. To the extent that funds are borrowed generally and used for the purpose of obtaining a *qualifying asset*, the amount of *borrowing costs* eligible for capitalization shall be determined by applying a capitalization rate to the expenditures on that *asset*. The capitalization rate shall be the weighted average of the *borrowing costs* applicable to the borrowings of the entity that are outstanding during the period, other than borrowings made specifically for the purpose of obtaining a *qualifying asset*. The amount of *borrowing costs* capitalized during a period shall not exceed the amount of *borrowing costs* incurred during that period.

10.8. The capitalization of *borrowing costs* as part of the *cost* of a *qualifying asset* shall commence when:

(a) expenditures for the *asset* are being incurred;

(b) *borrowing costs* are being incurred; and

(c) activities that are necessary to prepare the *asset* for its intended use or sale are in progress.

10.9. Capitalization of *borrowing costs* shall be suspended during extended periods in which active development is interrupted.

10.10. Capitalization of *borrowing costs* shall cease when substantially all the activities necessary to prepare the *qualifying asset* for its intended use or sale are complete.

10.11. When the construction of a *qualifying asset* is completed in parts and each part is capable of being used while construction continues on other parts, capitalization of *borrowing costs* shall cease when substantially all the activities necessary to prepare that part for its intended use or sale are completed.

10.12 When the carrying amount or the expected ultimate cost of the qualifying asset exceeds its recoverable amount or net realizable value, the carrying amount is written down or written off to the recoverable amount or net realizable value.

Disclosure

10.13 The financial statements shall disclose:

(a) the accounting policy adopted for *borrowing costs*;

(b) the amount of *borrowing costs* capitalized during the period; and

(c) the capitalization rate used to determine the amount of *borrowing costs* eligible for capitalization.

Section 11. Income Taxes

Current tax

11.1 *Current tax* for current and prior periods shall, to the extent unpaid, be recognized as a *liability*. If the amount already paid in respect of current and prior periods exceeds the amount due for those periods, the excess shall be recognized as an *asset*.

11.2 The benefit relating to a *tax loss* that can be carried back to recover *current tax* of a previous period shall be recognized as an *asset*.

11.3 *Current tax* liabilities (assets) for the current and prior periods shall be measured at the amount expected to be paid to (recovered from) the taxation authorities, using the tax rates (and tax laws) that have been enacted or substantively enacted by the balance sheet date.

Deferred Tax

11.4 A deferred tax liability shall be recognised for all taxable temporary differences, except to the extent that the deferred tax liability arises from:

(a) the initial recognition of goodwill; or

(b) the initial recognition of an asset or liability in a transaction which:

(i) is not a business combination; and

(ii) at the time of the transaction, affects neither accounting profit nor taxable profit (tax loss).

11.5 A deferred tax asset shall be recognised for all deductible temporary differences to the extent that it is probable that taxable profit will be available against which the deductible temporary difference can be utilised, unless the deferred tax asset arises from the initial recognition of an asset or liability in a transaction that:

(a) is not a business combination; and

(b) at the time of the transaction, affects neither accounting profit nor taxable profit (tax loss).

11.6 A deferred tax asset shall be recognised for the carry forward of unused tax losses and unused tax credits to the extent that it is probable that future taxable profit will be available against which the unused tax losses and unused tax credits can be utilised.

11.7 Deferred tax assets and liabilities shall be measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted by the balance sheet date.

11.8 The measurement of deferred tax liabilities and deferred tax assets shall reflect the tax consequences that would follow from the manner in which the entity expects, at the balance sheet date, to recover or settle the carrying amount of its assets and liabilities.

Income statement

11.9 Current and deferred tax shall be recognised as income or an expense and included in profit or loss for the period, except to the extent that the tax arises from:

(a) a transaction or event which is recognised, in the same or a different period, directly in equity); or

(b) a business combination.

11.10 Current tax and deferred tax shall be charged or credited directly to equity if the tax relates to items that are credited or charged, in the same or a different period, directly to equity

Presentation

11.11 Tax assets and tax liabilities shall be presented separately from other *assets* and *liabilities* in the balance sheet. *Deferred tax assets and liabilities*, if recognized, shall be distinguished from *current tax* assets and liabilities.

11.12 When an entity makes a distinction between current and non-current assets and liabilities in its financial statements, and has decided to account for deferred taxes, it shall not classify *deferred tax assets (liabilities)* as current assets (liabilities).

11.13 An entity shall offset *current and deferred tax* assets and *current and deferred tax* liabilities if, and only if, the entity:

(a) has a legally enforceable right to set off the recognized amounts; and

(b) intends either to settle on a net basis or to realize the *asset* and settle the *liability* simultaneously.

11.14 The major components of *tax expense* (income) shall be disclosed separately.

11.15 An entity shall disclose the amount of a deferred tax asset and the nature of the evidence supporting its recognition, when:

(a) the utilisation of the deferred tax asset is dependent on future taxable profits in excess of the profits arising from the reversal of existing taxable temporary differences; and

(b) the entity has suffered a loss in either the current or preceding period in the tax jurisdiction to which the deferred tax asset relates.

11.16 The entity shall disclose the amount (and expiry date, if any) of deductible temporary differences, unused tax losses, and unused tax credits for which no deferred tax asset is recognised in the balance sheet.

Section 12. Accounting Policies, Changes in Accounting Estimates and Errors

12.1. Management shall select and apply an entity's *accounting policies* so that the financial statements comply with all the requirements of this Standard. Where there is no specific requirement, management shall look in turn to the following for guidance:

(a) full IAS/IFRS issued by IASB;

(b) interpretations issued by SIC and IFRIC;

(c) appendices to standards issued by IASB;

(d) implementation guidance issued by IASB;

(e) the definitions, recognition criteria and measurement concepts set out in the conceptual framework of IASB; and

(f) pronouncements of the country and jurisdiction that use a similar conceptual framework to develop accounting standards; other accounting literature; and accepted industry practice, to the extent that these are consistent with items (a) to (e) above.

Management shall use its judgment in developing an accounting policy resulting in information that is relevant to the needs of investors and creditors and is reliable in nature.

12.2. An entity shall select and apply its *accounting policies* for a period consistently for similar transactions, other events and circumstances, unless the Standard elsewhere specifically requires or permits categorization of items for which different policies may be appropriate. If this Section requires or permits such categorization, an appropriate accounting policy shall be selected and applied consistently to each category.

12.3. A change in accounting policy shall be made only if it is required by the Standard or if it results in a more relevant and reliable presentation in the financial statements of the effects of transactions or other events on the entity's financial position, financial performance or *cash flows*.

12.4. The following are not changes in accounting policies:

(a) the adoption of an accounting policy for transactions or other events that differ in substance from those previously occurring; and

(b) the adoption of a new accounting policy for transactions or other events that did not occur previously or were immaterial.

The initial application of a policy to revalue assets in accordance with Section 3 *Property, Plant and Equipment* or Section 5 *Intangible Assets* is a change in an accounting policy to be dealt with as a revaluation in accordance with Sections 3 or 5, rather than in accordance with this Section.

12.5. A change in an accounting policy that is made following an amendment to the Standard shall be accounted for in accordance with the transitional provisions, if any, issued with the Standard.

12.6. Where application of a change in the Standard has a material effect on the current period or any prior period presented, an entity shall disclose the following:

(a) the fact that the change in accounting policy is made in accordance with the change in the Standard, with a description of those provisions;

(b) the amount of the adjustment for the current period and for each prior period presented;

(c) the amount of the adjustment relating to periods prior to those included in the comparative information; and

(d) the fact that comparative information has been restated, or that restatement for a particular prior period has not been made because it would require undue cost and effort.

12.7. A change in an accounting policy other than one mandated under paragraph 12.5 shall be applied retrospectively. The opening balance of retained earnings for the earliest prior period presented and the other comparative amounts disclosed for each prior period presented shall be adjusted, where applicable, as if the new accounting policy had always been in use.

