(b) each of the principal types of income, interest expense and commissions paid;

(c) the amount of the expense recognised in the period for losses on loans and advances and the amount of the provision at the balance sheet date; and

(d) irrevocable commitments and contingencies and commitments arising from off balance sheet items.

EFFECTIVE DATE

59. ***This International Accounting Standard becomes operative for the financial statements of banks covering periods beginning on or after 1 January 1991.***

INTERNATIONAL ACCOUNTING STANDARD IAS 31 (REVISED 2000)

Financial reporting of interests in joint ventures

IAS 31 was approved by the Board in November 1990.

In November 1994, the text of IAS 31 was reformatted to be presented in the revised format adopted for International Accounting Standards in 1991. No substantive changes were made to the original text. Certain terminology was changed to be in line with IASC practice at the time.

In July 1998, to be consistent with IAS 36, impairment of assets, paragraphs 39 and 40 were revised and a new paragraph 41 was added.

In December 1998, paragraphs 35 and 42 of IAS 31 were amended to replace references to IAS 25, accounting for investments, by references to IAS 39, financial instruments: recognition and measurement.

In March 1999, IAS 10 (revised 1999), events after the balance sheet date, amended paragraph 45 to be consistent with the terminology in IAS 37, provisions, contingent liabilities and contingent assets.

In October 2000, paragraph 35 was revised to be consistent with similar paragraphs in other related International Accounting Standards. The change to paragraph 35 becomes effective when an enterprise applies IAS 39 for the first time.

One SIC interpretation relates to IAS 31:

— SIC-13: jointly controlled entities — non-monetary contributions by venturers.

CONTENTS

The standards, which have been set in bold italic type, should be read in the context of the background material and implementation guidance in this Standard, and in the context of the 'Preface to International Accounting Standards'. International Accounting Standards are not intended to apply to immaterial items (see paragraph 12 of the Preface).

SCOPE

1. ***This Standard should be applied in accounting for interests in joint ventures and the reporting of joint venture assets, liabilities, income and expenses in the financial statements of venturers and investors, regardless of the structures or forms under which the joint venture activities take place.***

DEFINITIONS

2. ***The following terms are used in this Standard with the meanings specified:***

A joint venture is a contractual arrangement whereby two or more parties undertake an economic activity which is subject to joint control.

Control is the power to govern the financial and operating policies of an economic activity so as to obtain benefits from it.

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

Significant influence is the power to participate in the financial and operating policy decisions of an economic activity but is not control or joint control over those policies.

A venturer is a party to a joint venture and has joint control over that joint venture.

An investor in a joint venture is a party to a joint venture and does not have joint control over that joint venture.

Proportionate consolidation is a method of accounting and reporting whereby a venturer's share of each of the assets, liabilities, income and expenses of a jointly controlled entity is combined on a line-by-line basis with similar items in the venturer's financial statements or reported as separate line items in the venturer's financial statements.

The equity method is a method of accounting and reporting whereby an interest in a jointly controlled entity is initially recorded at cost and adjusted thereafter for the post acquisition change in the venturer's share of net assets of the jointly controlled entity. The income statement reflects the venturer's share of the results of operations of the jointly controlled entity.

Forms of joint venture

3. Joint ventures take many different forms and structures. This Standard identifies three broad types — jointly controlled operations, jointly controlled assets and jointly controlled entities — which are commonly described as, and meet the definition of, joint ventures. The following characteristics are common to all joint ventures:

(a) two or more venturers are bound by a contractual arrangement; and

(b) the contractual arrangement establishes joint control.

Contractual arrangement

4. The existence of a contractual arrangement distinguishes interests which involve joint control from investments in associates in which the investor has significant influence (see IAS 28, accounting for investments in associates). Activities which have no contractual arrangement to establish joint control are not joint ventures for the purposes of this Standard.

5. The contractual arrangement may be evidenced in a number of ways, for example by a contract between the venturers or minutes of discussions between the venturers. In some cases, the arrangement is incorporated in the articles or other by-laws of the joint venture. Whatever its form, the contractual arrangement is usually in writing and deals with such matters as:

(a) the activity, duration and reporting obligations of the joint venture;

(b) the appointment of the board of directors or equivalent governing body of the joint venture and the voting rights of the venturers;

(c) capital contributions by the venturers; and

(d) the sharing by the venturers of the output, income, expenses or results of the joint venture.

6. The contractual arrangement establishes joint control over the joint venture. Such a requirement ensures that no single venturer is in a position to control unilaterally the activity. The arrangement identifies those decisions in areas essential to the goals of the joint venture which require the consent of all the venturers and those decisions which may require the consent of a specified majority of the venturers.

7. The contractual arrangement may identify one venturer as the operator or manager of the joint venture. The operator does not control the joint venture but acts within the financial and operating policies which have been agreed by the venturers in accordance with the contractual arrangement and delegated to the operator. If the operator has the power to govern the financial and operating policies of the economic activity, it controls the venture and the venture is a subsidiary of the operator and not a joint venture.

JOINTLY CONTROLLED OPERATIONS

8. The operation of some joint ventures involves the use of the assets and other resources of the venturers rather than the establishment of a corporation, partnership or other entity, or a financial structure that is separate from the venturers themselves. Each venturer uses its own property, plant and equipment and carries its own inventories. It also incurs its own expenses and liabilities and raises its own finance, which represent its own obligations. The joint venture activities may be carried out by the venturer's employees alongside the venturer's similar activities. The joint venture agreement usually provides a means by which the revenue from the sale of the joint product and any expenses incurred in common are shared among the venturers.

9. An example of a jointly controlled operation is when two or more venturers combine their operations, resources and expertise in order to manufacture, market and distribute jointly a particular product, such as an aircraft. Different parts of the manufacturing process are carried out by each of the venturers. Each venturer bears its own costs and takes a share of the revenue from the sale of the aircraft, such share being determined in accordance with the contractual arrangement.

10. ***In respect of its interests in jointly controlled operations, a venturer should recognise in its separate financial statements and consequently in its consolidated financial statements:***

(a) ***the assets that it controls and the liabilities that it incurs; and***

(b) ***the expenses that it incurs and its share of the income that it earns from the sale of goods or services by the joint venture.***

11. Because the assets, liabilities, income and expenses are already recognised in the separate financial statements of the venturer, and consequently in its consolidated financial statements, no adjustments or other consolidation procedures are required in respect of these items when the venturer presents consolidated financial statements.

12. Separate accounting records may not be required for the joint venture itself and financial statements may not be prepared for the joint venture. However, the venturers may prepare management accounts so that they may assess the performance of the joint venture.

JOINTLY CONTROLLED ASSETS

13. Some joint ventures involve the joint control, and often the joint ownership, by the venturers of one or more assets contributed to, or acquired for the purpose of, the joint venture and dedicated to the purposes of the joint venture. The assets are used to obtain benefits for the venturers. Each venturer may take a share of the output from the assets and each bears an agreed share of the expenses incurred.

14. These joint ventures do not involve the establishment of a corporation, partnership or other entity, or a financial structure that is separate from the venturers themselves. Each venturer has control over its share of future economic benefits through its share in the jointly controlled asset.

15. Many activities in the oil, gas and mineral extraction industries involve jointly controlled assets; for example, a number of oil production companies may jointly control and operate an oil pipeline. Each venturer uses the pipeline to transport its own product in return for which it bears an agreed proportion of the expenses of operating the pipeline. Another example of a jointly controlled asset is when two enterprises jointly control a property, each taking a share of the rents received and bearing a share of the expenses.

16. ***In respect of its interest in jointly controlled assets, a venturer should recognise in its separate financial statements and consequently in its consolidated financial statements:***

(a) ***its share of the jointly controlled assets, classified according to the nature of the assets;***

(b) ***any liabilities which it has incurred;***

(c) ***its share of any liabilities incurred jointly with the other venturers in relation to the joint venture;***

(d) ***any income from the sale or use of its share of the output of the joint venture, together with its share of any expenses incurred by the joint venture; and***

(e) ***any expenses which it has incurred in respect of its interest in the joint venture.***

17. In respect of its interest in jointly controlled assets, each venturer includes in its accounting records and recognises in its separate financial statements and consequently in its consolidated financial statements:

(a) its share of the jointly controlled assets, classified according to the nature of the assets rather than as an investment. For example, a share of a jointly controlled oil pipeline is classified as property, plant and equipment;

(b) any liabilities which it has incurred, for example those incurred in financing its share of the assets;

(c) its share of any liabilities incurred jointly with other venturers in relation to the joint venture;

(d) any income from the sale or use of its share of the output of the joint venture, together with its share of any expenses incurred by the joint venture; and

(e) any expenses which it has incurred in respect of its interest in the joint venture, for example those related to financing the venturer's interest in the assets and selling its share of the output.

Because the assets, liabilities, income and expenses are already recognised in the separate financial statements of the venturer, and consequently in its consolidated financial statements, no adjustments or other consolidation procedures are required in respect of these items when the venturer presents consolidated financial statements.

18. The treatment of jointly controlled assets reflects the substance and economic reality and, usually, the legal form of the joint venture. Separate accounting records for the joint venture itself may be limited to those expenses incurred in common by the venturers and ultimately borne by the venturers according to their agreed shares. Financial statements may not be prepared for the joint venture, although the venturers may prepare management accounts so that they may assess the performance of the joint venture.

JOINTLY CONTROLLED ENTITIES

19. A jointly controlled entity is a joint venture which involves the establishment of a corporation, partnership or other entity in which each venturer has an interest. The entity operates in the same way as other enterprises, except that a contractual arrangement between the venturers establishes joint control over the economic activity of the entity.

20. A jointly controlled entity controls the assets of the joint venture, incurs liabilities and expenses and earns income. It may enter into contracts in its own name and raise finance for the purposes of the joint venture activity. Each venturer is entitled to a share of the results of the jointly controlled entity, although some jointly controlled entities also involve a sharing of the output of the joint venture.

21. A common example of a jointly controlled entity is when two enterprises combine their activities in a particular line of business by transferring the relevant assets and liabilities into a jointly controlled entity. Another example arises when an enterprise commences a business in a foreign country in conjunction with the government or other agency in that country, by establishing a separate entity which is jointly controlled by the enterprise and the government or agency.

22. Many jointly controlled entities are similar in substance to those joint ventures referred to as jointly controlled operations or jointly controlled assets. For example, the venturers may transfer a jointly controlled asset, such as an oil pipeline, into a jointly controlled entity, for tax or other reasons. Similarly, the venturers may contribute into a jointly controlled entity assets which will be operated jointly. Some jointly controlled operations also involve the establishment of a jointly controlled entity to deal with particular aspects of the activity, for example, the design, marketing, distribution or after-sales service of the product.

23. A jointly controlled entity maintains its own accounting records and prepares and presents financial statements in the same way as other enterprises in conformity with the appropriate national requirements and International Accounting Standards.

24. Each venturer usually contributes cash or other resources to the jointly controlled entity. These contributions are included in the accounting records of the venturer and recognised in its separate financial statements as an investment in the jointly controlled entity.

Consolidated financial statements of a venturer

Benchmark treatment — proportionate consolidation

25. ***In its consolidated financial statements, a venturer should report its interest in a jointly controlled entity using one of the two reporting formats for proportionate consolidation.***

26. When reporting an interest in a jointly controlled entity in consolidated financial statements, it is essential that a venturer reflects the substance and economic reality of the arrangement, rather than the joint venture's particular structure or form. In a jointly controlled entity, a venturer has control over its share of future economic benefits through its share of the assets and liabilities of the venture. This substance and economic reality is reflected in the consolidated financial statements of the venturer when the venturer reports its interests in the assets, liabilities, income and expenses of the jointly controlled entity by using one of the two reporting formats for proportionate consolidation described in paragraph 28.

27. The application of proportionate consolidation means that the consolidated balance sheet of the venturer includes its share of the assets that it controls jointly and its share of the liabilities for which it is jointly responsible. The consolidated income statement of the venturer includes its share of the income and expenses of the jointly controlled entity. Many of the procedures appropriate for the application of proportionate consolidation are similar to the procedures for the consolidation of investments in subsidiaries, which are set out in IAS 27, consolidated financial statements and accounting for investments in subsidiaries.

28. Different reporting formats may be used to give effect to proportionate consolidation. The venturer may combine its share of each of the assets, liabilities, income and expenses of the jointly controlled entity with the similar items in its consolidated financial statements on a line-by-line basis. For example, it may combine its share of the jointly controlled entity's inventory with the inventory of the consolidated group and its share of the jointly controlled entity's property, plant and equipment with the same items of the consolidated group. Alternatively, the venturer may include separate line items for its share of the assets, liabilities, income and expenses of the jointly controlled entity in its consolidated financial statements. For example, it may show its share of the current assets of the jointly controlled entity separately as part of the current assets of the consolidated group; it may show its share of the property, plant and equipment of the jointly controlled entity separately as part of the property, plant and equipment of the consolidated group. Both these reporting formats result in the reporting of identical amounts of net income and of each major classification of assets, liabilities, income and expenses; both formats are acceptable for the purposes of this Standard.

29. Whatever format is used to give effect to proportionate consolidation, it is inappropriate to offset any assets or liabilities by the deduction of other liabilities or assets or any income or expenses by the deduction of other expenses or income, unless a legal right of set-off exists and the offsetting represents the expectation as to the realisation of the asset or the settlement of the liability.

30. ***A venturer should discontinue the use of proportionate consolidation from the date on which it ceases to have joint control over a jointly controlled entity.***

31. A venturer discontinues the use of proportionate consolidation from the date on which it ceases to share in the control of a jointly controlled entity. This may happen, for example, when the venturer disposes of its interest or when external restrictions are placed on the jointly controlled entity such that it can no longer achieve its goals.

Allowed alternative treatment — equity method

32. ***In its consolidated financial statements, a venturer should report its interest in a jointly controlled entity using the equity method.***

33. Some venturers report their interests in jointly controlled entities using the equity method, as described in IAS 28, accounting for investments in associates. The use of the equity method is supported by those who argue that it is inappropriate to combine controlled items with jointly controlled items and by those who believe that venturers have significant influence, rather than joint control, in a jointly controlled entity. This Standard does not recommend the use of the equity method because proportionate consolidation better reflects the substance and economic reality of a venturer's interest in a jointly controlled entity, that is control over the venturer's share of the future economic benefits. Nevertheless, this Standard permits the use of the equity method, as an allowed alternative treatment, when reporting interests in jointly controlled entities.

34. ***A venturer should discontinue the use of the equity method from the date on which it ceases to have joint control over, or have significant influence in, a jointly controlled entity.***

Exceptions to benchmark and allowed alternative treatments

35. ***A venturer should account for the following interests in accordance with IAS 39, financial instruments: recognition and measurement:***

    (a) ***an interest in a jointly controlled entity which is acquired and held exclusively with a view to its subsequent disposal in the near future; and***

    (b) ***an interest in a jointly controlled entity which operates under severe long-term restrictions that significantly impair its ability to transfer funds to the venturer.***

36. The use of either proportionate consolidation or the equity method is inappropriate when the interest in a jointly controlled entity is acquired and held exclusively with a view to its subsequent disposal in the near future. It is also inappropriate when the jointly controlled entity operates under severe long-term restrictions which significantly impair its ability to transfer funds to the venturer.

37. ***From the date on which a jointly controlled entity becomes a subsidiary of a venturer, the venturer accounts for its interest in accordance with IAS 27, consolidated financial statements and accounting for investments in subsidiaries.***

Separate financial statements of a venturer

38. In many countries separate financial statements are presented by a venturer in order to meet legal or other requirements. Such separate financial statements are prepared in order to meet a variety of needs with the result that different reporting practices are in use in different countries. Accordingly, this Standard does not indicate a preference for any particular treatment.

TRANSACTIONS BETWEEN A VENTURER AND A JOINT VENTURE

39. ***When a venturer contributes or sells assets to a joint venture, recognition of any portion of a gain or loss from the transaction should reflect the substance of the transaction. While the assets are retained by the joint venture, and provided the venturer has transferred the significant risks and rewards of ownership, the venturer should recognise only that portion of the gain or loss which is attributable to the interests of the other venturers*** (1)***. The venturer should recognise the full amount of any loss when the contribution or sale provides evidence of a reduction in the net realisable value of current assets or an impairment loss.***

40. ***When a venturer purchases assets from a joint venture, the venturer should not recognise its share of the profits of the joint venture from the transaction until it resells the assets to an independent party. A venturer should recognise its share of the losses resulting from these transactions in the same way as profits except that losses should be recognised immediately when they represent a reduction in the net realisable value of current assets or an impairment loss.***

41. To assess whether a transaction between a venturer and a joint venture provides evidence of impairment of an asset, the venturer determines the recoverable amount of the asset under IAS 36, impairment of assets. In determining value in use, future cash flows from the asset are estimated based on continuing use of the asset and its ultimate disposal by the joint venture.

REPORTING INTERESTS IN JOINT VENTURES IN THE FINANCIAL STATEMENTS OF AN INVESTOR

42. ***An investor in a joint venture, which does not have joint control, should report its interest in a joint venture in its consolidated financial statements in accordance with IAS 39, financial instruments: recognition and measurement, or, if it has significant influence in the joint venture, in accordance with IAS 28, accounting for investments in associates. In the separate financial statements of an investor that issues consolidated financial statements, it may also report the investment at cost.***

OPERATORS OF JOINT VENTURES

43. ***Operators or managers of a joint venture should account for any fees in accordance with IAS 18, revenue.***

44. One or more venturers may act as the operator or manager of a joint venture. Operators are usually paid a management fee for such duties. The fees are accounted for by the joint venture as an expense.

DISCLOSURE

45. ***A venturer should disclose the aggregate amount of the following contingent liabilities, unless the probability of loss is remote, separately from the amount of other contingent liabilities:***

(a) ***any contingent liabilities that the venturer has incurred in relation to its interests in joint ventures and its share in each of the contingent liabilities which have been incurred jointly with other venturers;***

(b) ***its share of the contingent liabilities of the joint ventures themselves for which it is contingently liable; and***

(c) ***those contingent liabilities that arise because the venturer is contingently liable for the liabilities of the other venturers of a joint venture.***

(1) See also SIC-13: jointly controlled entities — non-monetary contributions by venturers.

46. ***A venturer should disclose the aggregate amount of the following commitments in respect of its interests in joint ventures separately from other commitments:***

    (a) ***any capital commitments of the venturer in relation to its interests in joint ventures and its share in the capital commitments that have been incurred jointly with other venturers; and***

    (b) ***its share of the capital commitments of the joint ventures themselves.***

47. ***A venturer should disclose a listing and description of interests in significant joint ventures and the proportion of ownership interest held in jointly controlled entities. A venturer which reports its interests in jointly controlled entities using the line-by-line reporting format for proportionate consolidation or the equity method should disclose the aggregate amounts of each of current assets, long-term assets, current liabilities, long-term liabilities, income and expenses related to its interests in joint ventures.***

48. ***A venturer which does not issue consolidated financial statements, because it does not have subsidiaries, should disclose the information required in paragraphs 45, 46 and 47.***

49. It is appropriate that a venturer which does not prepare consolidated financial statements because it does not have subsidiaries provides the same information about its interests in joint ventures as those venturers that issue consolidated financial statements.

EFFECTIVE DATE

50. ***Except for paragraphs 39, 40 and 41, this International Accounting Standard becomes operative for financial statements covering periods beginning on or after 1 January 1992.***

51. ***Paragraphs 39, 40 and 41 become operative when IAS 36 becomes operative, i.e. for annual financial statements covering periods beginning on or after 1 July 1999, unless IAS 36 is applied for earlier periods.***

52. Paragraphs 39 and 40 of this Standard were approved in July 1998 to supersede paragraphs 39 and 40 of IAS 31, financial reporting of interests in joint ventures, reformatted in 1994. Paragraph 41 of this Standard was added in July 1998 between paragraphs 40 and 41 of IAS 31 reformatted in 1994.

INTERNATIONAL ACCOUNTING STANDARD IAS 33

Earnings per share

This International Accounting Standard was approved by the IASC Board in January 1997 and became effective for financial statements covering periods beginning on or after 1 January 1998.

In 1999, paragraph 45 was amended to replace references to IAS 10, contingencies and events occurring after the balance sheet date, by references to IAS 10 (revised 1999), events after the balance sheet date.

The following SIC interpretation relates to IAS 33:

— SIC-24: earnings per share — financial instruments and other contracts that may be settled in shares.

CONTENTS

The standards, which have been set in bold italic type, should be read in the context of the background material and implementation guidance in this Standard, and in the context of the 'Preface to International Accounting Standards'. International Accounting Standards are not intended to apply to immaterial items (see paragraph 12 of the Preface).

OBJECTIVE

The objective of this Standard is to prescribe principles for the determination and presentation of earnings per share which will improve performance comparisons among different enterprises in the same period and among different accounting periods for the same enterprise. The focus of this Standard is on the denominator of the earnings per share calculation. Even though earnings per share data has limitations because of different accounting policies used for determining 'earnings', a consistently determined denominator enhances financial reporting.

SCOPE

Enterprises whose shares are publicly traded

1. ***This Standard should be applied by enterprises whose ordinary shares or potential ordinary shares are publicly traded and by enterprises that are in the process of issuing ordinary shares or potential ordinary shares in public securities markets.***

2. ***When both parent and consolidated financial statements are presented, the information called for by this Standard need be presented only on the basis of consolidated information.***

3. Users of the financial statements of a parent are usually concerned with, and need to be informed about, the results of operations of the group as a whole.

Enterprises whose shares are not publicly traded

4. ***An enterprise which has neither ordinary shares nor potential ordinary shares which are publicly traded, but which discloses earnings per share, should calculate and disclose earnings per share in accordance with this Standard.***

5. An enterprise which has neither ordinary shares nor potential ordinary shares which are publicly traded is not required to disclose earnings per share. However, comparability in financial reporting among enterprises is maintained if any such enterprise that chooses to disclose earnings per share calculates earnings per share in accordance with the principles in this Standard.

DEFINITIONS

6. ***The following terms are used in this Standard with the meanings specified:***

An ordinary share is an equity instrument that is subordinate to all other classes of equity instruments.

A potential ordinary share is a financial instrument or other contract that may entitle its holder to ordinary shares.

Warrants or options are financial instruments that give the holder the right to purchase ordinary shares.

7. Ordinary shares participate in the net profit for the period only after other types of shares such as preference shares. An enterprise may have more than one class of ordinary shares. Ordinary shares of the same class will have the same rights to receive dividends.

8. Examples of potential ordinary shares are:

(a) debt or equity instruments, including preference shares, that are convertible into ordinary shares;

(b) share warrants and options;

(c) employee plans that allow employees to receive ordinary shares as part of their remuneration and other share purchase plans; and

(d) shares which would be issued upon the satisfaction of certain conditions resulting from contractual arrangements, such as the purchase of a business or other assets.

9. ***The following terms are used with the meanings specified in IAS 32, financial instruments: disclosure and presentation:***

A financial instrument is any contract that gives rise to both a financial asset of one enterprise and a financial liability or equity instrument of another enterprise.

An equity instrument is any contract that evidences a residual interest in the assets of an enterprise after deducting all of its liabilities.

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

MEASUREMENT

Basic earnings per share

10. ***Basic earnings per share should be calculated by dividing the net profit or loss for the period attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the period.***

Earnings — basic

11. ***For the purpose of calculating basic earnings per share, the net profit or loss for the period attributable to ordinary shareholders should be the net profit or loss for the period after deducting preference dividends.***

12. All items of income and expense which are recognised in a period, including tax expense, extraordinary items and minority interests, are included in the determination of the net profit or loss for the period (see IAS 8, net profit or loss for the period, fundamental errors and changes in accounting policies). The amount of net profit attributable to preference shareholders, including preference dividends for the period, is deducted from the net profit for the period (or added to the net loss for the period) in order to calculate the net profit or loss for the period attributable to ordinary shareholders.

13. The amount of preference dividends that is deducted from the net profit for the period is:

(a) the amount of any preference dividends on non-cumulative preference shares declared in respect of the period; and

(b) the full amount of the required preference dividends for cumulative preference shares for the period, whether or not the dividends have been declared. The amount of preference dividends for the period does not include the amount of any preference dividends for cumulative preference shares paid or declared during the current period in respect of previous periods.

Per share — basic

14. ***For the purpose of calculating basic earnings per share, the number of ordinary shares should be the weighted average number of ordinary shares outstanding during the period.***

15. The weighted average number of ordinary shares outstanding during the period reflects the fact that the amount of shareholders' capital may have varied during the period as a result of a larger or lesser number of shares being outstanding at any time. It is the number of ordinary shares outstanding at the beginning of the period, adjusted by the number of ordinary shares bought back or issued during the period multiplied by a time-weighting factor. The time-weighting factor is the number of days that the specific shares are outstanding as a proportion of the total number of days in the period; a reasonable approximation of the weighted average is adequate in many circumstances.

Example: weighted average number of shares

		Shares issued	Treasury shares	Shares outstanding
1 January 20X1	Balance at beginning of year	2 000	300	1 700
31 May 20X1	Issue of new shares for cash	800	—	2 500
1 December 20X1	Purchase of treasury shares for cash	—	250	2 250
31 December 20X1	Balance at end of year	2 800	550	2 250

Computation of weighted average:
(1 700 × 5/12) + (2 500 × 6/12) + (2 250 × 1/12) = 2 146 shares or:
(1 700 × 12/12) + (800 × 7/12) − (250 × 1/12) = 2 146 shares

16. In most cases, shares are included in the weighted average number of shares from the date consideration is receivable (which is generally the date of their issue), for example:

(a) ordinary shares issued in exchange for cash are included when cash is receivable;

(b) ordinary shares issued on the voluntary reinvestment of dividends on ordinary or preference shares are included at the dividend payment date;

(c) ordinary shares issued as a result of the conversion of a debt instrument to ordinary shares are included as of the date interest ceases accruing;

(d) ordinary shares issued in place of interest or principal on other financial instruments are included as of the date interest ceases accruing;

(e) ordinary shares issued in exchange for the settlement of a liability of the enterprise are included as of the settlement date;

(f) ordinary shares issued as consideration for the acquisition of an asset other than cash are included as of the date on which the acquisition is recognised; and

(g) ordinary shares issued for the rendering of services to the enterprise are included as the services are rendered.

In these and other cases the timing of the inclusion of ordinary shares is determined by the specific terms and conditions attaching to their issue. Due consideration should be given to the substance of any contract associated with the issue.

17. Ordinary shares issued as part of the purchase consideration of a business combination which is an acquisition are included in the weighted average number of shares as of the date of the acquisition because the acquirer incorporates the results of the operations of the acquiree into its income statement as from the date of acquisition. Ordinary shares issued as part of a business combination which is a uniting of interests are included in the calculation of the weighted average number of shares for all periods presented because the financial statements of the combined enterprise are prepared as if the combined entity had always existed. Therefore, the number of ordinary shares used for the calculation of basic earnings per share in a business combination which is a uniting of interests is the aggregate of the weighted average number of shares of the combined enterprises, adjusted to equivalent shares of the enterprise whose shares are outstanding after the combination.

18. Where ordinary shares are issued in partly paid form, these partly paid shares are treated as a fraction of an ordinary share to the extent that they were entitled to participate in dividends relative to a fully paid ordinary share during the financial period.

19. Ordinary shares which are issuable upon the satisfaction of certain conditions (contingently issuable shares) are considered outstanding, and included in the computation of basic earnings per share from the date when all necessary conditions have been satisfied. Outstanding ordinary shares that are contingently returnable (that is subject to recall) are treated as contingently issuable shares.

20. ***The weighted average number of ordinary shares outstanding during the period and for all periods presented should be adjusted for events, other than the conversion of potential ordinary shares, that have changed the number of ordinary shares outstanding, without a corresponding change in resources.***

21. Ordinary shares may be issued, or the number of shares outstanding may be reduced, without a corresponding change in resources. Examples include:

(a) a capitalisation or bonus issue (known in some countries as a stock dividend);

(b) a bonus element in any other issue, for example a bonus element in a rights issue to existing shareholders;

(c) a share split; and

(d) a reverse share split (consolidation of shares).

22. In a capitalisation or bonus issue or a share split, ordinary shares are issued to existing shareholders for no additional consideration. Therefore, the number of ordinary shares outstanding is increased without an increase in resources. The number of ordinary shares outstanding before the event is adjusted for the proportionate change in the number of ordinary shares outstanding as if the event had occurred at the beginning of the earliest period reported. For example, on a two-for-one bonus issue, the number of shares outstanding prior to the issue is multiplied by a factor of three to obtain the new total number of shares, or by a factor of two to obtain the number of additional shares.

23. With reference to 21(b), the issue of ordinary shares at the time of exercise or conversion of potential ordinary shares will not usually give rise to a bonus element, since the potential ordinary shares will usually have been issued for full value, resulting in a proportionate change in the resources available to the enterprise. In a rights issue, the exercise price is often less than the fair value of the shares. Therefore such a rights issue includes a bonus element. The number of ordinary shares to be used in calculating basic earnings per share for all periods prior to the rights issue is the number of ordinary shares outstanding prior to the issue, multiplied by the following factor:

$$\frac{\text{Fair value per share immediately prior to the exercise of rights}}{\text{Theoretical ex-rights fair value per share}}$$

The theoretical ex-rights fair value per share is calculated by adding the aggregate fair value of the shares immediately prior to the exercise of the rights to the proceeds from the exercise of the rights, and dividing by the number of shares outstanding after the exercise of the rights. Where the rights themselves are to be publicly traded separately from the shares prior to the exercise date, fair value for the purposes of this calculation is established at the close of the last day on which the shares are traded together with the rights.

Example — bonus issue

Net profit 20X0	180
Net profit 20X1	600
Ordinary shares outstanding until 30 September 20X1	200
Bonus issue 1 October 20X1	Two ordinary shares for each ordinary share outstanding at 30 September 20X1 200 × 2 = 400
Earnings per share 20X1	$\frac{600}{(200 + 400)} = 1{,}00$
Adjusted earnings per share 20X0	$\frac{180}{(200 + 400)} = 0{,}30$

Since the bonus issue is an issue without consideration, the issue is treated as if it had occurred prior to the beginning of 20X0, the earliest period reported.

Example — rights issue

Net profit	20X0:1 100; 20X1:1 500; 20X2:1 800
Shares outstanding prior to rights issue	500 shares
Rights issue	One new share for each five outstanding (100 new shares total) Exercise price: 5,00 Last date to exercise rights: 1 March 20X1
Fair value of one ordinary share immediately prior to exercise on 1 March 20X1	11,00

Computation of theoretical ex-rights value per share

$$\frac{\text{Fair value of all outstanding shares + total amount received from exercise of rights}}{\text{Number of shares outstanding prior to exercise + number of shares issued in the exercise}}$$

$$\frac{(11{,}00 \times 500 \text{ shares}) + (5{,}00 \times 100 \text{ shares})}{(500 \text{ shares} + 100 \text{ shares})}$$

Theoretical ex-rights value per share = 10,00

Computation of adjustment factor

$$\frac{\text{Fair value per share prior to exercise of rights}}{\text{Theoretical ex-rights value per share}} \qquad \frac{11{,}00}{10{,}00} = 1{,}1$$

Computation of earnings per share

	20X0	20X1	20X2
20X0 EPS as originally reported: 1 100/500 shares	2,20		
20X0 EPS restated for rights issue: 1 100/(500 shares x 1,1)	2,00		
20X1 EPS including effects of rights issue $\frac{1\,500}{(500 \times 1{,}1 \times 2/12) + (600 \times 10/12)}$		2,54	
20X2 EPS 1 800/600 shares			3,00

Diluted earnings per share

24. ***For the purpose of calculating diluted earnings per share, the net profit attributable to ordinary shareholders and the weighted average number of shares outstanding should be adjusted for the effects of all dilutive potential ordinary shares*** [1]**.**

25. The calculation of diluted earnings per share is consistent with the calculation of basic earnings per share while giving effect to all dilutive potential ordinary shares that were outstanding during the period, that is:

(a) the net profit for the period attributable to ordinary shares is increased by the after-tax amount of dividends and interest recognised in the period in respect of the dilutive potential ordinary shares and adjusted for any other changes in income or expense that would result from the conversion of the dilutive potential ordinary shares.

(1) See also, SIC-24: earnings per share — financial instruments and other contracts that may be settled in shares.

(b) the weighted average number of ordinary shares outstanding is increased by the weighted average number of additional ordinary shares which would have been outstanding assuming the conversion of all dilutive potential ordinary shares.

Earnings — diluted

26. ***For the purpose of calculating diluted earnings per share, the amount of net profit or loss for the period attributable to ordinary shareholders, as calculated in accordance with paragraph 11, should be adjusted by the after-tax effect:***

(a) ***any dividends on dilutive potential ordinary shares which have been deducted in arriving at the net profit attributable to ordinary shareholders as calculated in accordance with paragraph 11;***

(b) ***interest recognised in the period for the dilutive potential ordinary shares; and***

(c) ***any other changes in income or expense that would result from the conversion of the dilutive potential ordinary shares.***

27. After the potential ordinary shares are converted into ordinary shares, the dividends, interest and other income or expense associated with those potential ordinary shares will no longer be incurred. Instead, the new ordinary shares will be entitled to participate in the net profit attributable to ordinary shareholders. Therefore, the net profit for the period attributable to ordinary shareholders calculated in accordance with paragraph 11 is increased by the amount of dividends, interest and other income or expense that will be saved on the conversion of the dilutive potential ordinary shares into ordinary shares. The expenses associated with potential ordinary shares include fees and discount or premium that are accounted for as yield adjustments (see IAS 32). The amounts of dividends, interest and other income or expense are adjusted for any taxes, borne by the enterprise, that are attributable to them.

Example — convertible bonds

Net profit	1 004
Ordinary shares outstanding	1 000
Basic earnings per share	1,0
Convertible bonds	100
Each block of 10 bonds is convertible into three ordinary shares	
Interest expense for the current year relating to the liability component of the convertible bond	10
Current and deferred tax relating to that interest expense	4

Note: the interest expense includes amortisation of the discount arising on initial recognition of the liability component (see IAS 32).

