

МІНІСТЕРСТВО ОСВІТИ І НАУКИ УКРАЇНИ  
МИКОЛАЇВСЬКИЙ НАЦІОНАЛЬНИЙ АГРАРНИЙ УНІВЕРСИТЕТ

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Кафедра обліку і оподаткування

**ОБЛІК І ФІНАНСОВА ЗВІТНІСТЬ ЗА  
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**КУРС ЛЕКЦІЙ**

для здобувачів другого (магістерського) рівня вищої освіти  
ОПП «Облік і оподаткування» спеціальності 071 «Облік і оподаткування»  
денної форми здобуття вищої освіти

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Друкується за рішенням науково-методичної комісії обліково-фінансового факультету Миколаївського національного аграрного університету від 25 вересня 2023 р. протокол № 2.

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**Облік і фінансова звітність за міжнародними стандартами (іноземною мовою)** (частина II) : курс лекцій / уклад. О. І. Лугова. – Миколаїв : МНАУ, 2023. – 74 с.

Курс лекцій призначений для підготовки здобувачів другого (магістерського) рівня вищої освіти спеціальності 071 «Облік і оподаткування».

Містить основні положення з дисципліни «Облік і фінансова звітність за міжнародними стандартами (іноземною мовою)». Розкриваються концептуальні засади на рівні міжнародних стандартів, а також розглядаються основні аспекти організації та подання фінансової звітності за міжнародними стандартами, зокрема, склад та вимоги до звітності, строки, формати і порядок її подання, механізм оприлюднення фінансової звітності. Курс лекцій допоможе сформуванню у здобувачів вищої освіти певну лексичну базу, виробити вміння та навички спілкуватися англійською мовою з фаху.

Може бути корисним також для спеціалістів з бухгалтерського обліку, викладачів та здобувачів вищої освіти, які бажають поглибити знання англійської мови за професійним спрямуванням.

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## INTRODUCTION

Financial statement preparation is a crucial aspect of a company's financial management, involving the recording and reporting of its financial transactions and activities.

Financial statements provide a comprehensive overview of a company's financial performance, position, and cash flows, aiding in decision-making and financial analysis.

Proper financial statement preparation requires a thorough understanding of accounting principles, standards, and regulations, as well as attention to detail and accuracy in recording and reporting financial data.

The preparation of financial statements involves the process of aggregating accounting information into a standardized set of financials. The completed financial statements are then distributed to management, lenders, creditors, and investors, who use them to evaluate the performance, liquidity, and cash flows of a business.

The Conceptual Framework for the Financial Reporting provides a conceptual foundation for the development of accounting standards and the preparation of financial statements. It ensures consistency, comparability, and transparency in financial reporting across different entities and jurisdictions. By adhering to the framework, stakeholders can have confidence in the reliability and relevance of the financial information provided in financial statements.

## **MODULE 4. PREPARATION AND PRESENTATION OF FINANCIAL STATEMENTS**

### **THEME 12. CONCEPTS THAT UNDERLIE THE PREPARATION AND PRESENTATION OF FINANCIAL STATEMENTS**

#### **12.1. Status and Purpose of the Conceptual Framework**

#### **12.2. The Objective of Financial Reporting**

#### **12.3. Qualitative Characteristics of Useful Financial Information**

#### **12.4. Financial Statements and the Reporting Entity**

#### **12.5. The Elements of Financial Statements**

#### **12.6. Recognition of the Elements of Financial Statements**

#### **12.7. Measurement of the Elements of Financial Statements**

#### **12.8. Concepts of Capital and Capital Maintenance**

Key words: fundamental qualitative characteristics, enhancing qualitative characteristics, assets, liabilities, equity, income, expense, financial concept of capital, physical concept of capital

#### **12.1. Status and Purpose of the Conceptual Framework**

The *Conceptual Framework for Financial Reporting* describes the objective of, and the concepts for, general purpose financial reporting

##### **Status:**

✓ provides concepts and guidance that underpin поддерживать the decisions the Board makes when developing Standards

✓ not a Standard

✓ does not override any Standard or any requirement in a Standard

##### **The purpose of the Conceptual Framework is**

✓ to assist the Board in developing Standards

✓ to assist preparers to develop consistent accounting policies when no Standard applies to a particular transaction or other event, or when a Standard allows a choice of accounting policy

✓ to assist all parties to understand and interpret the Standards

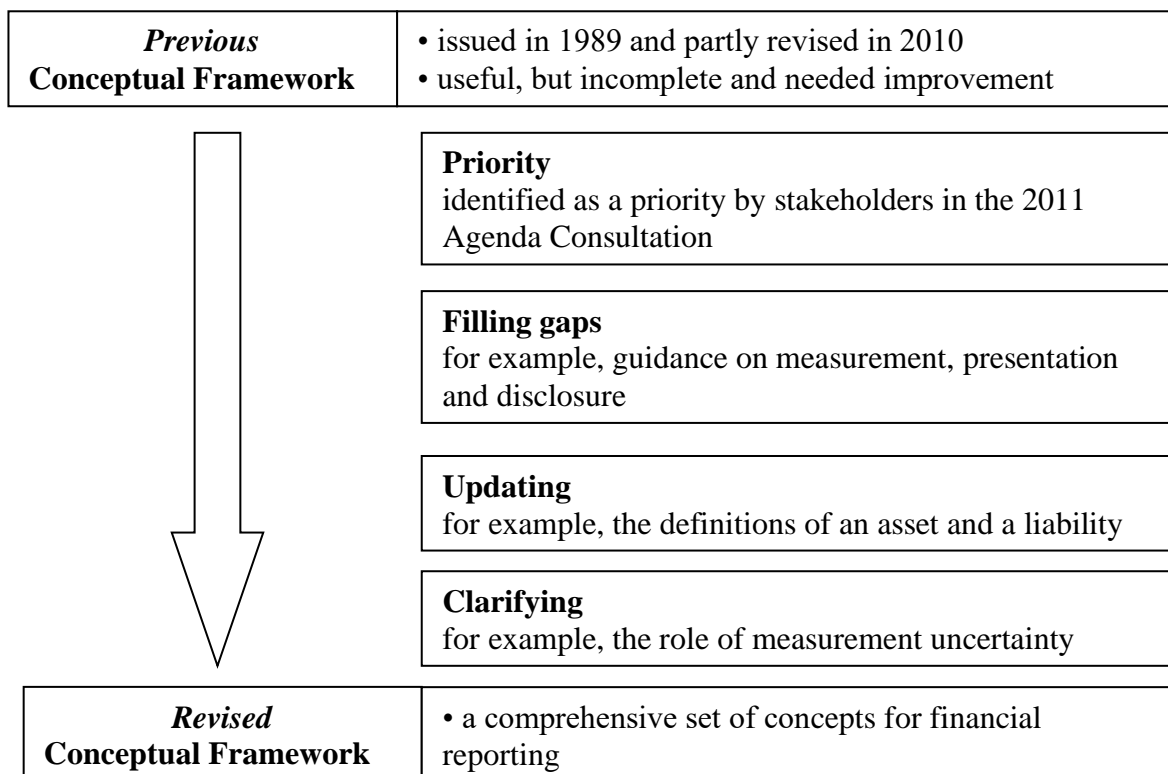
The International Accounting Standards Board issued the revised Conceptual Framework for Financial Reporting on 29 March 2018.

The revised version includes comprehensive changes to the previous Conceptual Framework, issued in 1989 and partly revised in 2010.

The previous Conceptual Framework (the 2010 Conceptual Framework) was criticised for its lack of clarity, the exclusion of certain important concepts and for being outdated in terms of the IASB’s current thinking.

In revising the Conceptual Framework, the Board was looking to underpin high-level concepts with sufficient detail for it to set standards and to help others to better understand and interpret the standards.

The revised Conceptual Framework includes some new concepts, provides updated definitions and recognition criteria for assets and liabilities and clarifies some important concepts



**The revised Conceptual Framework introduces the following main improvements:**

<b>New</b>			
<b>Measurement</b>	concepts on measurement, including factors to be considered when selecting a measurement basis		
<b>Presentation and disclosure</b>	concepts on presentation and disclosure, including when to classify income and expenses in other comprehensive income		
<b>Derecognition</b>	guidance on when assets and liabilities are removed from financial statements		
<b>Updated</b>			
<b>Definitions</b>	definitions of an asset and a liability		
<b>Recognition</b>	criteria for including assets and liabilities in financial statements		
<b>Clarified</b>			
<b>Prudence</b>	<b>Stewardship</b>	<b>Measurement uncertainty</b>	<b>Substance over form</b>

*Conceptual Framework for Financial Reporting* is arranged in **eight chapters**:

Chapter 1 – The objective of financial reporting

Chapter 2 – Qualitative characteristics of useful financial information

Chapter 3 – Financial statements and the reporting entity

Chapter 4 – The elements of financial statements

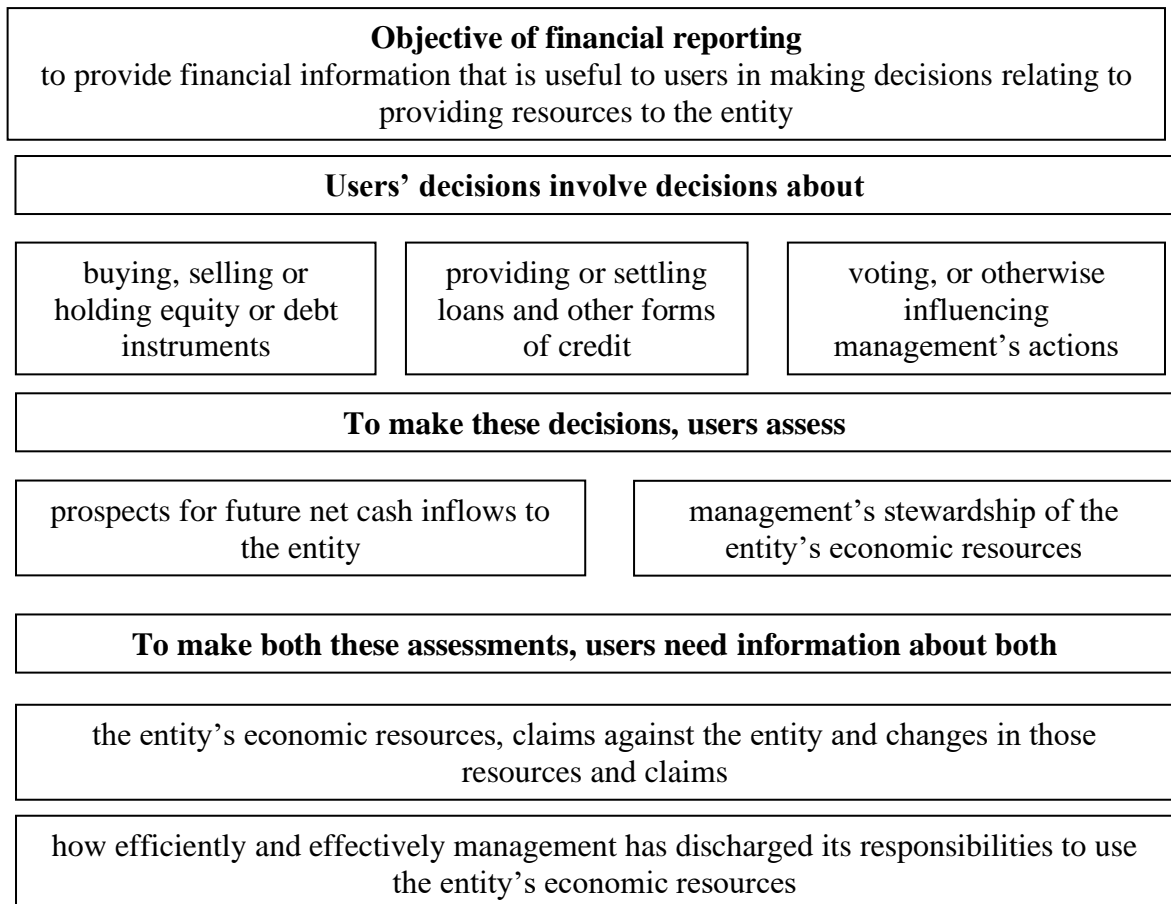
Chapter 5 – Recognition and derecognition

Chapter 6 – Measurement

Chapter 7 – Presentation and disclosure

Chapter 8 – Concepts of capital and capital maintenance

## 12.2. The Objective of Financial Reporting



Users of financial reports need information to help them assess management's **stewardship**. The *Conceptual Framework* explicitly discusses this need as well as the need for information that helps users assess the prospects for future net cash inflows to the entity.

**Users of financial reports** are an entity's existing and potential investors, lenders and other creditors. Those users must rely on financial reports for much of the financial information they need.

## 12.3. Qualitative Characteristics of Useful Financial Information

The qualitative characteristics of useful financial information identify the types of information that are likely to be most useful to the existing and potential investors, lenders and other creditors for making decisions about the reporting entity on the basis of information in its financial report (financial information).

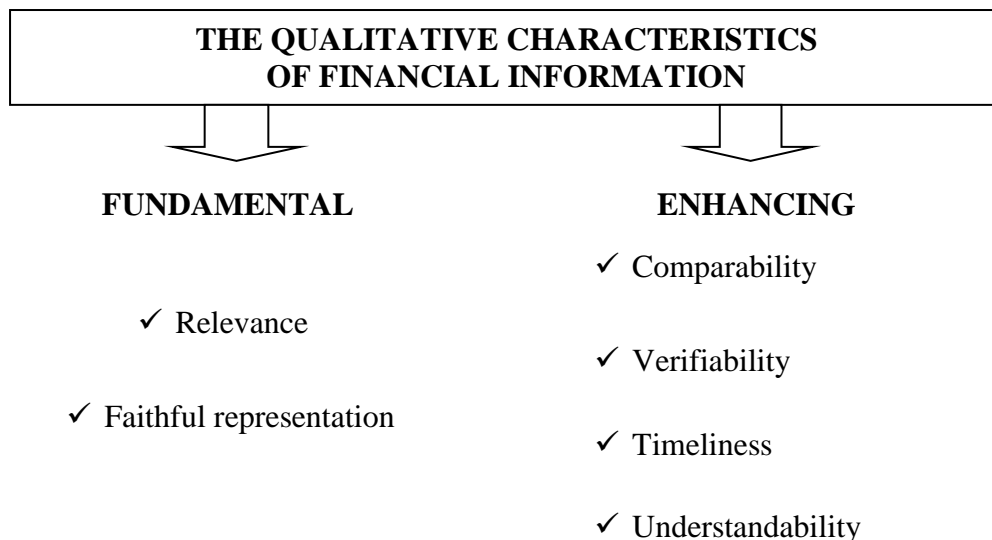
Financial reports provide information about the reporting entity's economic



resources, claims against the reporting entity and the effects of transactions and other events and conditions that change those resources and claims.