12.8. Comparative information presented for a particular prior period need not be restated if restating the information would require undue cost or effort. When comparative information for a particular prior period is not restated, the new accounting policy shall be applied to the balances of *assets* and *liabilities* as at the beginning of the next period, and a corresponding adjustment shall be made to the opening balance of retained earnings for the next period.

12.9. When a change in an accounting policy has an effect on the current period or any prior period presented, or may have an affect in subsequent periods, an entity shall disclose the following:

(a) the reasons for the change;

(b) the amount of the adjustment for the current period and for each prior period presented;

(c) the amount of the adjustment relating to periods prior to those presented; and

(d) that comparative information has been restated, or that restatement for a particular prior period has not been made because it would require undue cost or effort.

Changes in accounting estimates

12.10. The effect of a change in an accounting estimate shall be recognized prospectively by including it in profit or loss in:

(a) the period of the change, if the change affects that period only; or

(b) the period of the change and future periods, if the change affects both.

12.11 To the extent that a change in an accounting estimate gives rise to changes in assets and liabilities, or relates to an item of equity, it shall be recognised by adjusting the carrying amount of the related asset, liability or equity item in the period of the change.

12.12. The nature and amount of a change in an accounting estimate that has an affect on the current period or is expected to have an effect in subsequent periods shall be disclosed. If it is impractical to quantify that amount, this fact shall be disclosed.

Errors

12.13 An entity shall correct material prior period errors retrospectively in the first set of financial statements authorized for issue after their discovery by:

(a) restating the comparative amounts for the prior period(s) presented in which the error occurred; or

(b) if the error occurred before the earliest prior period presented, restating the opening balances of assets, liabilities and equity for the earliest prior period presented.

Limitations on retrospective restatement

12.14 A prior period error shall be corrected by retrospective restatement except to the extent that it is impracticable to determine either the period-specific effects or the cumulative effect of the error.

Disclosure

12.15. An entity shall disclose:

(a) the nature of the error; and

(b) the amount of the correction for each prior period presented.

Section 13. The Effects of Changes in Foreign Exchange Rates

Foreign currency transactions

13.1. A foreign currency transaction, other than derivative transactions, shall be recorded, on initial recognition in the *reporting currency*, by applying the spot exchange rate *between* the *reporting currency* and the *foreign currency* at the date of the transaction. The date of a transaction is the date on which the transaction first qualifies for recognition. For practical reasons, a rate that approximates the actual rate at the date of the transaction is often used, for example, an average rate for a week or a month might be used for all transactions in each foreign currency occurring during that period. However, if exchange rates fluctuate significantly, the use of the average rate for a period is inappropriate.

13.2. At each balance sheet date:

(a) foreign currency *monetary items* shall be reported using the *closing rate;*

(b) non-monetary items that are carried in terms of *historical cost* denominated in a *foreign currency* shall be reported using the *exchange rate* at the date of the transaction; and

(c) non-monetary items that are carried at *fair value* denominated in a *foreign currency* shall be reported using the *exchange rate* at the date when the fair values were determined.

13.3. *Exchange differences* arising on the settlement of *monetary items* or on reporting an entity's *monetary items* at rates different from those at which they were initially recorded during the period, or reported in previous financial statements, shall be recognized as income or as expenses in the period in which they arise.

13.4 When a gain or loss on a non-monetary item is recognised directly in equity, any exchange component of that gain or loss shall be recognised directly in equity. Conversely, when a gain or loss on a non-monetary item is recognised in profit or loss, any exchange component of that gain or loss shall be recognised in profit or loss.

Disclosure

13.5. An entity shall disclose the amount of *exchange differences* included in the net profit or loss for the period.

13.6. When the *reporting currency* is different from the currency of the country in which the entity is domiciled, the reason for using a different currency shall be disclosed. The reason for any change in the *reporting currency* shall also be disclosed.

Section 14. Events after Balance Sheet Date

14.1. An entity shall adjust the amounts recognized in its financial statements to reflect adjusting *events after the balance sheet date*.

14.2. The following are examples of adjusting *events after the balance sheet date* that require an entity to adjust the amounts recognized in its financial statements, or to recognize items that were not previously recognized:

(a) the resolution after the balance sheet date of a court case which, because it confirms that an entity already had a present obligation at the balance sheet date, requires the entity to adjust a *provision* already recognized, or to recognize a *provision* instead of merely disclosing a *contingent liability*;

(b) the receipt of information after the balance sheet date indicating that an *asset* was impaired at the balance sheet date, or that the amount of a previously recognized *impairment loss* for that *asset* needs to be adjusted. For example:

(i) when the bankruptcy of a customer occurs after the balance sheet date, it usually confirms that a loss already existed at the balance sheet date on a trade receivable account and that the entity needs to adjust the carrying amount of the trade receivable account; and

(ii) the sale of *inventories* after the balance sheet date may give evidence about their *net realizable value* at the balance sheet date;

(c) the determination after the balance sheet date of the *cost* of *assets* purchased, or the proceeds from *assets* sold, before the balance sheet date;

(d) the determination after the balance sheet date of the amount of profit-sharing or bonus payments, if the entity had a present legal or *constructive obligation* at the balance sheet date to make such payments as a result of events before that date; and

(e) the discovery of fraud or errors indicating that the financial statements were incorrect.

14.3. An entity shall not prepare its financial statements 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.

14.4. An entity shall not adjust the amounts recognized in its financial statements to reflect non-adjusting *events after the balance sheet date.*

14.5. An example of a non-adjusting event after the balance sheet date is a decline in market value of investments between the balance sheet date and the date when the financial statements are authorized for issue. The fall in market value does not normally relate to the condition of the investments at the balance sheet date, but reflects circumstances that arise in the following period. Therefore, an entity does not adjust the amounts recognized in its financial statements for the investments. Similarly, the entity does not update the amounts disclosed for the investments as at the balance sheet date, although it may need to give additional disclosure under paragraph 14.7.

14.6. If an entity receives information after the balance sheet date about conditions that existed at the balance sheet date, the entity shall, in light of the new information, update disclosures that relate to these conditions.

14.7. Where non-adjusting *events after the balance sheet date* are of such importance that nondisclosure would affect the ability of the users of the financial statements to make proper evaluations and decisions, an entity shall disclose the following information for each significant category of non-adjusting event after the balance sheet date:

(a) the nature of the event; and

(b) an estimate of its financial effect, or a statement that such an estimate cannot be made.

14.8. The following are examples of non-adjusting *events after the balance sheet date* that may be of such importance that non-disclosure would affect the ability of the users of the financial statements to make proper evaluations and decisions:

(a) announcing a plan to discontinue an operation, disposing of *assets* or settling *liabilities* attributable to a discontinuing operation, or entering into binding agreements to sell such *assets* or settle such *liabilities*;

(b) major purchases and disposals of *assets*, or expropriation of major *assets* by *government;*

(c) the destruction of a major production plant by a fire after the balance sheet date;

(d) abnormally large changes after the balance sheet date in asset prices or foreign *exchange rates*; and

(e) changes in tax rates or tax laws enacted or announced after the balance sheet date that have a significant effect on current and *deferred tax assets and liabilities*.

14.9. If dividends to holders of equity instruments (for example, common shares, certain preferred shares, warrants or options to purchase common shares) are proposed or declared after the balance sheet date, an entity shall not recognize those dividends as a *liability* at the balance sheet date.

14.10. An entity shall disclose the date when the financial statements were approved and who has approved the financial statements.