Adjusted net profit	1 004 + 10 – 4 = 1 010
Number of ordinary shares resulting from conversion of bond	30
Number of ordinary shares used to compute diluted earnings per share	1 000 + 30 = 1 030
Diluted earnings per share	$\frac{1\ 000}{1\ 030} = 0{,}98$

28. The conversion of some potential ordinary shares may lead to consequential changes in other income or expenses. For example, the reduction of interest expense related to potential ordinary shares and the resulting increase in net profit for the period may lead to an increase in the expense relating to a non-discretionary employee profit sharing plan. For the purpose of calculating diluted earnings per share, the net profit or loss for the period is adjusted for any such consequential changes in income or expense.

Per share — diluted

29. ***For the purpose of calculating diluted earnings per share, the number of ordinary shares should be the weighted average number of ordinary shares calculated in accordance with paragraphs 14 and 20, plus the weighted average number of ordinary shares which would be issued on the conversion of all the dilutive potential ordinary shares into ordinary shares. Dilutive potential ordinary shares should be deemed to have been converted into ordinary shares at the beginning of the period or, if later, the date of the issue of the potential ordinary shares.***

30. The number of ordinary shares which would be issued on the conversion of dilutive potential ordinary shares is determined from the terms of the potential ordinary shares. The computation assumes the most advantageous conversion rate or exercise price from the standpoint of the holder of the potential ordinary shares.

31. As in the computation of basic earnings per share, ordinary shares whose issue is contingent upon the occurrence of certain events shall be considered outstanding and included in the computation of diluted earnings per share if the conditions have been met (the events occurred). Contingently issuable shares should be included as of the beginning of the period (or as of the date of the contingent share agreement, if later). If the conditions have not been met, the number of contingently issuable shares included in the diluted earnings per share computation is based on the number of shares that would be issuable if the end of the reporting period was the end of the contingency period. Restatement is not permitted if the conditions are not met when the contingency period expires. The provisions of this paragraph apply equally to potential ordinary shares that are issuable upon the satisfaction of certain conditions (contingently issuable potential ordinary shares).

32. A subsidiary, joint venture or associate may issue potential ordinary shares which are convertible into either ordinary shares of the subsidiary, joint venture or associate, or ordinary shares of the reporting enterprise. If these potential ordinary shares of the subsidiary, associate or joint venture have a dilutive effect on the consolidated basic earnings per share of the reporting enterprise, they are included in the calculation of diluted earnings per share.

33. ***For the purpose of calculating diluted earnings per share, an enterprise should assume the exercise of dilutive options and other dilutive potential ordinary shares of the enterprise. The assumed proceeds from these issues should be considered to have been received from the issue of shares at fair value. The difference between the number of shares issued and the number of shares that would have been issued at fair value should be treated as an issue of ordinary shares for no consideration.***

34. Fair value for this purpose is calculated on the basis of the average price of the ordinary shares during the period.

35. Options and other share purchase arrangements are dilutive when they would result in the issue of ordinary shares for less than fair value. The amount of the dilution is fair value less the issue price. Therefore, in order to calculate diluted earnings per share, each such arrangement is treated as consisting of:

(a) a contract to issue a certain number of ordinary shares at their average fair value during the period. The shares so to be issued are fairly priced and are assumed to be neither dilutive nor anti-dilutive. They are ignored in the computation of diluted earnings per share; and

(b) a contract to issue the remaining ordinary shares for no consideration. Such ordinary shares generate no proceeds and have no effect on the net profit attributable to ordinary shares outstanding. Therefore such shares are dilutive and they are added to the number of ordinary shares outstanding in the computation of diluted earnings per share.

Example — effects of share options on diluted earnings per share

Net profit for year 20X1	1 200 000
Weighted average number of ordinary shares outstanding during year 20X1	500 000 shares
Average fair value of one ordinary share during year 20X1	20,00
Weighted average number of shares under option during year 20X1	100 000 shares
Exercise price for shares under option during year 20X1	15,00

Computation of earnings per share	per share	earnings	shares
Net profit for year 20X1		1 200 000	
Weighted average shares outstanding during year 20X1			500 000
Basic earnings per share	2,40		
Number of shares under option			100 000
Number of shares that would have been issued at fair value:			
(100 000 × 15,00)/20,00		(*)	(75 000)
Diluted earnings per share	2,29	1 200 000	525 000

(*) The earnings have not been increased as the total number of shares has been increased only by the number of shares (25 000) deemed for the purpose of the computation to have been issued for no consideration (see 35(b) above).

36. This method of calculating the effect of options and other share purchase arrangements produces the same result as the treasury stock method which is used in some countries. This does not imply that the enterprise has entered into a transaction to purchase its own shares, which may not be practicable in certain circumstances or legal in some jurisdictions.

37. To the extent that partly paid shares are not entitled to participate in dividends during the financial period they are considered the equivalent of warrants or options.

Dilutive potential ordinary shares

38. ***Potential ordinary shares should be treated as dilutive when, and only when, their conversion to ordinary shares would decrease net profit per share from continuing ordinary operations.***

39. An enterprise uses net profit from continuing ordinary activities as 'the control number' that is used to establish whether potential ordinary shares are dilutive or anti-dilutive. The net profit from continuing ordinary activities is the net profit from ordinary activities (as defined in IAS 8) after deducting preference dividends and after excluding items relating to discontinued operations; therefore, it excludes extraordinary items and the effects of changes in accounting policies and of corrections of fundamental errors.

40. Potential ordinary shares are anti-dilutive when their conversion to ordinary shares would increase earnings per share from continuing ordinary operations or decrease loss per share from continuing ordinary operations. The effects of anti-dilutive potential ordinary shares are ignored in calculating diluted earnings per share.

41. In considering whether potential ordinary shares are dilutive or anti-dilutive, each issue or series of potential ordinary shares is considered separately rather than in aggregate. The sequence in which potential ordinary shares are considered may affect whether or not they are dilutive. Therefore, in order to maximise the dilution of basic earnings per share, each issue or series of potential ordinary shares is considered in sequence from the most dilutive to the least dilutive.

Example — determining the order in which to include dilutive securities in the calculation of weighted average Number of Shares

Earnings — net profit attributable to ordinary shareholders	10 000 000
Ordinary shares outstanding	2 000 000
Average fair value of one ordinary share during year	75,00
Potential ordinary shares	
Options	100 000 with exercise price of 60
Convertible preference shares	800 000 shares entitled to a cumulative dividend of 8 per share. Each preference share is convertible to two ordinary shares
5 % convertible bond	Nominal amount 100 000 000. Each 1 000 bond is convertible to 20 ordinary shares. There is no amortisation of premium or discount affecting the determination of interest expense
Tax rate	40 %

Increase in earnings attributable to ordinary shareholders on conversion of potential ordinary shares

	Increase in earnings	Increase in number of ordinary shares	Earnings per incremental share
Options			
Increase in earnings	nil		
Incremental shares issued for no consideration 100 000 × (75 – 60)/75		20 000	nil
Convertible preference shares			
Increase in net profit 8 × 800 000	6 400 000		
Incremental shares 2 × 800 000		1 600 000	4,00
5 % convertible bonds			
Increase in net profit 100 000 000 × 0,05 × (1 – 0,4)	3 000 000		
Incremental shares 100 000 × 20		2 000 000	1,50

Computation of diluted earnings per share

	Net profit attributable	Ordinary shares	Per share
As reported options	10 000 000	2 000 000 20 000	5,00
	10 000 000	2 020 000	4,95 dilutive
5 % convertible bonds	3 000 000	2 000 000	
	13 000 000	4 020 000	3,23 dilutive
Convertible preference shares	6 400 000	1 600 000	
	19 400 000	5 620 000	3,45 anti-dilutive

Since diluted earnings per share are increased when taking the convertible preference shares into account (from 3,23 to 3,45), the convertible preference shares are anti-dilutive and are ignored in the calculation of diluted earnings per share. Therefore, diluted earnings per share are 3,23.

This example does not illustrate the classification of convertible financial instruments between liabilities and equity or the classification of related interest and dividends between expenses and equity as required by IAS 32.

42. Potential ordinary shares are weighted for the period they were outstanding. Potential ordinary shares that were cancelled or allowed to lapse during the reporting period are included in the computation of diluted earnings per share only for the portion of the period during which they were outstanding. Potential ordinary shares that have been converted into ordinary shares during the reporting period are included in the calculation of diluted earnings per share from the beginning of the period to the date of conversion; from the date of conversion, the resulting ordinary shares are included in both basic and diluted earnings per share.

RESTATEMENT

43. ***If the number of ordinary or potential ordinary shares outstanding increases as a result of a capitalisation or bonus issue or share split or decreases as a result of a reverse share split, the calculation of basic and diluted earnings per share for all periods presented should be adjusted retrospectively. If these changes occur after the balance sheet date but before issue of the financial statements, the per share calculations for those and any prior period financial statements presented should be based on the new number of shares. When per share calculations reflect such changes in the number of shares, that fact should be disclosed. In addition, basic and diluted earnings per share of all periods presented should be adjusted for:***

(a) ***the effects of fundamental errors, and adjustments resulting from changes in accounting policies, dealt with in accordance with the benchmark treatment in IAS 8; and***

(b) ***the effects of a business combination which is a uniting of interests.***

44. An enterprise does not restate diluted earnings per share of any prior period presented for changes in the assumptions used or for the conversion of potential ordinary shares into ordinary shares outstanding.

45. An enterprise is encouraged to disclose a description of ordinary share transactions or potential ordinary share transactions, other than capitalisation issues and share splits, which occur after the balance sheet date when they are of such importance that non-disclosure would affect the ability of the users of the financial statements to make proper evaluations and decisions (see IAS 10, events after the balance sheet date). Examples of such transactions include:

   (a) the issue of shares for cash;

   (b) the issue of shares when the proceeds are used to repay debt or preference shares outstanding at the balance sheet date;

   (c) the redemption of ordinary shares outstanding;

   (d) the conversion or exercise of potential ordinary shares, outstanding at the balance sheet date, into ordinary shares;

   (e) the issue of warrants, options or convertible securities; and

   (f) the achievement of conditions that would result in the issue of contingently issuable shares.

46. Earnings per share amounts are not adjusted for such transactions occurring after the balance sheet date because such transactions do not affect the amount of capital used to produce the net profit or loss for the period.

PRESENTATION

47. ***An enterprise should present basic and diluted earnings per share on the face of the income statement for each class of ordinary shares that has a different right to share in the net profit for the period. An enterprise should present basic and diluted earnings per share with equal prominence for all periods presented.***

48. ***This Standard requires an enterprise to present basic and diluted earnings per share, even if the amounts disclosed are negative (a loss per share).***

DISCLOSURE

49. ***An enterprise should disclose the following:***

   (a) ***the amounts used as the numerators in calculating basic and diluted earnings per share, and a reconciliation of those amounts to the net profit or loss for the period; and***

   (b) ***the weighted average number of ordinary shares used as the denominator in calculating basic and diluted earnings per share, and a reconciliation of these denominators to each other.***

50. Financial instruments and other contracts generating potential ordinary shares may incorporate terms and conditions which affect the measurement of basic and diluted earnings per share. These terms and conditions may determine whether or not any potential ordinary shares are dilutive and, if so, the effect on the weighted average number of shares outstanding and any consequent adjustments to the net profit attributable to ordinary shareholders. Whether or not the disclosure of the terms and conditions is required by IAS 32 such disclosure is encouraged by this Standard.

51. ***If an enterprise discloses, in addition to basic and diluted earnings per share, per share amounts using a reported component of net profit other than net profit or loss for the period attributable to ordinary shareholders, such amounts should be calculated using the weighted average number of ordinary shares determined in accordance with this Standard. If a component of net profit is used which is not reported as a line item in the income statement, a reconciliation should be provided between the component used and a line item which is reported in the income statement. Basic and diluted per share amounts should be disclosed with equal prominence.***

52. An enterprise may wish to disclose more information than this Standard requires. Such information may help the users to evaluate the performance of the enterprise and may take the form of per share amounts for various components of net profit. Such disclosures are encouraged. However, when such amounts are disclosed, the denominators are calculated in accordance with this Standard in order to ensure the comparability of the per share amounts disclosed.

EFFECTIVE DATE

53. ***This International Accounting Standard becomes operative for financial statements covering periods beginning on or after 1 January 1998. Earlier application is encouraged.***

INTERNATIONAL ACCOUNTING STANDARD IAS 34

Interim financial reporting

This International Accounting Standard was approved by the IASC Board in February 1998 and became effective for financial statements covering periods beginning on or after 1 January 1999.

In April 2000, Appendix C, paragraph 7, was amended by IAS 40, investment property.

INTRODUCTION

1. This Standard ('IAS 34') addresses interim financial reporting, a matter not covered in a prior International Accounting Standard. IAS 34 is effective for accounting periods beginning on or after 1 January 1999.

2. An interim financial report is a financial report that contains either a complete or condensed set of financial statements for a period shorter than an enterprise's full financial year.

3. This Standard does not mandate which enterprises should publish interim financial reports, how frequently, or how soon after the end of an interim period. In IASC's judgement, those matters should be decided by national governments, securities regulators, stock exchanges, and accountancy bodies. This Standard applies if a company is required or elects to publish an interim financial report in accordance with International Accounting Standards.

4. This Standard:

   (a) defines the minimum content of an interim financial report, including disclosures; and

   (b) identifies the accounting recognition and measurement principles that should be applied in an interim financial report.

5. Minimum content of an interim financial report is a condensed balance sheet, condensed income statement, condensed cash flow statement, condensed statement showing changes in equity, and selected explanatory notes.

6. On the presumption that anyone who reads an enterprise's interim report will also have access to its most recent annual report, virtually none of the notes to the annual financial statements are repeated or updated in the interim report. Instead, the interim notes include primarily an explanation of the events and changes that are significant to an understanding of the changes in financial position and performance of the enterprise since the last annual reporting date.

7. An enterprise should apply the same accounting policies in its interim financial report as are applied in its annual financial statements, except for accounting policy changes made after the date of the most recent annual financial statements that are to be reflected in the next annual financial statements. The frequency of an enterprise's reporting — annual, half-yearly, or quarterly — should not affect the measurement of its annual results. To achieve that objective, measurements for interim reporting purposes are made on a year-to-date basis.

8. An appendix to this Standard provides guidance for applying the basic recognition and measurement principles at interim dates to various types of asset, liability, income, and expense. Income tax expense for an interim period is based on an estimated average annual effective income tax rate, consistent with the annual assessment of taxes.

9. In deciding how to recognise, classify, or disclose an item for interim financial reporting purposes, materiality is to be assessed in relation to the interim period financial data, not forecasted annual data.

CONTENTS

The standards, which have been set in bold italic type, should be read in the context of the background material and implementation guidance in this Standard, and in the context of the 'Preface to International Accounting Standards'. International Accounting Standards are not intended to apply to immaterial items (see paragraph 12 of the Preface).

OBJECTIVE

The objective of this Standard is to prescribe the minimum content of an interim financial report and to prescribe the principles for recognition and measurement in complete or condensed financial statements for an interim period. Timely and reliable interim financial reporting improves the ability of investors, creditors, and others to understand an enterprise's capacity to generate earnings and cash flows and its financial condition and liquidity.

SCOPE

1. This Standard does not mandate which enterprises should be required to publish interim financial reports, how frequently, or how soon after the end of an interim period. However, governments, securities regulators, stock exchanges, and accountancy bodies often require enterprises whose debt or equity securities are publicly traded to publish interim financial reports. This Standard applies if an enterprise is required or elects to publish an interim financial report in accordance with International Accounting Standards. The International Accounting Standards Committee encourages publicly traded enterprises to provide interim financial reports that conform to the recognition, measurement, and disclosure principles set out in this Standard. Specifically, publicly traded enterprises are encouraged:

   (a) to provide interim financial reports at least as of the end of the first half of their financial year; and

   (b) to make their interim financial reports available not later than 60 days after the end of the interim period.

2. Each financial report, annual or interim, is evaluated on its own for conformity to International Accounting Standards. The fact that an enterprise may not have provided interim financial reports during a particular financial year or may have provided interim financial reports that do not comply with this Standard does not prevent the enterprise's annual financial statements from conforming to International Accounting Standards if they otherwise do so.

3. If an enterprise's interim financial report is described as complying with International Accounting Standards, it must comply with all of the requirements of this Standard. Paragraph 19 requires certain disclosures in that regard.

DEFINITIONS

4. ***The following terms are used in this Standard with the meanings specified:***

   Interim period is a financial reporting period shorter than a full financial year.

   Interim financial report means a financial report containing either a complete set of financial statements (as described in IAS 1, presentation of financial statements) or a set of condensed financial statements (as described in this Standard) for an interim period.

CONTENT OF AN INTERIM FINANCIAL REPORT

5. IAS 1 defines a complete set of financial statements as including the following components:

   (a) balance sheet;

   (b) income statement;

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

   (d) cash flow statement; and

   (e) accounting policies and explanatory notes.

6. In the interest of timeliness and cost considerations and to avoid repetition of information previously reported, an enterprise may be required to or may elect to provide less information at interim dates as compared with its annual financial statements. This Standard defines the minimum content of an interim financial report as including condensed financial statements and selected explanatory notes. The interim financial report is intended to provide an update on the latest complete set of annual financial statements. Accordingly, it focuses on new activities, events, and circumstances and does not duplicate information previously reported.

7. Nothing in this Standard is intended to prohibit or discourage an enterprise from publishing a complete set of financial statements (as described in IAS 1) in its interim financial report, rather than condensed financial statements and selected explanatory notes. Nor does this Standard prohibit or discourage an enterprise from including in condensed interim financial statements more than the minimum line items or selected explanatory notes as set out in this Standard. The recognition and measurement guidance in this Standard applies also to complete financial statements for an interim period, and such statements would include all of the disclosures required by this Standard (particularly the selected note disclosures in paragraph 16) as well as those required by other International Accounting Standards.

Minimum components of an interim financial report

8. ***An interim financial report should include, at a minimum, the following components:***

(a) ***condensed balance sheet;***

(b) ***condensed income statement;***

(c) ***condensed statement showing either (i) all changes in equity or (ii) changes in equity other than those arising from capital transactions with owners and distributions to owners;***

(d) ***condensed cash flow statement; and***

(e) ***selected explanatory notes.***

Form and content of interim financial statements

9. ***If an enterprise publishes a complete set of financial statements in its interim financial report, the form and content of those statements should conform to the requirements of IAS 1 for a complete set of financial statements.***

10. ***If an enterprise publishes a set of condensed financial statements in its interim financial report, those condensed statements should include, at a minimum, each of the headings and subtotals that were included in its most recent annual financial statements and the selected explanatory notes as required by this Standard. Additional line items or notes should be included if their omission would make the condensed interim financial statements misleading.***

11. ***Basic and diluted earnings per share should be presented on the face of an income statement, complete or condensed, for an interim period.***

12. IAS 1 provides guidance on the structure of financial statements and includes an appendix, 'Illustrative financial statement structure', that provides further guidance on major headings and subtotals.

13. While IAS 1 requires that a statement showing changes in equity be presented as a separate component of an enterprise's financial statements, it permits information about changes in equity arising from capital transactions with owners and distributions to owners to be shown either on the face of the statement or, alternatively, in the notes. An enterprise follows the same format in its interim statement showing changes in equity as it did in its most recent annual statement.

14. An interim financial report is prepared on a consolidated basis if the enterprise's most recent annual financial statements were consolidated statements. The parent's separate financial statements are not consistent or comparable with the consolidated statements in the most recent annual financial report. If an enterprise's annual financial report included the parent's separate financial statements in addition to consolidated financial statements, this Standard neither requires nor prohibits the inclusion of the parent's separate statements in the enterprise's interim financial report.

Selected explanatory notes

15. A user of an enterprise's interim financial report will also have access to the most recent annual financial report of that enterprise. It is unnecessary, therefore, for the notes to an interim financial report to provide relatively insignificant updates to the information that was already reported in the notes in the most recent annual report. At an interim date, an explanation of events and transactions that are significant to an understanding of the changes in financial position and performance of the enterprise since the last annual reporting date is more useful.

16. ***An enterprise should include the following information, as a minimum, in the notes to its interim financial statements, if material and if not disclosed elsewhere in the interim financial report. The information should normally be reported on a financial year-to-date basis. However, the enterprise should also disclose any events or transactions that are material to an understanding of the current interim period:***

(a) ***a statement that the same accounting policies and methods of computation are followed in the interim financial statements as compared with the most recent annual financial statements or, if those policies or methods have been changed, a description of the nature and effect of the change;***

(b) ***explanatory comments about the seasonality or cyclicality of interim operations;***

(c) ***the nature and amount of items affecting assets, liabilities, equity, net income, or cash flows that are unusual because of their nature, size, or incidence;***

(d) ***the nature and amount of changes in estimates of amounts reported in prior interim periods of the current financial year or changes in estimates of amounts reported in prior financial years, if those changes have a material effect in the current interim period;***

(e) ***issuances, repurchases, and repayments of debt and equity securities;***

(f) ***dividends paid (aggregate or per share) separately for ordinary shares and other shares;***

(g) ***segment revenue and segment result for business segments or geographical segments, whichever is the enterprise's primary basis of segment reporting (disclosure of segment data is required in an enterprise's interim financial report only if IAS 14, segment reporting, requires that enterprise to disclose segment data in its annual financial statements);***

(h) ***material events subsequent to the end of the interim period that have not been reflected in the financial statements for the interim period;***

(i) ***the effect of changes in the composition of the enterprise during the interim period, including business combinations, acquisition or disposal of subsidiaries and long-term investments, restructurings, and discontinuing operations; and***

(j) ***changes in contingent liabilities or contingent assets since the last annual balance sheet date.***

17. Examples of the kinds of disclosures that are required by paragraph 16 are set out below. Individual International Accounting Standards provide guidance regarding disclosures for many of these items:

(a) the write-down of inventories to net realisable value and the reversal of such a write-down;

(b) recognition of a loss from the impairment of property, plant, and equipment, intangible assets, or other assets, and the reversal of such an impairment loss;

(c) the reversal of any provisions for the costs of restructuring;

(d) acquisitions and disposals of items of property, plant, and equipment;

(e) commitments for the purchase of property, plant, and equipment;

(f) litigation settlements;

(g) corrections of fundamental errors in previously reported financial data;

(h) extraordinary items;

(i) any debt default or any breach of a debt covenant that has not been corrected subsequently; and

(j) related party transactions.

18. Other International Accounting Standards specify disclosures that should be made in financial statements. In that context, financial statements means complete sets of financial statements of the type normally included in an annual financial report and sometimes included in other reports. The disclosures required by those other International Accounting Standards are not required if an enterprise's interim financial report includes only condensed financial statements and selected explanatory notes rather than a complete set of financial statements.

Disclosure of compliance with IAS

19. ***If an enterprise's interim financial report is in compliance with this International Accounting Standard, that fact should be disclosed. An interim financial report should not be described as complying with International Accounting Standards unless it complies with all of the requirements of each applicable Standard and each applicable interpretation of the Standing Interpretations Committee.***

Periods for which interim financial statements are required to be presented

20. ***Interim reports should include interim financial statements (condensed or complete) for periods as follows:***

(a) ***balance sheet as of the end of the current interim period and a comparative balance sheet as of the end of the immediately preceding financial year;***

(b) ***income statements for the current interim period and cumulatively for the current financial year to date, with comparative income statements for the comparable interim periods (current and year-to-date) of the immediately preceding financial year;***

(c) ***statement showing changes in equity cumulatively for the current financial year to date, with a comparative statement for the comparable year-to-date period of the immediately preceding financial year; and***

(d) ***cash flow statement cumulatively for the current financial year to date, with a comparative statement for the comparable year-to-date period of the immediately preceding financial year.***

21. For an enterprise whose business is highly seasonal, financial information for the 12 months ending on the interim reporting date and comparative information for the prior 12-month period may be useful. Accordingly, enterprises whose business is highly seasonal are encouraged to consider reporting such information in addition to the information called for in the preceding paragraph.

22. Appendix A illustrates the periods required to be presented by an enterprise that reports half-yearly and an enterprise that reports quarterly.

Materiality

23. ***In deciding how to recognise, measure, classify, or disclose an item for interim financial reporting purposes, materiality should be assessed in relation to the interim period financial data. In making assessments of materiality, it should be recognised that interim measurements may rely on estimates to a greater extent than measurements of annual financial data.***

24. The ‘Preface to International Accounting Standards’ states that ‘International Accounting Standards are not intended to apply to immaterial items.’ The framework states that ‘information is material if its omission or misstatement could influence the economic decisions of users taken on the basis of the financial statements’. IAS 8, net profit or loss for the period, fundamental errors and changes in accounting policies, requires separate disclosure of material extraordinary items, unusual ordinary items, discontinued operations, changes in accounting estimates, fundamental errors, and changes in accounting policies. IAS 8 does not contain quantified guidance as to materiality.

25. While judgement is always required in assessing materiality for financial reporting purposes, this Standard bases the recognition and disclosure decision on data for the interim period by itself for reasons of understandability of the interim figures. Thus, for example, unusual or extraordinary items, changes in accounting policies or estimates, and fundamental errors are recognised and disclosed based on materiality in relation to interim period data to avoid misleading inferences that might result from nondisclosure. The overriding goal is to ensure that an interim financial report includes all information that is relevant to understanding an enterprise’s financial position and performance during the interim period.

DISCLOSURE IN ANNUAL FINANCIAL STATEMENTS

26. ***If an estimate of an amount reported in an interim period is changed significantly during the final interim period of the financial year but a separate financial report is not published for that final interim period, the nature and amount of that change in estimate should be disclosed in a note to the annual financial statements for that financial year.***

27. IAS 8 requires disclosure of the nature and (if practicable) the amount of a change in estimate that either has a material effect in the current period or is expected to have a material effect in subsequent periods. Paragraph 16(d) of this Standard requires similar disclosure in an interim financial report. Examples include changes in estimate in the final interim period relating to inventory write-downs, restructurings, or impairment losses that were reported in an earlier interim period of the financial year. The disclosure required by the preceding paragraph is consistent with the IAS 8 requirement and is intended to be narrow in scope — relating only to the change in estimate. An enterprise is not required to include additional interim period financial information in its annual financial statements.

RECOGNITION AND MEASUREMENT

Same accounting policies as annual

28. ***An enterprise should apply the same accounting policies in its interim financial statements as are applied in its annual financial statements, except for accounting policy changes made after the date of the most recent annual financial statements that are to be reflected in the next annual financial statements. However, the frequency of an enterprise’s reporting (annual, half-yearly, or quarterly) should not affect the measurement of its annual results. To achieve that objective, measurements for interim reporting purposes should be made on a year-to-date basis.***

29. Requiring that an enterprise apply the same accounting policies in its interim financial statements as in its annual statements may seem to suggest that interim period measurements are made as if each interim period stands alone as an independent reporting period. However, by providing that the frequency of an enterprise's reporting should not affect the measurement of its annual results, paragraph 28 acknowledges that an interim period is a part of a larger financial year. Year-to-date measurements may involve changes in estimates of amounts reported in prior interim periods of the current financial year. But the principles for recognising assets, liabilities, income, and expenses for interim periods are the same as in annual financial statements.

30. To illustrate:

(a) the principles for recognising and measuring losses from inventory write-downs, restructurings, or impairments in an interim period are the same as those that an enterprise would follow if it prepared only annual financial statements. However, if such items are recognised and measured in one interim period and the estimate changes in a subsequent interim period of that financial year, the original estimate is changed in the subsequent interim period either by accrual of an additional amount of loss or by reversal of the previously recognised amount;

(b) a cost that does not meet the definition of an asset at the end of an interim period is not deferred on the balance sheet either to await future information as to whether it has met the definition of an asset or to smooth earnings over interim periods within a financial year; and

(c) income tax expense is recognised in each interim period based on the best estimate of the weighted average annual income tax rate expected for the full financial year. Amounts accrued for income tax expense in one interim period may have to be adjusted in a subsequent interim period of that financial year if the estimate of the annual income tax rate changes.

31. Under the framework for the preparation and presentation of financial statements (the framework), recognition is the 'process of incorporating in the balance sheet or income statement an item that meets the definition of an element and satisfies the criteria for recognition'. The definitions of assets, liabilities, income, and expenses are fundamental to recognition, both at annual and interim financial reporting dates.

32. For assets, the same tests of future economic benefits apply at interim dates and at the end of an enterprise's financial year. Costs that, by their nature, would not qualify as assets at financial year end would not qualify at interim dates either. Similarly, a liability at an interim reporting date must represent an existing obligation at that date, just as it must at an annual reporting date.

33. An essential characteristic of income (revenue) and expenses is that the related inflows and outflows of assets and liabilities have already taken place. If those inflows or outflows have taken place, the related revenue and expense are recognised; otherwise they are not recognised. The framework says that 'expenses are recognised in the income statement when a decrease in future economic benefits related to a decrease in an asset or an increase of a liability has arisen that can be measured reliably ... . [The] framework does not allow the recognition of items in the balance sheet which do not meet the definition of assets or liabilities'.

34. In measuring the assets, liabilities, income, expenses, and cash flows reported in its financial statements, an enterprise that reports only annually is able to take into account information that becomes available throughout the financial year. Its measurements are, in effect, on a year-to-date basis.

35. An enterprise that reports half-yearly uses information available by mid-year or shortly thereafter in making the measurements in its financial statements for the first six-month period and information available by year-end or shortly thereafter for the 12-month period. The 12-month measurements will reflect possible changes

in estimates of amounts reported for the first six-month period. The amounts reported in the interim financial report for the first six-month period are not retrospectively adjusted. Paragraphs 16(d) and 26 require, however, that the nature and amount of any significant changes in estimates be disclosed.

36. An enterprise that reports more frequently than half-yearly measures income and expenses on a year-to-date basis for each interim period using information available when each set of financial statements is being prepared. Amounts of income and expenses reported in the current interim period will reflect any changes in estimates of amounts reported in prior interim periods of the financial year. The amounts reported in prior interim periods are not retrospectively adjusted. Paragraphs 16(d) and 26 require, however, that the nature and amount of any significant changes in estimates be disclosed.

Revenues received seasonally, cyclically, or occasionally

37. ***Revenues that are received seasonally, cyclically, or occasionally within a financial year should not be anticipated or deferred as of an interim date if anticipation or deferral would not be appropriate at the end of the enterprise's financial year.***

38. Examples include dividend revenue, royalties, and government grants. Additionally, some enterprises consistently earn more revenues in certain interim periods of a financial year than in other interim periods, for example, seasonal revenues of retailers. Such revenues are recognised when they occur.

Costs incurred unevenly during the financial year

39. ***Costs that are incurred unevenly during an enterprise's financial year should be anticipated or deferred for interim reporting purposes if, and only if, it is also appropriate to anticipate or defer that type of cost at the end of the financial year.***

Applying the recognition and measurement principles

40. Appendix B provides examples of applying the general recognition and measurement principles set out in paragraphs 28 to 39.

Use of estimates

41. ***The measurement procedures to be followed in an interim financial report should be designed to ensure that the resulting information is reliable and that all material financial information that is relevant to an understanding of the financial position or performance of the enterprise is appropriately disclosed. While measurements in both annual and interim financial reports are often based on reasonable estimates, the preparation of interim financial reports generally will require a greater use of estimation methods than annual financial reports.***

42. Appendix C provides examples of the use of estimates in interim periods.

RESTATEMENT OF PREVIOUSLY REPORTED INTERIM PERIODS

43. ***A change in accounting policy, other than one for which the transition is specified by a new International Accounting Standard, should be reflected by:***

(a) ***restating the financial statements of prior interim periods of the current financial year and the comparable interim periods of prior financial years (see paragraph 20), if the enterprise follows the benchmark treatment under IAS 8; or***

(b) ***restating the financial statements of prior interim periods of the current financial year, if the enterprise follows the allowed alternative treatment under IAS 8. In this case, comparable interim periods of prior financial years are not restated.***

44. One objective of the preceding principle is to ensure that a single accounting policy is applied to a particular class of transactions throughout an entire financial year. Under IAS 8, a change in accounting policy is reflected by retrospective application, with restatement of prior period financial data, if practicable. However, if the amount of the adjustment relating to prior financial years is not reasonably determinable, then under IAS 8 the new policy is applied prospectively. An allowed alternative is to include the entire cumulative retrospective adjustment in the determination of net profit or loss for the period in which the accounting policy is changed. The effect of the principle in paragraph 43 is to require that within the current financial year any change in accounting policy be applied retrospectively to the beginning of the financial year.

45. To allow accounting changes to be reflected as of an interim date within the financial year would allow two differing accounting policies to be applied to a particular class of transactions within a single financial year. The result would be interim allocation difficulties, obscured operating results, and complicated analysis and understandability of interim period information.

EFFECTIVE DATE

46. ***This International Accounting Standard becomes operative for financial statements covering periods beginning on or after 1 January 1999. Earlier application is encouraged.***

INTERNATIONAL ACCOUNTING STANDARD IAS 35

Discontinuing Operations

This International Accounting Standard was approved by the IASC Board in April 1998 and became effective for financial statements covering periods beginning on or after 1 January 1999.

This Standard supersedes paragraphs 19 to 22 of IAS 8, net profit or loss for the period, fundamental errors and changes in accounting policies.

In 1999, paragraph 8 of the introduction, paragraphs 20, 21, 29, 30 and 32 of the Standard, and paragraph 4 of Appendix B were amended to conform to the terminology used in IAS 10 (revised 1999), events after the balance sheet date and IAS 37, provisions, contingent liabilities and contingent assets.

INTRODUCTION

1. This Standard (IAS 35) addresses presentation and disclosures relating to discontinuing operations. That matter had been dealt with relatively briefly in paragraphs 19 to 22 of IAS 8, net profit or loss for the period, fundamental errors and changes in accounting policies. IAS 35 supersedes those paragraphs of IAS 8. IAS 35 is effective for financial statements for periods beginning on or after 1 January 1999. Earlier application is encouraged.

2. The objectives of IAS 35 are to establish a basis for segregating information about a major operation that an enterprise is discontinuing from information about its continuing operations and to specify minimum disclosures about a discontinuing operation. Distinguishing discontinuing and continuing operations improves the ability of investors, creditors, and other users of financial statements to make projections of the enterprise's cash flows, earnings-generating capacity, and financial position.

