# TREASURY ANALYSIS –
# INTERNATIONAL ACCOUNTING STANDARDS

## Summary of key differences arising from adoption of IAS

### *Framework for the Preparation and Presentation of Financial Statements*[1]

- Any gain or loss on disposal of assets must be recognised on a net basis, rather than gross (also refer to AASB 118 *Revenue*).

### *AASB 1 First Time Adoption of Australian Equivalents to International Financial Reporting Standards*[1]

- Requires retrospective application of the new Australian equivalents to International Financial Reporting Standards (AEIFRS) from the date of transition (i.e. 1 July 2004 for 30 June year end entities), except in limited circumstances. Previously, under Australian requirements, the preceding periods' primary financial statements were not restated for changes in accounting policies.
- AASB 1 includes some options or exemptions from the principle of retrospective application (e.g. use of deemed cost for PP&E). Treasury has mandated that agencies use certain options, as well as options in other AEIFRSs.
- For financial instruments (AASB 132 and AASB 139) and insurance contracts (AASB 4), Treasury has deferred the "date of transition" by 12 months to 1 July 2005, rather than 1 July 2004 (refer AASB 132 and AASB 139).

### *AASB 2 Share Based Payment*[2]

### *AASB 3 Business Combinations*[1]

- Business combinations involving entities or businesses under common control are excluded from the scope of AASB 3 (as a result of amendments by AASB 2005-6).
- Goodwill cannot be amortised. Instead, it is subject to an annual impairment test under AASB 136 *Impairment of Assets*.
- Discount on acquisition is immediately recognised as revenue.
- Fair value of assets acquired includes intangible assets and contingent liabilities of the acquiree.

### *AASB 4 Insurance Contracts*[2]

- Application is generally limited to fixed-fee service contracts that meet the definition of an 'insurance contract'. Accordingly, this Standard is expected to have a limited application and impact on the NSW public sector.

### *AASB* 5 *Non-current assets held for sale and discontinued operations*[1]

- Creates *held for sale* assets as a new class of assets and specifies new measurement and disclosure requirements:
  - Measured at the lower of carrying amount and fair value less costs to sell;
  - Not depreciated;
  - Re-classified from non-current to current;
  - Separately presented in the balance sheet.
- Requires disclosure of *discontinued operations* at a later point in the disposal process than previously.

***AASB 7 Financial Instruments: Disclosures* – not applicable until 2007/08**[1]

- Locates all disclosure requirements for financial instruments within one standard, replacing the disclosure requirements in AASB 132 (paras 51-95) and superseding AASB 130.
- Requires more extensive balance sheet and operating statement disclosures.
- Prescribes both quantitative and qualitative disclosures about entities' exposures to risks.
- Does not retain the relief from making parent disclosures previously available under AASB 130 and AASB 132.

***AASB 101 Presentation of Financial Statements***[1]

- Revised formats for Income Statement and Balance Sheet, including:
  - Prohibits the presentation of extraordinary items;
  - Netting of gains and losses on disposal of non-current assets;
  - Current / non-current liability classification ignores after balance date events.
- Separate Statement of Changes in Equity.
- Additional disclosures, including:
  - Management's judgements in applying the entity's accounting policies;
  - Management's judgements regarding estimation uncertainty;
  - An explicit and unreserved statement of compliance with IFRS (but not-for-profit entities will not be able to make this statement in most instances).

***AASB 102 Inventories***[1]

- Requires valuation of inventories "held for distribution" by not-for-profit entities at the lower of cost and current replacement cost (previously inventories were valued at the lower of cost and net realisable value).

***AASB 107 Cash Flow Statements***[1]

- There is no major impact arising from AASB 107. However, the AASB 107 definition of 'cash equivalents' is potentially wider than AAS 28. This should have a limited impact in the public sector.

***AASB 108 Accounting Policies, Changes in Accounting Estimates and Errors***[1]

- Changes in accounting policy (unless a new Standard mandates otherwise) and correction of errors must be accounted for retrospectively, by restating comparative information and adjusting the opening balance of accumulated funds, unless impracticable.
- Omission of the concept of fundamental errors; requires all material errors to be accounted for and disclosed in the same way.
- Disclosure of the expected impact of a new Standard that is not yet effective.