Section 15. Related-Party Disclosures

15.1. This section deals only with those *related-party* relationships described in (a) to (g) below:

A party is related to an entity if:

(a) directly or indirectly through one or more intermediaries, the party:

   (i) controls, is controlled by, or is under common control with, the entity (this includes parents, subsidiaries and fellow subsidiaries);

   (ii) has an interest in the entity that gives it significant influence over the entity; or

   (iii) has joint control over the entity;

(b) the party is an associate of the entity;

(c) the party is a joint venture in which the entity is a venturer

(d) the party is a member of the key management personnel of the entity or its parent;

(e) the party is a close member of the family of any individual referred to in (a) or (d);

(f) the party is an entity that is controlled, jointly controlled or significantly influenced by, or for which significant voting power in such entity resides with, directly or indirectly, any individual referred to in (d) or (e); or

(g) the party is a post-employment benefit plan for the benefit of employees of the entity, or of any entity that is a related party of the entity.

In considering each possible *related-party* relationship, attention is directed to the substance of the relationship, and not merely the legal form.

15.2. In the context of this Section, the following are not necessarily related parties:

(a) two entities simply because they have a director or other member of key management personnel in common, notwithstanding (d) and (f) in the definition of related party.

(b) two venturers simply because they share joint control over a joint venture.

(c) (i) providers of finance;

   (ii) trade unions;

   (iii) public utilities; and

   (iv) government departments and agencies,

   simply by virtue of their normal dealings with an entity by virtue only of (even though they may affect the freedom of action of an entity or participate in its decision-making process); and

(d) a customer, supplier, franchisor, distributor, or general agent with whom an entity transacts a significant volume of business, merely by virtue of the resulting economic dependence.

Disclosure

15.3 Relationships between parents and subsidiaries shall be disclosed irrespective of whether there have been transactions between those related parties. An entity shall disclose the name of the entity's parent and, if different, the ultimate controlling party. If neither the entity's parent nor the ultimate controlling party produces financial statements available for public use, the name of the next most senior parent that does so shall also be disclosed.

15.4. If there have been transactions between related parties, an entity shall disclose the nature of the *related-party* relationships as well as information about the transactions and outstanding balance necessary for an understanding of the potential effect of the relationship on the financial statements. At a minimum the disclosures shall include:

(a) the amount of the transactions;

(b) the amount of outstanding balances and:

(i) their terms and conditions, including whether they are secured, and the nature of the consideration to be provided in settlement; and

(ii) details of any guarantees given or received;

(c) provisions for doubtful debts related to the amount of outstanding balances; and

(d) the expense recognised during the period in respect of bad or doubtful debts due from related parties.

15.3. The following are examples of transactions that are disclosed if they are with a *related-party*:

(a) purchases or sales of goods (finished or unfinished);

(b) purchases or sales of property and other *assets*;

(c) rendering or receiving of services;

(d) leases;

(e) transfers of *research* and *development;*

(f) transfers under license agreements;

(g) transfers under finance arrangements (including loans and equity contributions in *cash* or in kind);

(h) provision of guarantees and collaterals; and

(i) settlement of liabilities on behalf of the entity or by the entity on behalf of another party.

15.4. The elements of transactions necessary for an understanding of the financial statements would normally include:

(a) an indication of the volume of the transactions, either as an amount or as an appropriate proportion; and

(b) amounts or appropriate proportions of outstanding items.

15.5. Disclosures that related party transactions were made on terms equivalent to those that prevail in arm's length transactions are made only if such terms can be substantiated.

15.6. Items of a similar nature may be disclosed in aggregate except when separate disclosure is necessary for an understanding of the effects of *related-party transactions* on the financial statements of the entity.

Section 16. Investments

Classification of Investments

16.1 Investments can be classified into following three categories:

(a) at fair value through profit or loss

(b) held to maturity

(c) available for sale

Initial Measurement of Investments

16.2 When an investment is recognised initially, an entity shall measure it at its fair value plus, in the case of an investment not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of an investment.

Subsequent Measurement of Investments

16.3 After initial recognition, an entity shall measure investments at their fair values, without any deduction for transaction costs it may incur on sale or other disposal, except for the following investments:

(a) held-to-maturity investments, which shall be measured at amortized cost using the effective interest method; and

(b) investments in equity instruments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured, which shall be measured at cost.

Reclassification of Investments

16.4 An entity shall not reclassify an investment into or out of the fair value through profit or loss category while it is held or issued.

16.5 If, as a result of a change in intention or ability, it is no longer appropriate to classify an investment as held to maturity, it shall be reclassified as available for sale and re-measured at fair value, and the difference between its carrying amount and fair value shall be accounted for in accordance with paragraph 16.9(b).

16.6 Whenever sales or reclassification of more than an insignificant amount of held-to-maturity investments do not meet any of the conditions specified in the definition of held-to-maturity investments, any remaining held-to-maturity investments shall be reclassified as available for sale. On such reclassification, the difference between their carrying amount and fair value shall be accounted for in accordance with paragraph 16.9(b).

16.7 If a reliable measure becomes available for an investment for which such a measure was previously not available, and the investment is required to be measured at fair value if a reliable measure is available, the investment shall be re-measured at fair value, and the difference between its carrying amount and fair value shall be accounted for in accordance with paragraph 16.9.

16.8 If, as a result of a change in intention or ability or in the rare circumstance that a reliable measure of fair value is no longer available or because the ‘two preceding financial years’ have passed, it becomes appropriate to carry an investment at cost or amortized cost rather than at fair value, the fair value carrying amount of the investment on that date becomes its new cost or amortized cost, as applicable. Any previous gain or loss on that asset that has been recognised directly in equity in accordance with paragraph 16.9(b) shall be accounted for as follows:

(a) In the case of an investment with a fixed maturity, the gain or loss shall be amortized to profit or loss over the remaining life of the held-to-maturity investment using the effective interest method. Any difference between the new amortized cost and maturity amount shall also be amortized over the remaining life of the investment using the effective interest method, similar to the amortization of a premium and a discount. If an investment is subsequently impaired, any gain or loss that has been recognised directly in equity is recognised in profit or loss in accordance with paragraph 16.14.

(b) In the case of an investment that does not have a fixed maturity, the gain or loss shall remain in equity until the investment is sold or otherwise disposed of, when it shall be recognised in profit or loss. If the investment is subsequently impaired any previous gain or loss that has been recognised directly in equity is recognised in profit or loss in accordance with paragraph 16.14.

Gains and Losses

16.9 A gain or loss arising from a change in the fair value of an investment shall be recognized as follows.

(a) A gain or loss on an investment classified as at fair value through profit or loss shall be recognised in profit or loss.

(b) A gain or loss on an available-for-sale investment shall be recognised directly in equity, through the statement of changes in equity, except for impairment losses and foreign exchange gains or losses, until the investment is derecognized, at which time the cumulative gain or loss previously recognised in equity shall be recognised in profit or loss. However, interest calculated using the effective interest method is recognised in profit or loss.

16.10 For investments carried at amortized cost, a gain or loss is recognised in profit or loss when an investment is derecognized or impaired, and through the amortization process.

Impairment and Uncollectibility of Investments

Investments carried at amortised cost

16.11 If there is objective evidence that an impairment loss on held-to-maturity investments carried at amortized cost has been incurred, the amount of the loss is measured as the difference between the investment's carrying amount and the present value of estimated future cash flows discounted at the investment's original effective interest rate (i.e., the effective interest rate computed at initial recognition). The carrying amount of an investment shall be reduced either directly or through use of an allowance account. The amount of the loss shall be recognised in profit or loss.

16.12 If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss shall be reversed either directly or by adjusting an allowance account. The reversal shall not result in a carrying amount of an investment that exceeds what the amortized cost would have been had the impairment not been recognised at the date the impairment is reversed. The amount of the reversal shall be recognised in profit or loss.

Investments carried at cost

16.13 If there is objective evidence that an impairment loss has been incurred on an unquoted equity instrument that is not carried at fair value because its fair value cannot be reliably measured, the amount of the impairment loss is measured as the difference between the carrying amount of the investment and the present value of estimated future cash flows discounted at the current market rate of return for a similar investment. Such impairment losses shall not be reversed.