If financial information is to be useful, it must be relevant and faithfully represent what it purports to represent.

The usefulness of financial information is enhanced if it is comparable, verifiable, timely and understandable



**Relevant financial information** is capable of making a difference in the decisions made by users. Financial information is capable of making a difference in decisions if it has predictive value, confirmatory value or both.

**Materiality** is an entity-specific aspect of relevance based on the nature or magnitude (or both) of the items to which the information relates in the context of an individual entity's financial report.

To be useful, financial information must not only represent relevant phenomena, but it must also faithfully represent the substance of the phenomena that it purports to represent.

To be a perfectly **faithful representation**, a depiction would have three characteristics. It would be complete, neutral and free from error.

A neutral depiction is supported by the exercise of **prudence**. Prudence is the exercise of caution when making judgements under conditions of uncertainty.

Information must be both relevant and faithfully represented if it is to be

useful.

Comparability, verifiability, timeliness and understandability are qualitative characteristics that enhance the usefulness of information that is relevant and faithfully represented.

Information about a reporting entity is more useful if it can be compared with a similar information about other entities and with similar information about the same entity for another period or another date. **Comparability** enables users to identify and understand similarities in, and differences among, items.]

**Verifiability** helps to assure users that information represents faithfully the economic phenomena it purports to represent. Verifiability means that different knowledgeable and independent observers could reach consensus, although not necessarily complete agreement, that a particular depiction is a faithful representation.

**Timeliness** means that information is available to decision-makers in time to be capable of influencing their decisions.

Classifying, characterising and presenting information clearly and concisely makes it **understandable**. While some phenomena are inherently complex and cannot be made easy to understand, to exclude such information would make financial reports incomplete and potentially misleading. Financial reports are prepared for users who have a reasonable knowledge of business and economic activities and who review and analyse the information with diligence.

Enhancing qualitative characteristics should be maximised to the extent necessary. However, enhancing qualitative characteristics (either individually or collectively) cannot render information useful if that information is irrelevant or not represented faithfully.

### ***The cost constraint on useful financial reporting***

Cost is a pervasive constraint on the information that can be provided by general purpose financial reporting. Reporting such information imposes costs and those costs should be justified by the benefits of reporting that information. The IASB assesses costs and benefits in relation to financial reporting generally, and

not solely in relation to individual reporting entities. The IASB will consider whether different sizes of entities and other factors justify different reporting requirements in certain situations.

#### **12.4. Financial Statements and the Reporting Entity**

**The objective of financial statements** is to provide information about an entity's assets, liabilities, equity, income and expenses that is useful to financial statements users in assessing the prospects for future net cash inflows to the entity and in assessing management's stewardship of the entity's resources.

The financial statements should provide the useful information about the reporting entity:

1. In the *statement of financial position*, by recognizing:
  - ✓ Assets,
  - ✓ Liabilities,
  - ✓ Equity
2. In the *statements of financial performance*, by recognizing
  - ✓ Income, and
  - ✓ Expenses
3. In *other statements*, by presenting and disclosing information about:
  - ✓ recognized and unrecognized assets, liabilities, equity, income and expenses, their nature and associated risks;
  - ✓ Cash flows;
  - ✓ Contributions from and distributions to equity holders, and
  - ✓ Methods, assumptions, judgements used, and their changes.

Financial statements are always prepared for a specified period of time, or the *reporting period*.

Normally, the financial statements are prepared on the *going concern* assumption. It means that an entity will continue to operate for the foreseeable future (usually 12 months after the reporting date).

**A reporting entity** is an entity that is required, or chooses, to prepare

financial statements. It can be:

- ✓ A *single entity* – for example, one company;
- ✓ A *portion* of an entity – for example, a division of one company;
- ✓ *More than one* entities – for example, a parent and its subsidiaries

reporting as a group.

A reporting entity is not necessarily a legal entity.

<b>Financial statements</b>		
a particular form of financial reports that provide information about the reporting entity's assets, liabilities, equity, income and expenses		
<i>Consolidated</i>	<i>Unconsolidated</i>	<i>Combined</i>
provide information about assets, liabilities, equity, income and expenses of both the parent and its subsidiaries as a single reporting entity	provide information about assets, liabilities, equity, income and expenses of the parent only	provide information about assets, liabilities, equity, income and expenses of two or more entities that are not all linked by a parent-subsiary relationship

## 12.5. The Elements of Financial Statements

The main purpose of financial statements is to provide financial information to the users to assist them in their economic decisions.

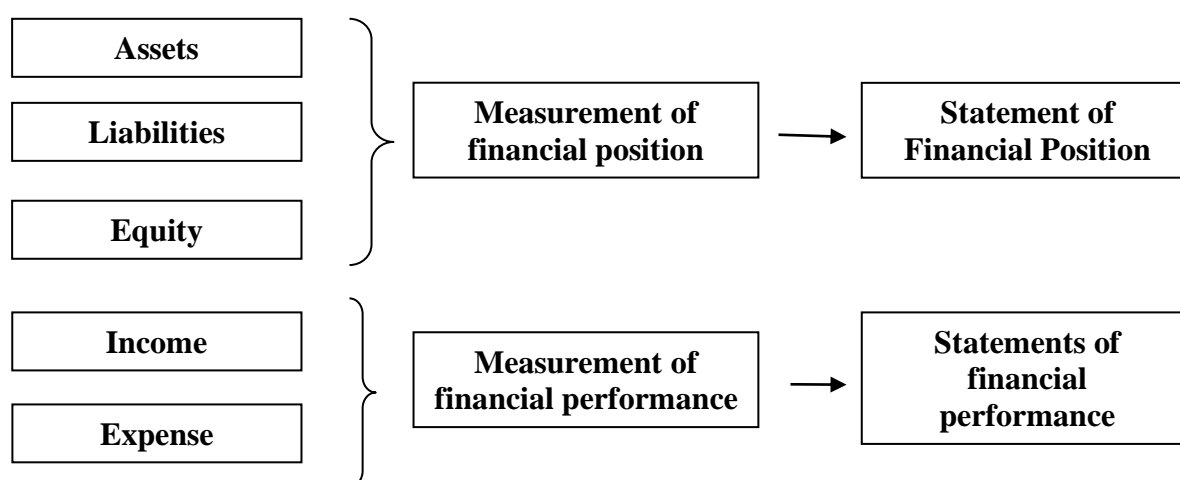
In order to enhance the quality of information in financial statements, business transactions are grouped in different classes or categories on the basis of their economic characteristics. The broad classes or categories are called **elements of financial statements**.

The elements of financial statements defined in the *Conceptual Framework* are:

- (a) assets, liabilities and equity, which relate to a reporting entity's financial position; and
- (b) income and expenses, which relate to a reporting entity's financial performance.

The elements directly related to the measurement of financial position of the entity are **assets**, **liabilities** and **equity**. These elements are presented in the **Statement of Financial Position** which was previously known as Balance Sheet.

The elements directly related to the measurement of financial performance of the entity are **income** and **expense**. These elements are presented in the **Income Statement**.



**Table —The elements of financial statements**

Item	Element
Economic resource	Asset
Claim	Liability
	Equity
Changes in economic resources and claims, reflecting financial performance	Income
	Expenses
Other changes in economic resources and claims	Contributions from holders of equity claims, and distributions to them.
	Exchanges of assets or liabilities that do not result in increases or decreases in equity.

**An asset** is a present economic resource controlled by the entity as a result of past events.

**An economic resource** is a right that has the potential to produce economic benefits.

There are three aspects of those definitions:

- a) right;
- b) potential to produce economic benefits; and
- c) control

**Rights** that have the potential to produce economic benefits take many forms.

An economic resource is a right that has the **potential to produce economic benefits**. For that potential to exist, it does not need to be certain, or even likely, that the right will produce economic benefits. It is only necessary that the right already exists and that, in at least one circumstance, it would produce for the entity economic benefits beyond those available to all other parties.

**Control** links an economic resource to an entity. Assessing whether control exists helps to identify the economic resource for which the entity accounts. For example, an entity may control a proportionate share in a property without controlling the rights arising from ownership of the entire property. In such cases, the entity's asset is the share in the property, which it controls, not the rights arising from ownership of the entire property, which it does not control.

Assets may be classified into Current and Non-Current.

**Current Assets** are ones that an entity expects to use within one-year time from the reporting date.

**Non-Current Assets** are those whose benefits are expected to last more than one year from the reporting date.

**A liability** is a present obligation of the entity to transfer an economic resource as a result of past events.

For a liability to exist, three criteria must all be satisfied:

- (a) the entity has an obligation;
- (b) the obligation is to transfer an economic resource; and
- (c) the obligation is a present obligation that exists as a result of past events

**An obligation** is a duty or responsibility that an entity has no practical ability to avoid. An obligation is always owed to another party (or parties). The other party (or parties) could be a person or another entity, a group of people or other entities, or society at large. It is not necessary to know the identity of the party (or parties) to whom the obligation is owed.

The second criterion for a liability is that the obligation is **to transfer an**

**economic resource.**

To satisfy this criterion, the obligation must have the potential to require the entity to transfer an economic resource to another party (or parties). For that potential to exist, it does not need to be certain, or even likely, that the entity will be required to transfer an economic resource—the transfer may, for example, be required only if a specified uncertain future event occurs. It is only necessary that the obligation already exists and that, in at least one circumstance, it would require the entity to transfer an economic resource.

**A present obligation exists as a result of past events** only if:

- a) the entity has already obtained economic benefits or taken an action;
- b) as a consequence, the entity will or may have to transfer an economic resource that it would not otherwise have had to transfer.

Liabilities may be classified into *Current* and *Non-Current*.

**Current Liability** is one which the entity expects to pay off within one year from the reporting date.

**Non-Current Liability** is one which the entity expects to settle after one year from the reporting date.

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

**Equity claims** are claims on the residual interest in the assets of the entity after deducting all its liabilities.

In other words, they are claims against the entity that do not meet the definition of a liability. Such claims may be established by contract, legislation or similar means, and include, to the extent that they do not meet the definition of a liability:

- a) shares of various types, issued by the entity; and
- b) some obligations of the entity to issue another equity claim.

Equity therefore includes share capital contributed by the shareholders along with any profits or surpluses retained in the entity. This is what the owners take home in the event of liquidation of the entity.

**The unit of account** is the right or the group of rights, the obligation or the group of obligations, or the group of rights and obligations, to which recognition criteria and measurement concepts are applied.

A unit of account is selected to provide useful information, which implies that:

- ✓ the information provided about the asset or liability and about any related income and expenses must be relevant;

- ✓ the information provided about the asset or liability and about any related income and expenses must faithfully represent the substance of the transaction or other event from which they have arisen.

**Income** is increases in assets, or decreases in liabilities, that result in increases in equity, other than those relating to contributions from holders of equity claims.

**Expenses** are decreases in assets, or increases in liabilities, that result in decreases in equity, other than those relating to distributions to holders of equity claims.

It follows from these definitions of income and expenses that contributions from holders of equity claims are not income, and distributions to holders of equity claims are not expenses.

There are two types of income:

- Sale Revenue: Income earned in the ordinary course of business activities of the entity;
- Gains: Income that does not arise from the core основной operations of the entity.

Following is a list of common types of expenses recognized in the financial statements:

- ✓ Salaries and wages
- ✓ Utility expenses
- ✓ Cost of goods sold
- ✓ Administration expenses



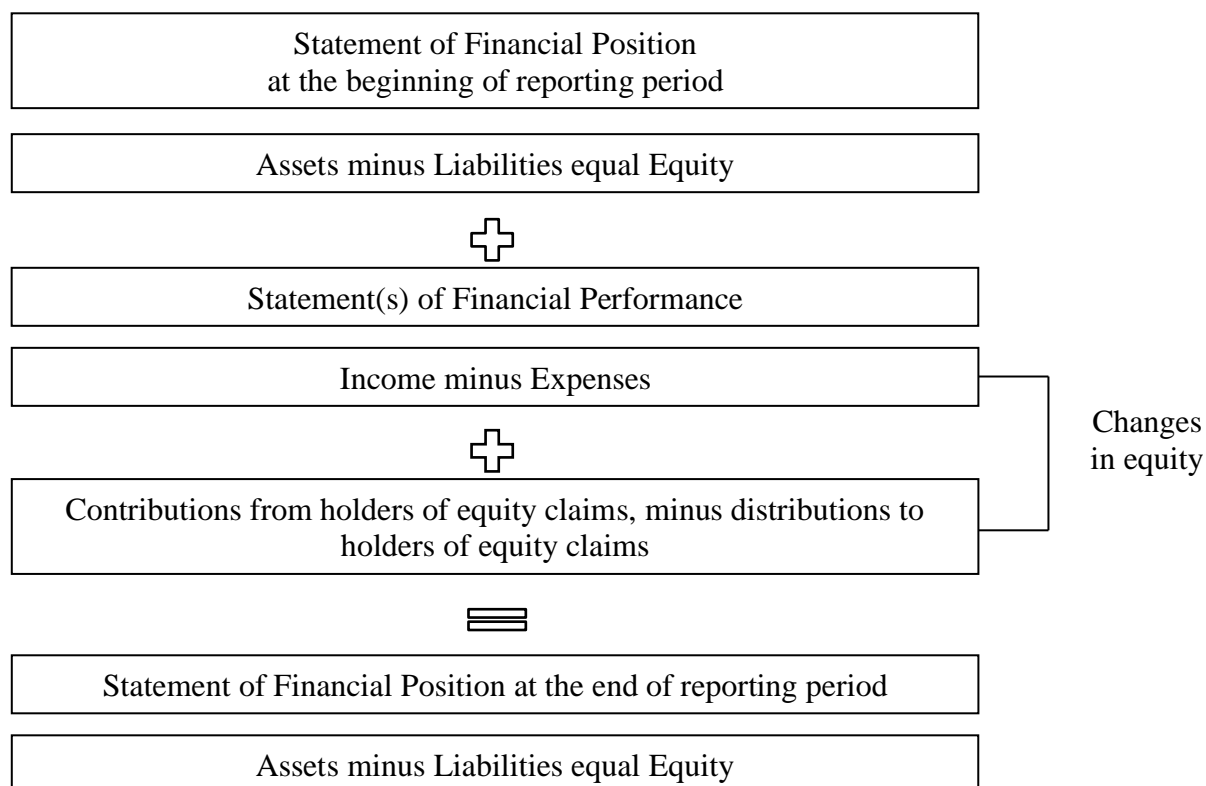
- ✓ Finance costs
- ✓ Depreciation
- ✓ Impairment losses

## 12.6. Recognition and Derecognition of the Elements of Financial Statements

**Recognition** is the process of capturing for inclusion in the statement of financial position or the statement(s) of financial performance an item that meets the definition of one of the elements of financial statements—an asset, a liability, equity, income or expenses.