***AASB 110 Events After Balance Sheet Date***[1]

- Requires that only dividends *declared* (appropriately authorised) before the reporting date can be recognised. This is more restrictive than raising a valid expectation under AASB 1044.
- In the NSW public sector, dividends are *declared* as part of the SCI/SBI process.
- Requires additional disclosures, including the date financial statements are authorised.

***AASB 111 Construction Contracts***[2]

| AASB 112 Income Taxes[1] |
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| • AASB 112 adopts a balance sheet approach to accounting for income tax based on the principle that current and future tax consequences of transactions and events should be recognised now. This will replace the "income statement" approach previously adopted in AAS 3.<br>• Although conceptually different, the tax assets and liabilities that arose under the previous AAS 3 also arise under AASB 112. But AASB 112 will produce additional deferred tax assets and liabilities, principally from asset revaluations and fair value adjustments to the assets and liabilities of acquired entities. |
| ***AASB 114 Segment Reporting[2] – only for-profit entities*** |
| • No significant changes from previous requirements. Both AASB 114 and AASB 1005 only apply to "for profit" agencies. |
| ***AASB 116 Property, Plant and Equipment[1]*** |
| • Cost of an asset includes both:<br>- restoration costs where recognised as a provision under AASB 137; and<br>- inspection costs.<br>• Borrowing costs may be capitalised or expensed, although Treasury has mandated expensing for general government sector entities consistent with GFS/GAAP convergence.<br>• Impairment of assets is contained in a separate standard, AASB 136.<br>• Not-for-profit exemptions have been added for Australian purposes.<br>• Guidance on fair value, frequency of revaluation and accounting for spares has been added[5]. This is not part of the standard and, regarding fair value, substantially replicates some material lost from AASB 1041.<br>• *For-profit entities* must account for revaluation reserve balances on an individual asset basis, rather than for a class of assets.<br>• Additional disclosures for items recognised at fair value, including methods and significant assumptions; and for *for-profit entities* for each class the amount that would have been recognised under the cost method. |
| ***AASB 117 Leases[1]*** |
| • AASB 117 has retained the *qualitative indicators* of when a lease is a finance lease, but does not have the *quantitative indicators* that were previously in AASB 1008.<br>• Long term leases of land must be accounted for as operating leases, irrespective of the lease term, unless title is expected to pass to the lessee or significant risks and rewards associated with the land at the end of the lease term pass to the lessee. |
| ***AASB 118 Revenue[1]*** |
| • AASB 118 has a narrower scope than AASB 1004, as it only addresses 'revenue' i.e. income attributable to ordinary activities (i.e. which is narrower than 'revenue' under AASB 1004). It does not address disposal of assets, contributions of assets or forgiveness of liabilities.<br>• Revenue from sale of goods can only be recognised when, among other things, the entity:<br>- has transferred the *risks and rewards* of ownership; and<br>- retains neither continuing managerial involvement to the degree associated with ownership nor effective control.<br>(previously only control i.e. rewards *not* risks)<br>• Any gain or loss on disposal of assets must be recognised on a net basis, rather than gross. |