Available for sale investments

16.14 When a decline in the fair value of an available-for-sale investment has been recognised directly in equity and there is objective evidence that the asset is impaired, the cumulative loss that had been recognised directly in equity shall be removed from equity and recognised in profit or loss even though the investment has not been derecognized.

16.15 The amount of the cumulative loss that is removed from equity and recognised in profit or loss under paragraph 16.14 shall be the difference between the acquisition cost (net of any principal repayment and amortization) and current fair value, less any impairment loss on that investment previously recognised in profit or loss.

16.16 Impairment losses recognized in profit or loss for an investment in an equity instrument classified as available for sale shall not be reversed through profit or loss.

16.17 If, in a subsequent period, the fair value of a debt instrument classified as available for sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognized in profit or loss, the impairment loss shall be reversed, with the amount of the reversal recognized in profit or loss.

Disposals of Investments

16.18 On disposal of an investment, the difference between:

(a) the carrying amount; and

(b) the sum of (i) the consideration received and (ii) any cumulative gain or loss that had been recognized directly in equity shall be recognized in profit or loss.

Disclosure

16.19 For each class of investment, an entity shall disclose:

(i) information about the extent and nature of investment, including significant terms and conditions that may affect the amount, timing and certainty of future cash flows; and

(ii) the accounting policies and methods adopted, including the criteria for recognition and the basis of measurement applied.

16.20 For each class of investment, an entity shall disclose the fair value of that class of investment in a way that permits it to be compared with the corresponding carrying amount in the balance sheet.

16.21 If investments in unquoted shares are measured at cost because their fair value cannot be measured reliably, that fact shall be disclosed together with a description of the investment, their carrying amount, an explanation of why fair value cannot be measured reliably and, if possible, the range of estimates within which fair value is highly likely to lie. Furthermore, if investments whose fair value previously could not be reliably measured are sold, that fact, the carrying amount of such investments at the time of sale and the amount of gain or loss recognized shall be disclosed.

16.22 An entity shall disclose the carrying amount of investments pledged as collateral for liabilities, the carrying amount of investments pledged as collateral for contingent liabilities, and any material terms and conditions relating to assets pledged as collateral.

16.23 If the entity has reclassified an investment as one measured at cost or amortized cost rather than at fair value, it shall disclose the reason for that reclassification.

16.24 An entity shall disclose the nature and amount of any impairment loss recognised in profit or loss for an investment, separately for each significant class of investment.

Section 17. Employee Benefits

17.1 Employee benefits among others include:

a. short term employee benefits such as wages, salaries and social security contributions, paid annual leave and paid sick leave, profit sharing and bonuses and non monetary benefits (such as medical care, housing, cars and free or subsidized goods or services) for current employees: and

b. Post-employment benefits such as pensions, other retirement benefits, etc.

The above two benefits are considered most common therefore this Section establishes requirement for these.

Short-term Employee Benefits

17.2 When an employee has rendered service to an entity during an accounting period, the entity shall recognize the undiscounted amount of short-term employee benefits expected to be paid in exchange for that service:

a. as a liability (accrued expenses), after deducting any amount already paid. If the amount already paid exceeds the undiscounted amount of the benefits, an entity shall recognize that excess as an asset (prepaid expenses) to the extent that the prepayment will lead to, for example, a reduction in future payments or a cash refund; and

b. as an expense, unless another Section requires or permits the inclusion of the benefits in the cost of an asset (for example, cost of production of inventories to be included in cost of inventories and cost incurred on acquisition of Property, Plant and Equipment).

17.3 The cost of short-term employee benefits in the form of compensated absences shall be recognized as follows:

a. in the case of accumulating compensated absences, when the employees render service that increases their entitlement to future compensated absences; and

b. in the case of non-accumulating compensated absences, when the absences occur.

17.4 An entity shall measure the expected cost of accumulating compensated absences as the additional amount that the entity expects to pay as a result of the unused entitlement that has accumulated at the balance sheet date.

17.5 An entity shall recognize the expected cost of profit sharing and bonus payments when and only when:

a. the entity has a present legal or constructive obligation to make such payments as a result of past events; and

b. a reliable estimate of the obligation can be made

A present obligation exists when, and only when, the entity has no realistic alternative but to make the payments.

Post–employment Benefits: Defined Contribution Plans

17.6 In respect of retirement benefits in the form of provident fund and other defined contribution schemes, the contribution payable by the employer for a year shall be charged to the statement of profit and loss for the year. Thus, besides the amount of contribution paid, a shortfall of the amount of contribution paid compared to the amount payable for the year shall also be charged to the statement of profit and loss for the year. On the other hand, if contribution paid is in excess of the amount payable for the year, the excess shall be treated as a pre-payment.

17.7 When an employee has rendered service to an entity during a period, the entity shall recognise the contribution payable to a defined contribution plan in exchange for that service:

(a) as a liability (accrued expense), after deducting any contribution already paid. If the contribution already paid exceeds the contribution due for service before the balance sheet date, an entity shall recognise that excess as an asset (prepaid expense) to the extent that the prepayment will lead to, for example, a reduction in future payments or a cash refund; and

(b) as an expense, unless another Section requires or permits the inclusion of the contribution in the cost of an asset (see, for example, Section 3 *Property, Plant and Equipment*).

Post–employment benefits: defined benefit plans

17.8 In respect of gratuity benefit and other defined benefit schemes, the accounting treatment will depend on the type of arrangement which the employer has chosen to make.

i. If the employer has chosen to make payment for retirement benefits out of his own funds, an appropriate charge to the statement of profit and loss for the year shall be made through a provision for the accruing liability. The accruing liability shall be calculated according to actuarial valuation. However, entities may opt to calculate the accrued liability by reference to any other rational method e.g. a method based on the assumption that such benefits are payable to all employees at the end of the accounting year.

ii. In case the liability for retirement benefits is funded through creation of a trust, the cost incurred for the year shall be determined actuarially. Such actuarial valuation shall normally be conducted at least once in every three years. However, where the actuarial valuations are not conducted annually, the actuary's report shall specify the contributions to be made by the employer on annual basis during the inter-valuation period. This annual contribution (which is in addition to the contribution that may be required to finance unfunded past service cost) reflects proper accrual of retirement benefit cost for each of the years during the inter-valuation period and shall be charged to the statement of profit and loss for each such year. Where the contribution paid during a year is lower than the amount required to be contributed during the year to meet the accrued liability as certified by the actuary, the shortfall shall be charged to the statement of profit and loss for the year. Where the contribution paid during a year is in excess of the amount required to be contributed during the year to meet the accrued liability as certified by the actuary, the excess shall be treated as a pre-payment.

In case the liability for retirement benefits is funded through a scheme administered by an insurer, an actuarial certificate or a confirmation from the insurer shall be obtained that the contribution payable to the insurer is the appropriate accrual of the liability for the year. Where the contribution paid during a year is lower than amount required to be contributed during the year to meet the accrued liability as certified by the actuary or confirmed by the insurer, as the case may be, the shortfall shall be charged to the statement of profit and loss for the year. Where the contribution paid during a year is in excess of the amount required to be contributed during the year to meet the accrued liability as certified by the actuary or confirmed by the insurer, as the case may be, the excess shall be treated as a pre-payment.

17.9 Where actuarial valuation is conducted, it shall be in accordance with requirements of IAS 19 – Employee Benefits

17.10 Any alterations in the retirement benefit costs arising from -

a. introduction of a retirement benefit scheme for existing employees or making of improvements to an existing scheme, or

b. changes in the assumptions adopted, shall be charged or credited to the statement of profit and loss as they arise in accordance with paragraphs 12.1 to 12.14.

17.11 When a retirement benefit scheme is amended with the result that additional benefits are provided to retired employees, the cost of the additional benefits shall be accounted for in accordance with paragraph 17.8 above.