Recognition involves depicting the item in one of those statements—either alone or in aggregation with other items—in words and by a monetary amount, and including that amount in one or more totals in that statement.

The amount at which an asset, a liability or equity is recognised in the statement of financial position is referred to as its ‘carrying amount’



### Diagram: How recognition links the elements of financial statements

Recognition links the elements, the statement of financial position and the

statement(s) of financial performance as follows:

(a) in the statement of financial position at the beginning and end of the reporting period, total assets minus total liabilities equal total equity;

and

(b) recognised changes in equity during the reporting period comprise:

- income minus expenses recognised in the statement(s) of financial performance; plus

- contributions from holders of equity claims, minus distributions to holders of equity claims.

The statements are linked because the recognition of one item (or a change in its carrying amount) requires the recognition or derecognition of one or more other items (or changes in the carrying amount of one or more other items).

For example:

(a) the recognition of income occurs at the same time as:

- the initial recognition of an asset, or an increase in the carrying amount of an asset; or

- the derecognition of a liability, or a decrease in the carrying amount of a liability.

(b) the recognition of expenses occurs at the same time as:

- the initial recognition of a liability, or an increase in the carrying amount of a liability; or

- the derecognition of an asset, or a decrease in the carrying amount of an asset.

Only items that meet the definition of an asset, a liability or equity are recognised in the statement of financial position.

Only items that meet the definition of income or expenses are recognised in the statement(s) of financial performance.

However, not all items that meet the definition of one of those elements are recognised.

**Derecognition** is the removal of all or part of a recognised asset or liability from an entity's statement of financial position.

Derecognition normally occurs when that item no longer meets the definition of an asset or of a liability:

(a) for an asset, derecognition normally occurs when the entity loses control of all or part of the recognised asset; and

(b) for a liability, derecognition normally occurs when the entity no longer has a present obligation for all or part of the recognised liability.

## **12.7. Measurement of the Elements of Financial Statements**

Elements recognised in financial statements are quantified in monetary terms. This requires the selection of a measurement basis.

A measurement basis is an identified feature—for example, historical cost, fair value or fulfilment value—of an item being measured.

Applying a measurement basis to an asset or liability creates a measure for that asset or liability and for related income and expenses.

Consideration of the qualitative characteristics of useful financial information and of the cost constraint is likely to result *приведе* in the selection of different measurement bases for different assets, liabilities, income and expenses.

The Framework discusses two basic measurement basis:

1. **Historical cost** – this measurement is based on the transaction price at the time of recognition of the element;
2. **Current value** – it measures the element updated to reflect the conditions at the measurement date. Here, several methods are included:
  - ✓ Fair value;
  - ✓ Value in use;
  - ✓ Current cost.

**Historical cost measures** provide information about elements that is derived from the historical price of the transaction or event that gave rise to the item being considered for measurement; so, for an asset, this would be the cost incurred in

acquiring/creating the asset.

For a liability, this would be the value of the consideration received to incur/take on the liability.

The historical cost of both an asset and a liability will be updated over time to depict, for example, any consumption of the asset or fulfilment ВИКОНАННЯ of the liability, or the impact of any events that cause the asset to become impaired or the liability onerous.

<b>Historical cost measurement bases</b>
<p>historical cost provides information derived, at least in part, from the price of the transaction or other event that gave rise to the item being measured</p> <p>historical cost of assets is reduced if they become impaired and historical cost of liabilities is increased if they become onerous</p> <p>one way to apply a historical cost measurement basis to financial assets and financial liabilities is to measure them at amortised cost</p>

**Current value measures** provide monetary information about elements, using information updated to reflect conditions at the measurement date.

Measurement bases may include fair value, value in use, fulfilment value and current cost.

The description of fair value in the revised Conceptual Framework is in line with IFRS 13 *Fair Value Measurement*, and the descriptions of value in use and fulfilment value are derived from IAS 36 *Impairment of Assets*.

<b>Current value measurement bases</b>	
current value provides information updated to reflect conditions at the measurement date	current value measurement bases include:
fair value	<p>the price that would be received to sell an asset, or paid to transfer a liability, in an orderly transaction between market participants at the measurement date</p> <p>reflects market participants' current expectations about the amount, timing and uncertainty of future cash flows</p>
value in use (for assets) fulfilment value (for liabilities)	reflects entity-specific current expectations about the amount, timing and uncertainty of future cash flows
current cost	reflects the current amount that would be: paid to acquire an equivalent asset received to take on an equivalent liability

The factors to be considered when selecting a measurement basis are **relevance** and **faithful representation**, because the aim is to provide information that is useful to investors, lenders and other creditors

<b>Factors to consider in selecting a measurement basis</b>	
<b>Relevance</b>	
<b>Relevance</b> of information provided by a measurement basis is affected by:	
characteristics of the asset or liability the variability of cash flows sensitivity of the value to market factors or other risks for example, amortised cost cannot provide relevant information about a derivative	contribution to future cash flows whether cash flows are produced directly or indirectly in combination with other economic resources the nature of the entity's business activities for example, if assets are used in combination to produce goods or services, historical cost can provide relevant information about margins achieved in a period
<b>Faithful representation</b>	
Whether a measurement basis can provide a <b>faithful representation</b> is affected by:	
measurement inconsistency if financial statements contain measurement inconsistencies (accounting mismatch), those financial statements may not faithfully represent some aspects of the entity's financial position and financial performance	measurement uncertainty does not necessarily prevent the use of a measurement basis that provides relevant information but if too high might make it necessary to consider selecting a different measurement basis
<b>Cost constraint</b>	
Cost constrains the selection of a measurement basis, just as it constrains other financial reporting decisions	

In selecting a measurement basis, it is necessary to consider the nature of the information in both the statement of financial position and the statement(s) of financial performance.

The relative importance of each factor to be considered depends upon the facts and circumstances of individual cases.

Consideration of the factors and the cost constraint is likely to result in the selection of different measurement bases for different assets, liabilities, income and expenses.

## 12.8. Concepts of Capital and Capital Maintenance

The Framework explains two concepts of capital:

1. **Financial capital** – this is synonymous with the net assets or equity of the entity.

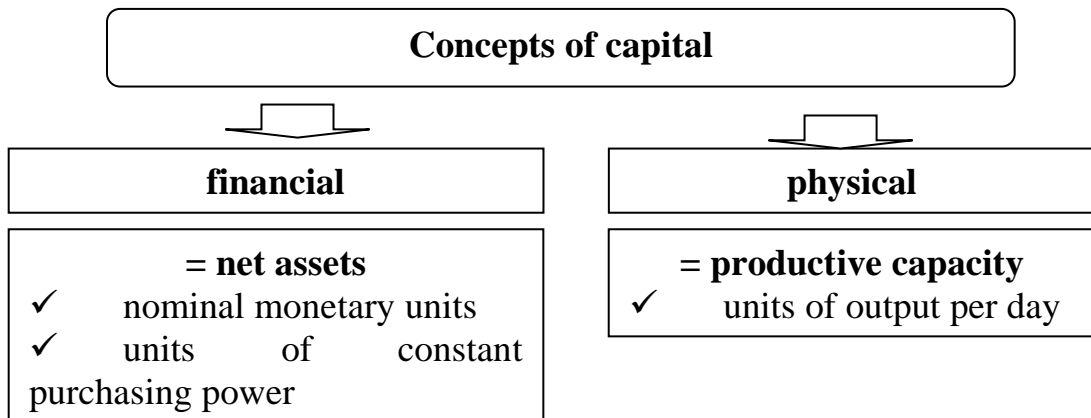
Under the financial maintenance concept, the profit is earned only when the amount of net assets at the end of the period is greater than the amount of net assets in the beginning, after excluding contributions from and distributions to equity holders.

The financial capital maintenance can be measured either in

- ✓ Nominal monetary units, or
- ✓ Units of constant purchasing power.

2. **Physical capital** – this is the productive capacity of the entity based on, for example, units of output per day.

Here the profit is earned if physical productive capacity increases during the period, after excluding the movements with equity holders.



The main difference between these concepts is how the entity treats the effects of changes in prices in assets and liabilities.

## THEME 13. PRESENTATION OF FINANCIAL STATEMENTS

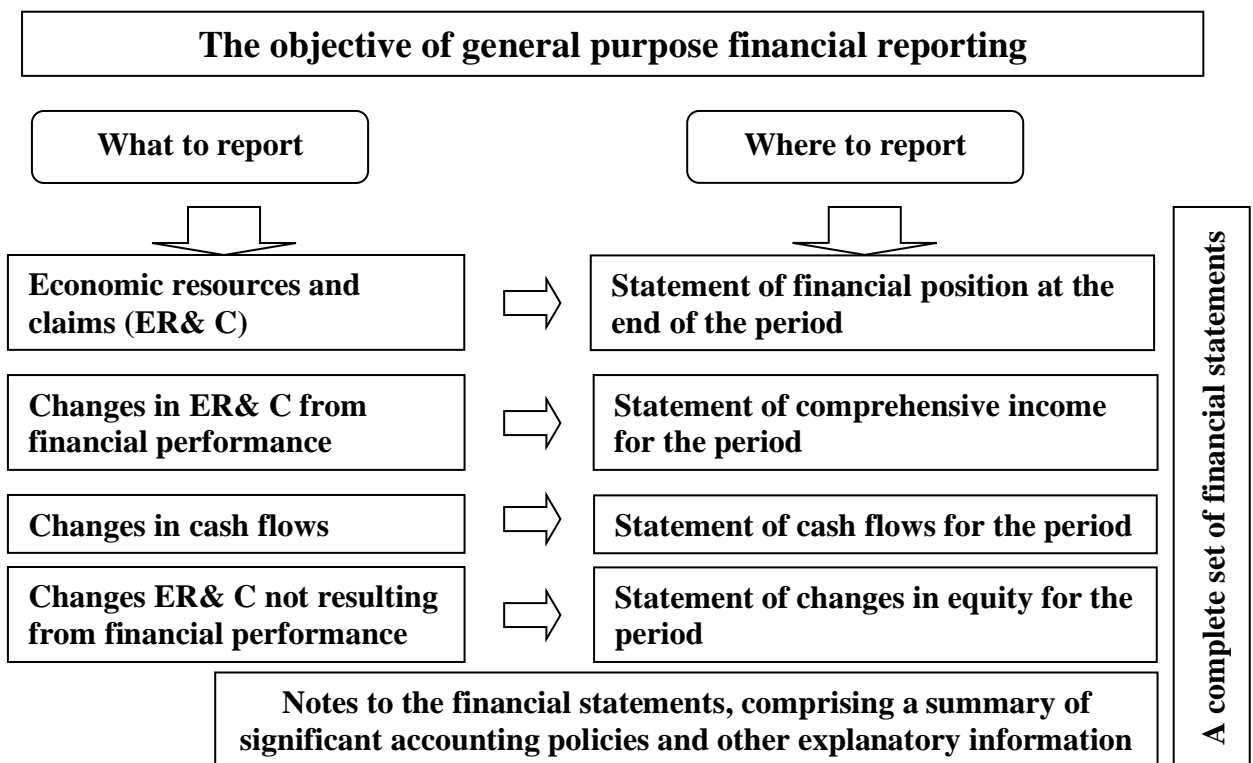
### 13.1. Purpose and Complete Set of Financial Statements

### 13.2. General Features of Financial Statements

Key words: objective of general purpose financial statements, fundamental principles, underlying assumption, going concern, accrual basis of accounting

### 13.1. Purpose and Complete Set of Financial Statements

The objective of general purpose financial statements is to provide information about the financial position, financial performance, and cash flows of an entity that is useful to a wide range of users in making economic decisions.



To meet that objective, financial statements provide information about an entity's:

- assets
- liabilities
- equity
- income and expenses, including gains and losses
- contributions by and distributions to owners (in their capacity as owners)

- cash flows.

That information, along with other information in the notes, assists users of financial statements in predicting the entity's future cash flows and, in particular, their timing and certainty.

At a more refined level, there is a different purpose associated with each of the financial statements.

The purpose of the balance sheet is to inform the reader about the current status of the business as of the date listed on the balance sheet. This information is used to estimate the liquidity, funding, and debt position of an entity, and is the basis for a number of liquidity ratios.

The income statement informs the reader about the ability of a business to generate a profit.

In addition, it reveals the volume of sales, and the nature of the various types of expenses, depending upon how expense information is aggregated. When reviewed over multiple; time periods, the income statement can also be used to analyze trends in the results of company operations.

Finally, the purpose of the statement of cash flows is to show the nature of cash receipts and disbursements, by a variety of categories. This information is of considerable use, since cash flows do not always match the revenues and expenses shown in the income statement.

Financial Statements provide useful information to a wide range of **users**:

**Managers** require Financial Statements to manage the affairs of the company by assessing its financial performance and position and taking important business decisions.

**Shareholders** use Financial Statements to assess the risk and return of their investment in the company and take investment decisions based on their analysis.

**Prospective Investors** need Financial Statements to assess the viability of investing in a company.

Investors may predict future dividends based on the profits disclosed in the Financial Statements. Furthermore, risks associated with the investment may be



gauged from the Financial Statements. For instance, fluctuating profits indicate higher risk. Therefore, Financial Statements provide a basis for the investment decisions of potential investors.

**Financial Institutions** (e.g. banks) use Financial Statements to decide whether to grant a loan or credit to a business. Financial institutions assess the financial health of a business to determine the probability of a bad loan. Any decision to lend must be supported by a sufficient asset base and liquidity.

**Suppliers** need Financial Statements to assess the credit worthiness of a business and ascertain whether to supply goods on credit. Suppliers need to know if they will be repaid. Terms of credit are set according to the assessment of their customers' financial health.

**Customers** use Financial Statements to assess whether a supplier has the resources to ensure the steady supply of goods in the future. This is especially vital where a customer is dependant on a supplier for a specialized component.

**Employees** use Financial Statements for assessing the company's profitability and its consequence on their future remuneration and job security.

**Competitors** compare their performance with rival companies to learn and develop strategies to improve their competitiveness.

**General Public** may be interested in the effects of a company on the economy, environment and the local community.

**Governments** require Financial Statements to determine the correctness of tax declared in the tax returns. Government also keeps track of economic progress through analysis of Financial Statements of businesses from different sectors of the economy.

In addition, financial statements can be presented for individual subsidiaries or business segments, to determine their results at a more refined level of detail.

In short, the financial statements have a number of purposes, depending upon who is reading the information and which financial statements are being perused.

Reports that are presented outside of the financial statements – including

financial reviews by management, environmental reports, and value added statements – are outside the scope of IFRSs.