3. A discontinuing operation is a relatively large component of an enterprise — such as a business or geographical segment under IAS 14, segment reporting — that the enterprise, pursuant to a single plan, either is disposing of substantially in its entirety or is terminating through abandonment or piecemeal sale.

4. This Standard uses the term 'discontinuing operation' rather than the traditional 'discontinued operation' because 'discontinued operation' (past tense) implies that recognition of a discontinuance is necessary only at or near the end of the process of discontinuing the operation. This Standard requires that disclosures about a discontinuing operation begin earlier than that — when a detailed formal plan for disposal has been adopted and announced or when the enterprise has already contracted for the disposal.

5. This is a presentation and disclosure Standard. It focuses on how to present a discontinuing operation in an enterprise's financial statements and what information to disclose. It does not establish any new principles for deciding when and how to recognise and measure the income, expenses, cash flows, and changes in assets and liabilities relating to a discontinuing operation. Instead, it requires that enterprises follow the recognition and measurement principles in other International Accounting Standards.

6. Under this Standard, information about a planned discontinuance must initially be disclosed in the first set of financial statements issued by an enterprise after (a) it has entered into an agreement to sell substantially all of the assets of the discontinuing operation or (b) its board of directors or other similar governing body has both approved and announced the planned discontinuance. Required disclosures include:

— a description of the discontinuing operation,

— the business or geographical segment(s) in which it is reported,

— the date and nature of the initial disclosure event,

— the timing of expected completion,

— the carrying amounts of the total assets and the total liabilities to be disposed of,

— the amounts of revenue, expenses, and pre-tax profit or loss attributable to the discontinuing operation, and related income tax expense,

— the net cash flows attributable to the operating, investing, and financing activities of the discontinuing operation,

— the amount of any gain or loss that is recognised on the disposal of assets or settlement of liabilities attributable to the discontinuing operation, and related income tax expense, and

— the net selling prices, after disposal costs, from the sale of those net assets for which the enterprise has entered into one or more binding sale agreements, and the expected timing thereof, and the carrying amounts of those net assets.

7. Financial statements for periods after initial disclosure must update those disclosures, including a description of any significant changes in the amount or timing of cash flows relating to the assets and liabilities to be disposed of or settled and the causes of those changes.

8. The disclosures would be made if a plan for disposal is approved and publicly announced after the end of an enterprise's financial reporting period but before the financial statements for that period are authorised for issue. The disclosures continue until completion of the disposal.

9. Comparative information for prior periods that is presented in financial statements prepared after initial disclosure must be restated to segregate the continuing and discontinuing assets, liabilities, income, expenses, and cash flows. By separating discontinuing and continuing operations retrospectively, the ability of a user of financial statements to make projections is improved.

IAS 35

CONTENTS

The standards, which have been set in bold italic type, should be read in the context of the background material and implementation guidance in this Standard, and in the context of the 'Preface to International Accounting Standards'. International Accounting Standards are not intended to apply to immaterial items (see paragraph 12 of the Preface).

OBJECTIVE

The objective of this Standard is to establish principles for reporting information about discontinuing operations, thereby enhancing the ability of users of financial statements to make projections of an enterprise's cash flows, earnings-generating capacity, and financial position by segregating information about discontinuing operations from information about continuing operations.

SCOPE

1. ***This Standard applies to all discontinuing operations of all enterprises.***

DEFINITIONS

Discontinuing operation

2. ***A discontinuing operation is a component of an enterprise:***

   (a) ***that the enterprise, pursuant to a single plan, is:***

      (i) ***disposing of substantially in its entirety, such as by selling the component in a single transaction, by demerger or spin-off of ownership of the component to the enterprise's shareholders;***

      (ii) ***disposing of piecemeal, such as by selling off the component's assets and settling its liabilities individually; or***

      (iii) ***terminating through abandonment;***

   (b) ***that represents a separate major line of business or geographical area of operations; and***

   (c) ***that can be distinguished operationally and for financial reporting purposes.***

3. Under criterion (a) of the definition (paragraph 2(a)), a discontinuing operation may be disposed of in its entirety or piecemeal, but always pursuant to an overall plan to discontinue the entire component.

4. If an enterprise sells a component substantially in its entirety, the result can be a net gain or net loss. For such a discontinuance, there is a single date at which a binding sale agreement is entered into, although the actual transfer of possession and control of the discontinuing operation may occur at a later date. Also, payments to the seller may occur at the time of the agreement, at the time of the transfer, or over an extended future period.

5. Instead of disposing of a major component in its entirety, an enterprise may discontinue and dispose of the component by selling its assets and settling its liabilities piecemeal (individually or in small groups). For piecemeal disposals, while the overall result may be a net gain or a net loss, the sale of an individual asset or settlement of an individual liability may have the opposite effect. Moreover, there is no single date at which an overall binding sale agreement is entered into. Rather, the sales of assets and settlements of liabilities may occur over a period of months or perhaps even longer, and the end of a financial reporting period may occur part way through the disposal period. To qualify as a discontinuing operation, the disposal must be pursuant to a single co-ordinated plan.

6. An enterprise may terminate an operation by abandonment without substantial sales of assets. An abandoned operation would be a discontinuing operation if it satisfies the criteria in the definition. However, changing the scope of an operation or the manner in which it is conducted is not an abandonment because that operation, although changed, is continuing.

7. Business enterprises frequently close facilities, abandon products or even product lines, and change the size of their work force in response to market forces. While those kinds of terminations generally are not, in and of themselves, discontinuing operations as that term is used in this Standard, they can occur in connection with a discontinuing operation.

8. Examples of activities that do not necessarily satisfy criterion (a) of paragraph 2, but that might do so in combination with other circumstances, include:

   (a) gradual or evolutionary phasing out of a product line or class of service;

(b) discontinuing, even if relatively abruptly, several products within an ongoing line of business;

(c) shifting of some production or marketing activities for a particular line of business from one location to another;

(d) closing of a facility to achieve productivity improvements or other cost savings; and

(e) selling a subsidiary whose activities are similar to those of the parent or other subsidiaries.

9. A reportable business segment or geographical segment as defined in IAS 14, segment reporting, would normally satisfy criterion (b) of the definition of a discontinuing operation (paragraph 2(b)), that is, it would represent a separate major line of business or geographical area of operations. A part of a segment as defined in IAS 14 may also satisfy criterion (b) of the definition. For an enterprise that operates in a single business or geographical segment and therefore does not report segment information, a major product or service line may also satisfy the criteria of the definition.

10. IAS 14 permits, but does not require, that different stages of vertically integrated operations be identified as separate business segments. Such vertically integrated business segments may satisfy criterion (b) of the definition of a discontinuing operation.

11. A component can be distinguished operationally and for financial reporting purposes — criterion (c) of the definition (paragraph 2(c)) — if:

(a) its operating assets and liabilities can be directly attributed to it;

(b) its income (gross revenue) can be directly attributed to it; and

(c) at least a majority of its operating expenses can be directly attributed to it.

12. Assets, liabilities, income, and expenses are directly attributable to a component if they would be eliminated when the component is sold, abandoned or otherwise disposed of. Interest and other financing cost is attributed to a discontinuing operation only if the related debt is similarly attributed.

13. As defined in this Standard, discontinuing operations are expected to occur relatively infrequently. Some changes that are not classified as discontinuing operations may qualify as restructurings (see IAS 37, provisions, contingent liabilities and contingent assets).

14. Also, some infrequently occurring events that do not qualify either as discontinuing operations or restructurings may result in items of income or expense that require separate disclosure pursuant to IAS 8, net profit or loss for the period, fundamental errors and changes in accounting policies, because their size, nature, or incidence make them relevant to explain the performance of the enterprise for the period.

15. The fact that a disposal of a component of an enterprise is classified as a discontinuing operation under this Standard does not, in itself, bring into question the enterprise's ability to continue as a going concern. IAS 1, presentation of financial statements, requires disclosure of uncertainties relating to an enterprise's ability to continue as a going concern and of any conclusion that an enterprise is not a going concern.

Initial disclosure event

16. ***With respect to a discontinuing operation, the initial disclosure event is the occurrence of one of the following, whichever occurs earlier:***

(a) ***the enterprise has entered into a binding sale agreement for substantially all of the assets attributable to the discontinuing operation; or***

(b) ***the enterprise's board of directors or similar governing body has both (i) approved a detailed, formal plan for the discontinuance and (ii) made an announcement of the plan.***

RECOGNITION AND MEASUREMENT

17. ***An enterprise should apply the principles of recognition and measurement that are set out in other International Accounting Standards for the purpose of deciding when and how to recognise and measure the changes in assets and liabilities and the income, expenses, and cash flows relating to a discontinuing operation.***

18. This Standard does not establish any recognition and measurement principles. Rather, it requires that an enterprise follow recognition and measurement principles established in other Standards. Two Standards that are likely to be relevant in this regard are:

    (a) IAS 36, impairment of assets; and

    (b) IAS 37, provisions, contingent liabilities and contingent assets.

19. Other Standards that may be relevant include IAS 19, employee benefits, with respect to recognition of termination benefits, and IAS 16, property, plant and equipment, with respect to disposals of those kinds of assets.

Provisions

20. A discontinuing operation is a restructuring as that term is defined in IAS 37, provisions, contingent liabilities and contingent assets. IAS 37 provides guidance for certain of the requirements of this Standard, including:

    (a) what constitutes a 'detailed, formal plan for the discontinuance' as that term is used in paragraph 16(b) of this Standard; and

    (b) what constitutes an 'announcement of the plan' as that term is used in paragraph 16(b) of this Standard.

21. IAS 37 defines when a provision should be recognised. In some cases, the event that obligates the enterprise occurs after the end of a financial reporting period but before the financial statements for that period have been authorised for issue. Paragraph 29 of this Standard requires disclosures about a discontinuing operation in such cases.

Impairment losses

22. The approval and announcement of a plan for discontinuance is an indication that the assets attributable to the discontinuing operation may be impaired or that an impairment loss previously recognised for those assets should be increased or reversed. Therefore, in accordance with IAS 36, impairment of assets, an enterprise estimates the recoverable amount of each asset of the discontinuing operation (the higher of the asset's net selling price and its value in use) and recognises an impairment loss or reversal of a prior impairment loss, if any.

23. In applying IAS 36 to a discontinuing operation, an enterprise determines whether the recoverable amount of an asset of a discontinuing operation is assessed for the individual asset or for the asset's cash-generating unit (defined in IAS 36 as the smallest identifiable group of assets that includes the asset under review and that generates cash inflows from continuing use that are largely independent of the cash inflows from other assets or groups of assets). For example:

    (a) if the enterprise sells the discontinuing operation substantially in its entirety, none of the assets of the discontinuing operation generate cash inflows independently from other assets within the discontinuing operation. Therefore, recoverable amount is determined for the discontinuing operation as a whole and an impairment loss, if any, is allocated among the assets of the discontinuing operation in accordance with IAS 36;

    (b) if the enterprise disposes of the discontinuing operation in other ways such as piecemeal sales, the recoverable amount is determined for individual assets, unless the assets are sold in groups; and

    (c) if the enterprise abandons the discontinuing operation, the recoverable amount is determined for individual assets as set out in IAS 36.

24. After announcement of a plan, negotiations with potential purchasers of the discontinuing operation or actual binding sale agreements may indicate that the assets of the discontinuing operation may be further impaired or that impairment losses recognised for these assets in prior periods may have decreased. As a consequence, when such events occur, an enterprise re-estimates the recoverable amount of the assets of the discontinuing operation and recognises resulting impairment losses or reversals of impairment losses in accordance with IAS 36.

25. A price in a binding sale agreement is the best evidence of an asset's (cash-generating unit's) net selling price or of the estimated cash inflow from ultimate disposal in determining the asset's (cash-generating unit's) value in use.

26. The carrying amount (recoverable amount) of a discontinuing operation includes the carrying amount (recoverable amount) of any goodwill that can be allocated on a reasonable and consistent basis to that discontinuing operation.

PRESENTATION AND DISCLOSURE

Initial disclosure

27. ***An enterprise should include the following information relating to a discontinuing operation in its financial statements beginning with the financial statements for the period in which the initial disclosure event (as defined in paragraph 16) occurs:***

(a) ***a description of the discontinuing operation;***

(b) ***the business or geographical segment(s) in which it is reported in accordance with IAS 14;***

(c) ***the date and nature of the initial disclosure event;***

(d) ***the date or period in which the discontinuance is expected to be completed if known or determinable;***

(e) ***the carrying amounts, as of the balance sheet date, of the total assets and the total liabilities to be disposed of;***

(f) ***the amounts of revenue, expenses, and pre-tax profit or loss from ordinary activities attributable to the discontinuing operation during the current financial reporting period, and the income tax expense relating thereto as required by paragraph 81(h) of IAS 12; and***

(g) ***the amounts of net cash flows attributable to the operating, investing, and financing activities of the discontinuing operation during the current financial reporting period.***

28. In measuring the assets, liabilities, revenues, expenses, gains, losses, and cash flows of a discontinuing operation for the purpose of the disclosures required by this Standard, such items can be attributed to a discontinuing operation if they will be disposed of, settled, reduced, or eliminated when the discontinuance is completed. To the extent that such items continue after completion of the discontinuance, they should not be allocated to the discontinuing operation.

29. ***If an initial disclosure event occurs after the end of an enterprise's financial reporting period but before the financial statements for that period are authorised for issue, those financial statements should include the disclosures specified in paragraph 27 for the period covered by those financial statements.***

30. For example, the board of directors of an enterprise whose financial year ends 31 December 20X5 approves a plan for a discontinuing operation on 15 December 20X5 and announces that plan on 10 January 20X6. The board authorises the financial statements for 20X5 for issue on 20 March 20X6. The financial statements for 20X5 include the disclosures required by paragraph 27.

Other disclosures

31. ***When an enterprise disposes of assets or settles liabilities attributable to a discontinuing operation or enters into binding agreements for the sale of such assets or the settlement of such liabilities, it should include in its financial statements the following information when the events occur:***

(a) ***for any gain or loss that is recognised on the disposal of assets or settlement of liabilities attributable to the discontinuing operation, (i) the amount of the pre-tax gain or loss and (ii) income tax expense relating to the gain or loss, as required by paragraph 81(h) of IAS 12; and***

(b) ***the net selling price or range of prices (which is after deducting the expected disposal costs) of those net assets for which the enterprise has entered into one or more binding sale agreements, the expected timing of receipt of those cash flows, and the carrying amount of those net assets.***

32. The asset disposals, liability settlements, and binding sale agreements referred to in the preceding paragraph may occur concurrently with the initial disclosure event, or in the period in which the initial disclosure event occurs, or in a later period. In accordance with IAS 10, events after the balance sheet date, if some of the assets attributable to a discontinuing operation have actually been sold or are the subject of one or more binding sale agreements entered into after the financial year end but before the board approves the financial statements for issue, the financial statements include the disclosures required by paragraph 31 if non-disclosure would affect the ability of the users of the financial statements to make proper evaluations and decisions.

Updating the disclosures

33. ***In addition to the disclosures in paragraphs 27 and 31, an enterprise should include in its financial statements for periods subsequent to the one in which the initial disclosure event occurs a description of any significant changes in the amount or timing of cash flows relating to the assets and liabilities to be disposed of or settled and the events causing those changes.***

34. Examples of events and activities that would be disclosed include the nature and terms of binding sale agreements for the assets, a demerger of the assets via spin-off of a separate equity security to the enterprise's shareholders, and legal or regulatory approvals.

35. ***The disclosures required by paragraphs 27 to 34 should continue in financial statements for periods up to and including the period in which the discontinuance is completed. A discontinuance is completed when the plan is substantially completed or abandoned, though payments from the buyer(s) to the seller may not yet be completed.***

36. ***If an enterprise abandons or withdraws from a plan that was previously reported as a discontinuing operation, that fact and its effect should be disclosed.***

37. For the purpose of applying the preceding paragraph, disclosure of the effect includes reversal of any prior impairment loss or provision that was recognised with respect to the discontinuing operation.

Separate disclosure for each discontinuing operation

38. ***Any disclosures required by this Standard should be presented separately for each discontinuing operation.***

Presentation of the required disclosures

Face of financial statements or notes

39. ***The disclosures required by paragraphs 27 to 37 may be presented either in the notes to the financial statements or on the face of the financial statements except that the disclosure of the amount of the pre-tax gain or loss recognised on the disposal of assets or settlement of liabilities attributable to the discontinuing operation (paragraph 31(a)) should be shown on the face of the income statement.***

40. The disclosures required by paragraphs 27(f) and 27(g) are encouraged to be presented on the face of the income statement and cash flow statement, respectively.

Not an extraordinary item

41. ***A discontinuing operation should not be presented as an extraordinary item.***

42. IAS 8 defines extraordinary items as 'income or expenses that arise from events or transactions that are clearly distinct from the ordinary activities of the enterprise and therefore are not expected to recur frequently or regularly.' The two examples of extraordinary items cited in IAS 8 are expropriations of assets and natural disasters, both of which are types of events that are not within the control of the management of the enterprise. As defined in this Standard, a discontinuing operation must be based on a single plan by an enterprise's management to sell or otherwise dispose of a major portion of the business.

Restricted use of the term 'discontinuing operation'

43. ***A restructuring, transaction, or event that does not meet the definition of a discontinuing operation in this Standard should not be called a discontinuing operation.***

Illustrative disclosures

44. Appendix A provides examples of the presentation and disclosures required by this Standard.

Restatement of prior periods

45. ***Comparative information for prior periods that is presented in financial statements prepared after the initial disclosure event should be restated to segregate continuing and discontinuing assets, liabilities, income, expenses, and cash flows in a manner similar to that required by paragraphs 27 to 43.***

46. Appendix B illustrates application of the preceding paragraph.

Disclosure in interim financial reports

47. ***The notes to an interim financial report should describe any significant activities or events since the end of the most recent annual reporting period relating to a discontinuing operation and any significant changes in the amount or timing of cash flows relating to the assets and liabilities to be disposed of or settled.***

48. This principle is consistent with the approach in IAS 34, interim financial reporting, that the notes to an interim financial report are intended to explain significant changes since the last annual reporting date.

EFFECTIVE DATE

49. ***This International Accounting Standard becomes operative for financial statements covering periods beginning on or after 1 January 1999. Earlier application is encouraged in financial statements for periods ending after this Standard is published.***

50. This Standard supersedes paragraphs 19 to 22 of IAS 8, net profit or loss for the period, fundamental errors and changes in accounting policies.

INTERNATIONAL ACCOUNTING STANDARD IAS 36

Impairment of assets

This International Accounting Standard was approved by the IASC Board in April 1998 and becomes effective for financial statements covering periods beginning on or after 1 July 1999.

In July 1998, the approval of IAS 38, intangible assets, and IAS 22 (revised 1998), business combinations, resulted in changes in cross-references and terminology to the introduction and paragraphs 39, 40 and 110. In addition, IAS 38 added a definition of 'active market' to paragraph 5. Finally, a minor wording inconsistency in Appendix A, paragraphs A47, A48 and A57, was corrected.

In April 2000, IAS 40, investment property, amended paragraph 1. The amendment is effective for financial statements covering periods beginning on or after 1 January 2001.

In January 2001, IAS 41, Agriculture amended paragraph 1. The amendment is effective for financial statements covering periods beginning on or after 1 January 2003.

INTRODUCTION

1. This Standard ('IAS 36') prescribes the accounting and disclosure for impairment of all assets. It replaces the requirements for assessing the recoverability of an asset and recognising impairment losses that were included in:

   (a) IAS 16 (revised 1993), property, plant and equipment (see IAS 16 (revised 1998));

   (b) IAS 22 (revised 1993), business combinations (see IAS 22 (revised 1998));

   (c) IAS 28 (reformatted 1994), accounting for investments in associates (see IAS 28 (revised 1998)); and

   (d) IAS 31 (reformatted 1994), financial reporting of interests in joint ventures (see IAS 31 (revised 1998)).

   The major changes from previous requirements and explanations for the principles in IAS 36 are set out in a separate basis for conclusions.

2. IAS 36 does not cover impairment of inventories, deferred tax assets, assets arising from construction contracts, assets arising from employee benefits or most financial assets.

3. IAS 36 requires that the recoverable amount of an asset should be estimated whenever there is an indication that the asset may be impaired. In specific cases, the International Accounting Standard applicable to an asset may include requirements for additional reviews. For example, IAS 38, intangible assets, and IAS 22 (revised 1998), business combinations, require that the recoverable amount of intangible assets and goodwill that are amortised over more than 20 years should be estimated annually.

4. IAS 36 requires an impairment loss to be recognised (an asset is impaired) whenever the carrying amount of an asset exceeds its recoverable amount. An impairment loss should be recognised in the income statement for assets carried at cost and treated as a revaluation decrease for assets carried at revalued amount.

5. IAS 36 requires recoverable amount to be measured as the higher of net selling price and value in use:

   (a) net selling price is the amount obtainable from the sale of an asset in an arm's length transaction between knowledgeable, willing parties, after deducting any direct incremental disposal costs; and

   (b) value in use is the present value of estimated future cash flows expected to arise from continuing use of an asset and from its disposal at the end of its useful life.

6. In determining an asset's value in use, IAS 36 requires that an enterprise should use, among other things:

   (a) cash flow projections based on reasonable and supportable assumptions that:

      (i) reflect the asset in its current condition; and

      (ii) represent management's best estimate of the set of economic conditions that will exist over the remaining useful life of the asset; and

   (b) a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. The discount rate should not reflect risks for which future cash flows have been adjusted.

7. Recoverable amount should be estimated for an individual asset. If it is not possible to do so, IAS 36 requires an enterprise to determine recoverable amount for the cash-generating unit to which the asset belongs. A cash-generating unit is the smallest identifiable group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows from other assets or groups of assets. However, if the output produced by an asset or group of assets is traded in an active market, this asset or group of assets should be identified as a separate cash-generating unit, even if some or all of the production of this asset or group of assets is used internally. Appendix A, illustrative examples, includes examples on the identification of cash-generating units.

8. In testing a cash-generating unit for impairment, IAS 36 requires that goodwill and corporate assets (such as head office assets) that relate to the cash-generating unit should be considered. IAS 36 specifies how this should be done.

9. Principles for recognising and measuring impairment losses for a cash-generating unit are the same as those for an individual asset. IAS 36 specifies how to determine the carrying amount of a cash-generating unit and how to allocate an impairment loss between the assets of the unit.

10. IAS 36 requires that an impairment loss recognised in prior years should be reversed if, and only if, there has been a change in the estimates used to determine recoverable amount since the last impairment loss was recognised. However, an impairment loss is reversed only to the extent that it does not increase the carrying amount of an asset above the carrying amount that would have been determined for the asset (net of amortisation or depreciation) had no impairment loss been recognised in prior years. A reversal of an impairment loss should be recognised in the income statement for assets carried at cost and treated as a revaluation increase for assets carried at revalued amount.

11. IAS 36 requires that an impairment loss for goodwill should not be reversed unless:

   (a) the impairment loss was caused by a specific external event of an exceptional nature that is not expected to recur; and

   (b) subsequent external events have reversed the effect of that event.

12. When impairment losses are recognised (reversed), IAS 36 requires certain information to be disclosed:

   (a) by class of assets; and

   (b) by reportable segments based on the enterprise's primary format (only required if an enterprise applies IAS 14, segment reporting).

   IAS 36 requires further disclosure if impairment losses recognised (reversed) during the period are material to the financial statements of the reporting enterprise as a whole.

13. On first adoption, IAS 36 should be applied on a prospective basis only. Impairment losses recognised (reversed) should be treated under IAS 36 and not under the benchmark or the allowed alternative treatment for other changes in accounting policies in IAS 8, net profit or loss for the period, fundamental errors and changes in accounting policies.

14. IAS 36 is effective for accounting periods beginning on or after 1 July 1999. Earlier application is encouraged.

CONTENTS

The standards, which have been set in bold italic type, should be read in the context of the background material and implementation guidance in this Standard, and in the context of the 'Preface to International Accounting Standards'. International Accounting Standards are not intended to apply to immaterial items (see paragraph 12 of the Preface).

OBJECTIVE

The objective of this Standard is to prescribe the procedures that an enterprise applies to ensure that its assets are carried at no more than their recoverable amount. An asset is carried at more than its recoverable amount if its carrying amount exceeds the amount to be recovered through use or sale of the asset. If this is the case, the asset is described as impaired and the Standard requires the enterprise to recognise an impairment loss. The Standard also specifies when an enterprise should reverse an impairment loss and it prescribes certain disclosures for impaired assets.

SCOPE

1. ***This Standard should be applied in accounting for the impairment of all assets, other than:***

   (a) ***inventories (see IAS 2, inventories);***

   (b) ***assets arising from construction contracts (see IAS 11, construction contracts);***

   (c) ***deferred tax assets (see IAS 12, income taxes);***

   (d) ***assets arising from employee benefits (see IAS 19, employee benefits);***

   (e) ***financial assets that are included in the scope of IAS 32, financial instruments: disclosure and presentation;***

   (f) ***investment property that is measured at fair value (see IAS 40, investment Property); and***

   (g) ***biological assets related to agricultural activity that are measured at fair value less estimated point-of-sale costs (see IAS 41, agriculture).***

2. This Standard does not apply to inventories, assets arising from construction contracts, deferred tax assets or assets arising from employee benefits because existing International Accounting Standards applicable to these assets already contain specific requirements for recognising and measuring these assets.

3. This Standard applies to:

   (a) subsidiaries, as defined in IAS 27, consolidated financial statements and accounting for investments in subsidiaries;

   (b) associates, as defined in IAS 28, accounting for investments in associates; and

   (c) joint ventures, as defined in IAS 31, financial reporting of interests in joint ventures.

   For impairment of other financial assets, refer to IAS 39, Financial Instruments: Recognition and Measurement.

4. This Standard applies to assets that are carried at revalued amount (fair value) under other International Accounting Standards, such as the allowed alternative treatment in IAS 16, property, plant and equipment. However, identifying whether a revalued asset may be impaired depends on the basis used to determine fair value:

   (a) if the asset's fair value is its market value, the only difference between the asset's fair value and its net selling price is the direct incremental costs to dispose of the asset:

(i) if the disposal costs are negligible, the recoverable amount of the revalued asset is necessarily close to, or greater than, its revalued amount (fair value). In this case, after the revaluation requirements have been applied, it is unlikely that the revalued asset is impaired and recoverable amount need not be estimated; and

(ii) if the disposal costs are not negligible, net selling price of the revalued asset is necessarily less than its fair value. Therefore, the revalued asset will be impaired if its value in use is less than its revalued amount (fair value). In this case, after the revaluation requirements have been applied, an enterprise applies this Standard to determine whether the asset may be impaired; and

(b) if the asset's fair value is determined on a basis other than its market value, its revalued amount (fair value) may be greater or lower than its recoverable amount. Hence, after the revaluation requirements have been applied, an enterprise applies this Standard to determine whether the asset may be impaired.

DEFINITIONS

5. ***The following terms are used in this Standard with the meanings specified:***

Recoverable amount is the higher of an asset's net selling price and its value in use.

Value in use is the present value of estimated future cash flows expected to arise from the continuing use of an asset and from its disposal at the end of its useful life.

Net selling price is the amount obtainable from the sale of an asset in an arm's length transaction between knowledgeable, willing parties, less the costs of disposal.

Costs of disposal are incremental costs directly attributable to the disposal of an asset, excluding finance costs and income tax expense.

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

Carrying amount is the amount at which an asset is recognised in the balance sheet after deducting any accumulated depreciation (amortisation) and accumulated impairment losses thereon.

Depreciation (amortisation) is the systematic allocation of the depreciable amount of an asset over its useful life (1)***.***

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

Useful life is either:

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

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

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

(1) In the case of an intangible asset or goodwill, the term 'amortisation' is generally used instead of 'depreciation'. Both terms have the same meaning.

Corporate assets are assets other than goodwill that contribute to the future cash flows of both the cash-generating unit under review and other cash-generating units.

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

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

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

(c) ***prices are available to the public.***

IDENTIFYING AN ASSET THAT MAY BE IMPAIRED

6. Paragraphs 7 to 14 specify when recoverable amount should be determined. These requirements use the term 'an asset' but apply equally to an individual asset or a cash-generating unit.

7. An asset is impaired when the carrying amount of the asset exceeds its recoverable amount. Paragraphs 9 to 11 describe some indications that an impairment loss may have occurred: if any of those indications is present, an enterprise is required to make a formal estimate of recoverable amount. If no indication of a potential impairment loss is present, this Standard does not require an enterprise to make a formal estimate of recoverable amount.

8. ***An enterprise should assess at each balance sheet date whether there is any indication that an asset may be impaired. If any such indication exists, the enterprise should estimate the recoverable amount of the asset.***

9. ***In assessing whether there is any indication that an asset may be impaired, an enterprise should consider, as a minimum, the following indications:***

External sources of information

(a) ***during the period, an asset's market value has declined significantly more than would be expected as a result of the passage of time or normal use;***

(b) ***significant changes with an adverse effect on the enterprise have taken place during the period, or will take place in the near future, in the technological, market, economic or legal environment in which the enterprise operates or in the market to which an asset is dedicated;***

(c) ***market interest rates or other market rates of return on investments have increased during the period, and those increases are likely to affect the discount rate used in calculating an asset's value in use and decrease the asset's recoverable amount materially;***

(d) ***the carrying amount of the net assets of the reporting enterprise is more than its market capitalisation;***

Internal sources of information

(e) ***evidence is available of obsolescence or physical damage of an asset;***

(f) ***significant changes with an adverse effect on the enterprise have taken place during the period, or are expected to take place in the near future, in the extent to which, or manner in which, an asset is used or is expected to be used. These changes include plans to discontinue or restructure the operation to which an asset belongs or to dispose of an asset before the previously expected date; and***

(g) ***evidence is available from internal reporting that indicates that the economic performance of an asset is, or will be, worse than expected.***

10. The list in paragraph 9 is not exhaustive. An enterprise may identify other indications that an asset may be impaired and these would also require the enterprise to determine the asset's recoverable amount.

11. Evidence from internal reporting that indicates that an asset may be impaired includes the existence of:

(a) cash flows for acquiring the asset, or subsequent cash needs for operating or maintaining it, that are significantly higher than those originally budgeted;

(b) actual net cash flows or operating profit or loss flowing from the asset that are significantly worse than those budgeted;

(c) a significant decline in budgeted net cash flows or operating profit, or a significant increase in budgeted loss, flowing from the asset; or

(d) operating losses or net cash outflows for the asset, when current period figures are aggregated with budgeted figures for the future.

12. The concept of materiality applies in identifying whether the recoverable amount of an asset needs to be estimated. For example, if previous calculations show that an asset's recoverable amount is significantly greater than its carrying amount, the enterprise need not re-estimate the asset's recoverable amount if no events have occurred that would eliminate that difference. Similarly, previous analysis may show that an asset's recoverable amount is not sensitive to one (or more) of the indications listed in paragraph 9.

13. As an illustration of paragraph 12, if market interest rates or other market rates of return on investments have increased during the period, an enterprise is not required to make a formal estimate of an asset's recoverable amount in the following cases:

(a) if the discount rate used in calculating the asset's value in use is unlikely to be affected by the increase in these market rates. For example, increases in short-term interest rates may not have a material effect on the discount rate used for an asset that has a long remaining useful life; or

(b) if the discount rate used in calculating the asset's value in use is likely to be affected by the increase in these market rates but previous sensitivity analysis of recoverable amount shows that:

(i) it is unlikely that there will be a material decrease in recoverable amount because future cash flows are also likely to increase. For example, in some cases, an enterprise may be able to demonstrate that it adjusts its revenues to compensate for any increase in market rates; or

(ii) the decrease in recoverable amount is unlikely to result in a material impairment loss.

14. If there is an indication that an asset may be impaired, this may indicate that the remaining useful life, the depreciation (amortisation) method or the residual value for the asset need to be reviewed and adjusted under the International Accounting Standard applicable to the asset, even if no impairment loss is recognised for the asset.

MEASUREMENT OF RECOVERABLE AMOUNT

15. This Standard defines recoverable amount as the higher of an asset's net selling price and value in use. Paragraphs 16 to 56 set out the requirements for measuring recoverable amount. These requirements use the term 'an asset' but apply equally to an individual asset or a cash-generating unit.

16. It is not always necessary to determine both an asset's net selling price and its value in use. For example, if either of these amounts exceeds the asset's carrying amount, the asset is not impaired and it is not necessary to estimate the other amount.

17. It may be possible to determine net selling price, even if an asset is not traded in an active market. However, sometimes it will not be possible to determine net selling price because there is no basis for making a reliable estimate of the amount obtainable from the sale of the asset in an arm's length transaction between knowledgeable and willing parties. In this case, the recoverable amount of the asset may be taken to be its value in use.

18. If there is no reason to believe that an asset's value in use materially exceeds its net selling price, the asset's recoverable amount may be taken to be its net selling price. This will often be the case for an asset that is held for disposal. This is because the value in use of an asset held for disposal will consist mainly of the net disposal proceeds, since the future cash flows from continuing use of the asset until its disposal are likely to be negligible.

19. Recoverable amount is determined for an individual asset, unless the asset does not generate cash inflows from continuing use that are largely independent of those from other assets or groups of assets. If this is the case, recoverable amount is determined for the cash-generating unit to which the asset belongs (see paragraphs 64 to 87), unless either:

    (a) the asset's net selling price is higher than its carrying amount; or

    (b) the asset's value in use can be estimated to be close to its net selling price and net selling price can be determined.

20. In some cases, estimates, averages and computational shortcuts may provide a reasonable approximation of the detailed computations illustrated in this Standard for determining net selling price or value in use.

Net selling price

21. The best evidence of an asset's net selling price is a price in a binding sale agreement in an arm's length transaction, adjusted for incremental costs that would be directly attributable to the disposal of the asset.

22. If there is no binding sale agreement but an asset is traded in an active market, net selling price is the asset's market price less the costs of disposal. The appropriate market price is usually the current bid price. When current bid prices are unavailable, the price of the most recent transaction may provide a basis from which to estimate net selling price, provided that there has not been a significant change in economic circumstances between the transaction date and the date at which the estimate is made.