17.12 The financial statements shall disclose the method by which retirement benefit costs for the period have been determined. In case the costs related to gratuity and other defined benefit schemes are based on an actuarial valuation, the financial statements shall also disclose whether the actuarial valuation was made at the end of period or at an earlier date. In the latter case, the date of the actuarial valuation shall be specified and the method by which the accrual for the period has been determined shall also be briefly described, if the same is not based on the report of the actuary.

Annex 1

Definitions

Accounting policies are the specific principles, bases, conventions, rules and practices adopted by an entity in preparing and presenting financial statements.

An ***active market*** is a market where all the following conditions exist:

(a) the items traded within the market are homogeneous;

(b) willing buyers and sellers can normally be found at any time; and

(c) prices are available to the public.

Amortization is the systematic allocation of the depreciable amount of an intangible asset over its useful life.

Amortized cost of an investment is the amount at which an investment is measured at initial recognition minus principal repayments, plus or minus the cumulative amortization using the effective interest method of any difference between that initial amount and the maturity amount, and minus any reduction (directly or through the use of an allowance account) for impairment or uncollectibility.

An ***asset*** is a resource;

(a) controlled by an entity as a result of past events; and

(b) from which future economic benefits are expected to flow to the entity.

Available-for-sale

These are investments that are designated as available for sale or are not classified as

(a) held-to-maturity investments; or

(b) investments at fair value through profit or loss.

Borrowing costs are interest and other costs incurred by an entity in connection with the borrowing of funds.

The ***carrying amount*** is the amount at which an asset is recognized in the balance sheet after deduction of any accumulated depreciation and accumulated impairment losses thereon.

Cash comprises cash on hand and demand deposits.

Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and are subject to an insignificant risk of changes in value.

Cash flows are inflows and outflows of cash and cash equivalents.

A ***cash-generating unit*** is the smallest identifiable group of assets that generates cash inflows from continuing use that are largely independent of the cash flows from other assets or groups of assets.

Close members of the family of an individual are those family members who may be expected to influence, or be influenced by, that individual in their dealings with the entity. They may include:

(a) the individual's domestic partner and children;

(b) children of the individual's domestic partner; and

(c) dependants of the individual or the individual's domestic partner.

The ***closing rate*** is the spot exchange rate at the balance sheet date.

A ***construction contract*** is a contract specifically negotiated for the construction of an asset or a combination of assets that are closely interrelated or interdependent in terms of their design, technology and function or their ultimate purpose or use.

A ***constructive obligation*** is an obligation that derives from an entity's actions where,

(a) by an established pattern of past practice, published policies or a sufficiently specific current statement, the entity has indicated to other parties that it will accept certain responsibilities; and

(b) as a result, the entity has created a valid expectation on the part of those other parties that it will discharge those responsibilities.

A ***contingent asset*** is a possible asset that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity.

A ***contingent liability*** is

(a) a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity; or

(b) a present obligation that arises from past events but is not recognized because:

    (i) it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation; or

    (ii) the amount of the obligation cannot be measured with sufficient reliability.

Contingent rent is that portion of the lease payments which is not fixed in amount but is based on a factor other than the passage of time (e.g. percentage of future sales, amount of future usage, future price indices, future market rates of interest).

Control (of an entity) is ownership, either directly or indirectly through subsidiaries, of more than one half of the voting power of an entity, or a substantial interest in voting power and the power to direct, by statute or agreement, the financial and operating policies of the management of the entity.

Cost is the amount of cash or cash equivalents paid or the fair value of the other consideration given to acquire an asset at the time of its acquisition, production or construction.

Current tax is the amount of income taxes payable (recoverable) in respect of the *taxable profit (tax loss)* for a period.

Deferred tax assets are the amounts of income taxes recoverable in future periods in respect of

(a) deductible temporary differences;

(b) the carry forward of unused tax losses; and

(c) the carry forward of unused tax credits.

Deferred tax liabilities are the amounts of income taxes payable in future periods in respect of taxable temporary differences.

Defined benefit plans *are post-employment benefit plans other than defined contribution plans.*

Defined contribution plans *are post-employment benefit plans under which an entity pays fixed contributions into a separate entity (a fund) and will have no legal or constructive obligation to pay further contributions if the fund does not hold sufficient assets to pay all employee benefits relating to employee service in the current and prior periods.*

Depreciable amount is the cost of an asset, or other amount substituted for cost in the financial statements, less its ***residual value***.

Depreciation is the systematic allocation of the depreciable amount of an asset over its useful life.

Development is the application of ***research*** findings or other knowledge to a plan or design for the production of new or substantially improved materials, devices, products, processes, systems or services prior to the commencement of commercial production or use.

Economic life is either

(a) the period over which an asset is expected to be economically usable by one or more users; or

(b) the number of production or similar units expected to be obtained from the asset by one or more users.

Effective interest method is a method of calculating the amortized cost of an investment and of allocating the interest income or interest expense over the relevant period.

The ***effective interest rate*** is the rate that exactly discounts estimated future cash payments or receipts through the expected life of an investment or, when appropriate, a shorter period to the net carrying amount of an investment. When calculating the effective interest rate, an entity shall estimate cash flows considering all contractual terms of an investment but shall not consider future credit losses. The calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs, and all other premiums or discounts. There is a presumption that the cash flows and the expected life of a group of similar investment can be estimated reliably. However, in those rare cases when it is not possible to estimate reliably the cash flows or the expected life of an investment, the entity shall use the contractual cash flows over the full contractual term of an investment.

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

Events after the balance sheet date are events, both favourable and unfavourable, that occur between the balance sheet date and the date when the financial statements are authorized for issue. Two types of events can be identified:

(a) those providing evidence of conditions that existed at the balance sheet date (adjusting events after the balance sheet date); and

(b) those indicative of conditions that arose after the balance sheet date (non-adjusting events after the balance sheet date).

The ***exchange difference*** is the difference resulting from translating a number of units of one currency into another currency at different exchange rates.

The ***exchange rate*** is the ratio for exchange of two currencies.

Executory contracts are contracts under which neither party has performed any of its obligations or both parties have partially performed their obligations to an equal extent.

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

A ***Finance Lease*** is a lease that transfers substantially all the risks and rewards incidental to ownership of an asset. Title may or may not eventually be transferred.

Financing activities are activities that result in changes in the size and composition of the equity capital and borrowings of the entity.

Foreign currency is a currency other than the reporting currency of an entity.

Government refers to government, government agencies and similar bodies, whether local, national or international.

Government assistance is action by government designed to provide an economic benefit specific to an entity or range of entities qualifying under certain criteria. Government assistance for the purpose of this Section does not include benefits provided only indirectly through action affecting general trading conditions, such as the provision of infrastructure in development areas or the imposition of trading constraints on competitors.

Government grants are assistance by government in the form of transfers of resources to an entity in return for past or future compliance with certain conditions relating to the operating activities of the entity. They exclude those forms of government assistance which cannot reasonably have a value placed on them and transactions with government which cannot be distinguished from the normal trading transactions of the entity.

Grants related to assets are government grants whose primary condition is that an entity qualifying for them shall purchase, construct or otherwise acquire long-term assets. Subsidiary conditions may also be attached restricting the type or location of the assets or the periods during which they are to be acquired or held.

Grants related to income are government grants other than those related to assets.

Held-to-maturity investments

These are investments with fixed or determinable payments and fixed maturity that an entity has the positive intention and ability to hold to maturity other than:

(a) those that the entity upon initial recognition designates as at fair value through profit or loss; and

(b) those that the entity designates as available for sale.

An entity shall not classify any investment as held to maturity if the entity has, during the current financial year or during the two preceding financial years, sold or reclassified more than an insignificant amount of held-to-maturity investments before maturity (more than insignificant in relation to the total amount of held-to-maturity investments) other than sales or reclassifications that:

(i) are so close to maturity or the investment's call date (for example, less than three months before maturity) that changes in the market rate of interest would not have a significant effect on the investment's fair value;

(ii) occur after the entity has collected substantially all of the investment's original principal through scheduled payments or prepayments; or

(iii) are attributable to an isolated event that is beyond the entity's control, is non-recurring and could not have been reasonably anticipated by the entity.