Term before 2007 revision of IAS	Term as amended by IAS 1 (2007)
balance sheet	statement of financial position
cash flow statement	statement of cash flows
income statement	statement of comprehensive income (income statement is retained in case of a two-statement approach)
recognised in the income statement	recognised in profit or loss
recognised [directly] in equity (only for OCI components)	recognised in other comprehensive income
recognised [directly] in equity (for recognition both in OCI and equity)	recognised outside profit or loss (either in OCI or equity)
removed from equity and recognised in profit or loss ('recycling')	reclassified from equity to profit or loss as a reclassification adjustment
Standard or/and Interpretation	IFRSs
on the face of	in
equity holders	owners (exception for 'ordinary equity holders')
balance sheet date	end of the reporting period
reporting date	end of the reporting period
after the balance sheet date	after the reporting period

### 13.2. General Features of Financial Statements

**IAS 1 Presentation of Financial Statements** represents a basis of the whole IFRS reporting, as it sets overall requirements for the presentation of financial statements, guidelines for their structure and minimum requirements for their content.

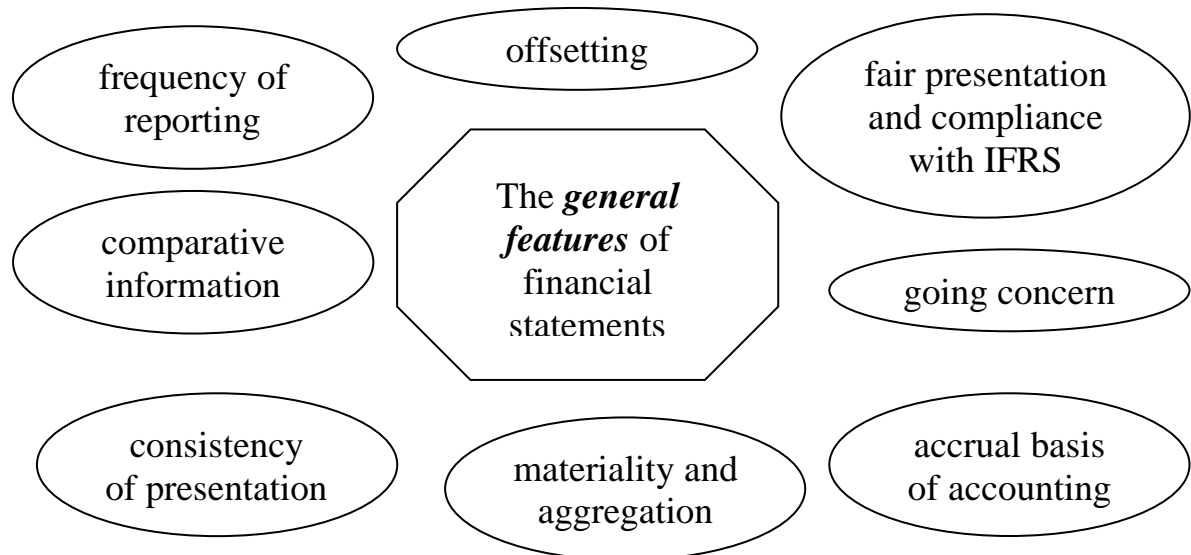
#### Underlying Assumption

↓  
is

#### **Going concern**

It means that an entity will continue to operate for the foreseeable future (usually 12 months after the reporting date).

According to IAS 1 general features of financial statements (which can also be called as fundamental principles for preparation and presentation of financial statements) are:



As you can see that underlying assumptions form part of the fundamental principles but not all of the principles are underlying assumptions as given in framework.

### **Fair presentation and compliance with IFRSs**

The financial statements must «present fairly» the financial position, financial performance and cash flows of an entity.

Fair presentation requires the faithful representation of the effects of transactions, other events, and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the Framework.

The application of IFRSs, with additional disclosure when necessary, is presumed to result in financial statements that achieve a fair presentation.

To achieve the fair presentation the entity should make sure the following:

- The selection and application of accounting policies as per IAS8
- The information contained in financial statements should have all the qualitative characteristics of financial statements
- Complete disclosure should be given as per the IFRS

IAS 1 requires an entity whose financial statements comply with IFRSs to make an explicit and unreserved statement of such compliance in the notes.

Financial statements cannot be described as complying with IFRSs unless

they comply with all the requirements of IFRSs (which includes International Financial Reporting Standards, International Accounting Standards, IFRIC Interpretations and SIC Interpretations).

### **Going concern**

The Conceptual Framework notes that financial statements are normally prepared assuming the entity is a going concern and will continue in operation for the foreseeable future.

At the end of each reporting period, when entity will prepare its financial statements, the management is required to assess of whether the entity has ability to continue its business as a going concern. If management identifies that it has ability to continue its business as a going concern then its financial statement will be prepared on a going concern basis.

The entity will be treated as going concern, if it can continue its operations for the foreseeable future such that neither the management has intention nor the circumstances are there that the entity will have to curtail its business activities.

If management has significant concerns about the entity's ability to continue as a going concern, the uncertainties must be disclosed. If management concludes that the entity is not a going concern, the financial statements should not be prepared on a going concern basis, in which case IAS 1 requires a series of disclosures.

### **Accrual basis of accounting**

IAS 1 requires that an entity prepare its financial statements, except for cash flow information, using the accrual basis of accounting.

### **Materiality and aggregation**

Each material class of similar items must be presented separately in the financial statements. Dissimilar items may be aggregated only if they are individually immaterial.

### **Offsetting**

The entity should not offset any assets and liabilities or any income and expense, except it is required by a IFRS.

### **Frequency of Reporting**

An entity shall present a complete set of financial statements (including comparative information) at least annually. When an entity changes the end of its reporting period and presents financial statements 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 for using a longer or shorter period, and
- (b) The fact that amounts presented in the financial statements are not entirely comparable.

### **Comparative Information**

IAS 1 requires an entity to disclose the comparative information in respect of the previous accounting period similar to those amounts which are presented in the financial statements of the current accounting period. If comparative amounts are changed or reclassified, various disclosures are required.

### **Consistency of presentation**

The presentation and classification of items in the financial statements shall be retained from one period to the next unless a change is justified either by a change in circumstances or a requirement of a new IFRS.

The entity should use the same accounting policies in the preparation and presentation of financial statements for the similar events and transactions, from one period to the next in order to ensure the comparability of financial statements unless the change is required by the circumstance laid down in IAS 8

## **THEME 14. STRUCTURE AND CONTENT OF FINANCIAL STATEMENTS**

### **14.1. Identification of the Financial Statements**

### **14.2. Statement of Financial Position**

### **14.3. Statement of Comprehensive Income**

### **14.4. Statement of Changes In Equity**

### **14.5. Statement of Cash Flows**

### **14.6. Notes**

### **14.7. Interim Financial Reporting**

Key words: financial statements, statement of financial position, statement of comprehensive income, statement of changes in equity, statement of cash flows, notes

### **14.1. Identification of the Financial Statements**

An entity shall clearly identify the financial statements and distinguish them from other information in the same published document.

The financial statements of the entity should be identified and distinguished from the other information using the following:

- The title of the entity presenting financial statements
- Whether these are the financial statements of an individual entity or consolidated financial statements for the group of entities
- The reporting date for which financial statements are presented
- The presentation currency for the amounts reported in financial statements
- The level of rounding up for the amounts reported in financial statements

### **14.2. Statement of Financial Position**

Statement of Financial Position, also known as the Balance Sheet, presents the financial position of an entity at a given date. It is comprised of three main components: assets, liabilities and equity (the acronym ALE).

The structure of the statement of financial position is similar to the basic

accounting equation:  $Assets = Liabilities + Equity$ .

**An asset** is something that an entity owns or controls in order to derive economic benefits from its use.

An entity shall present current and non-current assets, and current and non-current liabilities, as separate classifications in its statement of financial position except when a presentation based on liquidity provides information that is reliable and more relevant.

When that exception applies, an entity shall present all assets and liabilities in order of liquidity.

The entity will present an asset as **current asset**, if it meets any of the following criteria:

- It is held for trading in the normal course of business
- It will be realized within a period of 12 months from the reporting date
- It is expected to be sold or consumed in the normal course of business
- It is cash or cash equivalent as defined in IAS 7

The entity will present all other assets as non-current assets.

Assets are also classified in the statement of financial position on the basis of their nature:

- Tangible & intangible: Non-current assets with physical substance are classified as *property, plant and equipment* whereas assets without any physical substance are classified as *intangible assets*. Goodwill is a type of an intangible asset.
- Inventories balance includes goods that are held for sale in the ordinary course of the business. Inventories may include raw materials, finished goods and works in progress.
- Trade receivables include the amounts that are recoverable from customers upon credit sales. Trade receivables are presented in the statement of financial position after the deduction of allowance for bad debts.
- Cash and cash equivalents include cash in hand along with any short

term investments that are readily convertible into known amounts of cash.

A **liability** is an obligation that a business owes to someone and its settlement involves the transfer of cash or other resources. Liabilities must be classified in the statement of financial position as current or non-current depending on the duration over which the entity intends to settle the liability. A liability which will be settled over the long term is classified as non-current whereas those liabilities that are expected to be settled within one year from the reporting date are classified as current liabilities.

An entity shall classify a liability as current when:

- (a) it expects to settle the liability in its normal operating cycle;
- (b) it holds the liability primarily for the purpose of trading;
- (c) the liability is due to be settled within twelve months after the reporting period; or
- (d) it does not have an unconditional right to defer settlement of the liability for at least twelve months after the reporting period.

Terms of a liability that could, at the option of the counterparty result in its settlement by the issue of equity instruments do not affect its classification.

An entity shall classify all other liabilities as non-current.

Liabilities are also classified in the statement of financial position on the basis of their nature:

- Trade and other payables primarily include liabilities due to suppliers and contractors for credit purchases. Sundry payables which are too insignificant to be presented separately on the face of the balance sheet are also classified in this category.
- Short term borrowings typically include bank overdrafts and short term bank loans with a repayment schedule of less than 12 months.
- Long-term borrowings comprise of loans which are to be repaid over a period that exceeds one year. Current portion of long-term borrowings include the installments of long term borrowings that are due within one year of the reporting date.



- Current Tax Payable is usually presented as a separate line item in the statement of financial position due to the materiality of the amount.

**Equity** is what the business owes to its owners. Equity is derived by deducting total liabilities from the total assets. It therefore represents the residual interest in the business that belongs to the owners.

Equity is usually presented in the statement of financial position under the following categories:

- *Share capital* represents the amount invested by the owners in the entity
- *Retained Earnings* comprises the total net profit or loss retained in the business after distribution to the owners in the form of dividends.
- *Revaluation Reserve* contains the net surplus of any upward revaluation of property, plant and equipment recognized directly in equity.

As a minimum, the statement of financial position shall include line items that present the following amounts:

<b>ASSETS</b>	<b>EQUITY AND LIABILITIES</b>
Property, plant and equipment	Issued capital and reserves attributable to owners of the parent
Investment property	
Intangible assets	Non-controlling interests
Financial assets	Financial Liabilities
Investments accounted for using equity method	Provisions
Biological assets	
Inventories	
Trade and other receivables	Trade and other payables
Cash and cash equivalents	
Totals of assets in accordance with IFRS 5 Non-current assets Held for Sale and Discontinued Operations	Totals of liabilities in accordance with IFRS 5 Non-current assets Held for Sale and Discontinued Operations
Current tax assets	Current tax liabilities
Deferred tax assets	Deferred tax liabilities

The statement of financial position must reflect the basic accounting principles and guidelines such as the cost, matching, and full disclosure principle.

Accordingly, the statement of financial position is more meaningful when it is prepared under the accrual method of accounting.

Statement of Financial Position helps users of financial statements to assess the financial soundness of an entity in terms of liquidity risk, financial risk, credit risk and business risk.

Following is an illustrative **example of a Statement of Financial Position** prepared under the format prescribed by IAS 1 Presentation of Financial Statements.

**Statement of Financial Position as at 31<sup>st</sup> December 20x1**

	Notes	20x1 USD	20xx USD
<b>ASSETS</b>			
<b>Non-current assets</b>			
Property, plant & equipment	9	130,000	120,000
Goodwill	10	30,000	30,000
Intangible assets	11	60,000	50,000
		220,000	200,000
<b>Current assets</b>			
Inventories	12	12,000	10,000
Trade receivables	13	25,000	30,000
Cash and cash equivalents	14	8,000	10,000
		45,000	50,000
<b>TOTAL ASSETS</b>		<b>265,000</b>	<b>250,000</b>
<b>EQUITY AND LIABILITIES</b>			
<b>Equity</b>			
Share capital	4	100,000	100,000
Retained earnings		50,000	40,000
Revaluation reserve	5	15,000	10,000
<b>Total equity</b>		<b>165,000</b>	<b>150,000</b>
<b>Non-current liabilities</b>			
Long term borrowings	6	35,000	50,000
<b>Current liabilities</b>			
Trade and other payables	7	35,000	25,000
Short-term borrowings	8	10,000	8,000
Current portion of long-term borrowings	6	15,000	15,000
Current tax payable	9	5,000	2,000
<b>Total current liabilities</b>		<b>65,000</b>	<b>50,000</b>
<b>Total liabilities</b>		<b>100,000</b>	<b>100,000</b>
<b>TOTAL EQUITY AND LIABILITIES</b>		<b>265,000</b>	<b>250,000</b>

### 14.3. Statement of Comprehensive Income

Income Statement is a report of income, expenses and the resulting profit or loss earned during an accounting period.

An entity shall present all items of income and expense recognised in a period:

- (a) in a single statement of comprehensive income, or
- (b) in two statements: a statement displaying components of profit or loss (separate statement of comprehensive income) and a second statement beginning with profit or loss and displaying components of other comprehensive income (statement of comprehensive income).

The statement of comprehensive income has 2 basic elements:

***Profit or loss for the period:*** here, all items of income and expenses must be recognized.

***Other comprehensive income:*** items recognized directly to equity or reserves, such as changes in revaluation surplus, gains or losses from subsequent measurement of available-for-sale financial assets, etc.

As a minimum, the statement of comprehensive income shall include line items that present the following amounts for the period:

<b>PROFIT OR LOSS</b>
Revenue
Gains and losses arising from the derecognition of financial assets at amortized cost
Finance costs
Share of the profit or loss of associates and joint ventures accounted for using the equity method
Tax expense
Post-tax profit/gain or loss of operations or assets in accordance with IFRS 5 (Non-current assets Held for Sale and Discontinued Operations)
Profit or loss
<b>OTHER COMPREHENSIVE INCOME</b>
Each component of other comprehensive income classified by nature
Share of the other comprehensive income of associates and joint ventures accounted for using equity method

## PROFIT OR LOSS

Total comprehensive income

Profit or loss for the period, as well as total comprehensive income shall be both presented in allocation:

- attributable to non-controlling interests and
- attributable to owners of the parent.