23. If there is no binding sale agreement or active market for an asset, net selling price is based on the best information available to reflect the amount that an enterprise could obtain, at the balance sheet date, for the disposal of the asset in an arm's length transaction between knowledgeable, willing parties, after deducting the costs of disposal. In determining this amount, an enterprise considers the outcome of recent transactions for similar assets within the same industry. Net selling price does not reflect a forced sale, unless management is compelled to sell immediately.

24. Costs of disposal, other than those that have already been recognised as liabilities, are deducted in determining net selling price. Examples of such costs are legal costs, stamp duty and similar transaction taxes, costs of removing the asset, and direct incremental costs to bring an asset into condition for its sale. However, termination benefits (as defined in IAS 19, employee benefits) and costs associated with reducing or reorganising a business following the disposal of an asset are not direct incremental costs to dispose of the asset.

25. Sometimes, the disposal of an asset would require the buyer to take over a liability and only a single net selling price is available for both the asset and the liability. Paragraph 77 explains how to deal with such cases.

Value in use

26. Estimating the value in use of an asset involves the following steps:

(a) estimating the future cash inflows and outflows to be derived from continuing use of the asset and from its ultimate disposal; and

(b) applying the appropriate discount rate to these future cash flows.

Basis for estimates of future cash flows

27. ***In measuring value in use:***

(a) ***cash flow projections should be based on reasonable and supportable assumptions that represent management's best estimate of the set of economic conditions that will exist over the remaining useful life of the asset. Greater weight should be given to external evidence;***

(b) ***cash flow projections should be based on the most recent financial budgets/forecasts that have been approved by management. Projections based on these budgets/forecasts should cover a maximum period of five years, unless a longer period can be justified; and***

(c) ***cash flow projections beyond the period covered by the most recent budgets/forecasts should be estimated by extrapolating the projections based on the budgets/forecasts using a steady or declining growth rate for subsequent years, unless an increasing rate can be justified. This growth rate should not exceed the long-term average growth rate for the products, industries, or country or countries in which the enterprise operates, or for the market in which the asset is used, unless a higher rate can be justified.***

28. Detailed, explicit and reliable financial budgets/forecasts of future cash flows for periods longer than five years are generally not available. For this reason, management's estimates of future cash flows are based on the most recent budgets/forecasts for a maximum of five years. Management may use cash flow projections based on financial budgets/forecasts over a period longer than five years if management is confident that these projections are reliable and it can demonstrate its ability, based on past experience, to forecast cash flows accurately over that longer period.

29. Cash flow projections until the end of an asset's useful life are estimated by extrapolating the cash flow projections based on the financial budgets/forecasts using a growth rate for subsequent years. This rate is steady or declining, unless an increase in the rate matches objective information about patterns over a product or industry lifecycle. If appropriate, the growth rate is zero or negative.

30. Where conditions are very favourable, competitors are likely to enter the market and restrict growth. Therefore, enterprises will have difficulty in exceeding the average historical growth rate over the long term (say, 20 years) for the products, industries, or country or countries in which the enterprise operates, or for the market in which the asset is used.

31. In using information from financial budgets/forecasts, an enterprise considers whether the information reflects reasonable and supportable assumptions and represents management's best estimate of the set of economic conditions that will exist over the remaining useful life of the asset.

Composition of estimates of future cash flows

32. ***Estimates of future cash flows should include:***

    (a) ***projections of cash inflows from the continuing use of the asset;***

    (b) ***projections of cash outflows that are necessarily incurred to generate the cash inflows from continuing use of the asset (including cash outflows to prepare the asset for use) and that can be directly attributed, or allocated on a reasonable and consistent basis, to the asset; and***

    (c) ***net cash flows, if any, to be received (or paid) for the disposal of the asset at the end of its useful life.***

33. Estimates of future cash flows and the discount rate reflect consistent assumptions about price increases due to general inflation. Therefore, if the discount rate includes the effect of price increases due to general inflation, future cash flows are estimated in nominal terms. If the discount rate excludes the effect of price increases due to general inflation, future cash flows are estimated in real terms (but include future specific price increases or decreases).

34. Projections of cash outflows include future overheads that can be attributed directly, or allocated on a reasonable and consistent basis, to the use of the asset.

35. When the carrying amount of an asset does not yet include all the cash outflows to be incurred before it is ready for use or sale, the estimate of future cash outflows includes an estimate of any further cash outflow that is expected to be incurred before the asset is ready for use or sale. For example, this is the case for a building under construction or for a development project that is not yet completed.

36. To avoid double counting, estimates of future cash flows do not include:

    (a) cash inflows from assets that generate cash inflows from continuing use that are largely independent of the cash inflows from the asset under review (for example, financial assets such as receivables); and

    (b) cash outflows that relate to obligations that have already been recognised as liabilities (for example, payables, pensions or provisions).

37. ***Future cash flows should be estimated for the asset in its current condition. Estimates of future cash flows should not include estimated future cash inflows or outflows that are expected to arise from:***

    (a) ***a future restructuring to which an enterprise is not yet committed; or***

    (b) ***future capital expenditure that will improve or enhance the asset in excess of its originally assessed standard of performance.***

38. Because future cash flows are estimated for the asset in its current condition, value in use does not reflect:

    (a) future cash outflows or related cost savings (for example reductions in staff costs) or benefits that are expected to arise from a future restructuring to which an enterprise is not yet committed; or

    (b) future capital expenditure that will improve or enhance the asset in excess of its originally assessed standard of performance or the related future benefits from this future expenditure.

39. A restructuring is a programme that is planned and controlled by management and that materially changes either the scope of the business undertaken by an enterprise or the manner in which the business is conducted. IAS 37, provisions, contingent liabilities and contingent assets, gives guidance that may clarify when an enterprise is committed to a restructuring.

40. When an enterprise becomes committed to a restructuring, some assets are likely to be affected by this restructuring. Once the enterprise is committed to the restructuring:

(a) in determining value in use, estimates of future cash inflows and cash outflows reflect the cost savings and other benefits from the restructuring (based on the most recent financial budgets/forecasts that have been approved by management); and

(b) estimates of future cash outflows for the restructuring are dealt with in a restructuring provision under IAS 37, provisions, contingent liabilities and contingent assets.

Appendix A, Example 5, illustrates the effect of a future restructuring on a value in use calculation.

41. Until an enterprise incurs capital expenditure that improves or enhances an asset in excess of its originally assessed standard of performance, estimates of future cash flows do not include the estimated future cash inflows that are expected to arise from this expenditure (see Appendix A, Example 6).

42. Estimates of future cash flows include future capital expenditure necessary to maintain or sustain an asset at its originally assessed standard of performance.

43. ***Estimates of future cash flows should not include:***

(a) ***cash inflows or outflows from financing activities; or***

(b) ***income tax receipts or payments.***

44. Estimated future cash flows reflect assumptions that are consistent with the way the discount rate is determined. Otherwise, the effect of some assumptions will be counted twice or ignored. Because the time value of money is considered by discounting the estimated future cash flows, these cash flows exclude cash inflows or outflows from financing activities. Similarly, since the discount rate is determined on a pre-tax basis, future cash flows are also estimated on a pre-tax basis.

45. ***The estimate of net cash flows to be received (or paid) for the disposal of an asset at the end of its useful life should be the amount that an enterprise expects to obtain from the disposal of the asset in an arm's length transaction between knowledgeable, willing parties, after deducting the estimated costs of disposal.***

46. The estimate of net cash flows to be received (or paid) for the disposal of an asset at the end of its useful life is determined in a similar way to an asset's net selling price, except that, in estimating those net cash flows:

(a) an enterprise uses prices prevailing at the date of the estimate for similar assets that have reached the end of their useful life and that have operated under conditions similar to those in which the asset will be used; and

(b) those prices are adjusted for the effect of both future price increases due to general inflation and specific future price increases (decreases). However, if estimates of future cash flows from the asset's continuing use and the discount rate exclude the effect of general inflation, this effect is also excluded from the estimate of net cash flows on disposal.

Foreign currency future cash flows

47. Future cash flows are estimated in the currency in which they will be generated and then discounted using a discount rate appropriate for that currency. An enterprise translates the present value obtained using the spot exchange rate at the balance sheet date (described in IAS 21, the effects of changes in foreign exchange rates, as the closing rate).

Discount rate

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

49. A rate that reflects current market assessments of the time value of money and the risks specific to the asset is the return that investors would require if they were to choose an investment that would generate cash flows of amounts, timing and risk profile equivalent to those that the enterprise expects to derive from the asset. This rate is estimated from the rate implicit in current market transactions for similar assets or from the weighted average cost of capital of a listed enterprise that has a single asset (or a portfolio of assets) similar in terms of service potential and risks to the asset under review.

50. When an asset-specific rate is not directly available from the market, an enterprise uses surrogates to estimate the discount rate. The purpose is to estimate, as far as possible, a market assessment of:

   (a) the time value of money for the periods until the end of the asset's useful life; and

   (b) the risks that the future cash flows will differ in amount or timing from estimates.

51. As a starting point, the enterprise may take into account the following rates:

   (a) the enterprise's weighted average cost of capital determined using techniques such as the capital asset pricing model;

   (b) the enterprise's incremental borrowing rate; and

   (c) other market borrowing rates.

52. These rates are adjusted:

   (a) to reflect the way that the market would assess the specific risks associated with the projected cash flows; and

   (b) to exclude risks that are not relevant to the projected cash flows.

   Consideration is given to risks such as country risk, currency risk, price risk and cash flow risk.

53. To avoid double counting, the discount rate does not reflect risks for which future cash flow estimates have been adjusted.

54. The discount rate is independent of the enterprise's capital structure and the way the enterprise financed the purchase of the asset because the future cash flows expected to arise from an asset do not depend on the way in which the enterprise financed the purchase of the asset.

55. When the basis for the rate is post-tax, that basis is adjusted to reflect a pre-tax rate.

56. An enterprise normally uses a single discount rate for the estimate of an asset's value in use. However, an enterprise uses separate discount rates for different future periods where value in use is sensitive to a difference in risks for different periods or to the term structure of interest rates.

RECOGNITION AND MEASUREMENT OF AN IMPAIRMENT LOSS

57. Paragraphs 58 to 63 set out the requirements for recognising and measuring impairment losses for an individual asset. Recognition and measurement of impairment losses for a cash-generating unit are dealt with in paragraphs 88 to 93.

58. ***If, and only if, the recoverable amount of an asset is less than its carrying amount, the carrying amount of the asset should be reduced to its recoverable amount. That reduction is an impairment loss.***

59. ***An impairment loss should be recognised as an expense in the income statement immediately, unless the asset is carried at revalued amount under another International Accounting Standard (for example, under the allowed alternative treatment in IAS 16, property, plant and equipment). Any impairment loss of a revalued asset should be treated as a revaluation decrease under that other International Accounting Standard.***

60. An impairment loss on a revalued asset is recognised as an expense in the income statement. However, an impairment loss on a revalued asset is recognised directly against any revaluation surplus for the asset to the extent that the impairment loss does not exceed the amount held in the revaluation surplus for that same asset.

61. ***When the amount estimated for an impairment loss is greater than the carrying amount of the asset to which it relates, an enterprise should recognise a liability if, and only if, that is required by another International Accounting Standard.***

62. ***After the recognition of an impairment loss, the depreciation (amortisation) charge for the asset should be adjusted in future periods to allocate the asset's revised carrying amount, less its residual value (if any), on a systematic basis over its remaining useful life.***

63. If an impairment loss is recognised, any related deferred tax assets or liabilities are determined under IAS 12, income taxes, by comparing the revised carrying amount of the asset with its tax base (see Appendix A, Example 3).

CASH-GENERATING UNITS

64. Paragraphs 65 to 93 set out the requirements for identifying the cash-generating unit to which an asset belongs and determining the carrying amount of, and recognising impairment losses for, cash-generating units.

Identification of the cash-generating unit to which an asset belongs

65. ***If there is any indication that an asset may be impaired, recoverable amount should be estimated for the individual asset. If it is not possible to estimate the recoverable amount of the individual asset, an enterprise should determine the recoverable amount of the cash-generating unit to which the asset belongs (the asset's cash-generating unit).***

66. The recoverable amount of an individual asset cannot be determined if:

(a) the asset's value in use cannot be estimated to be close to its net selling price (for example, when the future cash flows from continuing use of the asset cannot be estimated to be negligible); and

(b) the asset does not generate cash inflows from continuing use that are largely independent of those from other assets. In such cases, value in use and, therefore, recoverable amount, can be determined only for the asset's cash-generating unit.

Example

A mining enterprise owns a private railway to support its mining activities. The private railway could be sold only for scrap value and the private railway does not generate cash inflows from continuing use that are largely independent of the cash inflows from the other assets of the mine.

It is not possible to estimate the recoverable amount of the private railway because the value in use of the private railway cannot be determined and it is probably different from scrap value. Therefore, the enterprise estimates the recoverable amount of the cash-generating unit to which the private railway belongs, that is, the mine as a whole.

67. As defined in paragraph 5, an asset's cash-generating unit is the smallest group of assets that includes the asset and that generates cash inflows from continuing use that are largely independent of the cash inflows from other assets or groups of assets. Identification of an asset's cash-generating unit involves judgement. If recoverable amount cannot be determined for an individual asset, an enterprise identifies the lowest aggregation of assets that generate largely independent cash inflows from continuing use.

Example

A bus company provides services under contract with a municipality that requires minimum service on each of five separate routes. Assets devoted to each route and the cash flows from each route can be identified separately. One of the routes operates at a significant loss.

Because the enterprise does not have the option to curtail any one bus route, the lowest level of identifiable cash inflows from continuing use that are largely independent of the cash inflows from other assets or groups of assets is the cash inflows generated by the five routes together. The cash-generating unit for each route is the bus company as a whole.

68. Cash inflows from continuing use are inflows of cash and cash equivalents received from parties outside the reporting enterprise. In identifying whether cash inflows from an asset (or group of assets) are largely independent of the cash inflows from other assets (or groups of assets), an enterprise considers various factors including how management monitors the enterprise's operations (such as by product lines, businesses, individual locations, districts or regional areas or in some other way) or how management makes decisions about continuing or disposing of the enterprise's assets and operations. Appendix A, Example 1, gives examples of identification of a cash-generating unit.

69. ***If an active market exists for the output produced by an asset or a group of assets, this asset or group of assets should be identified as a cash-generating unit, even if some or all of the output is used internally. If this is the case, management's best estimate of future market prices for the output should be used:***

(a) ***in determining the value in use of this cash-generating unit, when estimating the future cash inflows that relate to the internal use of the output; and***

(b) ***in determining the value in use of other cash-generating units of the reporting enterprise, when estimating the future cash outflows that relate to the internal use of the output.***

70. Even if part or all of the output produced by an asset or a group of assets is used by other units of the reporting enterprise (for example, products at an intermediate stage of a production process), this asset or group of assets forms a separate cash-generating unit if the enterprise could sell this output on an active market. This is because this asset or group of assets could generate cash inflows from continuing use that

would be largely independent of the cash inflows from other assets or groups of assets. In using information based on financial budgets/forecasts that relates to such a cash-generating unit, an enterprise adjusts this information if internal transfer prices do not reflect management's best estimate of future market prices for the cash-generating unit's output.

71. ***Cash-generating units should be identified consistently from period to period for the same asset or types of assets, unless a change is justified.***

72. If an enterprise determines that an asset belongs to a different cash-generating unit than in previous periods, or that the types of assets aggregated for the asset's cash-generating unit have changed, paragraph 117 requires certain disclosures about the cash-generating unit, if an impairment loss is recognised or reversed for the cash-generating unit and is material to the financial statements of the reporting enterprise as a whole.

Recoverable amount and carrying amount of a cash-generating unit

73. The recoverable amount of a cash-generating unit is the higher of the cash-generating unit's net selling price and value in use. For the purpose of determining the recoverable amount of a cash-generating unit, any reference in paragraphs 16 to 56 to 'an asset' is read as a reference to 'a cash-generating unit'.

74. ***The carrying amount of a cash-generating unit should be determined consistently with the way the recoverable amount of the cash-generating unit is determined.***

75. The carrying amount of a cash-generating unit:

(a) includes the carrying amount of only those assets that can be attributed directly, or allocated on a reasonable and consistent basis, to the cash-generating unit and that will generate the future cash inflows estimated in determining the cash-generating unit's value in use; and

(b) does not include the carrying amount of any recognised liability, unless the recoverable amount of the cash-generating unit cannot be determined without consideration of this liability.

This is because net selling price and value in use of a cash-generating unit are determined excluding cash flows that relate to assets that are not part of the cash-generating unit and liabilities that have already been recognised in the financial statements (see paragraphs 24 and 36).

76. Where assets are grouped for recoverability assessments, it is important to include in the cash-generating unit all assets that generate the relevant stream of cash inflows from continuing use. Otherwise, the cash-generating unit may appear to be fully recoverable when in fact an impairment loss has occurred. In some cases, although certain assets contribute to the estimated future cash flows of a cash-generating unit, they cannot be allocated to the cash-generating unit on a reasonable and consistent basis. This might be the case for goodwill or corporate assets such as head office assets. Paragraphs 79 to 87 explain how to deal with these assets in testing a cash-generating unit for impairment.

77. It may be necessary to consider certain recognised liabilities in order to determine the recoverable amount of a cash-generating unit. This may occur if the disposal of a cash-generating unit would require the buyer to take over a liability. In this case, the net selling price (or the estimated cash flow from ultimate disposal) of the cash-generating unit is the estimated selling price for the assets of the cash-generating unit and the liability together, less the costs of disposal. In order to perform a meaningful comparison between the carrying amount of the cash-generating unit and its recoverable amount, the carrying amount of the liability is deducted in determining both the cash-generating unit's value in use and its carrying amount.

Example

A company operates a mine in a country where legislation requires that the owner must restore the site on completion of its mining operations. The cost of restoration includes the replacement of the overburden, which must be removed before mining operations commence. A provision for the costs to replace the overburden was recognised as soon as the overburden was removed. The amount provided was recognised as part of the cost of the mine and is being depreciated over the mine's useful life. The carrying amount of the provision for restoration costs is 500, which is equal to the present value of the restoration costs.

The enterprise is testing the mine for impairment. The cash-generating unit for the mine is the mine as a whole. The enterprise has received various offers to buy the mine at a price of around 800; this price encompasses the fact that the buyer will take over the obligation to restore the overburden. Disposal costs for the mine are negligible. The value in use of the mine is approximately 1 200, excluding restoration costs. The carrying amount of the mine is 1 000.

The net selling price for the cash-generating unit is 800. This amount considers restoration costs that have already been provided for. As a consequence, the value in use for the cash-generating unit is determined after consideration of the restoration costs and is estimated to be 700 (1 200 less 500). The carrying amount of the cash-generating unit is 500, which is the carrying amount of the mine (1 000) less the carrying amount of the provision for restoration costs (500).

78. For practical reasons, the recoverable amount of a cash-generating unit is sometimes determined after consideration of assets that are not part of the cash-generating unit (for example, receivables or other financial assets) or liabilities that have already been recognised in the financial statements (for example, payables, pensions and other provisions). In such cases, the carrying amount of the cash-generating unit is increased by the carrying amount of those assets and decreased by the carrying amount of those liabilities.

Goodwill

79. Goodwill arising on acquisition represents a payment made by an acquirer in anticipation of future economic benefits. The future economic benefits may result from synergy between the identifiable assets acquired or from assets which, individually, do not qualify for recognition in the financial statements. Goodwill does not generate cash flows independently from other assets or groups of assets and, therefore, the recoverable amount of goodwill as an individual asset cannot be determined. As a consequence, if there is an indication that goodwill may be impaired, recoverable amount is determined for the cash-generating unit to which goodwill belongs. This amount is then compared to the carrying amount of this cash-generating unit and any impairment loss is recognised in accordance with paragraph 88.

80. ***In testing a cash-generating unit for impairment, an enterprise should identify whether goodwill that relates to this cash-generating unit is recognised in the financial statements. If this is the case, an enterprise should:***

(a) ***perform a 'bottom-up' test, that is, the enterprise should:***

(i) ***identify whether the carrying amount of goodwill can be allocated on a reasonable and consistent basis to the cash-generating unit under review; and***

(ii) ***then, compare the recoverable amount of the cash-generating unit under review to its carrying amount (including the carrying amount of allocated goodwill, if any) and recognise any impairment loss in accordance with paragraph 88.***

The enterprise should perform the second step of the 'bottom-up' test even if none of the carrying amount of goodwill can be allocated on a reasonable and consistent basis to the cash-generating unit under review; and

(b) ***if, in performing the 'bottom-up' test, the enterprise could not allocate the carrying amount of goodwill on a reasonable and consistent basis to the cash-generating unit under review, the enterprise should also perform a 'top-down' test, that is, the enterprise should:***

(i) ***identify the smallest cash-generating unit that includes the cash-generating unit under review and to which the carrying amount of goodwill can be allocated on a reasonable and consistent basis (the 'larger' cash-generating unit); and***

(ii) ***then, compare the recoverable amount of the larger cash-generating unit to its carrying amount (including the carrying amount of allocated goodwill) and recognise any impairment loss in accordance with paragraph 88.***

81. Whenever a cash-generating unit is tested for impairment, an enterprise considers any goodwill that is associated with the future cash flows to be generated by the cash-generating unit. If goodwill can be allocated on a reasonable and consistent basis, an enterprise applies the 'bottom-up' test only. If it is not possible to allocate goodwill on a reasonable and consistent basis, an enterprise applies both the 'bottom-up' test and 'top-down' test (see Appendix A, Example 7).

82. The 'bottom-up' test ensures that an enterprise recognises any impairment loss that exists for a cash-generating unit, including for goodwill that can be allocated on a reasonable and consistent basis. Whenever it is impracticable to allocate goodwill on a reasonable and consistent basis in the 'bottom-up' test, the combination of the 'bottom-up' and the 'top-down' test ensures that an enterprise recognises:

(a) first, any impairment loss that exists for the cash-generating unit excluding any consideration of goodwill; and

(b) then, any impairment loss that exists for goodwill. Because an enterprise applies the 'bottom-up' test first to all assets that may be impaired, any impairment loss identified for the larger cash-generating unit in the 'top-down' test relates only to goodwill allocated to the larger unit.

83. If the 'top-down' test is applied, an enterprise formally determines the recoverable amount of the larger cash-generating unit, unless there is persuasive evidence that there is no risk that the larger cash-generating unit is impaired (see paragraph 12).

Corporate assets

84. Corporate assets include group or divisional assets such as the building of a headquarters or a division of the enterprise, EDP equipment or a research centre. The structure of an enterprise determines whether an asset meets this Standard's definition of corporate assets for a particular cash-generating unit. Key characteristics of corporate assets are that they do not generate cash inflows independently from other assets or groups of assets and their carrying amount cannot be fully attributed to the cash-generating unit under review.

85. Because corporate assets do not generate separate cash inflows, the recoverable amount of an individual corporate asset cannot be determined unless management has decided to dispose of the asset. As a consequence, if there is an indication that a corporate asset may be impaired, recoverable amount is determined for the cash-generating unit to which the corporate asset belongs, compared to the carrying amount of this cash-generating unit and any impairment loss is recognised in accordance with paragraph 88.

86. ***In testing a cash-generating unit for impairment, an enterprise should identify all the corporate assets that relate to the cash-generating unit under review. For each identified corporate asset, an enterprise should then apply paragraph 80, that is:***

    (a) ***if the carrying amount of the corporate asset can be allocated on a reasonable and consistent basis to the cash-generating unit under review, an enterprise should apply the 'bottom-up' test only; and***

    (b) ***if the carrying amount of the corporate asset cannot be allocated on a reasonable and consistent basis to the cash-generating unit under review, an enterprise should apply both the 'bottom-up' and 'top-down' tests.***

87. An example of how to deal with corporate assets can be found in Appendix A, Example 8.

Impairment loss for a cash-generating unit

88. ***An impairment loss should be recognised for a cash-generating unit if, and only if, its recoverable amount is less than its carrying amount. The impairment loss should be allocated to reduce the carrying amount of the assets of the unit in the following order:***

    (a) ***first, to goodwill allocated to the cash-generating unit (if any); and***

    (b) ***then, to the other assets of the unit on a pro-rata basis based on the carrying amount of each asset in the unit.***

    These reductions in carrying amounts should be treated as impairment losses on individual assets and recognised in accordance with paragraph 59.

89. ***In allocating an impairment loss under paragraph 88, the carrying amount of an asset should not be reduced below the highest of:***

    (a) ***its net selling price (if determinable);***

    (b) ***its value in use (if determinable); and***

    (c) ***zero.***

    The amount of the impairment loss that would otherwise have been allocated to the asset should be allocated to the other assets of the unit on a pro-rata basis.

90. The goodwill allocated to a cash-generating unit is reduced before reducing the carrying amount of the other assets of the unit because of its nature.

91. If there is no practical way to estimate the recoverable amount of each individual asset of a cash-generating unit, this Standard requires an arbitrary allocation of an impairment loss between the assets of that unit, other than goodwill, because all assets of a cash-generating unit work together.

92. If the recoverable amount of an individual asset cannot be determined (see paragraph 66):

    (a) an impairment loss is recognised for the asset if its carrying amount is greater than the higher of its net selling price and the results of the allocation procedures described in paragraphs 88 and 89; and

    (b) no impairment loss is recognised for the asset if the related cash-generating unit is not impaired. This applies even if the asset's net selling price is less than its carrying amount.

Example

A machine has suffered physical damage but is still working, although not as well as it used to. The net selling price of the machine is less than its carrying amount. The machine does not generate independent cash inflows from continuing use. The smallest identifiable group of assets that includes the machine and generates cash inflows from continuing use that are largely independent of the cash inflows from other assets is the production line to which the machine belongs. The recoverable amount of the production line shows that the production line taken as a whole is not impaired.

Assumption 1: budgets/forecasts approved by management reflect no commitment of management to replace the machine.

The recoverable amount of the machine alone cannot be estimated since the machine's value in use:

(a) may differ from its net selling price; and

(b) can be determined only for the cash-generating unit to which the machine belongs (the production line).

The production line is not impaired, therefore, no impairment loss is recognised for the machine. Nevertheless, the enterprise may need to reassess the depreciation period or the depreciation method for the machine. Perhaps, a shorter depreciation period or a faster depreciation method is required to reflect the expected remaining useful life of the machine or the pattern in which economic benefits are consumed by the enterprise.

Assumption 2: budgets/forecasts approved by management reflect a commitment of management to replace the machine and sell it in the near future. Cash flows from continuing use of the machine until its disposal are estimated to be negligible.

The machine's value in use can be estimated to be close to its net selling price. Therefore, the recoverable amount of the machine can be determined and no consideration is given to the cash-generating unit to which the machine belongs (the production line). Since the machine's net selling price is less than its carrying amount, an impairment loss is recognised for the machine.

93. ***After the requirements in paragraphs 88 and 89 have been applied, a liability should be recognised for any remaining amount of an impairment loss for a cash-generating unit if, and only if, that is required by other International Accounting Standards.***

REVERSAL OF AN IMPAIRMENT LOSS

94. Paragraphs 95 to 101 set out the requirements for reversing an impairment loss recognised for an asset or a cash-generating unit in prior years. These requirements use the term 'an asset' but apply equally to an individual asset or a cash-generating unit. Additional requirements are set out for an individual asset in paragraphs 102 to 106, for a cash generating unit in paragraphs 107 to 108 and for goodwill in paragraphs 109 to 112.

95. ***An enterprise should assess at each balance sheet date whether there is any indication that an impairment loss recognised for an asset in prior years may no longer exist or may have decreased. If any such indication exists, the enterprise should estimate the recoverable amount of that asset.***

96. ***In assessing whether there is any indication that an impairment loss recognised for an asset in prior years may no longer exist or may have decreased, an enterprise should consider, as a minimum, the following indications:***

External sources of information

(a) ***the asset's market value has increased significantly during the period;***

(b) ***significant changes with a favourable effect on the enterprise have taken place during the period, or will take place in the near future, in the technological, market, economic or legal environment in which the enterprise operates or in the market to which the asset is dedicated;***

(c) ***market interest rates or other market rates of return on investments have decreased during the period, and those decreases are likely to affect the discount rate used in calculating the asset's value in use and increase the asset's recoverable amount materially;***

Internal sources of information

(d) ***significant changes with a favourable effect on the enterprise have taken place during the period, or are expected to take place in the near future, in the extent to which, or manner in which, the asset is used or is expected to be used. These changes include capital expenditure that has been incurred during the period to improve or enhance an asset in excess of its originally assessed standard of performance or a commitment to discontinue or restructure the operation to which the asset belongs; and***

(e) ***evidence is available from internal reporting that indicates that the economic performance of the asset is, or will be, better than expected.***

97. Indications of a potential decrease in an impairment loss in paragraph 96 mainly mirror the indications of a potential impairment loss in paragraph 9. The concept of materiality applies in identifying whether an impairment loss recognised for an asset in prior years may need to be reversed and the recoverable amount of the asset determined.

98. If there is an indication that an impairment loss recognised for an asset may no longer exist or may have decreased, this may indicate that the remaining useful life, the depreciation (amortisation) method or the residual value may need to be reviewed and adjusted in accordance with the International Accounting Standard applicable to the asset, even if no impairment loss is reversed for the asset.

99. ***An impairment loss recognised for an asset in prior years should be reversed if, and only if, there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised. If this is the case, the carrying amount of the asset should be increased to its recoverable amount. That increase is a reversal of an impairment loss.***

100. A reversal of an impairment loss reflects an increase in the estimated service potential of an asset, either from use or sale, since the date when an enterprise last recognised an impairment loss for that asset. An enterprise is required to identify the change in estimates that causes the increase in estimated service potential. Examples of changes in estimates include:

(a) a change in the basis for recoverable amount (i.e., whether recoverable amount is based on net selling price or value in use);

(b) if recoverable amount was based on value in use: a change in the amount or timing of estimated future cash flows or in the discount rate; or

(c) if recoverable amount was based on net selling price: a change in estimate of the components of net selling price.

101. An asset's value in use may become greater than the asset's carrying amount simply because the present value of future cash inflows increases as they become closer. However, the service potential of the asset has not increased. Therefore, an impairment loss is not reversed just because of the passage of time (sometimes called the 'unwinding' of the discount), even if the recoverable amount of the asset becomes higher than its carrying amount.

Reversal of an impairment loss for an individual asset

102. ***The increased carrying amount of an asset due to a reversal of an impairment loss should not exceed the carrying amount that would have been determined (net of amortisation or depreciation) had no impairment loss been recognised for the asset in prior years.***

103. Any increase in the carrying amount of an asset above the carrying amount that would have been determined (net of amortisation or depreciation) had no impairment loss been recognised for the asset in prior years is a revaluation. In accounting for such a revaluation, an enterprise applies the International Accounting Standard applicable to the asset.

104. ***A reversal of an impairment loss for an asset should be recognised as income immediately in the income statement, unless the asset is carried at revalued amount under another International Accounting Standard (for example, under the allowed alternative treatment in IAS 16, property, plant and equipment). Any reversal of an impairment loss on a revalued asset should be treated as a revaluation increase under that other International Accounting Standard.***

105. A reversal of an impairment loss on a revalued asset is credited directly to equity under the heading revaluation surplus. However, to the extent that an impairment loss on the same revalued asset was previously recognised as an expense in the income statement, a reversal of that impairment loss is recognised as income in the income statement.

106. ***After a reversal of an impairment loss is recognised, the depreciation (amortisation) charge for the asset should be adjusted in future periods to allocate the asset's revised carrying amount, less its residual value (if any), on a systematic basis over its remaining useful life.***

Reversal of an impairment loss for a cash-generating unit

107. ***A reversal of an impairment loss for a cash-generating unit should be allocated to increase the carrying amount of the assets of the unit in the following order:***

(a) ***first, assets other than goodwill on a pro-rata basis based on the carrying amount of each asset in the unit; and***

(b) ***then, to goodwill allocated to the cash-generating unit (if any), if the requirements in paragraph 109 are met.***

These increases in carrying amounts should be treated as reversals of impairment losses for individual assets and recognised in accordance with paragraph 104.

108. ***In allocating a reversal of an impairment loss for a cash-generating unit under paragraph 107, the carrying amount of an asset should not be increased above the lower of:***

(a) ***its recoverable amount (if determinable); and***

(b) ***the carrying amount that would have been determined (net of amortisation or depreciation) had no impairment loss been recognised for the asset in prior years.***

The amount of the reversal of the impairment loss that would otherwise have been allocated to the asset should be allocated to the other assets of the unit on a pro-rata basis.

Reversal of an impairment loss for goodwill

109. ***As an exception to the requirement in paragraph 99, an impairment loss recognised for goodwill should not be reversed in a subsequent period unless:***

(a) ***the impairment loss was caused by a specific external event of an exceptional nature that is not expected to recur; and***

(b) ***subsequent external events have occurred that reverse the effect of that event.***

110. IAS 38, intangible assets, prohibits the recognition of internally generated goodwill. Any subsequent increase in the recoverable amount of goodwill is likely to be an increase in internally generated goodwill, unless the increase relates clearly to the reversal of the effect of a specific external event of an exceptional nature.

111. This Standard does not permit an impairment loss to be reversed for goodwill because of a change in estimates (for example, a change in the discount rate or in the amount and timing of future cash flows of the cash-generating unit to which goodwill relates).

112. A specific external event is an event that is outside of the control of the enterprise. Examples of external events of an exceptional nature include new regulations that significantly curtail the operating activities, or decrease the profitability, of the business to which the goodwill relates.

DISCLOSURE

113. ***For each class of assets, the financial statements should disclose:***

(a) ***the amount of impairment losses recognised in the income statement during the period and the line item(s) of the income statement in which those impairment losses are included;***

(b) ***the amount of reversals of impairment losses recognised in the income statement during the period and the line item(s) of the income statement in which those impairment losses are reversed;***

(c) ***the amount of impairment losses recognised directly in equity during the period; and***

(d) ***the amount of reversals of impairment losses recognised directly in equity during the period.***

114. A class of assets is a grouping of assets of similar nature and use in an enterprise's operations.

115. The information required in paragraph 113 may be presented with other information disclosed for the class of assets. For example, this information may be included in a reconciliation of the carrying amount of property, plant and equipment, at the beginning and end of the period, as required under IAS 16, property, plant and equipment.