Historical cost assets are recorded at the amount of cash or cash equivalents paid or the fair value of the consideration given to acquire them at the time of their acquisition. Liabilities are recorded at the amount of proceeds received in exchange for the obligation, or, in some circumstances (for example, income taxes), at the amounts of cash or cash equivalents expected to be paid to satisfy the liability in the normal course of business.

An ***impairment loss*** is the amount by which the carrying amount of an asset exceeds its recoverable amount.

The ***inception of the lease*** is the earlier of the date of the lease agreement or the date of a commitment by the parties to the principal provisions of the lease.

An ***intangible asset*** is an identifiable non-monetary asset without physical substance held for use in the production or supply of goods or services, for rental to others, or for administrative purposes.

The ***interest rate implicit in the lease*** is the discount rate that, at the inception of the lease, causes the aggregate present value of:

(a) the minimum lease payments; and

(b) the unguaranteed residual value to be equal to the fair value of the leased asset.

Inventories are assets:

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

(b) in the process of production for such sale; or

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

Investment is an asset held by an entity for the accretion of wealth through distribution (such as interest, royalties and dividends), for capital appreciation or for other benefits to investing entity such as those obtained through trading relationships. Inventories and Property, plant and equipment as defined in the standard are not investments

Investments at fair value through profit or loss

An investment that meets either of the following conditions is classified as at fair value through profit or loss

(a) It is classified as held for trading. An investment is classified as held for trading if it is:

  (i) acquired or incurred principally for the purpose of selling or repurchasing it in the near term;

  (ii) part of a portfolio of identified investments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking.

(b) Upon initial recognition it is designated by the entity as at fair value through profit or loss. Any investment within the scope of this Section may be designated when initially recognized as an investment at fair value through profit or loss except for investments in equity instruments that do not have a quoted market price in an active market, and whose fair value cannot be reliably measured.

Investing activities are the acquisition and disposal of long-term assets and other investments not included in cash equivalents.

Joint control is the contractually agreed sharing of control over an economic activity.

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly, including any director (whether executive or otherwise) of that entity.

A ***lease*** is an agreement whereby the lessor conveys to the lessee, in return for a payment or series of payments, the right to use an asset for an agreed period of time.

The ***lease term*** is the non-cancellable period for which the lessee has contracted to lease the asset, together with any further terms for which the lessee has the option to continue to lease the asset, with or without further payment, which option at the inception of the lease it is reasonably certain that the lessee will exercise.

A ***legal obligation*** is an obligation that derives from

(a) a contract (through its explicit or implicit terms);

(b) legislation; or

(c) other operation of law.

A ***liability*** is a present obligation of an entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits.

Minimum lease payments are the payments over the lease term that the lessee is, or can be required, to make, excluding *contingent rent*, costs for services and taxes to be paid by and reimbursed to the lessor, together with, in the case of the lessee, any amounts guaranteed by the lessee or by a party related to the lessee. However, if the lessee has an option to purchase the asset at a price that is expected to be sufficiently lower than the fair value at the date the option becomes exercisable, and if, at the inception of the lease, it is reasonably certain that the option will be exercised, then the minimum lease payments comprise the minimum payments payable over the lease term and the payment required to exercise this purchase option.

Monetary items are money held and assets and liabilities to be received or paid in fixed or determinable amounts of money.

Net realizable 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.

A ***non-cancellable lease*** is a lease that is cancellable only

(a) upon the occurrence of some remote contingency;

(b) with the permission of the lessor;

(c) if the lessee enters into a new lease for the same or an equivalent asset with the same lessor; or

(d) upon payment by the lessee of an additional amount such that, at inception, continuation of the lease is reasonably certain.

An ***obligating event*** is an event that creates a legal or constructive obligation that results in an entity's having no realistic alternative to settling that obligation.

An ***onerous contract*** is a contract in which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it.

Operating activities are the principal revenue-producing activities of the entity and other activities that are not investing or financing activities.

An ***operating lease*** is a lease other than a finance lease.

Past service cost *is the increase in the present value of the defined benefit obligation for employee service in prior periods, resulting in the current period from the introduction of, or changes to, post-employment benefits or other long-term employee benefits. Past service cost may be either positive (where benefits are introduced or improved) or negative (where existing benefits are reduced).*

Post-employment benefits *are employee benefits (other than termination benefits) which are payable after the completion of employment.*

Post-employment benefit plans *are formal or informal arrangements under which an entity provides post-employment benefits for one or more employees.*

The present value of a defined benefit obligation *is the present value, without deducting any plan assets, of expected future payments required to settle the obligation resulting from employee service in the current and prior periods.*

Property, plant and equipment are tangible assets that:

(a) are held by an entity for use in the production or supply of goods or services, for rental to others, or for administrative purposes; and

(b) are expected to be used during more than one period.

A ***provision*** is a liability of uncertain timing or amount.

A ***qualifying asset*** is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale.

A ***related-party transaction*** is a transfer of resources, services or obligations between related parties, regardless of whether a price is charged.

Reporting currency is the currency used in presenting the financial statements.

Research is original and planned investigation undertaken with the prospect of gaining new scientific or technical knowledge and understanding.

Residual value is the net amount an entity expects to obtain for an asset at the end of its useful life after deducting the expected costs of disposal.

Revenue is the gross inflow of economic benefits during the period arising in the course of the ordinary activities of an entity when those inflows result in increases in equity, other than increases relating to contributions from equity participants.

Short-term employee benefits *are employee benefits (other than termination benefits) which fall due wholly within twelve months after the end of the period in which the employees render the related service.*

Significant influence is the power to participate in the financial and operating policy decisions of an entity but not control over those policies. Significant influence may be gained by share ownership, statute or agreement.

Tax expense (tax income) is the aggregate amount included in the determination of profit or loss for the period in respect of current tax and deferred tax.

Taxable profit (tax loss) is the profit (loss) for a period, determined in accordance with the rules established by the taxation authorities, on which income taxes are payable (recoverable).

Temporary differences are differences between the carrying amount of an asset or liability in the balance sheet and its tax base. Temporary differences may be either:

(a) ***taxable temporary differences***, which are temporary differences that will `result in taxable amounts in determining taxable profit (tax loss) of future periods when the carrying amount of the asset or liability is recovered or settled; or

(b) ***deductible temporary differences***, which are temporary differences that will result in amounts that are deductible in determining taxable profit (tax loss) of future periods when the carrying amount of the asset or liability is recovered or settled.

Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of an investment. An incremental cost is one that would not have been incurred if the entity had not acquired, issued or disposed of an investment.

Unguaranteed residual value is that portion of the residual value of the leased asset, the realisation of which by the lessor is not assured or is guaranteed solely by a party related to the lessor.

Useful life is either

(a) the period of time over which an asset is expected to be used by the entity; or

(b) the number of production or similar units expected to be obtained from the asset by the entity.

Annex 2

Qualifying Entities

This section forms only guidance and does not form part of the Standard.

***Each SAFA Member Country may amend the Qualifying Entities Criteria as per their Countries' requirement*.**

Qualifying Entities

1 Entities which qualify to use this Standard as framework for preparation of their financial statements are defined hereunder. Compliance with SME Framework and Standard is necessary for an SME in order to give a "true and fair view" while preparing its financial statements.