The entity might choose to *classify expenses* recognized in profit or loss for the period by their nature or by their function.

Income statement is prepared on the accruals basis of accounting.

This means that income (including revenue) is recognized when it is **earned** rather than when receipts are realized (*although in many instances income may be earned and received in the same accounting period*).

Conversely, expenses are recognized in the income statement when they are **incurred** even if they are paid for in the previous or subsequent accounting periods.

Following is an illustrative **example of an Income Statement** prepared in accordance with the format prescribed by IAS 1 Presentation of Financial Statements.

### Income Statement for the Year Ended 31<sup>st</sup> December 20x1

	Notes	20x1 USD	20xx USD
Revenue	16	120,000	100,000
Cost of Sales	17	(65,000)	(55,000)
<b>Gross Profit</b>		<b>55,000</b>	45,000
Other Income	18	17,000	12,000
Distribution Cost	19	(10,000)	(8,000)
Administrative Expenses	20	(18,000)	(16,000)
Other Expenses	21	(3,000)	(2,000)
Finance Charges	22	(1,000)	(1,000)
<b>Profit before tax</b>		<b>40,000</b>	30,000
Income tax	23	(12,000)	(9,000)
<b>Net Profit</b>		<b>28,000</b>	21,000

Income statement comprises of the following **main elements**:

**Revenue** includes income earned from the principal activities of an entity. So for example, in case of a manufacturer of electronic, revenue will comprise of the sales from electronic appliance business. Conversely, if the same manufacturer earns interest on its bank account, it shall not be classified as revenue but as other income.

**Cost of Sales** represents the cost of goods sold or services rendered during an accounting period.

Hence, for a retailer, cost of sales will be the sum of inventory at the start of the period and purchases during the period minus any closing inventory.

In case of a manufacturer however, cost of sales will also include production costs incurred in the manufacture of goods during a period such as the cost of direct labor, direct material consumption, depreciation of plant and machinery and factory overheads, etc.

**Other Income** consists of income earned from activities that are not related to the entity's main business. For example, other income of an entity that manufactures electronic appliances may include:

- Gain on disposal of fixed assets
- Interest income on bank deposits
- Exchange gain on translation of a foreign currency bank account

**Distribution Cost** includes expenses incurred in delivering goods from the business premises to customers.

**Administrative Expenses** generally comprise of costs relating to the management and support functions within an organization that are not directly involved in the production and supply of goods and services offered by the entity.

Examples of administrative expenses include:

- Salary cost of executive management
- Legal and professional charges
- Depreciation of head office building
- Rent expense of offices used for administration and management

purposes

- Cost of functions / departments not directly involved in production such as finance department, HR department and administration department

**Other Expenses** is essentially a residual category in which any expenses that are not suitably classifiable elsewhere are included.

**Finance Charges** usually comprise of interest expense on loans and debentures.

The effect of present value adjustments of discounted provisions are also included in finance charges (e.g. unwinding of discount on provision for decommissioning cost).

**Income tax** expense recognized during a period is generally comprised of the following three elements:

- Current period's estimated tax charge
- Prior period tax adjustments
- Deferred tax expense

**Prior period financial information** is presented along side current period's financial results **to facilitate comparison of performance** over a period.

It is therefore important that prior period comparative figures presented in the income statement relate to a similar period.

Income Statement provides the basis for measuring performance of an entity over the course of an accounting period.

Performance can be assessed from the income statement in terms of the following:

- Change in sales revenue over the period and in comparison to industry growth;
- Change in gross profit margin, operating profit margin and net profit margin over the period;
- Increase or decrease in net profit, operating profit and gross profit over the period;
- Comparison of the entity's profitability with other organizations operating in similar industries or sectors.

Income statement also forms the basis of important financial evaluation of an entity when it is analyzed in conjunction with information contained in other financial statements such as:

- Change in earnings per share over the period
- Analysis of working capital in comparison to similar income statement elements (e.g. the ratio of receivables reported in the balance sheet to the credit sales reported in the income statement, i.e. debtor turnover ratio)
- Analysis of interest cover and dividend cover ratios

Income statement does not report transactions with the owners of an entity.

Hence, dividends paid to ordinary shareholders are not presented as an expense in the income statement and proceeds from the issuance of shares is not recognized as an income. Transactions between the entity and its owners are accounted for separately in the statement of changes in equity.

#### **14.4. Statement of Cash Flows**

**Statement of Cash Flows** also known as Cash Flow Statement, presents the movement in cash flows over the period as classified under operating, investing and financing activities.

Cash and cash equivalents generally consist of the following:

- Cash in hand
- Cash at bank
- Short term investments that are highly liquid and involve very low risk of change in value (therefore usually excludes investments in equity instruments)
  - Bank overdrafts in cases where they comprise an integral element of the organization's treasury management (e.g. where bank account is allowed to float between a positive and negative balance (i.e. overdraft) as opposed to a bank overdraft facility specifically negotiated for financing a shortfall in funds (in which case the related cash flows will be classified under financing activities).

As income statement and balance sheet are prepared under the accruals basis

of accounting, it is necessary to adjust the amounts extracted from these financial statements (e.g. in respect of non cash expenses) in order to present only the movement in cash inflows and outflows during a period.

All cash flows are classified under operating, investing and financing activities.

### **Operating Activities**

Cash flow from operating activities presents the movement in cash during an accounting period from the **primary revenue generating** activities of the entity.

For example, operating activities of a hotel will include cash inflows and outflows from the hotel business (e.g. receipts from sales revenue, salaries paid during the year etc), but interest income on a bank deposit shall not be classified as such (i.e. the hotel's interest income shall be presented in investing activities).

Profit before tax as presented in the income statement could be used as a starting point to calculate the cash flows from operating activities.

Following adjustments are required to be made to the profit before tax to arrive at the cash flow from operations:

1. Elimination of non cash expenses (e.g. depreciation, amortization, impairment losses, bad debts written off, etc)
2. Removal of expenses to be classified elsewhere in the cash flow statement (e.g. interest expense should be classified under financing activities)
3. Elimination of non cash income (e.g. gain on revaluation of investments)
4. Removal of income to be presented elsewhere in the cash flow statement (e.g. dividend income and interest income should be classified under investing activities unless in case of for example an investment bank)
5. Working capital changes (e.g. an increase in trade receivables must be deducted to arrive at sales revenue that actually resulted in cash inflow during the period)

### **Investing Activities**

Cash flow from investing activities includes the movement in cash flow as a



result of the purchase and sale of assets other than those which the entity primarily trades in (e.g. inventory). So for example, in case of a manufacturer of cars, proceeds from the sale of factory plant shall be classified as cash flow from investing activities whereas the cash inflow from the sale of cars shall be presented under the operating activities.

Cash flow from investing activities consists primarily of the following:

Cash outflow expended on the purchase of investments and fixed assets

Cash inflow from income from investments

Cash inflow from disposal of investments and fixed assets

### **Financing activities**

Cash flow from financing activities includes the movement in cash flow resulting from the following:

- Proceeds from issuance of share capital, debentures & bank loans
- Cash outflow expended on the cost of finance (i.e. dividends and interest expense)
- Cash outflow on the repurchase of share capital and repayment of debentures & loans

Following is an illustrative cash flow statement presented according to the **indirect method** suggested in IAS 7 Statement of Cash Flows

### **ABC PLC Statement of Cash Flows for the year ended 31 December 20x1**

	Notes	20x1 USD	20xx USD
<b>Cash flows from operating activities</b>			
Profit before tax		<b>40,000</b>	35,000
Adjustments for:			
Depreciation	<b>4</b>	<b>10,000</b>	8,000
Amortization	<b>4</b>	<b>8,000</b>	7,500
Impairment losses	<b>5</b>	<b>12,000</b>	3,000
Bad debts written off	<b>14</b>	<b>500</b>	-
Interest expense	<b>16</b>	<b>800</b>	1,000
Gain on revaluation of investments		<b>(21,000)</b>	-

Interest income	15	(11,000)	(9,500)
Dividend income		(3,000)	(2,500)
Gain on disposal of fixed assets		(1,200)	(1,850)
		<b>35,100</b>	40,650
<b>Working Capital Changes:</b>			
Movement in current assets:			
(Increase) / Decrease in inventory		(1,000)	550
Decrease in trade receivables		3,000	1,400
Movement in current liabilities:			
Increase / (Decrease) in trade payables		2,500	(1,300)
Cash generated from operations		<b>39,600</b>	41,300
Dividend paid		(8,000)	(6,000)
Income tax paid		(12,000)	(10,000)
<b>Net cash from operating activities (A)</b>		<b>19,600</b>	25,300
<b>Cash flows from investing activities</b>			
Capital expenditure	4	(100,000)	(85,000)
Purchase of investments	11	(25,000)	-
Dividend received		5,000	3,000
Interest received		3,500	1,000
Proceeds from disposal of fixed assets		18,000	5,500
Proceeds from disposal of investments		2,500	2,200
<b>Net cash used in investing activities (B)</b>		<b>(96,000)</b>	(73,300)
<b>Cash flows from financing activities</b>			
Issuance of share capital	6	1000,000	-
Bank loan received		-	100,000
Repayment of bank loan		(100,000)	-
Interest expense		(3,600)	(7,400)
<b>Net cash from financing activities (C)</b>		<b>896,400</b>	92,600
<b>Net increase in cash &amp; cash equivalents (A+B+C)</b>		<b>820,000</b>	44,600
<b>Cash and cash equivalents at start of the year</b>		<b>77,600</b>	33,000
<b>Cash and cash equivalents at end of the year</b>	<b>24</b>	<b>897,600</b>	77,600

Statement of cash flows provides important insights about the liquidity and solvency of a company which are vital for survival and growth of any organization. It also enables analysts to use the information about historic cash flows to form projections of future cash flows of an entity (e.g. in NPV analysis) on which to base their economic decisions. By summarizing key changes in financial position

during a period, cash flow statement serves to highlight priorities of management.

For example, increase in capital expenditure and development costs may indicate a higher increase in future revenue streams whereas a trend of excessive investment in short term investments may suggest lack of viable long term investment opportunities. Furthermore, comparison of the cash flows of different entities may better reveal the relative quality of their earnings since cash flow information is more objective as opposed to the financial performance reflected in income statement which is susceptible to significant variations caused by the adoption of different accounting policies.

#### **14.5. Statement of Changes in Equity**

Statement of Changes in Equity details the change in owners' equity over an accounting period by presenting the movement in reserves comprising the shareholders' equity.

Movement in shareholders' equity over an accounting period comprises the following elements:

- Net profit or loss during the accounting period attributable to shareholders
- Increase or decrease in share capital reserves
- Dividend payments to shareholders
- Gains and losses recognized directly in equity
- Effect of changes in accounting policies
- Effect of correction of prior period error

As a *minimum*, the statement of changes in equity must contain the following items:

- total comprehensive income for the period, showing separately the total amounts attributable to owners of the parent and to non-controlling interest;
- for each component of equity, the effects of retrospective application or retrospective restatement recognised in accordance with IAS 8; and
- for each component of equity, a reconciliation between the carrying

amount at the beginning and the end of the period, separately disclosing changes resulting from:

- 1) profit or loss;
- 2) other comprehensive income; and
- 3) transactions with owners in their capacity as owners, showing separately contributions by and distributions to owners and changes in ownership interests in subsidiaries that do not result in a loss of control.

Also, IAS 1 prescribes to present amount of dividends recognized as distributions and the related amount per share on the face of the statement of changes in equity or in the notes.

Following are **the main elements of statement of changes in equity**:

**Opening Balance** represents the balance of shareholders' equity reserves at the start of the comparative reporting period as reflected in the prior period's statement of financial position. The opening balance is unadjusted in respect of the correction of prior period errors rectified in the current period and also the effect of changes in accounting policy implemented during the year as these are presented separately in the statement of changes in equity.

**Effect of Changes in Accounting Policies** Since changes in accounting policies are applied retrospectively, an adjustment is required in stockholders' reserves at the start of the comparative reporting period to restate the opening equity to the amount that would be arrived if the new accounting policy had always been applied.

**Effect of Correction of Prior Period Error** The effect of correction of prior period errors must be presented separately in the statement of changes in equity as an adjustment to opening reserves. The effect of the corrections may not be netted off against the opening balance of the equity reserves so that the amounts presented in current period statement might be easily reconciled and traced from prior period financial statements.

**Restated Balance** represents the equity attributable to stockholders at the start of the comparative period after the adjustments in respect of changes in

accounting policies and correction of prior period errors as explained above.

**Changes in Share Capital** Issue of further share capital during the period must be added in the statement of changes in equity whereas redemption of shares must be deducted therefrom. The effects of issue and redemption of shares must be presented separately for share capital reserve and share premium reserve.

**Dividends** Dividend payments issued or announced during the period must be deducted from shareholder equity as they represent distribution of wealth attributable to stockholders.

**Income / Loss for the period** represents the profit or loss attributable to shareholders during the period as reported in the income statement.

**Changes in Revaluation Reserve** Revaluation gains and losses recognized during the period must be presented in the statement of changes in equity to the extent that they are recognized outside the income statement. Revaluation gains recognized in income statement due to reversal of previous impairment losses however shall not be presented separately in the statement of changes in equity as they would already be incorporated in the profit or loss for the period.

**Other Gains & Losses** Any other gains and losses not recognized in the income statement may be presented in the statement of changes in equity such as actuarial gains and losses arising from the application of IAS 19 *Employee Benefit*.

**Closing Balance** represents the balance of shareholders' equity reserves at the end of the reporting period as reflected in the statement of financial position.

Statement of changes in equity helps users of financial statement to identify the factors that cause a change in the owners' equity over the accounting periods. Whereas movement in shareholder reserves can be observed from the balance sheet, statement of changes in equity discloses significant information about equity reserves that is not presented separately elsewhere in the financial statements which may be useful in understanding the nature of change in equity reserves. Examples of such information include share capital issue and redemption during the period, the effects of changes in accounting policies and correction of prior period errors, gains and losses recognized outside income statement, dividends

declared and bonus shares issued during the period.

Following is an illustrative **example of a Statement of Changes in Equity** prepared according to the format prescribed by IAS 1 Presentation of Financial Statements.