116. ***An enterprise that applies IAS 14, segment reporting, should disclose the following for each reportable segment based on an enterprise's primary format (as defined in IAS 14):***

(a) ***the amount of impairment losses recognised in the income statement and directly in equity during the period; and***

(b) ***the amount of reversals of impairment losses recognised in the income statement and directly in equity during the period.***

117. ***If an impairment loss for an individual asset or a cash-generating unit is recognised or reversed during the period and is material to the financial statements of the reporting enterprise as a whole, an enterprise should disclose:***

(a) ***the events and circumstances that led to the recognition or reversal of the impairment loss;***

(b) ***the amount of the impairment loss recognised or reversed;***

(c) ***for an individual asset:***

(i) ***the nature of the asset; and***

(ii) ***the reportable segment to which the asset belongs, based on the enterprise's primary format (as defined in IAS 14, segment reporting, if the enterprise applies IAS 14);***

(d) ***for a cash-generating unit:***

(i) ***a description of the cash-generating unit (such as whether it is a product line, a plant, a business operation, a geographical area, a reportable segment as defined in IAS 14 or other);***

(ii) ***the amount of the impairment loss recognised or reversed by class of assets and by reportable segment based on the enterprise's primary format (as defined in IAS 14, if the enterprise applies IAS 14); and***

(iii) ***if the aggregation of assets for identifying the cash-generating unit has changed since the previous estimate of the cash-generating unit's recoverable amount (if any), the enterprise should describe the current and former way of aggregating assets and the reasons for changing the way the cash-generating unit is identified;***

(e) ***whether the recoverable amount of the asset (cash-generating unit) is its net selling price or its value in use;***

(f) ***if recoverable amount is net selling price, the basis used to determine net selling price (such as whether selling price was determined by reference to an active market or in some other way); and***

(g) ***if recoverable amount is value in use, the discount rate(s) used in the current estimate and previous estimate (if any) of value in use.***

118. ***If impairment losses recognised (reversed) during the period are material in aggregate to the financial statements of the reporting enterprise as a whole, an enterprise should disclose a brief description of the following:***

(a) ***the main classes of assets affected by impairment losses (reversals of impairment losses) for which no information is disclosed under paragraph 117; and***

(b) ***the main events and circumstances that led to the recognition (reversal) of these impairment losses for which no information is disclosed under paragraph 117.***

119. An enterprise is encouraged to disclose key assumptions used to determine the recoverable amount of assets (cash-generating units) during the period.

TRANSITIONAL PROVISIONS

120. ***This Standard should be applied on a prospective basis only. Impairment losses (reversals of impairment losses) that result from adoption of this International Accounting Standard should be recognised in accordance with this Standard (i.e., in the income statement unless an asset is carried at revalued amount. An impairment loss (reversal of impairment loss) on a revalued asset should be treated as a revaluation decrease (increase)).***

121. Before the adoption of this Standard, various International Accounting Standards included requirements broadly similar to those included in this Standard for the recognition and reversal of impairment losses. However, changes may arise from previous assessments because this Standard details how to measure recoverable amount and how to consider an asset's cash-generating unit. It would be difficult to determine retrospectively what the estimate of recoverable amount would have been. Therefore, on adoption of this Standard, an enterprise does not apply the benchmark or the allowed alternative treatment for other changes in accounting policies in IAS 8, net profit or loss for the period, fundamental errors and changes in accounting policies.

EFFECTIVE DATE

122. ***This International Accounting Standard becomes operative for financial statements covering periods beginning on or after 1 July 1999. Earlier application is encouraged. If an enterprise applies this Standard for financial statements covering periods beginning before 1 July 1999, the enterprise should disclose that fact.***

INTERNATIONAL ACCOUNTING STANDARD IAS 37

Provisions, contingent liabilities and contingent assets

This International Accounting Standard was approved by the IASC Board in July 1998 and became effective for financial statements covering periods beginning on or after 1 July 1999.

INTRODUCTION

1. IAS 37 prescribes the accounting and disclosure for all provisions, contingent liabilities and contingent assets, except:

   (a) those resulting from financial instruments that are carried at fair value;

   (b) those resulting from executory contracts, except where the contract is onerous. Executory contracts are contracts under which neither party has performed any of its obligations or both parties have partially performed their obligations to an equal extent;

   (c) those arising in insurance enterprises from contracts with policyholders; or

   (d) those covered by another International Accounting Standard.

Provisions

2. The Standard defines provisions as liabilities of uncertain timing or amount. A provision should be recognised when, and only when:

   (a) an enterprise has a present obligation (legal or constructive) as a result of a past event;

   (b) it is probable (i.e. more likely than not) that an outflow of resources embodying economic benefits will be required to settle the obligation; and

   (c) a reliable estimate can be made of the amount of the obligation. The Standard notes that it is only in extremely rare cases that a reliable estimate will not be possible.

3. The Standard defines a constructive obligation as an obligation that derives from an enterprise's actions where:

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

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

4. In rare cases, for example in a law suit, it may not be clear whether an enterprise has a present obligation. In these cases, a past event is deemed to give rise to a present obligation if, taking account of all available evidence, it is more likely than not that a present obligation exists at the balance sheet date. An enterprise recognises a provision for that present obligation if the other recognition criteria described above are met. If it is more likely than not that no present obligation exists, the enterprise discloses a contingent liability, unless the possibility of an outflow of resources embodying economic benefits is remote.

5. The amount recognised as a provision should be the best estimate of the expenditure required to settle the present obligation at the balance sheet date, in other words, the amount that an enterprise would rationally pay to settle the obligation at the balance sheet date or to transfer it to a third party at that time.

6. The Standard requires that an enterprise should, in measuring a provision:

   (a) take risks and uncertainties into account. However, uncertainty does not justify the creation of excessive provisions or a deliberate overstatement of liabilities;

(b) discount the provisions, where the effect of the time value of money is material, using a pre-tax discount rate (or rates) that reflect(s) current market assessments of the time value of money and those risks specific to the liability that have not been reflected in the best estimate of the expenditure. Where discounting is used, the increase in the provision due to the passage of time is recognised as an interest expense;

(c) take future events, such as changes in the law and technological changes, into account where there is sufficient objective evidence that they will occur; and

(d) not take gains from the expected disposal of assets into account, even if the expected disposal is closely linked to the event giving rise to the provision.

7. An enterprise may expect reimbursement of some or all of the expenditure required to settle a provision (for example, through insurance contracts, indemnity clauses or suppliers' warranties). An enterprise should:

(a) recognise a reimbursement when, and only when, it is virtually certain that reimbursement will be received if the enterprise settles the obligation. The amount recognised for the reimbursement should not exceed the amount of the provision; and

(b) recognise the reimbursement as a separate asset. In the income statement, the expense relating to a provision may be presented net of the amount recognised for a reimbursement.

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

9. A provision should be used only for expenditures for which the provision was originally recognised.

Provisions — specific applications

10. The Standard explains how the general recognition and measurement requirements for provisions should be applied in three specific cases: future operating losses; onerous contracts; and restructurings.

11. Provisions should not be recognised for future operating losses. An expectation of future operating losses is an indication that certain assets of the operation may be impaired. In this case, an enterprise tests these assets for impairment under IAS 36, impairment of assets.

12. If an enterprise has a contract that is onerous, the present obligation under the contract should be recognised and measured as a provision. An onerous contract is one in which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it.

13. The Standard defines a restructuring as a programme that is planned and controlled by management, and materially changes either:

(a) the scope of a business undertaken by an enterprise; or

(b) the manner in which that business is conducted.

14. A provision for restructuring costs is recognised only when the general recognition criteria for provisions are met. In this context, a constructive obligation to restructure arises only when an enterprise:

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

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

(ii) the principal locations affected;

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

(iv) the expenditures that will be undertaken; and

(v) when the plan will be implemented; and

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

15. A management or board decision to restructure does not give rise to a constructive obligation at the balance sheet date unless the enterprise has, before the balance sheet date:

(a) started to implement the restructuring plan; or

(b) communicated the restructuring plan to those affected by it in a sufficiently specific manner to raise a valid expectation in them that the enterprise will carry out the restructuring.

16. Where a restructuring involves the sale of an operation, no obligation arises for the sale until the enterprise is committed to the sale, i.e. there is a binding sale agreement.

17. A restructuring provision should include only the direct expenditures arising from the restructuring, which are those that are both:

(a) necessarily entailed by the restructuring; and

(b) not associated with the ongoing activities of the enterprise. Thus, a restructuring provision does not include such costs as: retraining or relocating continuing staff; marketing; or investment in new systems and distribution networks.

Contingent liabilities

18. The Standard supersedes the parts of IAS 10, contingencies and events occurring after the balance sheet date [1], that deal with contingencies. The Standard defines a contingent liability as:

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

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

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

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

19. An enterprise should not recognise a contingent liability. An enterprise should disclose a contingent liability, unless the possibility of an outflow of resources embodying economic benefits is remote.

Contingent assets

20. The Standard defines a contingent asset as a possible asset that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the enterprise. An example is a claim that an enterprise is pursuing through legal processes, where the outcome is uncertain.

21. An enterprise should not recognise a contingent asset. A contingent asset should be disclosed where an inflow of economic benefits is probable.

22. When the realisation of income is virtually certain, then the related asset is not a contingent asset and its recognition is appropriate.

(1) IAS 10, contingencies and events occurring after the balance sheet date, was superseded by IAS 10 (revised 1999), events after the balance sheet date, effective 1 January 2000.

Effective date

23. The Standard becomes operative for annual financial statements covering periods beginning on or after 1 July 1999. Earlier application is encouraged.

CONTENTS

IAS 37

The standards, which have been set in bold italic type, should be read in the context of the background material and implementation guidance in this Standard, and in the context of the 'Preface to International Accounting Standards'. International Accounting Standards are not intended to apply to immaterial items (see paragraph 12 of the Preface).

OBJECTIVE

The objective of this Standard is to ensure that appropriate recognition criteria and measurement bases are applied to provisions, contingent liabilities and contingent assets and that sufficient information is disclosed in the notes to the financial statements to enable users to understand their nature, timing and amount.

SCOPE

1. ***This Standard should be applied by all enterprises in accounting for provisions, contingent liabilities and contingent assets, except:***

   (a) ***those resulting from financial instruments that are carried at fair value;***

   (b) ***those resulting from executory contracts, except where the contract is onerous;***

   (c) ***those arising in insurance enterprises from contracts with policyholders; and***

   (d) ***those covered by another International Accounting Standard.***

2. This Standard applies to financial instruments (including guarantees) that are not carried at fair value.

3. Executory contracts are contracts under which neither party has performed any of its obligations or both parties have partially performed their obligations to an equal extent. This Standard does not apply to executory contracts unless they are onerous.

4. This Standard applies to provisions, contingent liabilities and contingent assets of insurance enterprises other than those arising from contracts with policyholders.

5. Where another International Accounting Standard deals with a specific type of provision, contingent liability or contingent asset, an enterprise applies that Standard instead of this Standard. For example, certain types of provisions are also addressed in Standards on:

   (a) construction contracts (see IAS 11, construction contracts);

   (b) income taxes (see IAS 12, income taxes);

   (c) leases (see IAS 17, leases). However, as IAS 17 contains no specific requirements to deal with operating leases that have become onerous, this Standard applies to such cases; and

   (d) employee benefits (see IAS 19, employee benefits).

6. Some amounts treated as provisions may relate to the recognition of revenue, for example where an enterprise gives guarantees in exchange for a fee. This Standard does not address the recognition of revenue. IAS 18, revenue, identifies the circumstances in which revenue is recognised and provides practical guidance on the application of the recognition criteria. This Standard does not change the requirements of IAS 18.

7. This Standard defines provisions as liabilities of uncertain timing or amount. In some countries the term 'provision' is also used in the context of items such as depreciation, impairment of assets and doubtful debts: these are adjustments to the carrying amounts of assets and are not addressed in this Standard.

8. Other International Accounting Standards specify whether expenditures are treated as assets or as expenses. These issues are not addressed in this Standard. Accordingly, this Standard neither prohibits nor requires capitalisation of the costs recognised when a provision is made.

9. This Standard applies to provisions for restructuring (including discontinuing operations). Where a restructuring meets the definition of a discontinuing operation, additional disclosures may be required by IAS 35, discontinuing operations.

DEFINITIONS

10. ***The following terms are used in this Standard with the meanings specified:***

A provision is a liability of uncertain timing or amount.

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

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

A legal obligation is an obligation that derives from:

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

(b) ***legislation; or***

(c) ***other operation of law.***

A constructive obligation is an obligation that derives from an enterprise's actions where:

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

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

A contingent liability is:

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

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

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

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

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

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

A restructuring is a programme that is planned and controlled by management, and materially changes either:

(a) ***the scope of a business undertaken by an enterprise; or***

(b) ***the manner in which that business is conducted.***

Provisions and other liabilities

11. Provisions can be distinguished from other liabilities such as trade payables and accruals because there is uncertainty about the timing or amount of the future expenditure required in settlement. By contrast:

(a) trade payables are liabilities to pay for goods or services that have been received or supplied and have been invoiced or formally agreed with the supplier; and

(b) accruals are liabilities to pay for goods or services that have been received or supplied but have not been paid, invoiced or formally agreed with the supplier, including amounts due to employees (for example, amounts relating to accrued vacation pay). Although it is sometimes necessary to estimate the amount or timing of accruals, the uncertainty is generally much less than for provisions.

Accruals are often reported as part of trade and other payables, whereas provisions are reported separately.

Relationship between provisions and contingent liabilities

12. In a general sense, all provisions are contingent because they are uncertain in timing or amount. However, within this Standard the term 'contingent' is used for liabilities and assets that are not recognised because their existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the enterprise. In addition, the term 'contingent liability' is used for liabilities that do not meet the recognition criteria.

13. This Standard distinguishes between:

(a) provisions — which are recognised as liabilities (assuming that a reliable estimate can be made) because they are present obligations and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligations; and

(b) contingent liabilities — which are not recognised as liabilities because they are either:

(i) possible obligations, as it has yet to be confirmed whether the enterprise has a present obligation that could lead to an outflow of resources embodying economic benefits; or

(ii) present obligations that do not meet the recognition criteria in this Standard (because either it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation, or a sufficiently reliable estimate of the amount of the obligation cannot be made).

RECOGNITION

Provisions

14. ***A provision should be recognised when:***

(a) ***an enterprise has a present obligation (legal or constructive) as a result of a past event*** (2)***;***

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

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

If these conditions are not met, no provision should be recognised.

(2) See also SIC-6: costs of modifying existing software.

Present obligation

15. ***In rare cases it is not clear whether there is a present obligation. In these cases, a past event is deemed to give rise to a present obligation if, taking account of all available evidence, it is more likely than not that a present obligation exists at the balance sheet date.***

16. In almost all cases it will be clear whether a past event has given rise to a present obligation. In rare cases, for example in a law suit, it may be disputed either whether certain events have occurred or whether those events result in a present obligation. In such a case, an enterprise determines whether a present obligation exists at the balance sheet date by taking account of all available evidence, including, for example, the opinion of experts. The evidence considered includes any additional evidence provided by events after the balance sheet date. On the basis of such evidence:

    (a) where it is more likely than not that a present obligation exists at the balance sheet date, the enterprise recognises a provision (if the recognition criteria are met); and

    (b) where it is more likely that no present obligation exists at the balance sheet date, the enterprise discloses a contingent liability, unless the possibility of an outflow of resources embodying economic benefits is remote (see paragraph 86).

Past event

17. A past event that leads to a present obligation is called an obligating event. For an event to be an obligating event, it is necessary that the enterprise has no realistic alternative to settling the obligation created by the event. This is the case only:

    (a) where the settlement of the obligation can be enforced by law; or

    (b) in the case of a constructive obligation, where the event (which may be an action of the enterprise) creates valid expectations in other parties that the enterprise will discharge the obligation.

18. Financial statements deal with the financial position of an enterprise at the end of its reporting period and not its possible position in the future. Therefore, no provision is recognised for costs that need to be incurred to operate in the future. The only liabilities recognised in an enterprise's balance sheet are those that exist at the balance sheet date.

19. It is only those obligations arising from past events existing independently of an enterprise's future actions (i.e. the future conduct of its business) that are recognised as provisions. Examples of such obligations are penalties or clean-up costs for unlawful environmental damage, both of which would lead to an outflow of resources embodying economic benefits in settlement regardless of the future actions of the enterprise. Similarly, an enterprise recognises a provision for the decommissioning costs of an oil installation or a nuclear power station to the extent that the enterprise is obliged to rectify damage already caused. In contrast, because of commercial pressures or legal requirements, an enterprise may intend or need to carry out expenditure to operate in a particular way in the future (for example, by fitting smoke filters in a certain type of factory). Because the enterprise can avoid the future expenditure by its future actions, for example by changing its method of operation, it has no present obligation for that future expenditure and no provision is recognised.

20. An obligation always involves another party to whom the obligation is owed. It is not necessary, however, to know the identity of the party to whom the obligation is owed — indeed the obligation may be to the public at large. Because an obligation always involves a commitment to another party, it follows that a management or board decision does not give rise to a constructive obligation at the balance sheet date unless the decision has been communicated before the balance sheet date to those affected by it in a sufficiently specific manner to raise a valid expectation in them that the enterprise will discharge its responsibilities.

21. An event that does not give rise to an obligation immediately may do so at a later date, because of changes in the law or because an act (for example, a sufficiently specific public statement) by the enterprise gives rise to a constructive obligation. For example, when environmental damage is caused there may be no obligation to remedy the consequences. However, the causing of the damage will become an obligating event when a new law requires the existing damage to be rectified or when the enterprise publicly accepts responsibility for rectification in a way that creates a constructive obligation.

22. Where details of a proposed new law have yet to be finalised, an obligation arises only when the legislation is virtually certain to be enacted as drafted. For the purpose of this Standard, such an obligation is treated as a legal obligation. Differences in circumstances surrounding enactment make it impossible to specify a single event that would make the enactment of a law virtually certain. In many cases it will be impossible to be virtually certain of the enactment of a law until it is enacted.

Probable outflow of resources embodying economic benefits

23. For a liability to qualify for recognition there must be not only a present obligation but also the probability of an outflow of resources embodying economic benefits to settle that obligation. For the purpose of this Standard [3], an outflow of resources or other event is regarded as probable if the event is more likely than not to occur, i.e. the probability that the event will occur is greater than the probability that it will not. Where it is not probable that a present obligation exists, an enterprise discloses a contingent liability, unless the possibility of an outflow of resources embodying economic benefits is remote (see paragraph 86).

24. Where there are a number of similar obligations (e.g. product warranties or similar contracts) the probability that an outflow will be required in settlement is determined by considering the class of obligations as a whole. Although the likelihood of outflow for any one item may be small, it may well be probable that some outflow of resources will be needed to settle the class of obligations as a whole. If that is the case, a provision is recognised (if the other recognition criteria are met).

Reliable estimate of the obligation

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

26. In the extremely rare case where no reliable estimate can be made, a liability exists that cannot be recognised. That liability is disclosed as a contingent liability (see paragraph 86).

Contingent liabilities

27. ***An enterprise should not recognise a contingent liability.***

28. A contingent liability is disclosed, as required by paragraph 86, unless the possibility of an outflow of resources embodying economic benefits is remote.

29. Where an enterprise is jointly and severally liable for an obligation, the part of the obligation that is expected to be met by other parties is treated as a contingent liability. The enterprise recognises a provision for the part of the obligation for which an outflow of resources embodying economic benefits is probable, except in the extremely rare circumstances where no reliable estimate can be made.

30. Contingent liabilities may develop in a way not initially expected. Therefore, they are assessed continually to determine whether an outflow of resources embodying economic benefits has become probable. If it becomes probable that an outflow of future economic benefits will be required for an item previously dealt with as a contingent liability, a provision is recognised in the financial statements of the period in which the change in probability occurs (except in the extremely rare circumstances where no reliable estimate can be made).

(3) The interpretation of 'probable' in this Standard as 'more likely than not' does not necessarily apply in other International Accounting Standards.

Contingent assets

31. ***An enterprise should not recognise a contingent asset.***

32. Contingent assets usually arise from unplanned or other unexpected events that give rise to the possibility of an inflow of economic benefits to the enterprise. An example is a claim that an enterprise is pursuing through legal processes, where the outcome is uncertain.

33. Contingent assets are not recognised in financial statements since this may result in the recognition of income that may never be realised. However, when the realisation of income is virtually certain, then the related asset is not a contingent asset and its recognition is appropriate.

34. A contingent asset is disclosed, as required by paragraph 89, where an inflow of economic benefits is probable.

35. Contingent assets are assessed continually to ensure that developments are appropriately reflected in the financial statements. If it has become virtually certain that an inflow of economic benefits will arise, the asset and the related income are recognised in the financial statements of the period in which the change occurs. If an inflow of economic benefits has become probable, an enterprise discloses the contingent asset (see paragraph 89).

MEASUREMENT

Best estimate

36. ***The amount recognised as a provision should be the best estimate of the expenditure required to settle the present obligation at the balance sheet date.***

37. The best estimate of the expenditure required to settle the present obligation is the amount that an enterprise would rationally pay to settle the obligation at the balance sheet date or to transfer it to a third party at that time. It will often be impossible or prohibitively expensive to settle or transfer an obligation at the balance sheet date. However, the estimate of the amount that an enterprise would rationally pay to settle or transfer the obligation gives the best estimate of the expenditure required to settle the present obligation at the balance sheet date.

38. The estimates of outcome and financial effect are determined by the judgement of the management of the enterprise, supplemented by experience of similar transactions and, in some cases, reports from independent experts. The evidence considered includes any additional evidence provided by events after the balance sheet date.

39. Uncertainties surrounding the amount to be recognised as a provision are dealt with by various means according to the circumstances. Where the provision being measured involves a large population of items, the obligation is estimated by weighting all possible outcomes by their associated probabilities. The name for this statistical method of estimation is 'expected value'. The provision will therefore be different depending on whether the probability of a loss of a given amount is, for example, 60 % or 90 %. Where there is a continuous range of possible outcomes, and each point in that range is as likely as any other, the mid-point of the range is used.

Example

An enterprise sells goods with a warranty under which customers are covered for the cost of repairs of any manufacturing defects that become apparent within the first six months after purchase. If minor defects were detected in all products sold, repair costs of 1 000 000 would result. If major defects were detected in all products sold, repair costs of 4 million would result. The enterprise's past experience and future expectations indicate that, for the coming year, 75 % of the goods sold will have no defects, 20 % of the goods sold will have minor defects and 5 % of the goods sold will have major defects. In accordance with paragraph 24, an enterprise assesses the probability of an outflow for the warranty obligations as a whole.

The expected value of the cost of repairs is:

(75 % of nil) + (20 % of 1 000 000) + (5 % of 4 000 000) = 400 000

40. Where a single obligation is being measured, the individual most likely outcome may be the best estimate of the liability. However, even in such a case, the enterprise considers other possible outcomes. Where other possible outcomes are either mostly higher or mostly lower than the most likely outcome, the best estimate will be a higher or lower amount. For example, if an enterprise has to rectify a serious fault in a major plant that it has constructed for a customer, the individual most likely outcome may be for the repair to succeed at the first attempt at a cost of 1 000, but a provision for a larger amount is made if there is a significant chance that further attempts will be necessary.

41. The provision is measured before tax, as the tax consequences of the provision, and changes in it, are dealt with under IAS 12, income taxes.

Risks and uncertainties

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

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

44. Disclosure of the uncertainties surrounding the amount of the expenditure is made under paragraph 85(b).

Present value

45. ***Where the effect of the time value of money is material, the amount of a provision should be the present value of the expenditure expected to be required to settle the obligation.***

46. Because of the time value of money, provisions relating to cash outflows that arise soon after the balance sheet date are more onerous than those where cash outflows of the same amount arise later. Provisions are therefore discounted, where the effect is material.

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

Future events

48. ***Future events that may affect the amount required to settle an obligation should be reflected in the amount of a provision where there is sufficient objective evidence that they will occur.***

49. Expected future events may be particularly important in measuring provisions. For example, an enterprise may believe that the cost of cleaning up a site at the end of its life will be reduced by future changes in technology. The amount recognised reflects a reasonable expectation of technically qualified, objective observers, taking account of all available evidence as to the technology that will be available at the time of the clean-up. Thus it is appropriate to include, for example, expected cost reductions associated with increased experience in applying existing technology or the expected cost of applying existing technology to a larger or more complex clean-up operation than has previously been carried out. However, an enterprise does not anticipate the development of a completely new technology for cleaning up unless it is supported by sufficient objective evidence.

50. The effect of possible new legislation is taken into consideration in measuring an existing obligation when sufficient objective evidence exists that the legislation is virtually certain to be enacted. The variety of circumstances that arise in practice makes it impossible to specify a single event that will provide sufficient, objective evidence in every case. Evidence is required both of what legislation will demand and of whether it is virtually certain to be enacted and implemented in due course. In many cases sufficient objective evidence will not exist until the new legislation is enacted.

Expected disposal of assets

51. ***Gains from the expected disposal of assets should not be taken into account in measuring a provision.***

52. Gains on the expected disposal of assets are not taken into account in measuring a provision, even if the expected disposal is closely linked to the event giving rise to the provision. Instead, an enterprise recognises gains on expected disposals of assets at the time specified by the International Accounting Standard dealing with the assets concerned.

REIMBURSEMENTS

53. ***Where some or all of the expenditure required to settle a provision is expected to be reimbursed by another party, the reimbursement should be recognised when, and only when, it is virtually certain that reimbursement will be received if the enterprise settles the obligation. The reimbursement should be treated as a separate asset. The amount recognised for the reimbursement should not exceed the amount of the provision.***

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

55. Sometimes, an enterprise is able to look to another party to pay part or all of the expenditure required to settle a provision (for example, through insurance contracts, indemnity clauses or suppliers' warranties). The other party may either reimburse amounts paid by the enterprise or pay the amounts directly.

56. In most cases the enterprise will remain liable for the whole of the amount in question so that the enterprise would have to settle the full amount if the third party failed to pay for any reason. In this situation, a provision is recognised for the full amount of the liability, and a separate asset for the expected reimbursement is recognised when it is virtually certain that reimbursement will be received if the enterprise settles the liability.

57. In some cases, the enterprise will not be liable for the costs in question if the third party fails to pay. In such a case the enterprise has no liability for those costs and they are not included in the provision.

58. As noted in paragraph 29, an obligation for which an enterprise is jointly and severally liable is a contingent liability to the extent that it is expected that the obligation will be settled by the other parties.

Changes in provisions

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

60. Where discounting is used, the carrying amount of a provision increases in each period to reflect the passage of time. This increase is recognised as borrowing cost.

Use of provisions

61. ***A provision should be used only for expenditures for which the provision was originally recognised.***

62. Only expenditures that relate to the original provision are set against it. Setting expenditures against a provision that was originally recognised for another purpose would conceal the impact of two different events.

APPLICATION OF THE RECOGNITION AND MEASUREMENT RULES

Future operating losses

63. ***Provisions should not be recognised for future operating losses.***

64. Future operating losses do not meet the definition of a liability in paragraph 10 and the general recognition criteria set out for provisions in paragraph 14.

65. An expectation of future operating losses is an indication that certain assets of the operation may be impaired. An enterprise tests these assets for impairment under IAS 36, impairment of assets.

Onerous contracts

66. ***If an enterprise has a contract that is onerous, the present obligation under the contract should be recognised and measured as a provision.***

67. Many contracts (for example, some routine purchase orders) can be cancelled without paying compensation to the other party, and therefore there is no obligation. Other contracts establish both rights and obligations for each of the contracting parties. Where events make such a contract onerous, the contract falls within the scope of this Standard and a liability exists which is recognised. Executory contracts that are not onerous fall outside the scope of this Standard.

68. This Standard defines an onerous contract as a contract in which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it. The unavoidable costs under a contract reflect the least net cost of exiting from the contract, which is the lower of the cost of fulfilling it and any compensation or penalties arising from failure to fulfil it.

69. Before a separate provision for an onerous contract is established, an enterprise recognises any impairment loss that has occurred on assets dedicated to that contract (see IAS 36, impairment of assets).

Restructuring

70. The following are examples of events that may fall under the definition of restructuring:

    (a) sale or termination of a line of business;

    (b) the closure of business locations in a country or region or the relocation of business activities from one country or region to another;

    (c) changes in management structure, for example, eliminating a layer of management; and

    (d) fundamental reorganisations that have a material effect on the nature and focus of the enterprise's operations.

71. A provision for restructuring costs is recognised only when the general recognition criteria for provisions set out in paragraph 14 are met. Paragraphs 72 to 83 set out how the general recognition criteria apply to restructurings.

72. ***A constructive obligation to restructure arises only when an enterprise:***

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

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

(ii) ***the principal locations affected;***

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

(iv) ***the expenditures that will be undertaken; and***

(v) ***when the plan will be implemented; and***

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

73. Evidence that an enterprise has started to implement a restructuring plan would be provided, for example, by dismantling plant or selling assets or by the public announcement of the main features of the plan. A public announcement of a detailed plan to restructure constitutes a constructive obligation to restructure only if it is made in such a way and in sufficient detail (i.e. setting out the main features of the plan) that it gives rise to valid expectations in other parties such as customers, suppliers and employees (or their representatives) that the enterprise will carry out the restructuring.

74. For a plan to be sufficient to give rise to a constructive obligation when communicated to those affected by it, its implementation needs to be planned to begin as soon as possible and to be completed in a timeframe that makes significant changes to the plan unlikely. If it is expected that there will be a long delay before the restructuring begins or that the restructuring will take an unreasonably long time, it is unlikely that the plan will raise a valid expectation on the part of others that the enterprise is at present committed to restructuring, because the timeframe allows opportunities for the enterprise to change its plans.

75. A management or board decision to restructure taken before the balance sheet date does not give rise to a constructive obligation at the balance sheet date unless the enterprise has, before the balance sheet date:

(a) started to implement the restructuring plan; or

(b) announced the main features of the restructuring plan to those affected by it in a sufficiently specific manner to raise a valid expectation in them that the enterprise will carry out the restructuring.

In some cases, an enterprise starts to implement a restructuring plan, or announces its main features to those affected, only after the balance sheet date. Disclosure may be required under IAS 10, events after the balance sheet date, if the restructuring is of such importance that its non-disclosure would affect the ability of the users of the financial statements to make proper evaluations and decisions.

76. Although a constructive obligation is not created solely by a management decision, an obligation may result from other earlier events together with such a decision. For example, negotiations with employee representatives for termination payments, or with purchasers for the sale of an operation, may have been concluded subject only to board approval. Once that approval has been obtained and communicated to the other parties, the enterprise has a constructive obligation to restructure, if the conditions of paragraph 72 are met.

77. In some countries, the ultimate authority is vested in a board whose membership includes representatives of interests other than those of management (e.g. employees) or notification to such representatives may be necessary before the board decision is taken. Because a decision by such a board involves communication to these representatives, it may result in a constructive obligation to restructure.

78. ***No obligation arises for the sale of an operation until the enterprise is committed to the sale, i.e. there is a binding sale agreement.***

79. Even when an enterprise has taken a decision to sell an operation and announced that decision publicly, it cannot be committed to the sale until a purchaser has been identified and there is a binding sale agreement. Until there is a binding sale agreement, the enterprise will be able to change its mind and indeed will have to take another course of action if a purchaser cannot be found on acceptable terms. When the sale of an operation is envisaged as part of a restructuring, the assets of the operation are reviewed for impairment, under IAS 36, impairment of assets. When a sale is only part of a restructuring, a constructive obligation can arise for the other parts of the restructuring before a binding sale agreement exists.

80. ***A restructuring provision should include only the direct expenditures arising from the restructuring, which are those that are both:***

    (a) ***necessarily entailed by the restructuring; and***

    (b) ***not associated with the ongoing activities of the enterprise.***

81. A restructuring provision does not include such costs as:

    (a) retraining or relocating continuing staff;

    (b) marketing; or

    (c) investment in new systems and distribution networks.

    These expenditures relate to the future conduct of the business and are not liabilities for restructuring at the balance sheet date. Such expenditures are recognised on the same basis as if they arose independently of a restructuring.

82. Identifiable future operating losses up to the date of a restructuring are not included in a provision, unless they relate to an onerous contract as defined in paragraph 10.

83. As required by paragraph 51, gains on the expected disposal of assets are not taken into account in measuring a restructuring provision, even if the sale of assets is envisaged as part of the restructuring.

DISCLOSURE

84. ***For each class of provision, an enterprise should disclose:***

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

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

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

    (d) ***unused amounts reversed during the period; and***

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

    Comparative information is not required.

85. ***An enterprise should disclose the following for each class of provision:***

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

(b) ***an indication of the uncertainties about the amount or timing of those outflows. Where necessary to provide adequate information, an enterprise should disclose the major assumptions made concerning future events, as addressed in paragraph 48; and***

(c) ***the amount of any expected reimbursement, stating the amount of any asset that has been recognised for that expected reimbursement.***

86. ***Unless the possibility of any outflow in settlement is remote, an enterprise should disclose for each class of contingent liability at the balance sheet date a brief description of the nature of the contingent liability and, where practicable:***

(a) ***an estimate of its financial effect, measured under paragraphs 36 to 52;***

(b) ***an indication of the uncertainties relating to the amount or timing of any outflow; and***

(c) ***the possibility of any reimbursement.***

87. In determining which provisions or contingent liabilities may be aggregated to form a class, it is necessary to consider whether the nature of the items is sufficiently similar for a single statement about them to fulfil the requirements of paragraphs 85(a) and (b) and 86(a) and (b). Thus, it may be appropriate to treat as a single class of provision amounts relating to warranties of different products, but it would not be appropriate to treat as a single class amounts relating to normal warranties and amounts that are subject to legal proceedings.