| AASB 119 Employee Benefits[1] |
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| • Superannuation - defined benefit plans – AASB 119 impacts the Crown and agencies whose unfunded superannuation (or surplus) is *not* assumed by the Crown, as follows -<br>- Higher unfunded superannuation liability (or lower surplus) in the balance sheet because a lower discount rate must be used. The defined benefit obligation must be discounted using the government bond rate, rather than the expected rate of return on plan assets.<br>- Greater volatility in the income statement and balance sheet, because the discount rate is based on market expectations *at* each reporting date.<br>- Calculation and disclosure of the unfunded superannuation liability (or surplus) on two bases:<br>  - For recognition in the balance sheet - using the government bond rate;<br>  - For disclosure in the notes – using the expected rate of return on plan assets.<br>- Additional disclosures, including current service cost; interest cost; expected return on plan assets; actuarial gains and losses; and past service costs.<br>- Inclusion of both employer and employee superannuation assets and liabilities in the calculation of the net superannuation liability / asset.<br>• Other employee benefits<br>- A more detailed methodology is required to calculate other long-term employee benefits (e.g. LSL), based on the method used to calculate the defined benefit superannuation obligation.<br>- Annual leave that is a long term employee benefit must be measured at present value, where discounting is expected to have a material impact.<br>- All annual leave and any unconditional LSL (whether or not it is expected to be settled within 12 months) must be presented as a current liability in the Balance Sheet. |
| ***AASB 120 Accounting for Government Grants and Disclosure of Government Assistance[1]– only for-profit entities*** |
| • *For-profit entities* will be subject to either the current AASB 120 *or* a proposed revised AASB 120, based on the approach in AASB 141 *Agriculture*.<br>• Treasury's preference is to mandate early adoption of a revised AASB 120, based on AASB 141. However, because a revised AASB 120 is not yet available, for-profit entities have been instructed to apply the current AASB 120, until otherwise advised.<br>• Impacts of current AASB 120:<br>- Grants must be recognised as income on a systematic basis over the periods necessary to match them with the related costs they are intended to compensate.<br>- Grants related to the acquisition or construction of an asset must be presented as deferred income.<br>• Impacts of the proposed revised AASB 120, based on AASB 141:<br>- If a government grant is conditional, an entity must recognise the government grant as income when, and only when, the conditions attaching to the grant are met.<br>- Time may be a condition and grants may be recognised on a time basis.<br>• Both of these alternatives may delay revenue recognition compared to previously, where grants were recognised when controlled (i.e. normally on receipt). |
| ***AASB 121 Effects of Changes in Foreign Exchange Rates[1]*** |
| • AASB 121 permits an entity to present its financial report in any currency it chooses (para 38). Previously, AASB 1034 "Financial Report: Presentation and Disclosure" required entities to present their financial reports in Australian currency. Treasury has mandated that agencies continue to present their financial reports in Australian currency. |
| ***AASB 123 Borrowing Costs[1]*** |
| • Borrowing costs may be expensed or capitalised. No choice was available under AAS 34. Treasury has mandated expensing of borrowing costs for all general government sector entities, to harmonise with GFS. Public trading enterprises may choose either option. |

***AASB 124 Related Party Disclosures[2] – only for-profit entities***

***AASB 127 Consolidated and Separate Financial Statements[1]***

- In the parent entity's financial statements, an investment in subsidiaries, jointly controlled entities and associates must be recognised at cost or at fair value. Previously, AAS 24 did not address this, and AAS 19 and AAS 14 required the investments in joint ventures and associates be recognised at cost.

***AASB 128 Investments in Associates[1]***

- The scope exclusions are different under AASB 128 and AASB 1016; eg partnerships over which the investor has significant influence are included in the definition of "associate" under AASB 128 but were excluded under AASB 1016.
- Disclosure requirements are different under the two standards.

***AASB 129 Financial Reporting in Hyperinflationary Economies[2]***

***AASB 130 Disclosures in the Financial Statements of Banks and Similar Financial Institutions[2]***

***AASB 131 Interests in Joint Ventures[1]***

- A different definition of joint control under AASB 131 may result in a smaller number of arrangements meeting the requirements for a joint venture.
- There are additional disclosure requirements.

***AASB 132 Financial Instruments: Disclosure and Presentation[1]***

- *In-substance defeasance* **-** Prohibits offsetting a financial asset and financial liability when financial assets are set aside in trust by a debtor for the purposes of discharging an obligation, without assets having been accepted by the creditor in settlement of the obligation.
- *Changes to presentation and disclosure requirements with additional disclosure obligations* - including disclosing the sensitivities of fair value estimates to significant valuation assumptions.
- *Focuses on the substance rather than legal form of financial instruments* **-** hybrid securities may be classified as debt rather than equity.
- Comparative information for 2004/05 need not comply with AASB 132 (refer AASB 1). This defers the AASB 132 date of transition by 12 months to 1 July 2005, rather than 1 July 2004.