**ABC Plc Statement of changes in equity for the year ended 31<sup>st</sup> December 20x1**

	<b>Share Capital</b>	<b>Retained Earnings</b>	<b>Revaluation Surplus</b>	<b>Total Equity</b>
	USD	USD	USD	USD
<b>Balance at 1 January 2016</b>	<b>100,000</b>	<b>30,000</b>	-	<b>130,000</b>
Changes in accounting policy	-	-	-	-
Correction of prior period error	-	-	-	-
<b>Restated balance</b>	<b>100,000</b>	<b>30,000</b>	-	<b>130,000</b>
<b>Changes in equity for the year 2016</b>				
Issue of share capital	-	-	-	-
Income for the year	-	25,000	-	<b>25,000</b>
Revaluation gain	-	-	10,000	<b>10,000</b>
Dividends	-	(15,000)	-	<b>(15,000)</b>
<b>Balance at 31 December 2016</b>	<b>100,000</b>	<b>40,000</b>	<b>10,000</b>	<b>150,000</b>
<b>Changes in equity for the year 2017</b>				
Issue of share capital	-	-	-	-
Income for the year	-	30,000	-	<b>30,000</b>
Revaluation gain	-	-	5,000	<b>5,000</b>
Dividends	-	(20,000)	-	<b>(20,000)</b>
<b>Balance at 31 December 2017</b>	<b>100,000</b>	<b>50,000</b>	<b>15,000</b>	<b>165,000</b>

#### **14.6. Notes to the Financial Statements**

These contain the information (financial and non-financial) in addition to the information which is presented in the other components of financial statements such as statement of profit or loss and other comprehensive income, statement of changes in equity, statement of financial position and statement of cash flows.

These are in the form of narrative descriptions and include the following:

- Basis used by the entity for the preparation of the financial statements
- Accounting policies of the entity
- Disclosures required by the standards

## 14.7. Interim Financial Reporting

IAS 34 *Interim Financial Reporting* applies when an entity prepares an interim financial report, without mandating when an entity should prepare such a report.

The objective of IAS 34 is to prescribe the minimum content of an interim financial report and to prescribe the principles for recognition and measurement in financial statements presented for an interim period.

**Interim period:** a financial reporting period shorter than a full financial year (most typically a quarter or half-year).

**Interim financial report:** a financial report that contains either a complete or condensed set of financial statements for an interim period.

Interim financial statements for a corporation are the financial statements covering a period of less than one year.

Often interim financial statements are issued for the quarters between the annual financial statements.

The purpose is to give investors and other users updated information on the corporation's operations.

Unlike the annual financial statements, the interim financial statements are usually unaudited and condensed. Therefore, it is wise to also read the previously issued and complete annual financial statements and reports.

The minimum components specified for an interim financial report are:

- a condensed balance sheet (statement of financial position)
- either
  - (a) a condensed statement of comprehensive income or
  - (b) a condensed statement of comprehensive income and a condensed income statement
- a condensed statement of changes in equity
- a condensed statement of cash flows
- selected explanatory notes

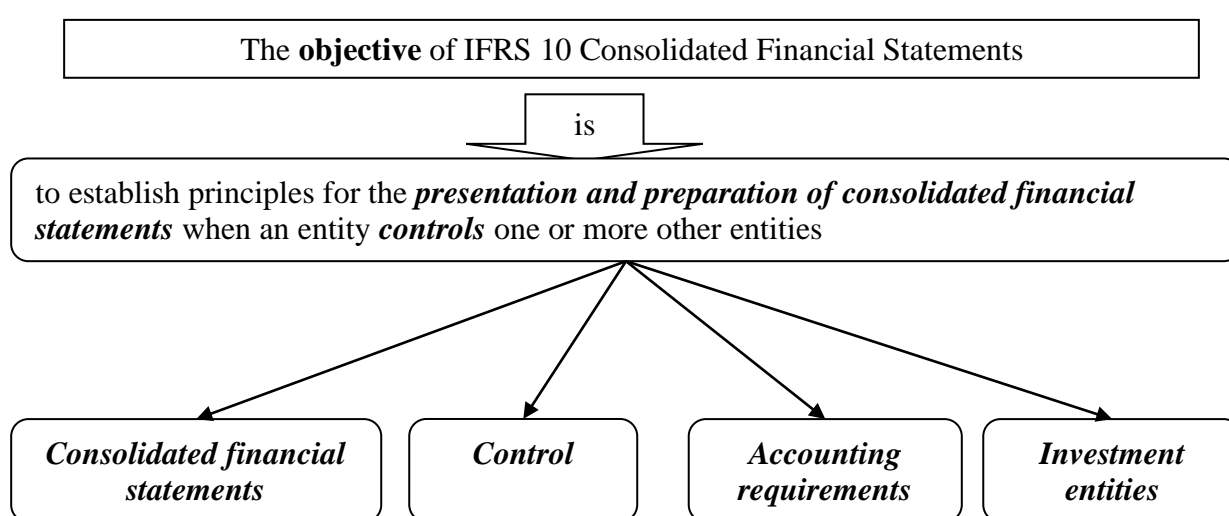
## THEME 15. CONSOLIDATED AND SEPARATE FINANCIAL STATEMENTS

### 15.1. Consolidated Financial Statements

### 15.2. Separate Financial Statements

Key words: consolidated financial statements, accounting requirements, investment entities, separate financial statements, subsidiaries, consolidation procedures

### 15.1. Consolidated Financial Statements



To meet this objective, the standard:

- Requires an entity (a parent) that **controls** one or more other entities (subsidiaries) **to present consolidated financial statements**;
- Defines the **principle of control** as the basis for consolidation and sets out how to identify whether the investor controls the investee;
- Sets out the **accounting requirements** for the preparation of consolidated financial statements, and
- Defines an **investment entity** and sets out an **exception** to consolidating particular subsidiaries of an investment entity.

#### Control as the basis for consolidation

Simply speaking, the basic rule is:

- If an investor **controls** its investee => **investor must consolidate**;



- If an investor *does NOT control* its investee =>; investor *does NOT consolidate*.

An investor *controls* an investee when the investor:

- ✓ is exposed to, or has right to *variable returns* from its involvement with the investee (= subsidiary)
- ✓ has the *ability to affect* those returns
- ✓ through its *power* over the investee

**Power** is the existing rights that give the current ability to affect the relevant activities of investee.

### How to assess control

Remember 3 basic elements inherent in control:

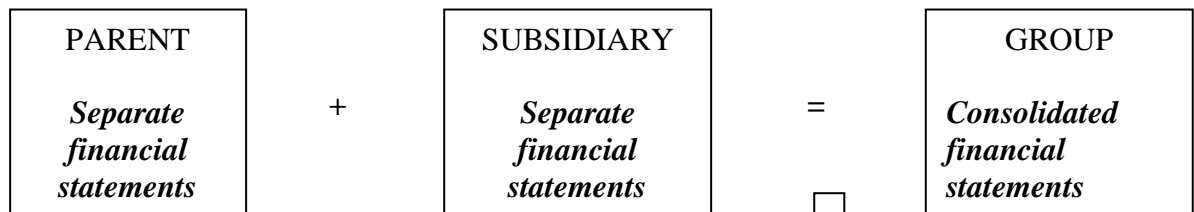
- ✓ *power*,
- ✓ *ability to use this power* and
- ✓ *variable returns*.

Let's break it down a bit:

- The rights must be substantive, not only some minor rights;
- The ability must be current, exercisable in the present time;
- The relevant activities must be significant and related to major activities of investee.

When assessing whether an investor controls an investee, more than one factor need to be considered. IFRS 10 contains guidance in this area.

**Consolidated financial statements** = the financial statements of a group presented as those of a single economic entity



**Consolidation procedures + Accounting requirements**

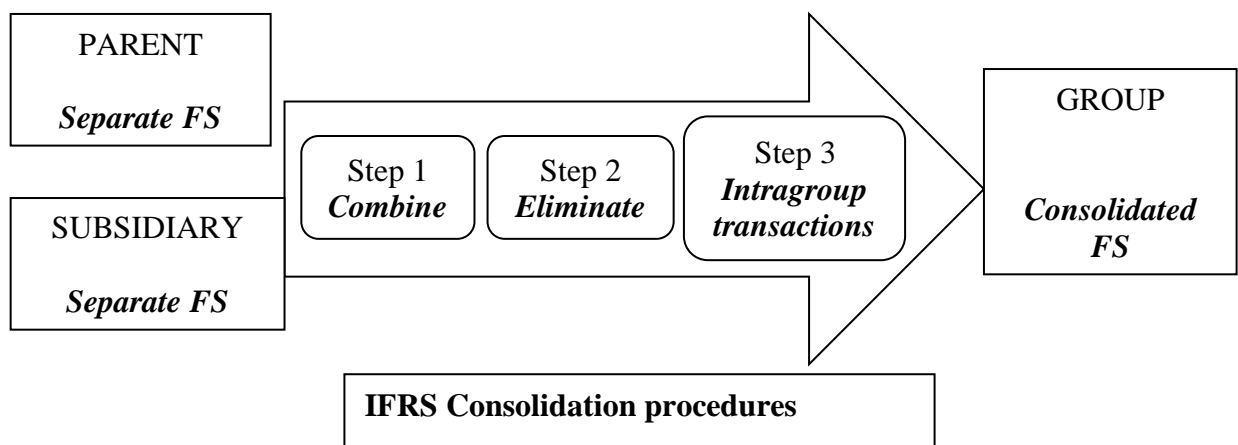
In order to prepare consolidated financial statements, IFRS 10 prescribes the following *consolidation procedures*:

**Consolidation procedures:**

**Step 1** *Combine* like items of assets, liabilities, equity, income, expenses and cash flows of the parent with those of its subsidiaries

**Step 2** **Offset (eliminate):**  
 - the carrying amount of the parent’s investment in each subsidiary;  
 - the parent’s portion of equity of each subsidiary;

**Step 3** Eliminate in full *intragroup* assets and liabilities, equity, income, expenses and cash flows relating to transactions between entities of the group



## **Other accounting requirements**

Except for basic consolidation procedures, IFRS 10 prescribes number of other rules for preparing consolidated financial statements, such as:

- Presentation of *non-controlling interests*: in equity, but separately from the equity of owners of the parent;
- *Uniform accounting policies* shall be used by both parent and subsidiary;
- The financial statements of the parent and the subsidiary shall have the *same reporting date*;
- How to deal when the *parent loses its control* over subsidiary, and number of other rules dealing with the specific circumstances.

## **Exceptions in IFRS 10**

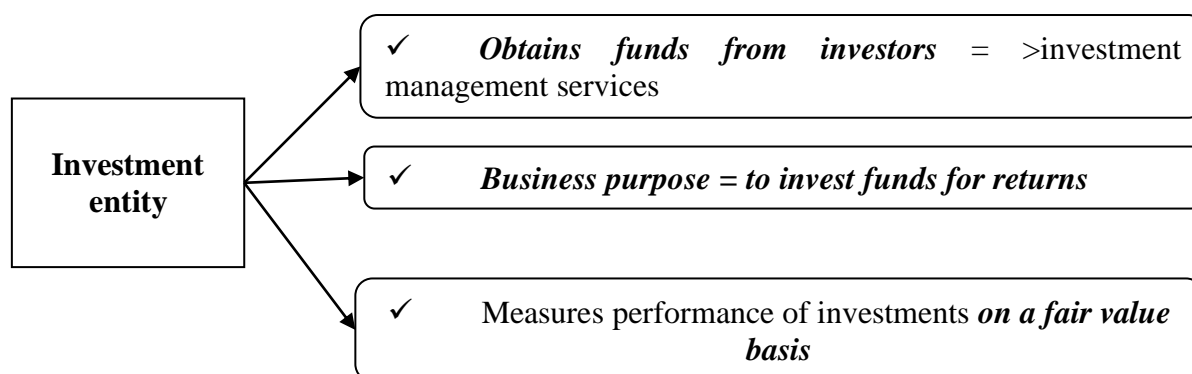
When a parent controls a subsidiary, then it should consolidate. But not always.

IFRS 10 sets the following *exceptions from consolidation*:

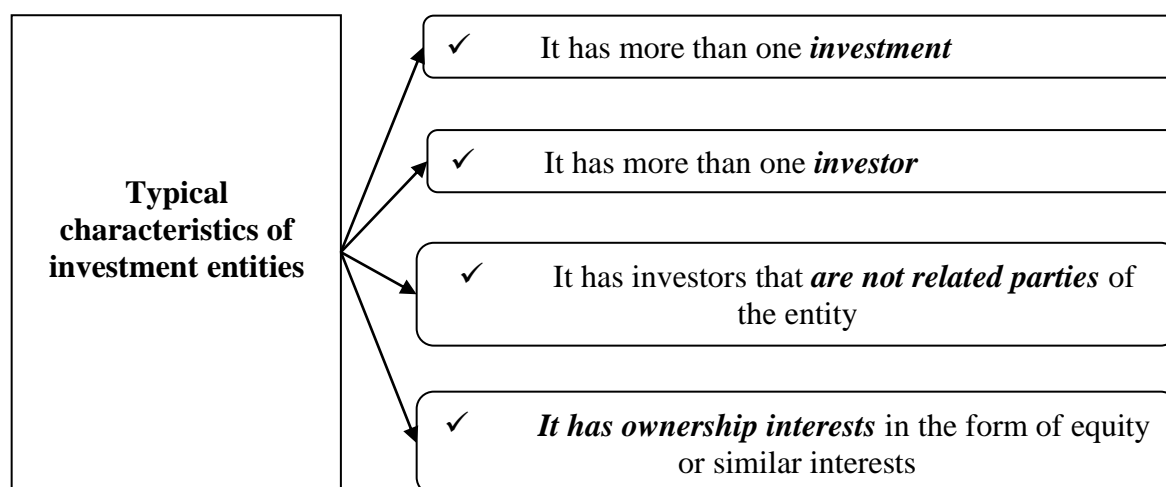
1. A parent does not need to present consolidated financial statements if it meets all of the following conditions:
  - It is a *wholly-owned subsidiary* or is a *partially-owned subsidiary* of another entity and its other owners agree;
  - Its debt or equity instruments are *not traded in a public market*;
  - It *did not file, nor is it in the process of filing*, its financial statements with a securities commission or other regulatory organization for the purpose of issuing any class of instruments in a public market, and
  - Its ultimate or any intermediate parent of the parent produces consolidated financial statements available for public use that comply with IFRSs.
2. *Post-employment benefit plans or other long-term employee benefit plans* to which IAS 19 Employee Benefits applies – they don't need to present consolidated financial statements;
3. *Investment entities*.

**Investment entity** is an entity that:

1. ***Obtains funds from one or more investors*** for the purpose of providing those investor(s) with investment management services;
2. Commits to its investor(s) that its ***business purpose is to invest funds solely for returns*** from capital appreciation, investment income, or both, and
3. Measures and evaluates the performance of substantially all of its investments ***on a fair value basis***.



IFRS 10 sets the guidance and rules about determining whether the entity is an investment entity or not.