88. Where a provision and a contingent liability arise from the same set of circumstances, an enterprise makes the disclosures required by paragraphs 84 to 86 in a way that shows the link between the provision and the contingent liability.

89. ***Where an inflow of economic benefits is probable, an enterprise should disclose a brief description of the nature of the contingent assets at the balance sheet date, and, where practicable, an estimate of their financial effect, measured using the principles set out for provisions in paragraphs 36 to 52.***

90. It is important that disclosures for contingent assets avoid giving misleading indications of the likelihood of income arising.

91. ***Where any of the information required by paragraphs 86 and 89 is not disclosed because it is not practicable to do so, that fact should be stated.***

92. ***In extremely rare cases, disclosure of some or all of the information required by paragraphs 84 to 89 can be expected to prejudice seriously the position of the enterprise in a dispute with other parties on the subject matter of the provision, contingent liability or contingent asset. In such cases, an enterprise need not disclose the information, but should disclose the general nature of the dispute, together with the fact that, and reason why, the information has not been disclosed.***

Transitional provisions

93. ***The effect of adopting this Standard on its effective date (or earlier) should be reported as an adjustment to the opening balance of retained earnings for the period in which the Standard is first adopted. Enterprises are encouraged, but not required, to adjust the opening balance of retained earnings for the earliest period presented and to restate comparative information. If comparative information is not restated, this fact should be disclosed.***

94. The Standard requires a different treatment from IAS 8, net profit or loss for the period, fundamental errors and changes in accounting policies. IAS 8 requires comparative information to be restated (benchmark treatment) or additional pro forma comparative information on a restated basis to be disclosed (allowed alternative treatment) unless it is impracticable to do so.

EFFECTIVE DATE

95. ***This International Accounting Standard becomes operative for annual financial statements covering periods beginning on or after 1 July 1999. Earlier application is encouraged. If an enterprise applies this Standard for periods beginning before 1 July 1999, it should disclose that fact.***

96. This Standard supersedes the parts of IAS 10, contingencies and events occurring after the balance sheet date [4], that deal with contingencies.

INTERNATIONAL ACCOUNTING STANDARD IAS 38

Intangible assets

This International Accounting Standard was approved by the IASC Board in July 1998 and became effective for financial statements covering periods beginning on or after 1 July 1999.

This Standard supersedes:

(a) IAS 4, depreciation accounting, with respect to the amortisation (depreciation) of intangible assets; and

(b) IAS 9, research and development costs.

In October 1998, the IASC staff published separately a 'Basis for conclusions for IAS 38, intangible assets and IAS 22 (revised 1998)'. Copies are available from IASC's Publications Department.

In 1998, IAS 39, financial instruments: recognition and measurement, amended paragraph 2(f) of IAS 38 to replace the reference to IAS 25, accounting for investments, by reference to IAS 39. Footnote 1 was also deleted.

One SIC interpretation relates to IAS 38:

— SIC-6: costs of modifying existing software,

— SIC-32: Intangible assets — Web site costs.

INTRODUCTION

1. IAS 38 prescribes the accounting and disclosure for intangible assets that are not specifically dealt with in other International Accounting Standards. IAS 38 does not apply to financial assets, mineral rights and expenditure on the exploration for, or development and extraction of, minerals, oil, natural gas and similar non-regenerative resources and intangible assets arising in insurance enterprises from contracts with policyholders. IAS 38 applies, among other things, to expenditure on advertising, training, start-up, research and development activities.

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

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

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

[4] IAS 10: contingencies and events occurring after the balance sheet date, was superseded by IAS 10 (revised 1999), events after the balance sheet date, effective 1 January 2000.

3. IAS 38 requires an enterprise to recognise an intangible asset (at cost) if, and only if:

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

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

   This requirement applies whether an intangible asset is acquired externally or generated internally. IAS 38 includes additional recognition criteria for internally generated intangible assets.

4. IAS 38 specifies that internally generated goodwill, brands, mastheads, publishing titles, customer lists and items similar in substance should not be recognised as assets.

5. If an intangible item does not meet both the definition and the criteria for the recognition of an intangible asset, IAS 38 requires the expenditure on this item to be recognised as an expense when it is incurred. However, if the item is acquired in a business combination that is an acquisition, this expenditure (included in the cost of acquisition) should form part of the amount attributed to goodwill (negative goodwill) at the date of acquisition.

6. IAS 38 requires all expenditure on research to be recognised as an expense when it is incurred. Examples of other expenditure that will not give rise to an intangible asset that can be recognised in the financial statements are as follows:

   (a) expenditure on starting up an operation or a business (start-up costs);

   (b) expenditure on training;

   (c) expenditure on advertising and/or promotion; and

   (d) expenditure on relocating or reorganising part or all of an enterprise.

   Expenditure on these items is recognised as an expense when it is incurred.

7. IAS 38 requires that subsequent expenditure on an intangible asset after its purchase or completion should be recognised as an expense when it is incurred unless:

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

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

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

8. If expenditure on an intangible item was initially recognised as an expense by a reporting enterprise in previous annual financial statements or interim financial reports, IAS 38 prohibits the enterprise from recognising this expenditure as part of the cost of an intangible asset at a later date.

9. After initial recognition, IAS 38 requires an intangible asset to be measured under one of the following two treatments:

   (a) benchmark treatment: cost less any accumulated amortisation and any accumulated impairment losses; or

   (b) allowed alternative treatment: revalued amount less any subsequent accumulated amortisation and any subsequent accumulated impairment losses. The revalued amount should be the fair value of the asset. However, this treatment is permitted if, and only if, fair value can be determined by reference to an active market for the intangible asset. In addition, once an enterprise elects this treatment, IAS 38 requires revaluations to be made with sufficient regularity such that the carrying amount of the intangible asset does not differ materially from that which would be determined using fair value at the balance sheet date. IAS 38 also specifies how intangible assets should be revalued and whether a revaluation increase (decrease) should be recognised in the income statement or directly in equity.

10. IAS 38 requires that an intangible asset should be amortised on a systematic basis over the best estimate of its useful life. There is a rebuttable presumption that the useful life of an intangible asset will not exceed 20 years from the date when the asset is available for use. IAS 38 does not permit an enterprise to assign an infinite useful life to an intangible asset. Amortisation should commence when the asset is available for use.

11. In rare cases, there may be persuasive evidence that the useful life of an intangible asset will be a specific period longer than 20 years. In these cases, IAS 38 requires an enterprise:

    (a) to amortise the intangible asset over the best estimate of its useful life;

    (b) to estimate the recoverable amount of the intangible asset at least annually to identify whether there is any impairment loss; and

    (c) to disclose the reasons why the presumption that the useful life of an intangible asset will not exceed 20 years is rebutted and the factor(s) that played a significant role in determining the useful life of the intangible asset.

12. IAS 38 requires that the amortisation method used should reflect the pattern in which the asset's economic benefits are consumed by the enterprise. If that pattern cannot be determined reliably, the straight-line method should be adopted. The amortisation charge should be recognised as an expense unless another International Accounting Standard permits or requires it to be included in the carrying amount of another asset.

13. IAS 38 requires the residual value of an intangible asset to be assumed to be zero unless:

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

    (b) there is an active market for that type of asset and it is probable that such a market will exist at the end of the asset's useful life.

14. To assess whether an intangible asset may be impaired, an enterprise applies IAS 36, impairment of assets. Also, IAS 38 requires an enterprise to estimate the recoverable amount of an intangible asset that is not yet available for use at least annually.

15. IAS 38 is effective for accounting periods beginning on or after 1 July 1999. Earlier application is encouraged.

16. On first application, IAS 38 includes transitional provisions that require retrospective application:

    (a) whenever this is necessary to eliminate an item that no longer qualifies for recognition under IAS 38; or

    (b) if the previous measurement of an intangible asset contradicted the principles set out in IAS 38 (for example, if an intangible asset was not amortised or was revalued but not by reference to an active market).

    In other cases, prospective application of the recognition and amortisation requirements is either required (for example, IAS 38 prohibits the recognition of an internally generated intangible asset that was not previously recognised) or permitted (for example, IAS 38 encourages the recognition of an intangible asset that was acquired in a business combination that was an acquisition and that was not previously recognised).

CONTENTS

The standards, which have been set in bold italic type, should be read in the context of the background material and implementation guidance in this Standard, and in the context of the 'Preface to International Accounting Standards'. International Accounting Standards are not intended to apply to immaterial items (see paragraph 12 of the Preface).

OBJECTIVE

The objective of this Standard is to prescribe the accounting treatment for intangible assets that are not dealt with specifically in another International Accounting Standard. This Standard requires an enterprise to recognise an intangible asset if, and only if, certain criteria are met. The Standard also specifies how to measure the carrying amount of intangible assets and requires certain disclosures about intangible assets.

SCOPE

1. ***This Standard should be applied by all enterprises in accounting for intangible assets, except:***

   (a) ***intangible assets that are covered by another International Accounting Standard;***

   (b) ***financial assets, as defined in IAS 32, financial instruments: disclosure and presentation;***

   (c) ***mineral rights and expenditure on the exploration for, or development and extraction of, minerals, oil, natural gas and similar non-regenerative resources; and***

   (d) ***intangible assets arising in insurance enterprises from contracts with policyholders.***

2. If another International Accounting Standard deals with a specific type of intangible asset, an enterprise applies that Standard instead of this Standard. For example, this Standard does not apply to:

   (a) intangible assets held by an enterprise for sale in the ordinary course of business (see IAS 2, inventories, and IAS 11, construction contracts);

   (b) deferred tax assets (see IAS 12, income taxes);

   (c) leases that fall within the scope of IAS 17, leases;

   (d) assets arising from employee benefits (see IAS 19, employee benefits);

(e) goodwill arising on a business combination (see IAS 22, business combinations); and

(f) financial assets as defined in IAS 32, financial instruments: disclosure and presentation. The recognition and measurement of some financial assets are covered by: IAS 27, consolidated financial statements and accounting for investments in subsidiaries; IAS 28, accounting for investments in associates; IAS 31, financial reporting of interests in joint ventures; and IAS 39, financial instruments: recognition and measurement.

3. Some intangible assets may be contained in or on a physical substance such as a compact disk (in the case of computer software), legal documentation (in the case of a licence or patent) or film. In determining whether an asset that incorporates both intangible and tangible elements should be treated under IAS 16, property, plant and equipment, or as an intangible asset under this Standard, judgement is required to assess which element is more significant. For example, computer software for a computer controlled machine tool that cannot operate without that specific software is an integral part of the related hardware and it is treated as property, plant and equipment. The same applies to the operating system of a computer. Where the software is not an integral part of the related hardware, computer software is treated as an intangible asset.

4. This Standard applies to, among other things, expenditure on advertising, training, start-up, research and development activities. Research and development activities are directed to the development of knowledge. Therefore, although these activities may result in an asset with physical substance (for example, a prototype), the physical element of the asset is secondary to its intangible component, that is the knowledge embodied in it.

5. In the case of a finance lease, the underlying asset may be either tangible or intangible. After initial recognition, a lessee deals with an intangible asset held under a finance lease under this Standard. Rights under licensing agreements for items such as motion picture films, video recordings, plays, manuscripts, patents and copyrights are excluded from the scope of IAS 17 and fall within the scope of this Standard.

6. Exclusions from the scope of an International Accounting Standard may occur if certain activities or transactions are so specialised that they give rise to accounting issues that may need to be dealt with in a different way. Such issues arise in the expenditure on the exploration for, or development and extraction of, oil, gas and mineral deposits in extractive industries and in the case of contracts between insurance enterprises and their policyholders. Therefore, this Standard does not apply to expenditure on such activities. However, this Standard applies to other intangible assets used (such as computer software), and other expenditure (such as start-up costs), in extractive industries or by insurance companies.

DEFINITIONS

7. ***The following terms are used in this Standard with the meanings specified:***

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

An asset is a resource:

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

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

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

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

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

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

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

***Useful life** is either:*

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

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

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

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

***Fair value** of an asset is the amount for which that asset could be exchanged between knowledgeable, willing parties in an arm's length transaction.*

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

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

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

(c) ***prices are available to the public.***

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

***Carrying amount** is the amount at which an asset is recognised in the balance sheet after deducting any accumulated amortisation and accumulated impairment losses thereon.*

Intangible assets

8. Enterprises frequently expend resources, or incur liabilities, on the acquisition, development, maintenance or enhancement of intangible resources such as scientific or technical knowledge, design and implementation of new processes or systems, licences, intellectual property, market knowledge and trade marks (including brand names and publishing titles). Common examples of items encompassed by these broad headings are computer software, patents, copyrights, motion picture films, customer lists, mortgage servicing rights, fishing licences, import quotas, franchises, customer or supplier relationships, customer loyalty, market share and marketing rights.

9. Not all the items described in paragraph 8 will meet the definition of an intangible asset, that is, identifiability, control over a resource and existence of future economic benefits. If an item covered by this Standard does not meet the definition of an intangible asset, expenditure to acquire it or generate it internally is recognised as an expense when it is incurred. However, if the item is acquired in a business combination that is an acquisition, it forms part of the goodwill recognised at the date of acquisition (see paragraph 56).

Identifiability

10. The definition of an intangible asset requires that an intangible asset be identifiable to distinguish it clearly from goodwill. Goodwill arising on a business combination that is an acquisition represents a payment made by the acquirer in anticipation of future economic benefits. The future economic benefits may result from synergy between the identifiable assets acquired or from assets which, individually, do not qualify for recognition in the financial statements but for which the acquirer is prepared to make a payment in the acquisition.

11. An intangible asset can be clearly distinguished from goodwill if the asset is separable. An asset is separable if the enterprise could rent, sell, exchange or distribute the specific future economic benefits attributable to the asset without also disposing of future economic benefits that flow from other assets used in the same revenue earning activity.

12. Separability is not a necessary condition for identifiability since an enterprise may be able to identify an asset in some other way. For example, if an intangible asset is acquired with a group of assets, the transaction may involve the transfer of legal rights that enable an enterprise to identify the intangible asset. Similarly, if an internal project aims to create legal rights for the enterprise, the nature of these rights may assist the enterprise in identifying an underlying internally generated intangible asset. Also, even if an asset generates future economic benefits only in combination with other assets, the asset is identifiable if the enterprise can identify the future economic benefits that will flow from the asset.

Control

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

14. Market and technical knowledge may give rise to future economic benefits. An enterprise controls those benefits if, for example, the knowledge is protected by legal rights such as copyrights, a restraint of trade agreement (where permitted) or by a legal duty on employees to maintain confidentiality.

15. An enterprise may have a team of skilled staff and may be able to identify incremental staff skills leading to future economic benefits from training. The enterprise may also expect that the staff will continue to make their skills available to the enterprise. However, usually an enterprise has insufficient control over the expected future economic benefits arising from a team of skilled staff and from training to consider that these items meet the definition of an intangible asset. For a similar reason, specific management or technical talent is unlikely to meet the definition of an intangible asset, unless it is protected by legal rights to use it and to obtain the future economic benefits expected from it, and it also meets the other parts of the definition.

16. An enterprise may have a portfolio of customers or a market share and expect that, due to its efforts in building customer relationships and loyalty, the customers will continue to trade with the enterprise. However, in the absence of legal rights to protect, or other ways to control, the relationships with customers or the loyalty of the customers to the enterprise, the enterprise usually has insufficient control over the economic benefits from customer relationships and loyalty to consider that such items (portfolio of customers, market shares, customer relationships, customer loyalty) meet the definition of intangible assets.

Future economic benefits

17. The future economic benefits flowing from an intangible asset may include revenue from the sale of products or services, cost savings, or other benefits resulting from the use of the asset by the enterprise. For example, the use of intellectual property in a production process may reduce future production costs rather than increase future revenues.

RECOGNITION AND INITIAL MEASUREMENT OF AN INTANGIBLE ASSET

18. The recognition of an item as an intangible asset requires an enterprise to demonstrate that the item meets the:

    (a) definition of an intangible asset (see paragraphs 7 to 17); and

    (b) recognition criteria set out in this Standard (see paragraphs 19 to 55).

19. ***An intangible asset should be recognised if, and only if:***

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

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

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

21. An enterprise uses judgement to assess the degree of certainty attached to the flow of future economic benefits that are attributable to the use of the asset on the basis of the evidence available at the time of initial recognition, giving greater weight to external evidence.

22. ***An intangible asset should be measured initially at cost.***

Separate acquisition

23. If an intangible asset is acquired separately, the cost of the intangible asset can usually be measured reliably. This is particularly so when the purchase consideration is in the form of cash or other monetary assets.

24. The cost of an intangible asset comprises its purchase price, including any import duties and non-refundable purchase taxes, and any directly attributable expenditure on preparing the asset for its intended use. Directly attributable expenditure includes, for example, professional fees for legal services. Any trade discounts and rebates are deducted in arriving at the cost.

25. If payment for an intangible asset is deferred beyond normal credit terms, its cost is the cash price equivalent; the difference between this amount and the total payments is recognised as interest expense over the period of credit unless it is capitalised under the allowed alternative treatment in IAS 23, borrowing costs.

26. If an intangible asset is acquired in exchange for equity instruments of the reporting enterprise, the cost of the asset is the fair value of the equity instruments issued, which is equal to the fair value of the asset.

Acquisition as part of a business combination

27. Under IAS 22 (revised 1998), business combinations, if an intangible asset is acquired in a business combination that is an acquisition, the cost of that intangible asset is based on its fair value at the date of acquisition.

28. Judgement is required to determine whether the cost (i.e. fair value) of an intangible asset acquired in a business combination can be measured with sufficient reliability for the purpose of separate recognition. Quoted market prices in an active market provide the most reliable measurement of fair value (see also paragraph 67). The appropriate market price is usually the current bid price. If current bid prices are unavailable, the price of the most recent similar transaction may provide a basis from which to estimate fair value, provided that there has not been a significant change in economic circumstances between the transaction date and the date at which the asset's fair value is estimated.

29. If no active market exists for an asset, its cost reflects the amount that the enterprise would have paid, at the date of the acquisition, for the asset in an arm's length transaction between knowledgeable and willing parties, based on the best information available. In determining this amount, an enterprise considers the outcome of recent transactions for similar assets.

30. Certain enterprises that are regularly involved in the purchase and sale of unique intangible assets have developed techniques for estimating their fair values indirectly. These techniques may be used for initial measurement of an intangible asset acquired in a business combination that is an acquisition if their objective is to estimate fair value as defined in this Standard and if they reflect current transactions and practices in the industry to which the asset belongs. These techniques include, where appropriate, applying multiples reflecting current market transactions to certain indicators driving the profitability of the asset (such as revenue, market shares, operating profit, etc.) or discounting estimated future net cash flows from the asset.

31. In accordance with this Standard and the requirements in IAS 22 (revised 1998) for the recognition of identifiable assets and liabilities:

    (a) an acquirer recognises an intangible asset that meets the recognition criteria in paragraphs 19 and 20, even if that intangible asset had not been recognised in the financial statements of the acquiree; and

    (b) if the cost (i.e. fair value) of an intangible asset acquired as part of a business combination that is an acquisition cannot be measured reliably, that asset is not recognised as a separate intangible asset but is included in goodwill (see paragraph 56).

32. Unless there is an active market for an intangible asset acquired in a business combination that is an acquisition, IAS 22 (revised 1998) limits the cost initially recognised for the intangible asset to an amount that does not create or increase any negative goodwill arising at the date of acquisition.

Acquisition by way of a government grant

33. In some cases, an intangible asset may be acquired free of charge, or for nominal consideration, by way of a government grant. This may occur when a government transfers or allocates to an enterprise intangible assets such as airport landing rights, licences to operate radio or television stations, import licences or quotas or rights to access other restricted resources. Under IAS 20, accounting for government grants and disclosure of government assistance, an enterprise may choose to recognise both the intangible asset and the grant at fair value initially. If an enterprise chooses not to recognise the asset initially at fair value, the enterprise recognises the asset initially at a nominal amount (under the other treatment permitted by IAS 20) plus any expenditure that is directly attributable to preparing the asset for its intended use.

Exchanges of assets

34. An intangible asset may be acquired in exchange or part exchange for a dissimilar intangible asset or other asset. The cost of such an item is measured at the fair value of the asset received, which is equivalent to the fair value of the asset given up, adjusted by the amount of any cash or cash equivalents transferred.

35. An intangible asset may be acquired in exchange for a similar asset that has a similar use in the same line of business and that has a similar fair value. An intangible asset may also be sold in exchange for an equity interest in a similar asset. In both cases, since the earnings process is incomplete, no gain or loss is recognised on the transaction. Instead, the cost of the new asset is the carrying amount of the asset given up. However, the fair value of the asset received may provide evidence of an impairment loss in the asset given up. Under these circumstances an impairment loss is recognised for the asset given up and the carrying amount after impairment is assigned to the new asset.

Internally generated goodwill

36. ***Internally generated goodwill should not be recognised as an asset.***

37. In some cases, expenditure is incurred to generate future economic benefits, but it does not result in the creation of an intangible asset that meets the recognition criteria in this Standard. Such expenditure is often described as contributing to internally generated goodwill. Internally generated goodwill is not recognised as an asset because it is not an identifiable resource controlled by the enterprise that can be measured reliably at cost.

38. Differences between the market value of an enterprise and the carrying amount of its identifiable net assets at any point in time may capture a range of factors that affect the value of the enterprise. However, such differences cannot be considered to represent the cost of intangible assets controlled by the enterprise.

Internally generated intangible assets

39. It is sometimes difficult to assess whether an internally generated intangible asset qualifies for recognition. It is often difficult:

(a) to identify whether, and the point of time when, there is an identifiable asset that will generate probable future economic benefits; and

(b) to determine the cost of the asset reliably. In some cases, the cost of generating an intangible asset internally cannot be distinguished from the cost of maintaining or enhancing the enterprise's internally generated goodwill or of running day-to-day operations.

Therefore, in addition to complying with the general requirements for the recognition and initial measurement of an intangible asset, an enterprise applies the requirements and guidance in paragraphs 40-55 below to all internally generated intangible assets.

40. To assess whether an internally generated intangible asset meets the criteria for recognition, an enterprise classifies the generation of the asset into:

(a) a research phase; and

(b) a development phase.

Although the terms 'research' and 'development' are defined, the terms 'research phase' and 'development phase' have a broader meaning for the purpose of this Standard.

41. If an enterprise cannot distinguish the research phase from the development phase of an internal project to create an intangible asset, the enterprise treats the expenditure on that project as if it were incurred in the research phase only.

Research phase

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

43. This Standard takes the view that, in the research phase of a project, an enterprise cannot demonstrate that an intangible asset exists that will generate probable future economic benefits. Therefore, this expenditure is always recognised as an expense when it is incurred.

44. Examples of research activities are:

(a) activities aimed at obtaining new knowledge;

(b) the search for, evaluation and final selection of, applications of research findings or other knowledge;

(c) the search for alternatives for materials, devices, products, processes, systems or services; and

(d) the formulation, design, evaluation and final selection of possible alternatives for new or improved materials, devices, products, processes, systems or services.

Development phase

45. ***An intangible asset arising from development (or from the development phase of an internal project) should be recognised if, and only if, an enterprise can demonstrate all of the following:***

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

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

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

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

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

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

46. In the development phase of a project, an enterprise can, in some instances, identify an intangible asset and demonstrate that the asset will generate probable future economic benefits. This is because the development phase of a project is further advanced than the research phase.

47. Examples of development activities are:

(a) the design, construction and testing of pre-production or pre-use prototypes and models;

(b) the design of tools, jigs, moulds and dies involving new technology;

(c) the design, construction and operation of a pilot plant that is not of a scale economically feasible for commercial production; and

(d) the design, construction and testing of a chosen alternative for new or improved materials, devices, products, processes, systems or services.

48. To demonstrate how an intangible asset will generate probable future economic benefits, an enterprise assesses the future economic benefits to be received from the asset using the principles in IAS 36, impairment of assets. If the asset will generate economic benefits only in combination with other assets, the enterprise applies the concept of cash-generating units as set out in IAS 36.

49. Availability of resources to complete, use and obtain the benefits from an intangible asset can be demonstrated by, for example, a business plan showing the technical, financial and other resources needed and the enterprise's ability to secure those resources. In certain cases, an enterprise demonstrates the availability of external finance by obtaining a lender's indication of its willingness to fund the plan.

50. An enterprise's costing systems can often measure reliably the cost of generating an intangible asset internally, such as salary and other expenditure incurred in securing copyrights or licences or developing computer software.

51. ***Internally generated brands, mastheads, publishing titles, customer lists and items similar in substance should not be recognised as intangible assets.***

52. This Standard takes the view that expenditure on internally generated brands, mastheads, publishing titles, customer lists and items similar in substance cannot be distinguished from the cost of developing the business as a whole. Therefore, such items are not recognised as intangible assets.

Cost of an internally generated intangible asset

53. The cost of an internally generated intangible asset for the purpose of paragraph 22 is the sum of expenditure incurred from the date when the intangible asset first meets the recognition criteria in paragraphs 19-20 and 45. Paragraph 59 prohibits reinstatement of expenditure recognised as an expense in previous annual financial statements or interim financial reports.

54. The cost of an internally generated intangible asset comprises all expenditure that can be directly attributed, or allocated on a reasonable and consistent basis, to creating, producing and preparing the asset for its intended use. The cost includes, if applicable:

    (a) expenditure on materials and services used or consumed in generating the intangible asset;

    (b) the salaries, wages and other employment related costs of personnel directly engaged in generating the asset;

    (c) any expenditure that is directly attributable to generating the asset, such as fees to register a legal right and the amortisation of patents and licences that are used to generate the asset; and

    (d) overheads that are necessary to generate the asset and that can be allocated on a reasonable and consistent basis to the asset (for example, an allocation of the depreciation of property, plant and equipment, insurance premiums and rent). Allocations of overheads are made on bases similar to those used in allocating overheads to inventories (see IAS 2, inventories). IAS 23, borrowing costs, establishes criteria for the recognition of interest as a component of the cost of an internally generated intangible asset.

55. The following are not components of the cost of an internally generated intangible asset:

    (a) selling, administrative and other general overhead expenditure unless this expenditure can be directly attributed to preparing the asset for use;

    (b) clearly identified inefficiencies and initial operating losses incurred before an asset achieves planned performance; and

    (c) expenditure on training staff to operate the asset.

Example illustrating paragraph 53

An enterprise is developing a new production process. During 20X5, expenditure incurred was 1 000, of which 900 was incurred before 1 December 20X5 and 100 was incurred between 1 December 20X5 and 31 December 20X5. The enterprise is able to demonstrate that, at 1 December 20X5, the production process met the criteria for recognition as an intangible asset. The recoverable amount of the know-how embodied in the process (including future cash outflows to complete the process before it is available for use) is estimated to be 500.

At the end of 20X5, the production process is recognised as an intangible asset at a cost of 100 (expenditure incurred since the date when the recognition criteria were met, that is, 1 December 20X5). The 900 expenditure incurred before 1 December 20X5 is recognised as an expense because the recognition criteria were not met until 1 December 20X5. This expenditure will never form part of the cost of the production process recognised in the balance sheet.

During 20X6, expenditure incurred is 2 000. At the end of 20X6, the recoverable amount of the know-how embodied in the process (including future cash outflows to complete the process before it is available for use) is estimated to be 1 900.

At the end of 20X6, the cost of the production process is 2 100 (100 expenditure recognised at the end of 20X5 plus 2 000 expenditure recognised in 20X6). The enterprise recognises an impairment loss of 200 to adjust the carrying amount of the process before impairment loss (2 100) to its recoverable amount (1 900). This impairment loss will be reversed in a subsequent period if the requirements for the reversal of an impairment loss in IAS 36, impairment of assets, are met.

RECOGNITION OF AN EXPENSE

56. ***Expenditure on an intangible item should be recognised as an expense when it is incurred unless:***

    (a) ***it forms part of the cost of an intangible asset that meets the recognition criteria (see paragraphs 18 to 55); or***

    (b) ***the item is acquired in a business combination that is an acquisition and cannot be recognised as an intangible asset. If this is the case, this expenditure (included in the cost of acquisition) should form part of the amount attributed to goodwill (negative goodwill) at the date of acquisition (see IAS 22 (revised 1998), business combinations).***

57. In some cases, expenditure is incurred to provide future economic benefits to an enterprise, but no intangible asset or other asset is acquired or created that can be recognised. In these cases, the expenditure is recognised as an expense when it is incurred. For example, expenditure on research is always recognised as an expense when it is incurred (see paragraph 42). Examples of other expenditure that is recognised as an expense when it is incurred include:

    (a) expenditure on start-up activities (start-up costs), unless this expenditure is included in the cost of an item of property, plant and equipment under IAS 16. Start-up costs may consist of establishment costs such as legal and secretarial costs incurred in establishing a legal entity, expenditure to open a new facility or business (pre-opening costs) or expenditures for commencing new operations or launching new products or processes (pre-operating costs);

    (b) expenditure on training activities;

    (c) expenditure on advertising and promotional activities; and

    (d) expenditure on relocating or reorganising part or all of an enterprise.

58. Paragraph 56 does not preclude recognising a prepayment as an asset when payment for the delivery of goods or services has been made in advance of the delivery of goods or the rendering of services.

Past expenses not to be recognised as an asset

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

SUBSEQUENT EXPENDITURE

60. ***Subsequent expenditure on an intangible asset after its purchase or its completion should be recognised as an expense when it is incurred unless:***

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

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

    If these conditions are met, the subsequent expenditure should be added to the cost of the intangible asset (1)***.***

61. Subsequent expenditure on a recognised intangible asset is recognised as an expense if this expenditure is required to maintain the asset at its originally assessed standard of performance. The nature of intangible assets is such that, in many cases, it is not possible to determine whether subsequent expenditure is likely to enhance or maintain the economic benefits that will flow to the enterprise from those assets. In addition, it is often difficult to attribute such expenditure directly to a particular intangible asset rather than the business as a whole. Therefore, only rarely will expenditure incurred after the initial recognition of a purchased intangible asset or after completion of an internally generated intangible asset result in additions to the cost of the intangible asset.

62. Consistent with paragraph 51, subsequent expenditure on brands, mastheads, publishing titles, customer lists and items similar in substance (whether externally purchased or internally generated) is always recognised as an expense to avoid the recognition of internally generated goodwill.

MEASUREMENT SUBSEQUENT TO INITIAL RECOGNITION

Benchmark treatment

63. ***After initial recognition, an intangible asset should be carried at its cost less any accumulated amortisation and any accumulated impairment losses.***

Allowed alternative treatment

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

65. The allowed alternative treatment does not allow:

    (a) the revaluation of intangible assets that have not previously been recognised as assets; or

    (b) the initial recognition of intangible assets at amounts other than their cost.

(1) See also SIC-6: cost of modifying existing software.

66. The allowed alternative treatment is applied after an asset has been initially recognised at cost. However, if only part of the cost of an intangible asset is recognised as an asset because the asset did not meet the criteria for recognition until part of the way through the process (see paragraph 53), the allowed alternative may be applied to the whole of that asset. Also, the allowed alternative treatment may be applied to an intangible asset that was received by way of a government grant and recognised at a nominal amount (see paragraph 33).

67. It is uncommon for an active market with the characteristics described in paragraph 7 to exist for an intangible asset, although this may occur. For example, in certain jurisdictions, an active market may exist for freely-transferable taxi licences, fishing licences or production quotas. However, an active market cannot exist for brands, newspaper mastheads, music and film publishing rights, patents or trade marks, because each such asset is unique. Also, although intangible assets are bought and sold, contracts are negotiated between individual buyers and sellers, and transactions are relatively infrequent. For these reasons, the price paid for one asset may not provide sufficient evidence of the fair value of another. Finally, prices are often not available to the public.

68. The frequency of revaluations depends on the volatility of the fair values of the intangible assets being revalued. If the fair value of a revalued asset differs materially from its carrying amount, a further revaluation is necessary. Some intangible assets may experience significant and volatile movements in fair value thus necessitating annual revaluation. Such frequent revaluations are unnecessary for intangible assets with only insignificant movements in fair value.

69. If an intangible asset is revalued, any accumulated amortisation at the date of the revaluation is either:

(a) restated proportionately with the change in the gross carrying amount of the asset so that the carrying amount of the asset after revaluation equals its revalued amount; or

(b) eliminated against the gross carrying amount of the asset and the net amount restated to the revalued amount of the asset.

70. ***If an intangible asset is revalued, all the other assets in its class should also be revalued, unless there is no active market for those assets.***

71. A class of intangible assets is a grouping of assets of a similar nature and use in an enterprise's operations. The items within a class of intangible assets are revalued simultaneously in order to avoid selective revaluation of assets and the reporting of amounts in the financial statements representing a mixture of costs and values as at different dates.

72. ***If an intangible asset in a class of revalued intangible assets cannot be revalued because there is no active market for this asset, the asset should be carried at its cost less any accumulated amortisation and impairment losses.***

73. ***If the fair value of a revalued intangible asset can no longer be determined by reference to an active market, the carrying amount of the asset should be its revalued amount at the date of the last revaluation by reference to the active market less any subsequent accumulated amortisation and any subsequent accumulated impairment losses.***

74. The fact that an active market no longer exists for a revalued intangible asset may indicate that the asset may be impaired and that it needs to be tested under IAS 36, impairment of assets.

75. If the fair value of the asset can be determined by reference to an active market at a subsequent measurement date, the allowed alternative treatment is applied from that date.

76. ***If an intangible asset's carrying amount is increased as a result of a revaluation, the increase should be credited directly to equity under the heading of revaluation surplus. However, a revaluation increase should be recognised as income to the extent that it reverses a revaluation decrease of the same asset and that revaluation decrease was previously recognised as an expense.***

77. ***If an asset's carrying amount is decreased as a result of a revaluation, the decrease should be recognised as an expense. However, a revaluation decrease should be charged directly against any related revaluation surplus to the extent that the decrease does not exceed the amount held in the revaluation surplus in respect of that same asset.***

78. The cumulative revaluation surplus included in equity may be transferred directly to retained earnings when the surplus is realised. The whole surplus may be realised on the retirement or disposal of the asset. However, some of the surplus may be realised as the asset is used by the enterprise; in such a case, the amount of the surplus realised is the difference between amortisation based on the revalued carrying amount of the asset and amortisation that would have been recognised based on the asset's historical cost. The transfer from revaluation surplus to retained earnings is not made through the income statement.