***AASB 133 Earnings per Share[2]***

***AASB 134 Interim Financial Reporting[2]***

| ***AASB 136 Impairment of Assets*** [1] |
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| • AASB 136 applies to all assets with limited exemptions. AASB1010 and AASB 1041 combined only applied to non-current assets, with different exemptions.<br>• It requires an entity to assess at each reporting date whether there is any indication that an asset (or cash-generating unit) may be impaired. If such indication exists, the entity must estimate the recoverable amount.<br>• In addition, goodwill and indefinite-life intangibles must be assessed annually for impairment.<br>• Detailed guidance is provided on:<br>  - indicators of impairment assets;<br>  - identifying cash-generating units;<br>  - how to measure value in use based on cash-flow projections.<br>AASB1041/AA1010 did not address these.<br>• Future cash flows must be discounted to determine value in use.<br>• Management's estimates of future cash flows are used, not market participants' estimates as was required by AASB1041.<br>• Additional disclosures for material impairment losses and for each class of asset. |
| ***AASB 137 Provisions, Contingent Liabilities and Contingent Assets*** [1] |
| • Changed treatment applies for contingent assets and recoveries receivable:<br>  - Assets only recognised when the related realisation of revenue or expected recovery receivable is *virtually certain* (previously when probable).<br>  - Contingent assets disclosed when realisation of revenue or the expected recovery is *probable* (previously when higher than remote but less than probable).<br>• Recognition of provisions associated with the retirement or disposal of long-lived assets.<br>• Where an operation is to be sold, a provision for restructuring can only arise where there is a binding sale agreement.<br>• Where discounting is used, the increase in the carrying amount of the provision due to the passage of time must be recognised as a borrowing cost.<br>• Additional disclosures, including the expected timing and uncertainty about timing of outflows of economic benefits to settle the provisions. |
| ***AASB 138 Intangible Assets*** [1] |
| • This is a new standard for Australia – previously there was no one Australian Standard that comprehensively addressed intangible assets; rather intangible assets were addressed across a number of Standards, including the R&D (AAS 13) and Goodwill Standards (AAS 18).<br>• Prohibits internally generated brands, mastheads, publishing titles, customer lists and items similar in substance from being recognised as intangible assets.<br>• Intangible assets may have a finite or indefinite useful life:<br>  - Intangible assets with finite lives are amortised and must be assessed annually for indicators of impairment.<br>  - Intangibles with indefinite lives are not amortised but must be tested for impairment annually.<br>• All research costs are expensed.<br>• Development costs can only be capitalised when certain criteria are met e.g. technically feasible.<br>• Intangible assets must be recognised using the cost or revaluation model. An intangible asset can only be revalued where there is an "active market", which will rarely occur.<br>• Residual value of an intangible asset with a finite life is assumed to be zero, except in limited circumstances.<br>• Some assets may need to be accounted for as intangible assets rather than property, plant and equipment, as previously (e.g. easements and computer software not integral to the related hardware).<br>• Additional disclosures are required for each class of intangible assets. |