Most investment entities CANNOT present consolidated financial statements and instead, they need to measure an investment in a subsidiary at fair value through profit or loss in line with IFRS 9 Financial Instruments.

## 15.2. Separate Financial Statements

The **objective** of IAS 27 Separate Financial Statements

is

to prescribe the accounting and disclosure requirements for investments in subsidiaries, joint ventures and associates when an entity prepares separate financial statements

This Standard shall be applied in accounting for investments in subsidiaries, joint ventures and associates when an entity elects, or is required by local regulations, to present separate financial statements

### **Defined terms**

**Consolidated financial statements** are the financial statements of a group in which the assets, liabilities, equity, income, expenses and cash flows of the parent and its subsidiaries are presented as those of a single economic entity.

**Separate financial statements** are those presented by an entity in which the entity could elect, subject to the requirements in this Standard, to account for its investments in subsidiaries, joint ventures and associates either at cost, in accordance with IFRS 9 *Financial Instruments*, or using the equity method as described in IAS 28 *Investments in Associates and Joint Ventures*.

When an entity prepares separate financial statements, it shall account for investments in subsidiaries, joint ventures and associates either:

- (a) at cost;
- (b) in accordance with IFRS 9 *Financial Instruments*; or
- (c) using the equity method as described in IAS 28 *Investments in Associates and Joint Ventures*.

The entity shall apply the same accounting for each category of investments. Investments accounted for at cost or using the equity method shall be accounted for in accordance with IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations* when they are classified as held for sale or for distribution (or included in a disposal group that is classified as held for sale or for distribution).

The measurement of investments accounted for in accordance with IFRS 9 *Financial Instruments* is not changed in such circumstances.

Dividends from a subsidiary, a joint venture or an associate are recognised in the separate financial statements of an entity when the entity's right to receive the dividend is established.

The dividend is recognized in profit or loss unless the entity elects to use the equity method, in which case the dividend is recognized as a reduction from the carrying amount of the investment.

An entity shall **present and disclose** information that enables users of the financial statements to evaluate the financial effects of investments in subsidiaries, joint ventures and associates when an entity prepares separate financial statements  
**In the Notes to the financial statements**

An entity shall apply all applicable IFRSs when providing disclosures in its separate financial statements, including the requirements below:

When a parent elects not to prepare consolidated financial statements and instead prepares separate financial statements, it shall disclose in those separate financial statements:

- 1) the fact that the financial statements are separate financial statements;
- 2) that the exemption from consolidation has been used;
- 3) the name and principal place of business (and country of incorporation, if different) of the entity whose consolidated financial statements that comply with IFRSs have been produced for public use;
- 4) the address where those consolidated financial statements are obtainable;
- 5) a list of significant investments in subsidiaries, joint ventures and associates, including:
  - the name of those investees.
  - the principal place of business (and country of incorporation, if different) of those investees.
  - its proportion of the ownership interest (and its proportion of the voting rights, if different) held in those investees;
- 6) a description of the method used to account for the investments.

## THEME 16. ACCOUNTING POLICIES, CHANGES IN ACCOUNTING ESTIMATES AND ERRORS

### 16.1. Accounting Policies

### 16.2. Accounting Estimates

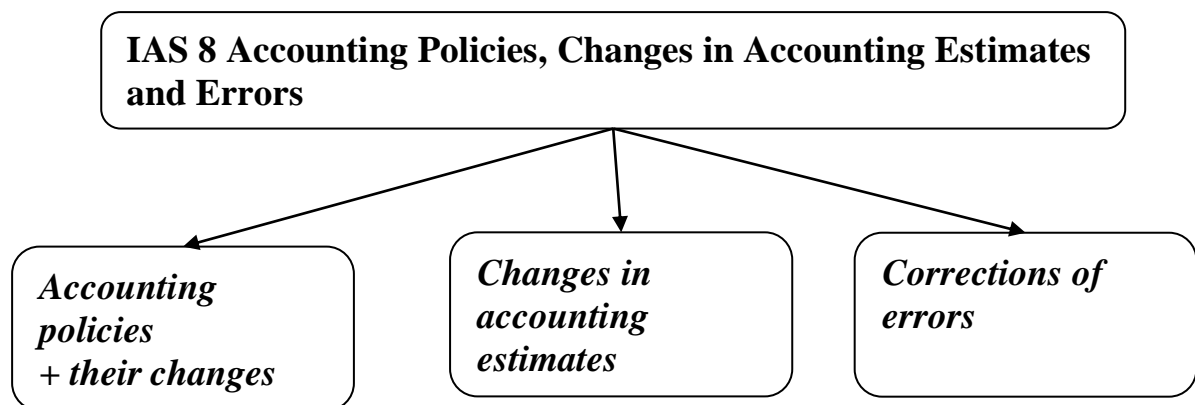
### 16.3. Errors

Key words: accounting policies, changes in accounting policies, accounting estimates, changes in accounting estimates, accounting errors

### 16.1. Accounting Policies

The IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors tells us:

- How to select and apply *accounting policies*;
- How to account for the *changes in accounting policies*;
- How to account for *changes in accounting estimates*; and
- How to correct *errors* made in the previous reporting periods.



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

Following are **Examples** of accounting policies:

- Valuation of inventory using FIFO, Average Cost or other suitable basis as per IAS 2
- Classification, presentation and measurement of financial assets and liabilities under categories specified under IAS 32 and IAS 39 such as held to maturity, available for sale or fair value through profit and loss

- Timing of recognition of assets, liabilities, expenses and income
- Basis of measurement of non-current assets such as historical cost and revaluation basis

- Accruals basis of preparation of financial statements

Management must consistently review its accounting policies to ensure they comply with the latest pronouncements by IASCF and that the adopted policies result in presentation of most relevant and reliable financial information for users.

### **Changes in Accounting Policies**

Accounting Policies must be applied consistently to promote comparability between financial statements of different accounting periods.

However, a change in accounting policy may be necessary to enhance the relevance and reliability of information contained in the financial statements.

Such changes may be required as a result of changes in IFRS or may be applied voluntarily by the management.

An entity shall change an accounting policy only if the change:

(a) is required by an IFRS; or

(b) results in the financial statements providing reliable and more relevant information about the effects of transactions, other events or conditions on the entity's financial position, financial performance or cash flows.

As a general rule, changes in Accounting Policies must be applied retrospectively in the financial statements.

Retrospective application means that entity implements the change in accounting policy as though it had always been applied.

Consequently, entity shall adjust all comparative amounts presented in the financial statements affected by the change in accounting policy for each prior period presented.

### **Exemption from Retrospective Application of Accounting Policies**

**Retrospective application** is applying a new accounting policy to transactions, other events and conditions as if that policy had always been applied.

Retrospective application of a change in accounting policy may be exempted



in the following circumstances:

- A change in accounting policy is required by a new IFRS or a change to an existing IFRS / IAS and the transitional provisions of those standards allow or require prospective application of a new accounting policy. Specific transitional guidance of IFRS must be followed in such circumstances.
- The application of a new accounting policy is in respect of transactions, events and circumstances that are substantially different from those that transpired in the past.
  - The effect of retrospective application of a change in accounting policy is immaterial.
- The retrospective application of a change in accounting policy is impracticable.

Following must be **disclosed** in the financial statements of the accounting period in which a change in accounting policy is implemented:

- Title of IFRS
- Nature of change in accounting policy
- Reasons for change in accounting policy
- Amount of adjustments in current and prior period presented
  - Where retrospective application is impracticable, the conditions that caused the impracticality

## **16.2. Accounting Estimates**

Preparation of financial statements may involve the **use of accounting estimates** in determining the carrying amounts of assets & liabilities and the associated expense or income for the period where such amounts cannot be measured precisely

**Examples of accounting estimates** include the following:

- Valuation of land where it is accounted for at revalued cost
- Impairment of non-current assets
- Useful lives of non-current assets

- Pattern of economic benefits expected to be received from non-current assets for calculating depreciation
- Impairment of receivables (bad debts)
- Pension Benefit obligations
- Provision for slow moving and obsolete inventory

Accounting Estimates involve management's judgment of expected future benefits and obligations relating to assets and liabilities (and associated expense and income) based on information that best reflects the conditions and circumstances that exist at the reporting date.

By its nature, estimates are subjective and may require frequent revisions in future. Revision of estimates must be distinguished correction of errors which occur because of not using information that was available at the time of preparation of financial statements.

### **Changes in Accounting Estimates**

**A change in accounting estimate** is an adjustment of the carrying amount of an asset or a liability, or the amount of the periodic consumption of an asset, that results from the assessment of the present status of, and expected future benefits and obligations associated with, assets and liabilities.

Changes in accounting estimates result from new information or new developments and, accordingly, are not corrections of errors.

Estimates must be revised when new information becomes available which indicates a change in circumstances upon which the estimates were formed.

When you change the accounting estimate, you change either some amount of an asset or a liability, or pattern of its consumption in both current and future reporting periods.

- If these changes result from some new information or new trend, or development, then they are changes in accounting estimates.
- If these changes result from some error, such as incorrect calculation or wrong application of accounting policies – then they are NOT changes in accounting estimates, but errors and they must be accounted for as for errors.

Typical examples of changes in accounting estimates are:

- Bad debt provisions,
- Depreciation rates and useful lives of your assets,
- Provisions for warranty repairs, etc.

Changes in Accounting Estimates must be accounted for **prospectively** in the financial statements, i.e. the effects of the change must be incorporated in the accounting period in which the estimates are revised. Therefore, carrying amounts of assets and liabilities and any associated expense and gains are adjusted in the period of change in estimate.

### **Difference between accounting policy and accounting estimate**

Sometimes, it's very difficult to assess whether we deal with an accounting policy or an accounting estimate.

What are the main differences?

1. While accounting policy is a *principle or rule, or a measurement basis*, accounting estimate is the *amount* determined based on selected basis or *some pattern* of future consumption of the asset.

For example: choice fair value vs. historical cost is a choice in accounting policy (remember, measurement basis), but updating some provision based on fair value change is a change in accounting estimate.

2. While change accounting policy is accounted for retrospectively, you need to account for change in accounting estimate prospectively.

	<b>ACCOUNTING POLICIES</b>	VERSUS	<b>ACCOUNTING ESTIMATES</b>
<b>What is it?</b>	<i>Principles / measurement basis</i>		<i>Amounts / patterns</i>
<b>Examples</b>	Change from historical cost to fair value		Change of the provision amount based on fair value
<b>Accounting</b>	<b>Retrospectively</b>		<b>Prospectively</b>

### 16.3. Errors

**Prior period errors** are omissions from, and misstatements in, the entity's financial statements for one or more prior periods arising from a failure to use, or misuse of, reliable information that:

(a) was available when financial statements for those periods were authorised for issue; and

(b) could reasonably be expected to have been obtained and taken into account in the preparation and presentation of those financial statements.

Such errors include the effects of mathematical mistakes, mistakes in applying accounting policies, oversights or misinterpretations of facts, and fraud.

**Examples of accounting errors included the following:**

- Misapplication of accounting policies: e.g. not recognizing sale upon transfer of goods to a customer
- Fraud: e.g. overstating sales revenue by issuing fake invoices before the reporting date
- Misunderstanding of, or failure to notice, information at the time of preparation of financial statements: e.g. not writing off a receivable who had been announced as insolvent before the authorization of financial statements
- Arithmetical Errors

- Omission of transactions and events from the financial statements

Errors must be distinguished from changes made to prior period estimates that had been based on information that best reflected the conditions and circumstances that existed at the reporting date.

Errors in financial statements reduce the reliability of information presented. Errors must therefore be discovered and corrected on a timely basis to ensure that users can rely on the information contained in the financial statements.

### **Correction of Prior Period Accounting Errors**

Prior Period Errors must be corrected **retrospectively** in the financial statements. Retrospective application means that the correction affects only prior period comparative figures. Current period amounts are unaffected.

### **Errors discovered after reporting date**

Accounting Errors discovered after the reporting date but before the authorization of financial statements are adjusting events after the reporting date as per IAS 10 and must therefore be corrected in the current period prior to the issuance of financial statements.

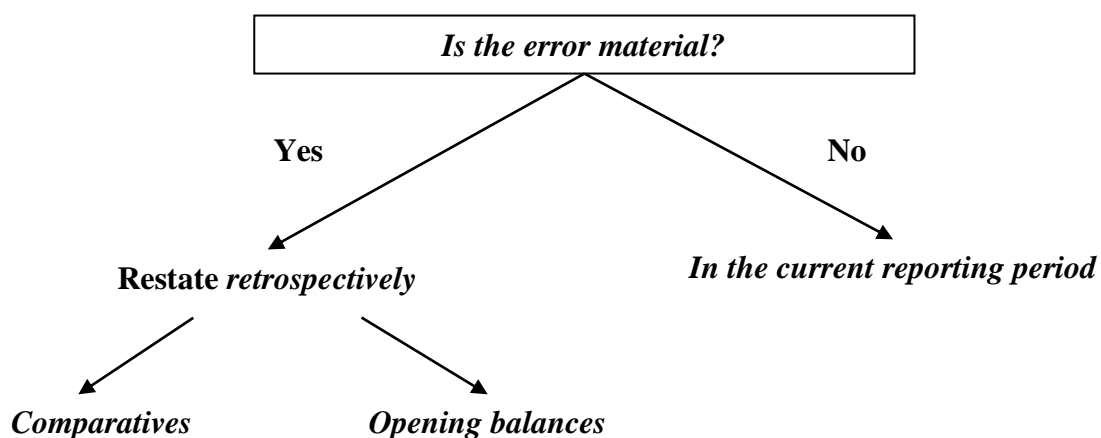
It does not really matter why the error happened – whether it was intentional (fraud) or unintentional, you still need to correct it if it is material.

### ***Is the error material?***

The concept of **materiality** is explained in IAS 1 Presentation of Financial Statements, but to simplify: anything that can affect the decisions of users of financial statements is material. In other words – anything significant.

1. If the error **is NOT material**, then you can correct it **in the current reporting period**. Remember, if the error is NOT material, then your financial statements still might be reliable and relevant.

2. If the error **IS MATERIAL**, then you always correct it **retrospectively**, by going back and restating your figures in the previous periods.



### **Impracticability in Correction of Prior Period Errors**

The retrospective correction of accounting errors may be impracticable. This may be the case for example where entity has not collected sufficient data to enable it to determine the effect of correction of an accounting error and it would be unfeasible or impractical to reconstruct such data.

Where impracticability impairs an entity's ability to correct an accounting error retrospectively from the earliest prior period presented, the correction must be applied prospectively from the beginning of the earliest period feasible (which may be the current period).