Small and Medium Entities (SMEs)

2 A Small and Medium Entity (SME) is an entity that:

(a) is not a listed company or a subsidiary of a listed company;

(b) has not filed, or is in the process of filing, its financial statements with the Securities and Exchange Commission of the respective Country or other regulatory organization for the purpose of issuing any class of instruments in a public market;

(c) does not hold assets in a fiduciary capacity for a broad group of outsiders, such as a bank, insurance company, securities broker/dealer, pension fund, mutual fund or investment banking entity;

(d) is not a public utility or similar entity that provides an essential public service;

(e) is not economically significant on the basis of criteria such as total assets, total income, number of employees, and nature and extent of external borrowings as defined in paragraph 3 below; or

(f) is not a Micro Entity (ME) as defined in paragraph 4 below.

Economically Significant Entity

3 An entity is considered to be economically significant if it has:

(i) Turnover in excess of CU 1 billion, excluding other income

(ii) Number of employees in excess of 750

(iii) Total borrowings (excluding creditors and accrued liabilities) in excess of CU 500 million.

In order to be called economically significant any two of the criterion mentioned in (i), (ii) and (iii) above have to be met. The criterion followed will be based on the previous year's audited financial statements. Entities can be de-listed from this category where they do not fall under the criteria as aforementioned for two consecutive years.

Micro Entities (MEs)

4 These are entities that:

(i) have paid up capital plus undistributed reserves (total equity after taking into account any dividend proposed for the year) not exceeding CU 25 million; and

(ii) have annual turnover not exceeding CU 200 million, excluding other income;

In order to qualify as a micro entity, both of the above mentioned conditions must be satisfied.

Annex 3

Examples

These examples illustrate the application of the related Sections and are provided to assist in clarifying their meaning.

A. Recognition of provisions

Example 1: Warranties

A manufacturer gives warranties at the time of sale to purchasers of its product. Under the terms of the contract for sale, the manufacturer undertakes to make good, by repair or replacement, manufacturing defects that become apparent within three years from the date of sale. Based on past experience, it is probable (i.e. more likely than not) that there will be some claims under the warranties.

Present obligation as a result of a past obligating event: The *obligating event* is the sale of the product with a warranty, which gives rise to a *legal obligation*.

An outflow of resources embodying economic benefits in settlement: Probable for the warranties as a whole.

Conclusion: A *provision* is recognized for the best estimate of the costs of making good under the warranty products sold before the balance sheet date.

Example 2: Legal Requirement to Fit Smoke Filters

If for example, under new legislation, an entity is required to install smoke filters in its factories by 30 June 2000. The entity has not fitted the smoke filters.

(a) At the balance sheet date of 31 December 1999:

Present obligation as a result of a past obligating event: There is no obligation because there is no *obligating event* either for the costs of fitting smoke filters or for fines under the legislation.

Conclusion: No *provision* is recognized for the cost of fitting the smoke filters.

(b) At the balance sheet date of 31 December 2000:

Present obligation as a result of a past obligating event: There is still no obligation for the costs of fitting smoke filters because no *obligating event* has occurred (the fitting of the filters). However, an obligation might arise to pay fines or penalties under the legislation because the *obligating event* has occurred (the non-compliant operation of the factory).

An outflow of resources embodying economic benefits in settlement: The likelihood of incurring fines and penalties for non-compliant operation depends on the details of the legislation and the stringency of the enforcement regime.

Conclusion: No *provision* is recognized for the costs of fitting smoke filters. However, a *provision* is recognized for the best estimate of any fines and penalties that are more likely than not to be imposed.

Example 3: A Court Case

After a wedding in 2000, 10 people died, possibly as a result of food poisoning from products sold by the entity. Legal proceedings are underway seeking damages from the entity, but it disputes its *liability*. Up to the date of authorization of the financial statements for the year to 31 December 2000 for issue, the entity's lawyers advise that it is probable that the entity will not be found liable. However, when the entity prepares the financial statements for the year ending 31 December 2001, its lawyers advise that, because of new developments in the case, it is probable that the entity will be found liable.

(a) At the balance sheet date of 31 December 2000:

Present obligation as a result of a past obligating event: On the basis of the evidence available when the financial statements were approved, there is no obligation as a result of past events.

Conclusion: No *provision* is recognized. The matter is disclosed as a *contingent liability* unless the probability of any outflow is regarded as remote.

(b) At the balance sheet date of 31 December 2001:

Present obligation as a result of a past obligating event: On the basis of the evidence available, there is a present obligation.

An outflow of resources embodying economic benefits in settlement: Probable.

Conclusion: A *provision* is recognized for the best estimate of the amount required to settle the obligation.

Example 4: Refurbishment Costs – No Legislative Requirement

A furnace has a lining that needs to be replaced every five years for technical reasons. At the balance sheet date, the lining has been in use for three years.

Present obligation as a result of a past obligating event: There is no present obligation.

Conclusion: No *provision* is recognized.

The cost of replacing the lining is not recognized because, at the balance sheet date, no obligation to replace the lining exists independently of the company's future actions; even the intention to incur the expenditure depends on the company's deciding to continue operating the furnace or to replace the lining. Instead of a *provision* being recognized, the depreciation of the lining takes into account its consumption (i.e. it is depreciated over five years). The relining costs then incurred are capitalized, with the consumption of each new lining shown by depreciation over the subsequent five years.

B. Revenue recognition

The following examples illustrate the application of the standard in a number of commercial situations in order to clarifying their meaning. The examples focus on particular aspects of a transaction and do not constitute comprehensive discussions of all the relevant factors that might influence the recognition of *revenue*. The examples generally assume that the amount of *revenue* can be measured reliably; that it is probable that the economic benefits will flow to the entity; and that the costs incurred or to be incurred can be measured reliably. The examples do not modify or override the standard.

Sale of goods

Since laws vary from country to country, the recognition criteria in this standard will be met at different times. In particular, the law may determine the point in time at which the entity transfers the significant risks and rewards of ownership. Therefore, the examples in this section of the appendix need to be read in the context of the laws relating to the sale of goods in the country in which the transaction takes place.

1. *"Bill and hold" sales, in which delivery is delayed at the buyer's request but the buyer takes title and accepts billing.*

   Revenue is recognized when the buyer takes title, provided:

   (a) it is probable that delivery will be made;

   (b) the item is on hand, identified and ready for delivery to the buyer at the time the sale is recognized;

   (c) the buyer specifically acknowledges the deferred delivery instructions; and

   (d) the usual payment terms apply.

   Revenue is not recognized when there is simply an intention to acquire or manufacture the goods in time for delivery.

2. *Goods shipped subject to conditions, including the following situations:*

   (a) *Installation and inspection.*

   Revenue is normally recognized when the buyer accepts delivery and installation and inspection are complete. However, *revenue* is recognized immediately upon the buyer's acceptance of delivery when:

   (i) the installation process is simple in nature (e.g. the installation of a factory-tested television receiver that only requires unpacking and connection of power and antennae); or

   (ii) the inspection is performed only for purposes of final determination of contract prices (e.g. for shipments of iron ore, sugar or soya beans).

   (b) *On approval when the buyer has negotiated a limited right of return.* If there is uncertainty about the possibility of return, *revenue* is recognized when the shipment has been formally accepted by the buyer or the goods have been delivered and the time period for rejection has elapsed.

   (c) *Consignment sales under which the recipient (buyer) undertakes to sell the goods on behalf of the shipper (seller).*

   Revenue is recognized by the shipper when the goods are sold by the recipient to a third party.

   (d) *Cash on delivery sales.*

   Revenue is recognized when delivery is made and cash is received by the seller or its agent.

3. *Layaway sales, in which the goods are delivered only when the buyer makes the final payment in a series of instalments.*

   Revenue from such sales is recognized when the goods are delivered. However, when experience indicates that most such sales are consummated, *revenue* may be recognized when a significant deposit is received, provided the goods are on hand, identified and ready for delivery to the buyer.

4. *Orders in which payment (or partial payment) is received in advance of delivery for goods not presently held in inventory (e.g. the goods are still to be manufactured or will be delivered directly to the customer from a third party).*

   Revenue is recognized when the goods are delivered to the buyer.