AMORTISATION

Amortisation Period

79. ***The depreciable amount of an intangible asset should be allocated on a systematic basis over the best estimate of its useful life. There is a rebuttable presumption that the useful life of an intangible asset will not exceed 20 years from the date when the asset is available for use. Amortisation should commence when the asset is available for use.***

80. As the future economic benefits embodied in an intangible asset are consumed over time, the carrying amount of the asset is reduced to reflect that consumption. This is achieved by systematic allocation of the cost or revalued amount of the asset, less any residual value, as an expense over the asset's useful life. Amortisation is recognised whether or not there has been an increase in, for example, the asset's fair value or recoverable amount. Many factors need to be considered in determining the useful life of an intangible asset including:

(a) the expected usage of the asset by the enterprise and whether the asset could be efficiently managed by another management team;

(b) typical product life cycles for the asset and public information on estimates of useful lives of similar types of assets that are used in a similar way;

(c) technical, technological or other types of obsolescence;

(d) the stability of the industry in which the asset operates and changes in the market demand for the products or services output from the asset;

(e) expected actions by competitors or potential competitors;

(f) the level of maintenance expenditure required to obtain the expected future economic benefits from the asset and the company's ability and intent to reach such a level;

(g) the period of control over the asset and legal or similar limits on the use of the asset, such as the expiry dates of related leases; and

(h) whether the useful life of the asset is dependent on the useful life of other assets of the enterprise.

81. Given the history of rapid changes in technology, computer software and many other intangible assets are susceptible to technological obsolescence. Therefore, it is likely that their useful life will be short.

82. Estimates of the useful life of an intangible asset generally become less reliable as the length of the useful life increases. This Standard adopts a presumption that the useful life of intangible assets is unlikely to exceed 20 years.

83. In rare cases, there may be persuasive evidence that the useful life of an intangible asset will be a specific period longer than 20 years. In these cases, the presumption that the useful life generally does not exceed 20 years is rebutted and the enterprise:

(a) amortises the intangible asset over the best estimate of its useful life;

(b) estimates the recoverable amount of the intangible asset at least annually in order to identify any impairment loss (see paragraph 99); and

(c) discloses the reasons why the presumption is rebutted and the factor(s) that played a significant role in determining the useful life of the asset (see paragraph 111(a)).

Examples

A. An enterprise has purchased an exclusive right to generate hydro-electric power for 60 years. The costs of generating hydro-electric power are much lower than the costs of obtaining power from alternative sources. It is expected that the geographical area surrounding the power station will demand a significant amount of power from the power station for at least 60 years.

The enterprise amortises the right to generate power over 60 years, unless there is evidence that its useful life is shorter.

B. An enterprise has purchased an exclusive right to operate a toll motorway for 30 years. There is no plan to construct alternative routes in the area served by the motorway. It is expected that this motorway will be in use for at least 30 years.

The enterprise amortises the right to operate the motorway over 30 years, unless there is evidence that its useful life is shorter.

84. The useful life of an intangible asset may be very long but it is always finite. Uncertainty justifies estimating the useful life of an intangible asset on a prudent basis, but it does not justify choosing a life that is unrealistically short.

85. ***If control over the future economic benefits from an intangible asset is achieved through legal rights that have been granted for a finite period, the useful life of the intangible asset should not exceed the period of the legal rights unless:***

(a) ***the legal rights are renewable; and***

(b) ***renewal is virtually certain.***

86. There may be both economic and legal factors influencing the useful life of an intangible asset: economic factors determine the period over which future economic benefits will be received; legal factors may restrict the period over which the enterprise controls access to these benefits. The useful life is the shorter of the periods determined by these factors.

87. The following factors, among others, indicate that renewal of a legal right is virtually certain:

(a) the fair value of the intangible asset does not reduce as the initial expiry date approaches, or does not reduce by more than the cost of renewing the underlying right;

(b) there is evidence (possibly based on past experience) that the legal rights will be renewed; and

(c) there is evidence that the conditions necessary to obtain the renewal of the legal right (if any) will be satisfied.

Amortisation method

88. ***The amortisation method used should reflect the pattern in which the asset's economic benefits are consumed by the enterprise. If that pattern cannot be determined reliably, the straight-line method should be used. The amortisation charge for each period should be recognised as an expense unless another International Accounting Standard permits or requires it to be included in the carrying amount of another asset.***

89. A variety of amortisation methods can be used to allocate the depreciable amount of an asset on a systematic basis over its useful life. These methods include the straight-line method, the diminishing balance method and the unit of production method. The method used for an asset is selected based on the expected pattern of consumption of economic benefits and is consistently applied from period to period, unless there is a change in the expected pattern of consumption of economic benefits to be derived from that asset. There will rarely, if ever, be persuasive evidence to support an amortisation method for intangible assets that results in a lower amount of accumulated amortisation than under the straight-line method.

90. Amortisation is usually recognised as an expense. However, sometimes, the economic benefits embodied in an asset are absorbed by the enterprise in producing other assets rather than giving rise to an expense. In these cases, the amortisation charge forms part of the cost of the other asset and is included in its carrying amount. For example, the amortisation of intangible assets used in a production process is included in the carrying amount of inventories (see IAS 2, inventories).

Residual Value

91. ***The residual value of an intangible asset should be assumed to be zero unless:***

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

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

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

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

92. The depreciable amount of an asset is determined after deducting its residual value. A residual value other than zero implies that an enterprise expects to dispose of the intangible asset before the end of its economic life.

93. If the benchmark treatment is adopted, the residual value is estimated using prices prevailing at the date of acquisition of the asset, for the sale of a similar asset that has reached the end of its estimated useful life and that has operated under conditions similar to those in which the asset will be used. The residual value is not subsequently increased for changes in prices or value. If the allowed alternative treatment is adopted, a new estimate of residual value is made at the date of each revaluation of the asset using prices prevailing at that date.

Review of amortisation period and amortisation method

94. ***The amortisation period and the amortisation method should be reviewed at least at each financial year end. If the expected useful life of the asset is significantly different from previous estimates, the amortisation period should be changed accordingly. If there has been a significant change in the expected pattern of economic benefits from the asset, the amortisation method should be changed to reflect the changed pattern. Such changes should be accounted for as changes in accounting estimates under IAS 8, net profit or loss for the period, fundamental errors and changes in accounting policies, by adjusting the amortisation charge for the current and future periods.***

95. During the life of an intangible asset, it may become apparent that the estimate of its useful life is inappropriate. For example, the useful life may be extended by subsequent expenditure that improves the condition of the asset beyond its originally assessed standard of performance. Also, the recognition of an impairment loss may indicate that the amortisation period needs to be changed.

96. Over time, the pattern of future economic benefits expected to flow to an enterprise from an intangible asset may change. For example, it may become apparent that a diminishing balance method of amortisation is appropriate rather than a straight-line method. Another example is if use of the rights represented by a licence is deferred pending action on other components of the business plan. In this case, economic benefits that flow from the asset may not be received until later periods.

RECOVERABILITY OF THE CARRYING AMOUNT — IMPAIRMENT LOSSES

97. To determine whether an intangible asset is impaired, an enterprise applies IAS 36, impairment of assets. That Standard explains how an enterprise reviews the carrying amount of its assets, how it determines the recoverable amount of an asset and when it recognises or reverses an impairment loss.

98. Under IAS 22 (revised 1998), business combinations, if an impairment loss occurs before the end of the first annual accounting period commencing after acquisition for an intangible asset acquired in a business combination that was an acquisition, the impairment loss is recognised as an adjustment to both the amount assigned to the intangible asset and the goodwill (negative goodwill) recognised at the date of acquisition. However, if the impairment loss relates to specific events or changes in circumstances occurring after the date of acquisition, the impairment loss is recognised under IAS 36 and not as an adjustment to the amount assigned to the goodwill (negative goodwill) recognised at the date of acquisition.

99. ***In addition to following the requirements included in IAS 36, impairment of assets, an enterprise should estimate the recoverable amount of the following intangible assets at least at each financial year end, even if there is no indication that the asset is impaired:***

(a) ***an intangible asset that is not yet available for use; and***

(b) ***an intangible asset that is amortised over a period exceeding 20 years from the date when the asset is available for use.***

The recoverable amount should be determined under IAS 36 and impairment losses recognised accordingly.

100. The ability of an intangible asset to generate sufficient future economic benefits to recover its cost is usually subject to great uncertainty until the asset is available for use. Therefore, this Standard requires an enterprise to test for impairment, at least annually, the carrying amount of an intangible asset that is not yet available for use.

101. It is sometimes difficult to identify whether an intangible asset may be impaired because, among other things, there is not necessarily any obvious evidence of obsolescence. This difficulty arises particularly if the asset has a long useful life. As a consequence, this Standard requires, as a minimum, an annual calculation of the recoverable amount of an intangible asset if its useful life exceeds 20 years from the date when it becomes available for use.

102. The requirement for an annual impairment test of an intangible asset applies whenever the current total estimated useful life of the asset exceeds 20 years from when it became available for use. Therefore, if the useful life of an intangible asset was estimated to be less than 20 years at initial recognition, but the useful life is extended by subsequent expenditure to exceed 20 years from when the asset became available for use, an enterprise performs the impairment test required under paragraph 99(b) and also makes the disclosure required under paragraph 111(a).

RETIREMENTS AND DISPOSALS

103. ***An intangible asset should be derecognised (eliminated from the balance sheet) on disposal or when no future economic benefits are expected from its use and subsequent disposal.***

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

105. If an intangible asset is exchanged for a similar asset under the circumstances described in paragraph 35, the cost of the acquired asset is equal to the carrying amount of the asset disposed of and no gain or loss results.

106. An intangible asset that is retired from active use and held for disposal is carried at its carrying amount at the date when the asset is retired from active use. At least at each financial year end, an enterprise tests the asset for impairment under IAS 36, impairment of assets, and recognises any impairment loss accordingly.

DISCLOSURE

General

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

(a) ***the useful lives or the amortisation rates used;***

(b) ***the amortisation methods used;***

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

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

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

(i) ***additions, indicating separately those from internal development and through business combinations;***

(ii) ***retirements and disposals;***

(iii) ***increases or decreases during the period resulting from revaluations under paragraphs 64, 76 and 77 and from impairment losses recognised or reversed directly in equity under IAS 36, impairment of assets (if any);***

(iv) ***impairment losses recognised in the income statement during the period under IAS 36 (if any);***

(v) ***impairment losses reversed in the income statement during the period under IAS 36 (if any);***

(vi) ***amortisation recognised during the period;***

(vii) ***net exchange differences arising on the translation of the financial statements of a foreign entity; and***

(viii) ***other changes in the carrying amount during the period.***

Comparative information is not required.

108. A class of intangible assets is a grouping of assets of a similar nature and use in an enterprise's operations. Examples of separate classes may include:

(a) brand names;

(b) mastheads and publishing titles;

(c) computer software;

(d) licences and franchises;

(e) copyrights, patents and other industrial property rights, service and operating rights;

(f) recipes, formulae, models, designs and prototypes; and

(g) intangible assets under development.

The classes mentioned above are disaggregated (aggregated) into smaller (larger) classes if this results in more relevant information for the users of the financial statements.

109. An enterprise discloses information on impaired intangible assets under IAS 36 in addition to the information required by paragraph 107(e)(iii) to (v).

110. An enterprise discloses the nature and effect of a change in an accounting estimate that has a material effect in the current period or that is expected to have a material effect in subsequent periods, under IAS 8, net profit or loss for the period, fundamental errors and changes in accounting policy. Such disclosure may arise from changes in:

(a) the amortisation period;

(b) the amortisation method; or

(c) residual values.

111. ***The financial statements should also disclose:***

(a) ***if an intangible asset is amortised over more than 20 years, the reasons why the presumption that the useful life of an intangible asset will not exceed 20 years from the date when the asset is available for use is rebutted. In giving these reasons, the enterprise should describe the factor(s) that played a significant role in determining the useful life of the asset;***

(b) ***a description, the carrying amount and remaining amortisation period of any individual intangible asset that is material to the financial statements of the enterprise as a whole;***

(c) ***for intangible assets acquired by way of a government grant and initially recognised at fair value (see paragraph 33):***

(i) ***the fair value initially recognised for these assets;***

(ii) ***their carrying amount; and***

(iii) ***whether they are carried under the benchmark or the allowed alternative treatment for subsequent measurement;***

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

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

112. When an enterprise describes the factor(s) that played a significant role in determining the useful life of an intangible asset that is amortised over more than 20 years, the enterprise considers the list of factors in paragraph 80.

Intangible assets carried under the allowed alternative treatment

113. ***If intangible assets are carried at revalued amounts, the following should be disclosed:***

(a) ***by class of intangible assets:***

(i) ***the effective date of the revaluation;***

(ii) ***the carrying amount of revalued intangible assets; and***

(iii) ***the carrying amount that would have been included in the financial statements had the revalued intangible assets been carried under the benchmark treatment in paragraph 63; and***

(b) ***the amount of the revaluation surplus that relates to intangible assets at the beginning and end of the period, indicating the changes during the period and any restrictions on the distribution of the balance to shareholders.***

114. It may be necessary to aggregate the classes of revalued assets into larger classes for disclosure purposes. However, classes are not aggregated if this would result in the combination of a class of intangible assets that includes amounts measured under both benchmark and allowed alternative treatments for subsequent measurement.

Research and development expenditure

115. ***The financial statements should disclose the aggregate amount of research and development expenditure recognised as an expense during the period.***

116. Research and development expenditure comprises all expenditure that is directly attributable to research or development activities or that can be allocated on a reasonable and consistent basis to such activities (see paragraphs 54 to 55 for guidance on the type of expenditure to be included for the purpose of the disclosure requirement in paragraph 115).

Other information

117. An enterprise is encouraged, but not required, to give the following information:

(a) a description of any fully amortised intangible asset that is still in use; and

(b) a brief description of significant intangible assets controlled by the enterprise but not recognised as assets because they did not meet the recognition criteria in this Standard or because they were acquired or generated before this Standard was effective.

TRANSITIONAL PROVISIONS

118. ***At the date when this Standard becomes effective (or at the date of adoption, if earlier), it should be applied as set out in the following tables. In all cases other than those detailed in these tables, this Standard should be applied retrospectively, unless it is impracticable to do so.***

119. The tables below require retrospective application whenever this is necessary to eliminate an item that no longer qualifies for recognition under this Standard or if the previous measurement of an intangible asset contradicted the principles set out in this Standard (for example, intangible assets that have never been amortised or that have been revalued but not by reference to an active market). In other cases, prospective application of the recognition and amortisation requirements is required or, in some cases, permitted.

120. ***The effect of adopting this Standard on its effective date (or earlier) should be recognised under IAS 8, net profit or loss for the period, fundamental errors and changes in accounting policies, that is, as an adjustment either to the opening balance of retained earnings of the earliest period presented (IAS 8 benchmark treatment) or to the net profit or loss for the current period (IAS 8 allowed alternative treatment).***

121. ***In the first annual financial statements issued under this Standard, an enterprise should disclose the transitional provisions adopted where transitional provisions under this Standard permit a choice.***

Transitional Provisions — Recognition

Circumstances	Requirements
1. An intangible item was recognised as a separate asset — whether or not described as an intangible asset — and, at the effective date of this Standard (or at the date of adoption of this Standard, if earlier), the item does not meet the definition of, or recognition criteria for, an intangible asset.	
(a) The item was acquired in a business combination that was an acquisition.	(i) Reallocate the item to the goodwill (negative goodwill) resulting from the same acquisition; and (ii) adjust the goodwill (negative goodwill) recognised at the date of acquisition retrospectively, as if the item had always been included in the goodwill (negative goodwill) recognised at the date of acquisition. For example, if the goodwill was recognised as an asset and amortised, estimate the accumulated amortisation that would have been recognised, had the item been included in the goodwill recognised at the date of acquisition, and adjust the carrying amount of the goodwill accordingly.
(b) The item was not acquired in a business combination that was an acquisition (for example, it was purchased separately or generated internally).	Derecognise the item (eliminate it from the balance sheet).
2. An intangible item was recognised as a separate asset — whether or not described as an intangible asset — and, at the effective date of this Standard (or at the date of adoption of this Standard, if earlier), the item meets the definition of, and recognition criteria for, an intangible asset.	
(a) The asset was recognised initially at cost.	Classify the asset as an intangible asset. The cost initially recognised for the asset is deemed to have been properly determined. See transitional provisions for subsequent measurement and amortisation under circumstances 4 and 5 below.
(b) The asset was recognised initially at an amount other than cost.	(i) Classify the asset as an intangible asset; and (ii) re-estimate the carrying amount of the asset at cost (or revalued amount, after initial recognition at cost) less accumulated amortisation, determined under this Standard. If the cost of the intangible asset cannot be determined, derecognise the asset (eliminate it from the balance sheet).

3. At the effective date of this Standard (or at the date of adoption of this Standard, if earlier), an item meets the definition of, and recognition criteria for, an intangible asset but it was not previously recognised as an asset.

(a)	The intangible asset was acquired in a business combination that was an acquisition and formed part of the goodwill recognised.	Recognition of the intangible asset is encouraged, but not required. If the intangible asset is recognised: (i) measure the carrying amount of the asset at cost (or revalued amount) less accumulated amortisation determined under this Standard; and (ii) adjust the goodwill recognised at the date of acquisition retrospectively, as if the intangible asset had never been included in the goodwill recognised at the date of acquisition. For example, if the goodwill was recognised as an asset and amortised, estimate the effect on the accumulated amortisation of the goodwill of distinguishing the intangible asset separately and adjust the carrying amount of the goodwill accordingly.
(b)	The intangible asset was not acquired in a business combination that was an acquisition (for example, it was purchased separately or generated internally).	The intangible asset should not be recognised.

Transitional Provisions — Amortisation of an intangible asset carried under the benchmark treatment

	Circumstances	Requirements
4.	The asset was not previously amortised or the amortisation charge was deemed to be nil.	Restate the carrying amount of the asset as if the accumulated amortisation had always been determined under this Standard.
5.	The asset was previously amortised. Accumulated amortisation determined under this Standard is different to that previously determined (because the amortisation period and/or the amortisation method is different).	Do not restate the carrying amount of the intangible asset for any difference between the accumulated amortisation in prior years and that calculated under this Standard. Amortise any carrying amount of the asset over its remaining useful life determined under this Standard (i.e. any change is treated as a change in accounting estimate — see paragraph 94).

Transitional Provisions — Revalued intangible asset

	Circumstances	Requirements
6.	An intangible asset was carried at a revalued amount not determined by reference to an active market:	
(a)	There is an active market for the asset.	The asset should be revalued by reference to this active market at the effective date of this Standard (or at the date of adoption of this Standard, if earlier).
(b)	There is no active market for the asset.	(i) Eliminate the effect of any revaluation; and (ii) measure the carrying amount of the asset at cost less accumulated amortisation, determined under this Standard.

EFFECTIVE DATE

122. ***This International Accounting Standard becomes operative for annual financial statements covering periods beginning on or after 1 July 1999. Earlier application is encouraged. If an enterprise applies this Standard for annual financial statements covering periods beginning before 1 July 1999, the enterprise should:***

(a) ***disclose that fact; and***

(b) ***adopt IAS 22 (revised 1998), business combinations, and IAS 36, impairment of assets, at the same time.***

123. This Standard supersedes:

(a) IAS 4, depreciation accounting, with respect to the amortisation (depreciation) of intangible assets; and

(b) IAS 9, research and development costs.

INTERNATIONAL ACCOUNTING STANDARD IAS 40

Investment property

This International Accounting Standard was approved by the IASC Board in March 2000 and became effective for financial statements covering periods beginning on or after 1 January 2001.

This Standard supersedes IAS 25, Accounting for Investments, with respect to accounting for investment property. IAS 25 was withdrawn when this Standard came into effect.

In January 2001, IAS 41, agriculture, amended paragraph 3. The amended text is operative for annual financial statements covering periods beginning on or after 1 January 2003.

INTRODUCTION

1. IAS 40 prescribes the accounting treatment for investment property and related disclosure requirements. The Standard is effective for annual financial statements covering periods beginning on or after 1 January 2001. Earlier application is encouraged.

2. The Standard replaces previous requirements in IAS 25, accounting for investments. Under IAS 25, an enterprise was permitted to choose from among a variety of accounting treatments for investment property (depreciated cost under the benchmark treatment in IAS 16, property, plant and equipment, revaluation with depreciation under the allowed alternative treatment in IAS 16, cost less impairment under IAS 25 or revaluation under IAS 25). IAS 25 is withdrawn when this Standard comes into effect.

3. Investment property is defined as property (land or a building — or part of a building — or both) held (by the owner or by the lessee under a finance lease) to earn rentals or for capital appreciation or both, rather than for:

(a) use in the production or supply of goods or services or for administrative purposes; or

(b) sale in the ordinary course of business.

4. The Standard does not deal with:

(a) owner-occupied property (that is, property held for use in the production or supply of goods or services or for administrative purposes) — carried under IAS 16, property, plant and equipment, at either depreciated cost or revalued amount less subsequent depreciation;

(b) property held for sale in the ordinary course of business — carried at the lower of cost and net realisable value under IAS 2, inventories;

(c) property being constructed or developed for future use as investment property — IAS 16 applies to such property until the construction or development is complete, at which time the property becomes investment property and this Standard applies. However, this Standard does apply to existing investment property that is being redeveloped for continued future use as investment property;

(d) an interest held by a lessee under an operating lease — covered by IAS 17, leases;

(e) biological assets attached to land related to agricultural activity — covered by IAS 41, agriculture; and

(f) mineral rights, the exploration for and development of minerals, oil, natural gas and similar non-regenerative natural resources.

5. The Standard permits enterprises to choose either:

(a) a fair value model: investment property should be measured at fair value and changes in fair value should be recognised in the income statement; or

(b) a cost model. The cost model is the benchmark treatment in IAS 16, property, plant and equipment: investment property should be measured at depreciated cost (less any accumulated impairment losses). An enterprise that chooses the cost model should disclose the fair value of its investment property.

6. The fair value model differs from the revaluation model that the Board already permits for certain non-financial assets. Under the revaluation model, increases in carrying amount above a cost-based measure are recognised as revaluation surplus. However, under the fair value model, all changes in fair value are recognised in the income statement.

7. This is the first time that the Board has introduced a fair value accounting model for non-financial assets. The comment letters on Exposure Draft E64 showed that although many support this step, many others still have significant conceptual and practical reservations about extending a fair value model to non-financial assets. Also, some believe that certain property markets are not yet sufficiently mature for a fair value model to work satisfactorily. Furthermore, some believe that it is impossible to create a rigorous definition of investment property and that this makes it impracticable to require a fair value model at present.

8. For those reasons, the Board believes that it is impracticable, at this stage, to require a fair value model for investment property. At the same time, the Board believes that it is desirable to permit a fair value model. This evolutionary step forward will allow preparers and users to gain greater experience working with a fair value model and will allow time for certain property markets to achieve greater maturity.

9. The Standard requires that an enterprise should apply the model chosen to all its investment property. A change from one model to the other model should be made only if the change will result in a more appropriate presentation. The Standard states that this is highly unlikely to be the case for a change from the fair value model to the cost model.

10. In exceptional cases, there is clear evidence when an enterprise first acquires an investment property (or when an existing property first becomes investment property following the completion of construction or development, or after a change in use) that the enterprise will not be able to determine the fair value of the investment property reliably on a continuing basis. In such cases, the Standard requires an enterprise to measure that investment property using the benchmark treatment in IAS 16 until the disposal of the investment property. The residual value of the investment property should be assumed to be zero. An enterprise that has chosen the fair value model measures all its other investment property at fair value.

11. Appendix A is a decision tree that summarises how an enterprise determines whether it applies IAS 40 (for investment property), rather than IAS 16, property, plant and equipment (for owner-occupied property or property that is being constructed or developed for future use as investment property), or IAS 2, inventories (for property held for sale in the ordinary course of business).

12. Appendix B, Basis for conclusions, summarises the Board's reasons for adopting the requirements set out in IAS 40.

CONTENTS

The standards, which have been set in bold italic type, should be read in the context of the background material and implementation guidance in this Standard, and in the context of the Preface to International Accounting Standards. International Accounting Standards are not intended to apply to immaterial items (see paragraph 12 of the Preface).

OBJECTIVE

The objective of this Standard is to prescribe the accounting treatment for investment property and related disclosure requirements.

SCOPE

1. ***This Standard should be applied in the recognition, measurement and disclosure of investment property.***

2. Among other things, this Standard deals with the measurement in a lessee's financial statements of investment property held under a finance lease and with the measurement in a lessor's financial statements of investment property leased out under an operating lease. This Standard does not deal with matters covered in IAS 17, leases, including:

   (a) classification of leases as finance leases or operating leases;

   (b) recognition of lease income earned on investment property (see also IAS 18, revenue);

   (c) measurement in a lessee's financial statements of property held under an operating lease;

   (d) measurement in a lessor's financial statements of property leased out under a finance lease;

   (e) accounting for sale and leaseback transactions; and

   (f) disclosure about finance leases and operating leases.

3. This Standard does not apply to:

   (a) biological assets attached to land related to agricultural activity (see IAS 41, agriculture); and

   (b) mineral rights, the exploration for and extraction of minerals, oil, natural gas and similar non-regenerative resources.

DEFINITIONS

4. ***The following terms are used in this Standard with the meanings specified:***

   Investment property is property (land or a building — or part of a building — or both) held (by the owner or by the lessee under a finance lease) to earn rentals or for capital appreciation or both, rather than for:

   (a) ***use in the production or supply of goods or services or for administrative purposes; or***

(b) ***sale in the ordinary course of business.***

Owner-occupied property is property held (by the owner or by the lessee under a finance lease) for use in the production or supply of goods or services or for administrative purposes.

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

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

Carrying amount is the amount at which an asset is recognised in the balance sheet.

5. Investment property is held to earn rentals or for capital appreciation or both. Therefore, an investment property generates cash flows largely independently of the other assets held by an enterprise. This distinguishes investment property from owner-occupied property. The production or supply of goods or services (or the use of property for administrative purposes) generates cash flows that are attributable not merely to property, but also to other assets used in the production or supply process. IAS 16, property, plant and equipment, applies to owner-occupied property.

6. The following are examples of investment property:

(a) land held for long-term capital appreciation rather than for short-term sale in the ordinary course of business;

(b) land held for a currently undetermined future use. (If an enterprise has not determined that it will use the land either as owner-occupied property or for short-term sale in the ordinary course of business, the land is considered to be held for capital appreciation);

(c) a building owned by the reporting enterprise (or held by the reporting enterprise under a finance lease) and leased out under one or more operating leases; and

(d) a building that is vacant but is held to be leased out under one or more operating leases.

7. The following are examples of items that are not investment property and therefore fall outside the scope of this Standard:

(a) property held for sale in the ordinary course of business or in the process of construction or development for such sale (see IAS 2, inventories), for example property acquired exclusively with a view to subsequent disposal in the near future or for development and resale;

(b) property being constructed or developed on behalf of third parties (see IAS 11, construction contracts);

(c) owner-occupied property (see IAS 16, property, plant and equipment), including (among other things) property held for future use as owner-occupied property, property held for future development and subsequent use as owner-occupied property, property occupied by employees (whether or not the employees pay rent at market rates) and owner-occupied property awaiting disposal; and

(d) property that is being constructed or developed for future use as investment property. IAS 16 applies to such property until construction or development is complete, at which time the property becomes investment property and this Standard applies. However, this Standard does apply to existing investment property that is being redeveloped for continued future use as investment property (see paragraph 52).

8. Certain properties include a portion that is held to earn rentals or for capital appreciation and another portion that is held for use in the production or supply of goods or services or for administrative purposes. If these portions could be sold separately (or leased out separately under a finance lease), an enterprise accounts for the portions separately. If the portions could not be sold separately, the property is investment property only if an insignificant portion is held for use in the production or supply of goods or services or for administrative purposes.

9. In certain cases, an enterprise provides ancillary services to the occupants of a property held by the enterprise. An enterprise treats such a property as investment property if the services are a relatively insignificant component of the arrangement as a whole. An example would be where the owner of an office building provides security and maintenance services to the lessees who occupy the building.

10. In other cases, the services provided are a more significant component. For example, if an enterprise owns and manages a hotel, services provided to guests are a significant component of the arrangement as a whole. Therefore, an owner-managed hotel is owner-occupied property, rather than investment property.

11. It may be difficult to determine whether ancillary services are so significant that a property does not qualify as investment property. For example, the owner of a hotel sometimes transfers certain responsibilities to third parties under a management contract. The terms of such management contracts vary widely. At one end of the spectrum, the owner's position may, in substance, be that of a passive investor. At the other end of the spectrum, the owner may simply have outsourced certain day-to-day functions while retaining significant exposure to variation in the cash flows generated by the operations of the hotel.

12. Judgement is needed to determine whether a property qualifies as investment property. An enterprise develops criteria so that it can exercise that judgement consistently in accordance with the definition of investment property and with the related guidance in paragraphs 5 to 11. Paragraph 66(a) requires an enterprise to disclose these criteria when classification is difficult.

13. Under IAS 17, leases, a lessee does not capitalise property held under an operating lease. Therefore, the lessee does not treat its interest in such property as investment property.

14. In some cases, an enterprise owns property that is leased to, and occupied by, its parent or another subsidiary. The property does not qualify as investment property in consolidated financial statements that include both enterprises, because the property is owner-occupied from the perspective of the group as a whole. However, from the perspective of the individual enterprise that owns it, the property is investment property if it meets the definition in paragraph 4. Therefore, the lessor treats the property as investment property in its individual financial statements.

RECOGNITION

15. ***Investment property should be recognised as an asset when, and only when:***

    (a) ***it is probable that the future economic benefits that are associated with the investment property will flow to the enterprise; and***

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

16. In determining whether an item satisfies the first criterion for recognition, an enterprise needs to assess the degree of certainty attaching to the flow of future economic benefits on the basis of the available evidence at the time of initial recognition. The second criterion for recognition is usually readily satisfied because the exchange transaction evidencing the purchase of the asset identifies its cost.

INITIAL MEASUREMENT

17. ***An investment property should be measured initially at its cost. Transaction costs should be included in the initial measurement.***

18. The cost of a purchased investment property comprises its purchase price, and any directly attributable expenditure. Directly attributable expenditure includes, for example, professional fees for legal services, property transfer taxes and other transaction costs.

19. The cost of a self-constructed investment property is its cost at the date when the construction or development is complete. Until that date, an enterprise applies IAS 16, property, plant and equipment. At that date, the property becomes investment property and this Standard applies (see paragraphs 51(e) and 59).

20. The cost of an investment property is not increased by start-up costs (unless they are necessary to bring the property to its working condition), initial operating losses incurred before the investment property achieves the planned level of occupancy or abnormal amounts of wasted material, labour or other resources incurred in constructing or developing the property.

21. If payment for an investment property is deferred, its cost is the cash price equivalent. The difference between this amount and the total payments is recognised as interest expense over the period of credit.

SUBSEQUENT EXPENDITURE

22. ***Subsequent expenditure relating to an investment property that has already been recognised should be added to the carrying amount of the investment property when it is probable that future economic benefits, in excess of the originally assessed standard of performance of the existing investment property, will flow to the enterprise. All other subsequent expenditure should be recognised as an expense in the period in which it is incurred.***

23. The appropriate accounting treatment for expenditure incurred subsequently to the acquisition of an investment property depends on the circumstances which were taken into account on the initial measurement and recognition of the related investment. For instance, when the carrying amount of an investment property already takes into account a loss in future economic benefits, subsequent expenditure to restore the future economic benefits expected from the asset is capitalised. This is also the case when the purchase price of an asset reflects the enterprise’s obligation to incur expenditure that is necessary in the future to bring the asset to its working condition. An example of this might be the acquisition of a building requiring renovation. In such circumstances, the subsequent expenditure is added to the carrying amount.

MEASUREMENT SUBSEQUENT TO INITIAL RECOGNITION

24. ***An enterprise should choose either the fair value model in paragraphs 27 to 49 or the cost model in paragraph 50 as its accounting policy and should apply that policy to all of its investment property.***

25. IAS 8, net profit or loss for the period, fundamental errors and changes in accounting policies, states that a voluntary change in accounting policy should be made only if the change will result in a more appropriate presentation of events or transactions in the financial statements of the enterprise. It is highly unlikely that a change from the fair value model to the cost model will result in a more appropriate presentation.

26. This Standard requires all enterprises to determine the fair value of investment property for the purpose of measurement (fair value model) or disclosure (cost model). An enterprise is encouraged, but not required, to determine the fair value of investment property on the basis of a valuation by an independent valuer who holds a recognised and relevant professional qualification and who has recent experience in the location and category of the investment property being valued.

Fair value model

27. ***After initial recognition, an enterprise that chooses the fair value model should measure all of its investment property at its fair value, except in the exceptional cases described in paragraph 47.***

28. ***A gain or loss arising from a change in the fair value of investment property should be included in net profit or loss for the period in which it arises.***

29. The fair value of investment property is usually its market value. Fair value is measured as the most probable price reasonably obtainable in the market at the balance sheet date in keeping with the fair value definition. It is the best price reasonably obtainable by the seller and the most advantageous price reasonably obtainable by the buyer. This estimate specifically excludes an estimated price inflated or deflated by special terms or circumstances such as atypical financing, sale and leaseback arrangements, special considerations or concessions granted by anyone associated with the sale.

30. An enterprise determines fair value without any deduction for transaction costs that the enterprise may incur on sale or other disposal.

31. ***The fair value of investment property should reflect the actual market state and circumstances as of the balance sheet date, not as of either a past or future date.***

32. The estimated fair value is time specific as of a given date. Because markets and market conditions may change, the estimated value may be incorrect or inappropriate at another time. The definition of fair value also assumes simultaneous exchange and completion of the contract for sale without any variation in price that might be made in an arm's length transaction between knowledgeable, willing parties if exchange and completion are not simultaneous.