### **Disclosure**

- The nature of prior period errors corrected during the period
- The amount of restatement made at the start of the earliest prior period presented
- The circumstances that resulted in impracticability to correct an accounting error retrospectively and how and from when the error has been corrected

**Material** Omissions or misstatements of items are material if they could, individually or collectively, influence the economic decisions that users make on the basis of the financial statements. Materiality depends on the size and nature of the omission or misstatement judged in the surrounding circumstances. The size or nature of the item, or a combination of both, could be the determining factor.

**Retrospective restatement** is correcting the recognition, measurement and

disclosure of amounts of elements of financial statements as if a prior period error had never occurred.

**Consistency of accounting policies**

An entity shall select and apply its accounting policies consistently for similar transactions, other events and conditions, unless an IFRS specifically requires or permits categorisation of items for which different policies may be appropriate. If an IFRS requires or permits such categorisation, an appropriate accounting policy shall be selected and applied consistently to each category.

**Events after Reporting Period** are those that occur between the end of the reporting period and when the financial statements are authorized for issue.

## **THEME 17. INTEGRATED REPORTING**

### **17.1. The Integrated Reporting Framework: History of the Development, Objective, Fundamental Concepts**

#### **17.2. Guiding Principles and Content Elements of Integrated Report**

#### **17.3. Benefits of Integrated Reports**

Key words: business model, integrated report, integrated reporting, integrated thinking, six capitals, stakeholders, value creation

### **17.1. The Integrated Reporting Framework: History of the Development, Objective, Fundamental Concepts**

The Integrated Reporting Framework was originally published by the International Integrated Reporting Council (IIRC) (previously the International Integrated Reporting Committee). The IIRC was formed in August 2010 and had the objective to create a globally accepted framework for a process that results in communications by an organisation about value creation over time.

In June 2021, the IIRC merged with the Sustainability Accounting Standards Board (SASB) to form the Value Reporting Foundation (VRF). The objective of the merger was to provide investors and corporates with a comprehensive corporate reporting framework across the full range of enterprise value drivers and standards to drive global sustainability performance. As such, the Framework was taken on by the VRF as one of its key resources and will now be maintained under its auspices.

After a consultation process, the IIRC published the first version of its 'International Integrated Reporting <IR> Framework' (<IR> Framework) in December 2013. In February 2020, the IIRC launched a revision process and identified three key themes of the revision:

- a) business model considerations,
- b) responsibility for an integrated report,
- c) charting a path forward.

The third theme was not directly related to the revision but focused on future



of corporate reporting, including extended assurance and the role of technology, and was intended to inform the IIRC's longer-term strategy.

In January 2021, the IIRC published revisions of the Framework that focused on a simplification of the required statement of responsibility for the integrated report, improved insight into the quality and integrity of the underlying reporting process, a clearer distinction between outputs and outcomes, and a greater emphasis on the balanced reporting of outcomes and value preservation and erosion scenarios.

**The purpose of the Framework** is to establish guiding principles and content elements that govern the overall content of an integrated report, and to explain the fundamental concepts that underpin them.

The Framework is written primarily in the context of private sector, for-profit companies of any size but it can also be applied, adapted as necessary, by public sector and not-for-profit organisations.

The Framework identifies information to be included in an integrated report for use in assessing an organisation's ability to create value; it does not set benchmarks for such things as the quality of an organisation's strategy or the level of its performance.

In the Framework, reference to the creation of value includes instances when value is preserved and when it is eroded and relates to value creation over time.

There are **three fundamental concepts** underpinning <IR>:

1. Value creation, preservation or erosion for the organisation and for others.
2. The capitals, which are identified in the Framework as financial, manufactured, intellectual, human, social and relationship, and natural capital.
3. Process through which value is created, preserved or eroded.

## **17.2. Guiding Principles and Content Elements of Integrated Report**

**The primary purpose of an integrated report** is to explain to providers of financial capital how an organisation creates, preserves or erodes value over time.

It therefore contains relevant information, both financial and other.

An integrated report benefits all stakeholders interested in an organisation's ability to create value over time, including employees, customers, suppliers, business partners, local communities, legislators, regulators and policy-makers.

The 'building blocks' of an integrated report are:

**Guiding principles** – these underpin the preparation of an integrated report, informing the content of the report and how information is presented. They include:

✓ **Strategic focus and future orientation.** An integrated report should provide insight into the organization's strategy, and how it relates to the organization's ability to create value in the short, medium and long term and to its use of and effects on the capitals.

✓ **Connectivity of information.** An integrated report should show a holistic picture of the combination, interrelatedness and dependencies between the factors that affect the organization's ability to create value over time.

✓ **Stakeholder relationships.** An integrated report should provide insight into the nature and quality of the organization's relationships with its key stakeholders, including how and to what extent the organization understands, takes into account and responds to their legitimate needs and interests.

✓ **Materiality.** An integrated report should disclose information about matters that substantively affect the organization's ability to create value over the short, medium and long term.

✓ **Conciseness.** An integrated report should be concise. An integrated report includes sufficient context to understand the organization's strategy, governance, performance and prospects without being burdened with less relevant information.

✓ **Reliability and completeness.** An integrated report should include all material matters, both positive and negative, in a balanced way and without material error.

✓ **Consistency and comparability.** The information in an integrated

report should be presented:

- on a basis that is consistent over time
- in a way that enables comparison with other organizations to the extent it is material to the organization's own ability to create value over time.

**Content elements** – the key categories of information required to be included in an integrated report under the Framework. They include:

✓ **Organisational overview and external environment.** An integrated report should answer the question: What does the organization do and what are the circumstances under which it operates?

✓ **Governance.** An integrated report should answer the question: How does the organization's governance structure support its ability to create value in the short, medium and long term?

✓ **Business model.** An integrated report should answer the question: What is the organization's business model?

✓ **Risks and opportunities.** An integrated report should answer the question: What are the specific risks and opportunities that affect the organization's ability to create value over the short, medium and long term, and how is the organization dealing with them?

✓ **Strategy and resource allocation.** An integrated report should answer the question: Where does the organization want to go and how does it intend to get there?

✓ **Performance.** An integrated report should answer the question: To what extent has the organization achieved its strategic objectives for the period and what are its outcomes in terms of effects on the capitals?

✓ **Outlook.** An integrated report should answer the question: What challenges and uncertainties is the organization likely to encounter in pursuing its strategy, and what are the potential implications for its business model and future performance?

✓ **Basis of preparation and presentation.** An integrated report should answer the question: How does the organization determine what matters to include

in the integrated report and how are such matters quantified or evaluated?

### **17.3. Benefits of Integrated Reports**

Integrated reporting incorporates conventional financial accounting with firm's sustainability and corporate governance related issues in order to increase the decision usefulness of business reporting and posited that one main reason is that as stakeholders needs change and evolve, a demand for diverse set of information intensifies, which in turn, forces companies to rethink their external reporting practices.

Integrated reporting is viewed by many as the next evolution in corporate reporting, an antidote to the narrow and siloed focus on short-term, financial profit of traditional annual reports which is now accepted to have far-reaching destructive consequences for the environment, society and the economy.

Integrated reporting enhances the way organizations think, plan and report the story of their business. Many organizations use integrated reporting as an opportunity to communicate a clear, concise, integrated story that explains how value is created within these organizations. Integrated reporting is an approach that helps businesses think holistically about their strategy and plans, make informed decisions, manage key opportunities and risks to build investor and stakeholder confidence, and help manage the organization's performance.

The International Integrated Reporting Council (IIRC) contrasts eight differences between current and Integrated Reporting.

**Table Differences between current and integrated reporting**

Feature	Current Reporting	Integrated Reporting
Trust	Narrow disclosures	Greater transparency
Stewardship	Past, financial	Past and future; connected; strategic
Thinking	Isolated	Integrated
Focus	Past, financial	Past and future; connected; strategic
Time frame	Short term	Short, medium and long term
Adaptive	Rule bound	Responsive to individual circumstances
Concise	Long and complex	Concise and material
Technology enabled	Paper based	Technology enabled

Subjects who benefit integrated reporting:

✓ Organizations – integrated reporting helps organizations to understand and communicate their impact and how they create value in a holistic way. This improves relationships with all stakeholders, reduces cost of capital, and facilitates improved long-term performance and sustainable development.

✓ Investors and other key stakeholders e.g., customers, employees, and regulators – integrated reporting provides a comprehensive understanding of businesses and their prospects in the short, medium, and long-term, particularly enabling better informed investment decisions.

✓ Society – enhanced business and investor performance increases economic prosperity, while appropriate consideration and management of all the capitals over the short, medium, and long term promotes sustainable development and financial stability.

**Table Benefits of preparing integrated reports**

<b>Internal</b>	<b>External</b>
Critical thinking about the business and the positive and negative value it creates	Disclosure of strategy gives context to performance and outlook
A good management tool	More future-focused information
An organization-wide focus on environmental, social and governance matters that are core to the organization and its future, including improved data quality	Clear depiction of the business model increases understanding of the value creation process
Improved risk management	Succinct and connected reporting is easier to interpret and analyse
Improved knowledge-management processes and information for decision-making	Improvement in balanced reporting and transparency through: – providing information about all material capitals; – positive and negative performance and outcomes; and – addressing both historic performance and future outlook.
Focused integration of key performance indicators (KPIs), risks, and strategic objectives determined after consideration of all material capitals	Improves quality of communication between the organization and stakeholders that can set the foundation for trust and legitimacy
Breaking down internal silos and promoting sharing of information in the organization	Reduces information asymmetry
Greater alignment of internal and external reporting	

It is possible to identify three classes of benefits.

The first is internal benefits, including better internal resource allocation decisions, greater engagement with shareholders and other stakeholders, and lower reputational risk.

The second is external market benefits, including meeting the needs of mainstream investors who want ESG information, appearing on sustainability indices, and ensuring that data vendors report accurate nonfinancial information on the company.

The third is managing regulatory risk, including being prepared for a likely wave of global regulation, responding to requests from stock exchanges, and having a seat at the table as frameworks and standards are developed.

## SUGGESTED READING

### International Financial Reporting Standards (IFRS)

№	Name	Issued
IFRS 1	First-time Adoption of International Financial Standards	2008*
IFRS 2	Share-based Payment	2004
IFRS 3	Business Combinations	2008*
IFRS 4	Insurance Contracts	2004
IFRS 5	Non-current Assets Held for Sale and Discontinued Operations	2004
IFRS 6	Exploration for and Evaluation of Mineral Assets	2004
IFRS 7	Financial Instruments: Disclosures	2005
IFRS 8	Operating Segments	2006
IFRS 9	Financial Instruments	2013*
IFRS 10	Consolidated Financial Statements	2011
IFRS 11	Joint Arrangements	2011
IFRS 12	Disclosure of Interests in Other Entities	2011
IFRS 13	Fair Value Measurement	2011
IFRS 14	Regulatory Deferral Accounts	2014
IFRS 15	Revenue from Contracts with Customers	2014
IFRS 16	Leases	2016
IFRS 17	Insurance Contracts	2017

### International Accounting Standards (IASs)

№	Name	Issued
IAS 1	Presentation of Financial Statements	2007*
IAS 2	Inventories	2005*
IAS 7	Statement of Cash Flows	1992
IAS 8	Accounting Policies, Changes in Accounting Estimates and Errors	2003
IAS 10	Events After the Reporting Period	2003
IAS 12	Income Taxes	1996*
IAS 16	Property, Plant and Equipment	2003*
IAS 19	Employee Benefits (2011)	2011*
IAS 20	Accounting for Government Grants and Disclosure of Government Assistance	1983
IAS 21	The Effects of Changes in Foreign Exchange Rates	2003*
IAS 23	Borrowing Costs	2007*
IAS 24	Related Party Disclosures	2009*
IAS 26	Accounting and Reporting by Retirement Benefit Plans	1987
IAS 27	Separate Financial Statements (2011)	2011

IAS 28	Investments in Associates and Joint Ventures (2011)	2011
IAS 29	Financial Reporting in Hyperinflationary Economies	1989
IAS 32	Financial Instruments: Presentation	2003*
IAS 33	Earnings Per Share	2003*
IAS 34	Interim Financial Reporting	1998
IAS 36	Impairment of Assets	2004*
IAS 37	Provisions, Contingent Liabilities and Contingent Assets	1998
IAS 38	Intangible Assets	2004*
IAS 40	Investment Property	2003*
IAS 41	Agriculture	2001

### **IFRIC Interpretations**

№	Name	Issued
IFRIC 1	Changes in Existing Decommissioning, Restoration and Similar Liabilities	2004
IFRIC 2	Members' Shares in Co-operative Entities and Similar Instruments	2004
IFRIC 4	Determining Whether an Arrangement Contains a Lease	2004
IFRIC 5	Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds	2004
IFRIC 6	Liabilities Arising from Participating in a Specific Market - Waste Electrical and Electronic Equipment	2005
IFRIC 7	Applying the Restatement Approach under IAS 29 Financial Reporting in Hyperinflationary Economies	2005
IFRIC 9	Reassessment of Embedded Derivatives	2006
IFRIC 10	Interim Financial Reporting and Impairment	2006
IFRIC 12	Service Concession Arrangements	2006
IFRIC 14	IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction	2007
IFRIC 16	Hedges of a Net Investment in a Foreign Operation	2008
IFRIC 17	Distributions of Non-cash Assets to Owners	2008
IFRIC 18	Transfers of Assets from Customers	2009
IFRIC 19	Extinguishing Financial Liabilities with Equity Instruments	2009
IFRIC 20	Stripping Costs in the Production Phase of a Surface Mine	2011
IFRIC 21	Levies	2013
IFRIC 22	Foreign Currency Transactions and Advance Consideration	2016
IFRIC 23	Uncertainty over Income Tax Treatments	2017



## SIC Interpretations

No	Name	Issued
SIC-7	Introduction of the Euro	1998
SIC-10	Government Assistance – No Specific Relation to Operating Activities	1998
SIC-15	Operating Leases – Incentives	1999
SIC-25	Income Taxes – Changes in the Tax Status of an Enterprise or its Shareholders	2000
SIC-27	Evaluating the Substance of Transactions in the Legal Form of a Lease	2000
SIC-29	Disclosure – Service Concession Arrangements	2001
SIC-32	Intangible Assets – Web Site Costs	2001

1. Conceptual Framework for Financial Reporting. March 2018. Retrieved from: <https://www.ifrs.org/content/dam/ifrs/publications/pdf-standards/english/2021/issued/part-a/conceptual-framework-for-financial-reporting.pdf>

2. Integrated Reporting Framework. January 2021. Retrieved from: <https://www.integratedreporting.org/wp-content/uploads/2021/01/InternationalIntegratedReportingFramework.pdf>

3. The IFRS<sup>®</sup> Foundation. Retrieved from: <http://www.ifrs.org>

4. *The #1* website for global accounting news. Retrieved from: <https://www.iasplus.com/en>

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