| ***AASB 139 Financial Instruments: Recognition and Measurement***[1] |
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| • Recognition of many financial instruments that were previously "off-balance sheet" (e.g. derivatives) and only disclosed in the notes to accounts under AASB 1033 *Presentation and Disclosure of Financial Instruments.*<br>• Provides a mixed measurement model. Held for trading and available for sale financial instruments are measured at fair value and changes are recognised in profit or loss, or equity, respectively. Other financial instruments are measured at amortised cost.<br>• Hedge accounting treatment is available only if strict conditions are met.<br>• Fair value methodologies may be a significant issue where there is no liquid market for the relevant financial instrument.<br>• Major changes may be required to the contracts management and accounting system in order to satisfy valuation and hedge accounting requirements.<br>• Requires that all financial assets, except those measured at fair value through profit and loss, be subject to review for impairment.<br>• Potential increased volatility in operating profit and possible capital structure implications.<br>• Comparative information for 2004/05 need not comply with AASB 139 (refer AASB 1). This defers the AASB 139 date of transition by 12 months to 1 July 2005, rather than 1 July 2004.<br>• Treasury has mandated a number of different options under AASB 139 which are included in TPP 06-4. |
| ***AASB 140 Investment Property***[1] |
| • This is a new standard for Australia – investment properties were previously accounted for under AASB 1041 *Revaluation of Non-Current Assets* and AASB 1010 *Recoverable Amount of Non-Current Assets*.<br>• Investment properties may be measured at fair value or cost. Treasury has mandated fair value.<br>• Changes in fair value are recognised in the income statement and depreciation is not recognised.<br>• Any investment property interest held by a lessee under an operating lease may be classified and accounted for as investment property if the lessee uses the fair value model.<br>• Additional disclosures are required. |
| **AASB** ***141 Agriculture***[3] ***– grant relates to a biological asset at fair value – only for-profit entities*** |
| • If a government grant is conditional, an entity must recognise the government grant as income when, and only when, the conditions attaching to the grant are met.<br>• Time may be a condition and grants may be recognised on a time basis.<br>• Unconditional grants are revenue when they become receivable. |
| **AASB 1004** ***Contributions***[1]***- only not-for-profit entities*** |
| • *Not-for-profit entities* will be subject to the AASB 1004 requirements regarding contributions of assets (including grants) and forgiveness of liabilities (i.e. which is identical to previous requirements) OR the proposals in ED 125 *Financial Reporting by Local Governments* or ED 147 *Revenue from Non-Exchange Transactions (including Taxes and Transfers).*<br>• Treasury's preference is to mandate early adoption of the ED 125 or ED 147 proposals. However, because deliberations on ED 125 and ED 147 are not yet complete, agencies have been instructed NOT to adjust the current treatment of grants, until otherwise advised.<br>• If the ED 125 or ED 147 approach is applied, revenue and / or expense recognition will not occur until, either, the agency supplies the related goods and services (where grants are in-substance agreements for the provision of goods and services) or until conditions are satisfied.<br>• ED 125 and ED 147 may therefore delay revenue recognition compared to AASB 1004, where grants were recognised when controlled. |

| ***AASB 1023 General Insurance Contracts***[1] |
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| • Increases scope of Standard i.e. may apply to certain contracts that were not previously subject to AASB 1023, because of the wide definition of an 'insurance contract'.<br>• Increases outstanding claims liability, compared to previously, because of:<br>- *Risk margin* – requirement to include a risk margin to reflect the inherent uncertainty in the central estimate, where previously no risk margin was required.<br>- *Discount rate* – must be discounted for the time value of money using risk free rates, where previously the discount rate was based on the expected rates of return on assets.<br>• Applies an expanded liability adequacy test to the unearned premium liability.<br>• Requires assets backing general insurance liabilities to be measured at fair value, wherever possible, where previously they were generally recognised at net market value.<br>• Increases disclosure requirements, compared to previously.<br>• Comparative information for 2004/05 need not comply with the revised AASB 1023 (refer AASB 1). This defers the AASB 1023 date of transition by 12 months to 1 July 2005, rather than 1 July 2004. |
| ***AASB 1031 Materiality***[2] |
| ***AASB 1038 Life Insurance Contracts***[2] |
| ***AASB 1048 Interpretation and Application of Standards***[2] |
| ***Other Standards retained and applicable for 2005***[4]<br>• AAS 25 *Financial Reporting by Superannuation Plans*<br>• AAS 27 *Financial Reporting by Local Governments*<br>• AAS 29 *Financial Reporting by Government Departments*<br>• AAS 31 *Financial Reporting by Governments* |

This summary has been written in general terms and is intended for general reference only. Agencies should review the contents of the AASB Standard to determine its application in particular circumstances.

[1] Issued as a separate *Treasury Analysis* – refer IAS Treasury website
[2] Limited impact on NSW public sector – no *Treasury Analysis* expected to be issued.
[3] Addressed as part of *Treasury Analysis* on AASB 120.
[4] Existing Standards retained – no *Treasury Analysis* to be issued.
[5] However, this Guidance has subsequently been omitted by the AASB.