5. *Sale and repurchase agreements (other than swap transactions) under which the seller concurrently agrees to repurchase the same goods at a later date, or when the seller has a call option to repurchase, or the buyer has a put option to require the repurchase by the seller of the goods.*

   The terms of the agreement need to be analyzed to ascertain whether, in substance, the seller has transferred the risks and rewards of ownership to the buyer and hence *revenue* is recognized. When the seller has retained the risks and rewards of ownership, even though legal title has been transferred, the transaction is a financing arrangement and does not give rise to *revenue*.

6. *Sales to intermediate parties, such as distributors, dealers or others, for resale*
   Revenue from such sales is generally recognized when the risks and rewards of ownership have passed. However, when the buyer is acting, in substance, as an agent, the sale is treated as a consignment sale.

7. *Subscriptions to publications and similar items.*

   When the items involved are of similar value in each time period, *revenue* is recognized on a straight-line basis over the period in which the items are dispatched. When the items vary in value from period to period, *revenue* is recognized on the basis of the sales value of the item dispatched in relation to the total estimated sales value of all items covered by the subscription.

8. *Instalment sales, under which the consideration is receivable in instalments.*

   Revenue attributable to the sales price, exclusive of interest, is recognized at the date of sale. The sale price is the present value of the consideration, determined by discounting the instalments receivable at the imputed rate of interest. The interest element is recognized as *revenue* as it is earned, on a time proportion basis that takes into account the imputed rate of interest.

9. *Real estate sales.*

   Revenue is normally recognized when legal title passes to the buyer. However, in some jurisdictions the equitable interest in a property may vest in the buyer before legal title passes and, therefore, the risks and rewards of ownership have been transferred at that stage. In such cases, provided that the seller has no further substantial acts to complete under the contract, it may be appropriate to recognize *revenue*. In either case, if the seller is obliged to perform any significant acts after the transfer of the equitable and/or legal title, *revenue* is recognized as the acts are performed. An example is a building or other facility on which construction has not been completed.

   In some cases, real estate may be sold with a degree of continuing involvement by the seller such that the risks and rewards of ownership have not been transferred. Examples are sale and repurchase agreements that include put and call options, and agreements whereby the seller guarantees occupancy of the property for a specified period, or guarantees a return on the buyer's investment for a specified period. In such cases, the nature and extent of the seller's continuing involvement determine how the transaction is accounted for. It may be accounted for as a sale, or as a financing, a leasing or some other profit-sharing arrangement. If it is accounted for as a sale, the continuing involvement of the seller may delay the recognition of *revenue*.

   A seller must also consider the means of payment and evidence of the buyer's commitment to complete payment. For example, when the aggregate of the payments received, including the buyer's initial down payment or continuing payments by the buyer, provide insufficient evidence of the buyer's commitment to complete payment, *revenue* is recognized only to the extent that cash is received.

Rendering of services

10. *Installation fees.*

Installation fees are recognized as *revenue* by reference to the stage of completion of the installation, unless they are incidental to the sale of a product, in which case they are recognized when the goods are sold.

11. *Servicing fees included in the price of the product.*

When the selling price of a product includes an identifiable amount for subsequent servicing (e.g. after sales support and product enhancement on the sale of software), that amount is deferred and recognized as *revenue* over the period during which the service is performed. The amount deferred is that which will cover the expected costs of the services under the agreement, together with a reasonable profit on those services.

12. *Advertising commissions.*

Media commissions are recognized when the related advertisement or commercial appears before the public. Production commissions are recognized by reference to the stage of completion of the project.

13. *Insurance agency commissions.*

Insurance agency commissions received or receivable that do not require the agent to render further service are recognized as *revenue* by the agent on the effective commencement or renewal dates of the related policies. However, when it is probable that the agent will be required to render further services during the life of the policy, the commission, or part thereof, is deferred and recognized as *revenue* over the period during which the policy is in force.

14. *Admission fees.*

Revenue from artistic performances, banquets and other special events is recognized when the event takes place. When a subscription to a number of events is sold, the fee is allocated to each event on a basis that reflects the extent to which services are performed at each event.

15. *Tuition fees.*

Revenue is recognized over the period of instruction.

16. *Initiation, entrance and membership fees.*

Revenue recognition depends on the nature of the services provided. If the fee permits only membership, and all other services or products are paid for separately, or if there is a separate annual subscription, the fee is recognized as *revenue* when no significant uncertainty as to its collectability exists. If the fee entitles the member to services or publications to be provided during the membership period, or to the purchase of goods or services at prices lower than those charged to non-members, it is recognized on a basis that reflects the timing, nature and value of the benefits provided.

17. *Franchise fees.*

Franchise fees may cover the supply of initial and subsequent services, equipment and other tangible assets, and know-how. Accordingly, franchise fees are recognized as *revenue* on a basis that reflects the purpose for which the fees were charged. The following methods of franchise fee recognition are appropriate:

(a) *Supplies of equipment and other tangible assets.*

The amount, based on the *fair value* of the *assets* sold, is recognized as *revenue* when the items are delivered or title passes.

(b) *Supplies of initial and subsequent services.*

Fees for the *provision* of continuing services, whether part of the initial fee or a separate fee, are recognized as *revenue* as the services are rendered. When the separate fee does not cover the cost of continuing services together with a reasonable profit, part of the initial fee, sufficient to cover the costs of continuing services and to provide a reasonable profit on those services, is deferred and recognized as *revenue* as the services are rendered.

The franchise agreement may provide for the franchisor to supply equipment, inventories, or other tangible assets at a price lower than that charged to others or a price that does not provide a reasonable profit on those sales. In these circumstances, part of the initial fee, sufficient to cover estimated costs in excess of that price and to provide a reasonable profit on those sales, is deferred and recognized over the period during which the goods are likely to be sold to the franchisee. The balance of an initial fee is recognized as *revenue* when performance of all the initial services and other obligations required of the franchisor (e.g. assistance with site selection, staff training, financing and advertising) has been substantially accomplished.

The initial services and other obligations under an area franchise agreement may depend on the number of individual outlets established in the area. In this case, the fees attributable to the initial services are recognized as *revenue* in proportion to the number of outlets for which the initial services have been substantially completed. If the initial fee is collectable over an extended period and there is a significant uncertainty that it will be collected in full, the fee is recognized as cash instalments are received.

(c) *Continuing franchise fees.*

Fees charged for the use of continuing rights granted by the agreement, or for other services provided during the period of the agreement, are recognized as *revenue* as the services are provided or the rights used.

(d) *Agency transactions.*

Transactions may take place between the franchisor and the franchisee which, in substance, involve the franchisor's acting as agent for the franchisee. For example, the franchisor may order supplies and arrange for their delivery to the franchisee at no profit. Such transactions do not give rise to *revenue*.

18. *Fees from the development of customized software.*

Fees from the development of customized software are recognized as *revenue* by reference to the stage of completion of the development, including completion of services provided for post delivery service support.

Interest, royalties and dividends

19. *License fees and royalties.*

Fees and royalties paid for the use of an entity's assets (e.g. trademarks, patents, software, music copyright, record masters and motion picture films) are normally recognized in accordance with the substance of the agreement. As a practical matter, this may be on a straight-line basis over the life of the agreement – for example, when a licensee has the right to use certain technology for a specified period of time.

An assignment of rights for a fixed fee or non-refundable guarantee under a non-cancellable contract that permits the licensee to exploit those rights freely such that the licensor has no remaining obligations to perform is, in substance, a sale. An example is a licensing agreement for the use of software when the licensor has no obligations subsequent to delivery. Another example is the granting of rights to exhibit a motion picture film in markets where the licensor has no control over the distributor and expects to receive no further *revenues* from the box office receipts. In such cases, *revenue* is recognized at the time of sale.

In some cases, whether or not a license fee or royalty will be received is contingent on the occurrence of a future event. In such cases, revenue is recognized only when it is probable that the fee or royalty will be received, which is normally when the event has occurred.