33. The fair value of investment property reflects, among other things, rental income from current leases and reasonable and supportable assumptions that represent the market's view of what knowledgeable, willing parties would assume about rental income from future leases in the light of current market conditions.

34. The definition of fair value refers to 'knowledgeable, willing parties'. In this context, 'knowledgeable' means that both the willing buyer and the willing seller are reasonably informed about the nature and characteristics of the investment property, its actual and potential uses, and the state of the market as of the balance sheet date.

35. A willing buyer is motivated, but not compelled to buy. This buyer is neither over-eager nor determined to buy at any price. This buyer is also one who purchases in accordance with the realities of the current market, and with the current market expectations, rather than an imaginary or hypothetical market that cannot be demonstrated or anticipated to exist. The assumed buyer would not pay a higher price than the market requires. The present owner of an investment property is included among those who constitute the market.

36. A willing seller is neither an over-eager nor a forced seller, prepared to sell at any price, nor one prepared to hold out for a price not considered reasonable in the current market. The willing seller is motivated to sell the investment property at market terms for the best price obtainable in the open market after proper marketing, whatever that price may be. The factual circumstances of the actual investment property owner are not a part of this consideration because the willing seller is a hypothetical owner.

37. The expression 'after proper marketing' means that the investment property would be exposed to the market in the most appropriate manner to effect its disposal at the best price reasonably obtainable. The length of exposure time may vary with market conditions, but must be sufficient to allow the investment property to be brought to the attention of an adequate number of potential purchasers. The exposure period is assumed to occur prior to the balance sheet date.

38. The definition of fair value refers to an arm's length transaction. An arm's length transaction is one between parties who do not have a particular or special relationship that makes prices of transactions uncharacteristic of the market. The transaction is presumed to be between unrelated parties, each acting independently.

39. The best evidence of fair value is normally given by current prices on an active market for similar property in the same location and condition and subject to similar lease and other contracts. An enterprise takes care to identify any differences in the nature, location or condition of the property, or in the contractual terms of the leases and other contracts relating to the property.

40. In the absence of current prices on an active market of the kind described in paragraph 39, an enterprise considers information from a variety of sources, including:

(a) current prices on an active market for properties of different nature, condition or location (or subject to different lease or other contracts), adjusted to reflect those differences;

(b) recent prices on less active markets, with adjustments to reflect any changes in economic conditions since the date of the transactions that occurred at those prices; and

(c) discounted cash flow projections based on reliable estimates of future cash flows, supported by the terms of any existing lease and other contracts and (where possible) by external evidence such as current market rents for similar properties in the same location and condition, and using discount rates that reflect current market assessments of the uncertainty in the amount and timing of the cash flows.

41. In some cases, the various sources listed in the previous paragraph may suggest different conclusions as to the fair value of an investment property. An enterprise considers the reasons for those differences, in order to arrive at the most reliable estimate of fair value within a relatively narrow range of reasonable fair value estimates.

42. In exceptional cases, there is clear evidence when an enterprise first acquires an investment property (or when an existing property first becomes investment property following the completion of construction or development, or after a change in use) that the variability in the range of reasonable fair value estimates will be so great and the probabilities of the various outcomes will be so difficult to assess, that the usefulness of a single estimate of fair value is negated. This may indicate that the fair value of the property will not be determinable reliably on a continuing basis (see paragraph 47).

43. Fair value differs from value in use, as defined in IAS 36, impairment of assets. Fair value reflects knowledge and estimates of participants in the market, as well as factors that are relevant to market participants in general. In contrast, value in use reflects the enterprise's knowledge and estimates, as well as entity-specific factors that may be specific to the enterprise and that are not applicable to enterprises in general. For example, fair value does not reflect any:

(a) additional value derived from the creation of a portfolio of properties in different locations;

(b) synergies between investment property and other assets;

(c) legal rights or legal restrictions that are specific only to the current owner; and

(d) tax benefits or tax burdens that are specific to the current owner.

44. In determining the fair value of investment property, an enterprise avoids double counting of assets or liabilities that are recognised in the balance sheet as separate assets or liabilities. For example:

(a) equipment such as elevators or air-conditioning is often an integral part of a building and is generally included in the investment property, rather than being recognised separately as property, plant and equipment;

(b) if an office is leased on a furnished basis, the fair value of the office generally includes the fair value of the furniture, because the rental income relates to the furnished office. When furniture is included in the fair value of investment property, an enterprise does not recognise that furniture as a separate asset; and

(c) the fair value of investment property excludes prepaid or accrued operating lease income, as the enterprise recognises it as a separate liability or asset.

45. The fair value of investment property does not reflect future capital expenditure that will improve or enhance the property and does not reflect the related future benefits from this future expenditure.

46. In some cases, an enterprise expects that the present value of its payments relating to an investment property (other than payments relating to recognised financial liabilities) will exceed the present value of the related cash receipts. An enterprise uses IAS 37, provisions, contingent liabilities and contingent assets, to determine whether the enterprise recognises a liability and how the enterprise measures any such liability.

Inability to measure fair value reliably

47. ***There is a rebuttable presumption that an enterprise will be able to determine the fair value of an investment property reliably on a continuing basis. However, in exceptional cases, there is clear evidence when an enterprise first acquires an investment property (or when an existing property first becomes investment property following the completion of construction or development, or after a change in use) that the enterprise will not be able to determine the fair value of the investment property reliably on a continuing basis. This arises when, and only when, comparable market transactions are infrequent and alternative estimates of fair value (for example, based on discounted cash flow projections) are not available. In such cases, an enterprise should measure that investment property using the benchmark treatment in IAS 16, property, plant and equipment. The residual value of the investment property should be assumed to be zero. The enterprise should continue to apply IAS 16 until the disposal of the investment property.***

48. In the exceptional cases when an enterprise is compelled, for the reason given in the previous paragraph, to measure an investment property using the IAS 16 benchmark treatment, the enterprise measures all its other investment property at fair value.

49. ***If an enterprise has previously measured an investment property at fair value, the enterprise should continue to measure the property at fair value until disposal (or until the property becomes owner-occupied property or the enterprise begins to develop the property for subsequent sale in the ordinary course of business) even if comparable market transactions become less frequent or market prices become less readily available.***

Cost model

50. ***After initial recognition, an enterprise that chooses the cost model should measure all of its investment property using the benchmark treatment in IAS 16, property, plant and equipment, that is, at cost less any accumulated depreciation and any accumulated impairment losses.***

TRANSFERS

51. ***Transfers to, or from, investment property should be made when, and only when, there is a change in use, evidenced by:***

(a) ***commencement of owner-occupation, for a transfer from investment property to owner-occupied property;***

(b) ***commencement of development with a view to sale, for a transfer from investment property to inventories;***

(c) ***end of owner-occupation, for a transfer from owner-occupied property to investment property;***

(d) ***commencement of an operating lease to another party, for a transfer from inventories to investment property; or***

(e) ***end of construction or development, for a transfer from property in the course of construction or development (covered by IAS 16, property, plant and equipment) to investment property.***

52. Paragraph 51(b) above requires an enterprise to transfer a property from investment property to inventories when, and only when, there is a change in use, evidenced by commencement of development with a view to sale. When an enterprise decides to dispose of an investment property without development, the enterprise continues to treat the property as an investment property until it is derecognised (eliminated from the balance sheet) and does not treat it as inventory. Similarly, if an enterprise begins to redevelop an existing investment property for continued future use as investment property, it remains an investment property and is not reclassified as owner-occupied property during the redevelopment.

53. Paragraphs 54 to 59 deal with recognition and measurement issues that apply when an enterprise uses the fair value model for investment property. When an enterprise uses the cost model, transfers between investment property, owner-occupied property and inventories do not change the carrying amount of the property transferred and they do not change the cost of that property for measurement or disclosure purposes.

54. ***For a transfer from investment property carried at fair value to owner-occupied property or inventories, the property's cost for subsequent accounting under IAS 16 or IAS 2 should be its fair value at the date of change in use.***

55. ***If an owner-occupied property becomes an investment property that will be carried at fair value, an enterprise should apply IAS 16 up to the date of change in use. The enterprise should treat any difference at that date between the carrying amount of the property under IAS 16 and its fair value in the same way as a revaluation under IAS 16.***

56. Up to the date when an owner-occupied property becomes an investment property carried at fair value, an enterprise continues to depreciate the property and to recognise any impairment losses that have occurred. The enterprise treats any difference at that date between the carrying amount of the property under IAS 16 and its fair value in the same way as a revaluation under IAS 16. In other words:

(a) any resulting decrease in the carrying amount of the property is recognised in net profit or loss for the period. However, to the extent that an amount is included in revaluation surplus for that property, the decrease is charged against that revaluation surplus; and

(b) any resulting increase in the carrying amount is treated as follows:

(i) to the extent that the increase reverses a previous impairment loss for that property, the increase is recognised in net profit or loss for the period. The amount recognised in net profit or loss for the period does not exceed the amount needed to restore the carrying amount to the carrying amount that would have been determined (net of depreciation) had no impairment loss been recognised; and

(ii) any remaining part of the increase is credited directly to equity under the heading of revaluation surplus. On subsequent disposal of the investment property, the revaluation surplus included in equity may be transferred to retained earnings. The transfer from revaluation surplus to retained earnings is not made through the income statement.

57. ***For a transfer from inventories to investment property that will be carried at fair value, any difference between the fair value of the property at that date and its previous carrying amount should be recognised in net profit or loss for the period.***

58. The treatment of transfers from inventories to investment property that will be carried at fair value is consistent with the treatment of sales of inventories.

59. ***When an enterprise completes the construction or development of a self-constructed investment property that will be carried at fair value, any difference between the fair value of the property at that date and its previous carrying amount should be recognised in net profit or loss for the period.***

DISPOSALS

60. ***An investment property should be derecognised (eliminated from the balance sheet) on disposal or when the investment property is permanently withdrawn from use and no future economic benefits are expected from its disposal.***

61. The disposal of an investment property may occur by sale or by entering into a finance lease. In determining the date of disposal for investment property, an enterprise applies the criteria in IAS 18, revenue, for recognising revenue from the sale of goods and considers the related guidance in the Appendix to IAS 18. IAS 17, leases, applies on a disposal by entering into a finance lease or by a sale and leaseback.

62. ***Gains or losses arising from the retirement or disposal of investment property should be determined as the difference between the net disposal proceeds and the carrying amount of the asset and should be recognised as income or expense in the income statement (unless IAS 17, leases, requires otherwise on a sale and leaseback).***

63. The consideration receivable on disposal of an investment property is recognised initially at fair value. In particular, if payment for an investment property is deferred, the consideration received is recognised initially at the cash price equivalent. The difference between the nominal amount of the consideration and the cash price equivalent is recognised as interest revenue under IAS 18 on a time proportion basis that takes into account the effective yield on the receivable.

64. An enterprise applies IAS 37, provisions, contingent liabilities and contingent assets, or other International Accounting Standards, as appropriate, to any liabilities that the enterprise retains after disposal of an investment property.

DISCLOSURE

Fair value model and cost model

65. The disclosures set out below apply in addition to those in IAS 17, leases. Under IAS 17, the owner of an investment property gives a lessor's disclosures about operating leases. Under IAS 17, an enterprise that holds an investment property under a finance lease gives a lessee's disclosures about that finance lease and a lessor's disclosure about any operating leases that the enterprise has granted.

66. ***An enterprise should disclose:***

(a) ***when classification is difficult (see paragraph 12), the criteria developed by the enterprise to distinguish investment property from owner-occupied property and from property held for sale in the ordinary course of business;***

(b) ***the methods and significant assumptions applied in determining the fair value of investment property, including a statement whether the determination of fair value was supported by market evidence or was more heavily based on other factors (which the enterprise should disclose) because of the nature of the property and lack of comparable market data;***

(c) ***the extent to which the fair value of investment property (as measured or disclosed in the financial statements) is based on a valuation by an independent valuer who holds a recognised and relevant professional qualification and who has recent experience in the location and category of the investment property being valued. If there has been no such valuation, that fact should be disclosed;***

(d) ***the amounts included in the income statement for:***

(i) ***rental income from investment property;***

(ii) ***direct operating expenses (including repairs and maintenance) arising from investment property that generated rental income during the period; and***

(iii) ***direct operating expenses (including repairs and maintenance) arising from investment property that did not generate rental income during the period;***

(e) ***the existence and amounts of restrictions on the realisability of investment property or the remittance of income and proceeds of disposal; and***

(f) ***material contractual obligations to purchase, construct or develop investment property or for repairs, maintenance or enhancements.***

Fair value model

67. ***In addition to the disclosure required by paragraph 66, an enterprise that applies the fair value model in paragraphs 27 to 49 should also disclose a reconciliation of the carrying amount of investment property at the beginning and end of the period showing the following (comparative information is not required):***

(a) ***additions, disclosing separately those additions resulting from acquisitions and those resulting from capitalised subsequent expenditure;***

(b) ***additions resulting from acquisitions through business combinations;***

(c) ***disposals;***

(d) ***net gains or losses from fair value adjustments;***

(e) ***the net exchange differences arising on the translation of the financial statements of a foreign entity;***

(f) ***transfers to and from inventories and owner-occupied property; and***

(g) ***other movements.***

68. ***In the exceptional cases when an enterprise measures investment property using the benchmark treatment in IAS 16, property, plant and equipment (because of the lack of a reliable fair value, see paragraph 47 above), the reconciliation required by the previous paragraph should disclose amounts relating to that investment property separately from amounts relating to other investment property. In addition, an enterprise should disclose:***

(a) ***a description of the investment property;***

(b) ***an explanation of why fair value cannot be reliably measured;***

(c) ***if possible, the range of estimates within which fair value is highly likely to lie; and***

(d) ***on disposal of investment property not carried at fair value:***

(i) ***the fact that the enterprise has disposed of investment property not carried at fair value;***

(ii) ***the carrying amount of that investment property at the time of sale; and***

(iii) ***the amount of gain or loss recognised.***

Cost model

69. ***In addition to the disclosure required by paragraph 66, an enterprise that applies the cost model in paragraph 50 should also disclose:***

(a) ***the depreciation methods used;***

(b) ***the useful lives or the depreciation rates used;***

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

(d) ***a reconciliation of the carrying amount of investment property at the beginning and end of the period showing the following (comparative information is not required):***

(i) ***additions, disclosing separately those additions resulting from acquisitions and those resulting from capitalised subsequent expenditure;***

(ii) ***additions resulting from acquisitions through business combinations;***

(iii) ***disposals;***

(iv) ***depreciation;***

(v) ***the amount of impairment losses recognised, and the amount of impairment losses reversed, during the period under IAS 36, impairment of assets;***

(vi) ***the net exchange differences arising on the translation of the financial statements of a foreign entity;***

(vii) ***transfers to and from inventories and owner-occupied property; and***

(viii) ***other movements; and***

(e) ***the fair value of investment property. In the exceptional cases described in paragraph 47, when an enterprise cannot determine the fair value of the investment property reliably, the enterprise should disclose:***

(i) ***a description of the investment property;***

(ii) ***an explanation of why fair value cannot be determined reliably; and***

(iii) ***if possible, the range of estimates within which fair value is highly likely to lie.***

TRANSITIONAL PROVISIONS

Fair value model

70. ***Under the fair value model, an enterprise should report the effect of adopting this Standard on its effective date (or earlier) as an adjustment to the opening balance of retained earnings for the period in which the Standard is first adopted. In addition:***

(a) ***if the enterprise has previously disclosed publicly (in financial statements or otherwise) the fair value of its investment property in earlier periods (determined on a basis that satisfies the definition of fair value in paragraph 4 and the guidance in paragraphs 29 to 46), the enterprise is encouraged, but not required, to:***

(i) ***adjust the opening balance of retained earnings for the earliest period presented for which such fair value was disclosed publicly; and***

(ii) ***restate comparative information for those periods; and***

(b) ***if the enterprise has not previously disclosed publicly the information described in (a), the enterprise should not restate comparative information and should disclose that fact.***

71. This Standard requires a different treatment from the benchmark and allowed alternative treatments for changes in accounting policies under IAS 8, net profit or loss for the period, fundamental errors and changes in accounting policies. IAS 8 requires comparative information to be restated (benchmark treatment) or additional pro forma comparative information on a restated basis to be disclosed (allowed alternative treatment) unless it is impracticable to do so.

72. When an enterprise first adopts this Standard, the adjustment to the opening balance of retained earnings includes the reclassification of any amount held in revaluation surplus for investment property.

Cost model

73. IAS 8 applies to any change in accounting policies that occurs when an enterprise first adopts this Standard and chooses to use the cost model. The effect of the change in accounting policies includes the reclassification of any amount held in revaluation surplus for investment property.

EFFECTIVE DATE

74. ***This International Accounting Standard becomes operative for annual financial statements covering periods beginning on or after 1 January 2001. Earlier application is encouraged. If an enterprise applies this Standard for periods beginning before 1 January 2001, it should disclose that fact.***

75. This Standard supersedes IAS 25, accounting for investments, with respect to investment property.

INTERNATIONAL ACCOUNTING STANDARD IAS 41

Agriculture

This International Accounting Standard was approved by the IASC Board in December 2000 and becomes effective for financial statements covering periods beginning on or after 1 January 2003.

INTRODUCTION

1. IAS 41 prescribes the accounting treatment, financial statement presentation, and disclosures related to agricultural activity, a matter not covered in other International Accounting Standards. Agricultural activity is the management by an enterprise of the biological transformation of living animals or plants (biological assets) for sale, into agricultural produce, or into additional biological assets.

2. IAS 41 prescribes, among other things, the accounting treatment for biological assets during the period of growth, degeneration, production, and procreation, and for the initial measurement of agricultural produce at the point of harvest. It requires measurement at fair value less estimated point-of-sale costs from initial recognition of biological assets up to the point of harvest, other than when fair value cannot be measured reliably on initial recognition. However, IAS 41 does not deal with processing of agricultural produce after harvest; for example, processing grapes into wine and wool into yarn.

3. There is a presumption that fair value can be measured reliably for a biological asset. However, that presumption can be rebutted only on initial recognition for a biological asset for which market-determined prices or values are not available and for which alternative estimates of fair value are determined to be clearly unreliable. In such a case, IAS 41 requires an enterprise to measure that biological asset at its cost less any accumulated depreciation and any accumulated impairment losses. Once the fair value of such a biological asset becomes reliably measurable, an enterprise should measure it at its fair value less estimated point-of-sale costs. In all cases, an enterprise should measure agricultural produce at the point of harvest at its fair value less estimated point-of-sale costs.

4. IAS 41 requires that a change in fair value less estimated point-of-sale costs of a biological asset be included in net profit or loss for the period in which it arises. In agricultural activity, a change in physical attributes of a living animal or plant directly enhances or diminishes economic benefits to the enterprise. Under a transaction-based, historical cost accounting model, a plantation forestry enterprise might report no income until first harvest and sale, perhaps 30 years after planting. On the other hand, an accounting model that recognises and measures biological growth using current fair values reports changes in fair value throughout the period between planting and harvest.

5. IAS 41 does not establish any new principles for land related to agricultural activity. Instead, an enterprise follows IAS 16, property, plant and equipment, or IAS 40, investment property, depending on which standard is appropriate in the circumstances. IAS 16 requires land to be measured either at its cost less any accumulated impairment losses, or at a revalued amount. IAS 40 requires land that is investment property to be measured at its fair value, or cost less any accumulated impairment losses. Biological assets that are physically attached to land (for example, trees in a plantation forest) are measured at their fair value less estimated point-of-sale costs separately from the land.

6. IAS 41 requires that an unconditional government grant related to a biological asset measured at its fair value less estimated point-of-sale costs be recognised as income when, and only when, the government grant becomes receivable. If a government grant is conditional, including where a government grant requires an enterprise not to engage in specified agricultural activity, an enterprise should recognise the government grant as income when, and only when, the conditions attaching to the government grant are met. If a government grant relates to a biological asset measured at its cost less any accumulated depreciation and any accumulated impairment losses, IAS 20, accounting for government grants and disclosure of government assistance, is applied.

7. IAS 41 is effective for annual financial statements covering periods beginning on or after 1 January 2003. Earlier application is encouraged.

8. IAS 41 does not establish any specific transitional provisions. The adoption of IAS 41 is accounted for in accordance with IAS 8, net profit or loss for the period, fundamental errors and changes in accounting policies.

9. Appendix A provides illustrative examples of the application of IAS 41. Appendix B, Basis for conclusions, summarises the Board's reasons for adopting the requirements set out in IAS 41.

CONTENTS

The standards, which have been set in bold italic type, should be read in the context of the background material and implementation guidance in this Standard, and in the context of the 'Preface to International Accounting Standards'. International Accounting Standards are not intended to apply to immaterial items (see paragraph 12 of the Preface).

OBJECTIVE

The objective of this Standard is to prescribe the accounting treatment, financial statement presentation, and disclosures related to agricultural activity.

SCOPE

1. ***This Standard should be applied to account for the following when they relate to agricultural activity:***

   (a) ***biological assets;***

   (b) ***agricultural produce at the point of harvest; and***

   (c) ***government grants covered by paragraphs 34 to 35.***

2. This Standard does not apply to:

   (a) land related to agricultural activity (see IAS 16, property, plant and equipment, and IAS 40, investment property); and

   (b) intangible assets related to agricultural activity (see IAS 38, intangible assets).

3. This Standard is applied to agricultural produce, which is the harvested product of the enterprise's biological assets, only at the point of harvest. Thereafter, IAS 2, inventories, or another applicable International Accounting Standard is applied. Accordingly, this Standard does not deal with the processing of agricultural produce after harvest; for example, the processing of grapes into wine by a vintner who has grown the grapes. While such processing may be a logical and natural extension of agricultural activity, and the events taking place may bear some similarity to biological transformation, such processing is not included within the definition of agricultural activity in this Standard.

4. The table below provides examples of biological assets, agricultural produce, and products that are the result of processing after harvest:

Biological assets	Agricultural produce	Products that are the result of processing after harvest
Sheep	Wool	Yarn, carpet
Trees in a plantation forest	Logs	Lumber
Plants	Cotton Harvested cane	Thread, clothing Sugar
Dairy cattle	Milk	Cheese
Pigs	Carcase	Sausages, cured hams
Bushes	Leaf	Tea, cured tobacco
Vines	Grapes	Wine
Fruit trees	Picked fruit	Processed fruit

DEFINITIONS

Agriculture-related definitions

5. ***The following terms are used in this Standard with the meanings specified:***

Agricultural activity is the management by an enterprise of the biological transformation of biological assets for sale, into agricultural produce, or into additional biological assets.

Agricultural produce is the harvested product of the enterprise's biological assets.

A biological asset is a living animal or plant.

Biological transformation comprises the processes of growth, degeneration, production, and procreation that cause qualitative or quantitative changes in a biological asset.

A group of biological assets is an aggregation of similar living animals or plants.

Harvest is the detachment of produce from a biological asset or the cessation of a biological asset's life processes.

6. Agricultural activity covers a diverse range of activities; for example, raising livestock, forestry, annual or perennial cropping, cultivating orchards and plantations, floriculture, and aquaculture (including fish farming). Certain common features exist within this diversity:

(a) Capability to change: living animals and plants are capable of biological transformation;

(b) Management of change: management facilitates biological transformation by enhancing, or at least stabilising, conditions necessary for the process to take place (for example, nutrient levels, moisture, temperature, fertility, and light). Such management distinguishes agricultural activity from other activities. For example, harvesting from unmanaged sources (such as ocean fishing and deforestation) is not agricultural activity; and

(c) Measurement of change: the change in quality (for example, genetic merit, density, ripeness, fat cover, protein content, and fibre strength) or quantity (for example, progeny, weight, cubic metres, fibre length or diameter, and number of buds) brought about by biological transformation is measured and monitored as a routine management function.

7. Biological transformation results in the following types of outcomes:

(a) asset changes through (i) growth (an increase in quantity or improvement in quality of an animal or plant); (ii) degeneration (a decrease in the quantity or deterioration in quality of an animal or plant); or (iii) procreation (creation of additional living animals or plants); or

(b) production of agricultural produce such as latex, tea leaf, wool, and milk.

General definitions

8. ***The following terms are used in this Standard with the meanings specified:***

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

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

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

(c) ***prices are available to the public.***

Carrying amount is the amount at which an asset is recognised in the balance sheet.

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

***Government grants** are as defined in IAS 20, accounting for government grants and disclosure of government assistance.*

9. The fair value of an asset is based on its present location and condition. As a result, for example, the fair value of cattle at a farm is the price for the cattle in the relevant market less the transport and other costs of getting the cattle to that market.

RECOGNITION AND MEASUREMENT

10. ***An enterprise should recognise a biological asset or agricultural produce when, and only when:***

    (a) ***the enterprise controls the asset as a result of past events;***

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

    (c) ***the fair value or cost of the asset can be measured reliably.***

11. In agricultural activity, control may be evidenced by, for example, legal ownership of cattle and the branding or otherwise marking of the cattle on acquisition, birth, or weaning. The future benefits are normally assessed by measuring the significant physical attributes.

12. ***A biological asset should be measured on initial recognition and at each balance sheet date at its fair value less estimated point-of-sale costs, except for the case described in paragraph 30 where the fair value cannot be measured reliably.***

13. ***Agricultural produce harvested from an enterprise's biological assets should be measured at its fair value less estimated point-of-sale costs at the point of harvest. Such measurement is the cost at that date when applying IAS 2, inventories, or another applicable International Accounting Standard.***

14. Point-of-sale costs include commissions to brokers and dealers, levies by regulatory agencies and commodity exchanges, and transfer taxes and duties. Point-of-sale costs exclude transport and other costs necessary to get assets to a market.

15. The determination of fair value for a biological asset or agricultural produce may be facilitated by grouping biological assets or agricultural produce according to significant attributes; for example, by age or quality. An enterprise selects the attributes corresponding to the attributes used in the market as a basis for pricing.

16. Enterprises often enter into contracts to sell their biological assets or agricultural produce at a future date. Contract prices are not necessarily relevant in determining fair value, because fair value reflects the current market in which a willing buyer and seller would enter into a transaction. As a result, the fair value of a biological asset or agricultural produce is not adjusted because of the existence of a contract. In some cases, a contract for the sale of a biological asset or agricultural produce may be an onerous contract, as defined in IAS 37, provisions, contingent liabilities and contingent assets. IAS 37 applies to onerous contracts.

17. If an active market exists for a biological asset or agricultural produce, the quoted price in that market is the appropriate basis for determining the fair value of that asset. If an enterprise has access to different active markets, the enterprise uses the most relevant one. For example, if an enterprise has access to two active markets, it would use the price existing in the market expected to be used.

18. If an active market does not exist, an enterprise uses one or more of the following, when available, in determining fair value:

(a) the most recent market transaction price, provided that there has not been a significant change in economic circumstances between the date of that transaction and the balance sheet date;

(b) market prices for similar assets with adjustment to reflect differences; and

(c) sector benchmarks such as the value of an orchard expressed per export tray, bushel, or hectare, and the value of cattle expressed per kilogram of meat.

19. In some cases, the information sources listed in paragraph 18 may suggest different conclusions as to the fair value of a biological asset or agricultural produce. An enterprise considers the reasons for those differences, in order to arrive at the most reliable estimate of fair value within a relatively narrow range of reasonable estimates.

20. In some circumstances, market-determined prices or values may not be available for a biological asset in its present condition. In these circumstances, an enterprise uses the present value of expected net cash flows from the asset discounted at a current market-determined pre-tax rate in determining fair value.

21. The objective of a calculation of the present value of expected net cash flows is to determine the fair value of a biological asset in its present location and condition. An enterprise considers this in determining an appropriate discount rate to be used and in estimating expected net cash flows. The present condition of a biological asset excludes any increases in value from additional biological transformation and future activities of the enterprise, such as those related to enhancing the future biological transformation, harvesting, and selling.

22. An enterprise does not include any cash flows for financing the assets, taxation, or re-establishing biological assets after harvest (for example, the cost of replanting trees in a plantation forest after harvest).

23. In agreeing an arm's length transaction price, knowledgeable, willing buyers and sellers consider the possibility of variations in cash flows. It follows that fair value reflects the possibility of such variations. Accordingly, an enterprise incorporates expectations about possible variations in cash flows into either the expected cash flows, or the discount rate, or some combination of the two. In determining a discount rate, an enterprise uses assumptions consistent with those used in estimating the expected cash flows, to avoid the effect of some assumptions being double-counted or ignored.

24. Cost may sometimes approximate fair value, particularly when:

(a) little biological transformation has taken place since initial cost incurrence (for example, for fruit tree seedlings planted immediately prior to a balance sheet date); or

(b) the impact of the biological transformation on price is not expected to be material (for example, for the initial growth in a 30-year pine plantation production cycle).

25. Biological assets are often physically attached to land (for example, trees in a plantation forest). There may be no separate market for biological assets that are attached to the land but an active market may exist for the combined assets, that is, for the biological assets, raw land, and land improvements, as a package. An enterprise may use information regarding the combined assets to determine fair value for the biological assets. For example, the fair value of raw land and land improvements may be deducted from the fair value of the combined assets to arrive at the fair value of biological assets.

Gains and losses

26. ***A gain or loss arising on initial recognition of a biological asset at fair value less estimated point-of-sale costs and from a change in fair value less estimated point-of-sale costs of a biological asset should be included in net profit or loss for the period in which it arises.***

27. A loss may arise on initial recognition of a biological asset, because estimated point-of-sale costs are deducted in determining fair value less estimated point-of-sale costs of a biological asset. A gain may arise on initial recognition of a biological asset, such as when a calf is born.

28. ***A gain or loss arising on initial recognition of agricultural produce at fair value less estimated point-of-sale costs should be included in net profit or loss for the period in which it arises.***

29. A gain or loss may arise on initial recognition of agricultural produce as a result of harvesting.

Inability to measure fair value reliably

30. ***There is a presumption that fair value can be measured reliably for a biological asset. However, that presumption can be rebutted only on initial recognition for a biological asset for which market-determined prices or values are not available and for which alternative estimates of fair value are determined to be clearly unreliable. In such a case, that biological asset should be measured at its cost less any accumulated depreciation and any accumulated impairment losses. Once the fair value of such a biological asset becomes reliably measurable, an enterprise should measure it at its fair value less estimated point-of-sale costs.***

31. The presumption in paragraph 30 can be rebutted only on initial recognition. An enterprise that has previously measured a biological asset at its fair value less estimated point-of-sale costs continues to measure the biological asset at its fair value less estimated point-of-sale costs until disposal.

32. In all cases, an enterprise measures agricultural produce at the point of harvest at its fair value less estimated point-of-sale costs. This Standard reflects the view that the fair value of agricultural produce at the point of harvest can always be measured reliably.

33. In determining cost, accumulated depreciation and accumulated impairment losses, an enterprise considers IAS 2, inventories, IAS 16, property, plant and equipment, and IAS 36, impairment of assets.

GOVERNMENT GRANTS

34. ***An unconditional government grant related to a biological asset measured at its fair value less estimated point-of-sale costs should be recognised as income when, and only when, the government grant becomes receivable.***

35. ***If a government grant related to a biological asset measured at its fair value less estimated point-of-sale costs is conditional, including where a government grant requires an enterprise not to engage in specified agricultural activity, an enterprise should recognise the government grant as income when, and only when, the conditions attaching to the government grant are met.***

36. Terms and conditions of government grants vary. For example, a government grant may require an enterprise to farm in a particular location for five years and require the enterprise to return all of the government grant if it farms for less than five years. In this case, the government grant is not recognised as income until the five years have passed. However, if the government grant allows part of the government grant to be retained based on the passage of time, the enterprise recognises the government grant as income on a time proportion basis.

37. If a government grant relates to a biological asset measured at its cost less any accumulated depreciation and any accumulated impairment losses (see paragraph 30), IAS 20, accounting for government grants and disclosure of government assistance, is applied.

38. This Standard requires a different treatment from IAS 20, if a government grant relates to a biological asset measured at its fair value less estimated point-of-sale costs or a government grant requires an enterprise not to engage in specified agricultural activity. IAS 20 is applied only to a government grant related to a biological asset measured at its cost less any accumulated depreciation and any accumulated impairment losses.

PRESENTATION AND DISCLOSURE

Presentation

39. ***An enterprise should present the carrying amount of its biological assets separately on the face of its balance sheet.***

Disclosure

General

40. ***An enterprise should disclose the aggregate gain or loss arising during the current period on initial recognition of biological assets and agricultural produce and from the change in fair value less estimated point-of-sale costs of biological assets.***

41. ***An enterprise should provide a description of each group of biological assets.***

42. The disclosure required by paragraph 41 may take the form of a narrative or quantified description.

43. An enterprise is encouraged to provide a quantified description of each group of biological assets, distinguishing between consumable and bearer biological assets or between mature and immature biological assets, as appropriate. For example, an enterprise may disclose the carrying amounts of consumable biological assets and bearer biological assets by group. An enterprise may further divide those carrying amounts between mature and immature assets. These distinctions provide information that may be helpful in assessing the timing of future cash flows. An enterprise discloses the basis for making any such distinctions.

44. Consumable biological assets are those that are to be harvested as agricultural produce or sold as biological assets. Examples of consumable biological assets are livestock intended for the production of meat, livestock held for sale, fish in farms, crops such as maize and wheat, and trees being grown for lumber. Bearer biological assets are those other than consumable biological assets; for example, livestock from which milk is produced, grape vines, fruit trees, and trees from which firewood is harvested while the tree remains. Bearer biological assets are not agricultural produce but, rather, are self-regenerating.

45. Biological assets may be classified either as mature biological assets or immature biological assets. Mature biological assets are those that have attained harvestable specifications (for consumable biological assets) or are able to sustain regular harvests (for bearer biological assets).

46. ***If not disclosed elsewhere in information published with the financial statements, an enterprise should describe:***

(a) ***the nature of its activities involving each group of biological assets; and***

(b) ***non-financial measures or estimates of the physical quantities of:***

(i) ***each group of the enterprise's biological assets at the end of the period; and***

(ii) ***output of agricultural produce during the period.***

47. ***An enterprise should disclose the methods and significant assumptions applied in determining the fair value of each group of agricultural produce at the point of harvest and each group of biological assets.***

48. ***An enterprise should disclose the fair value less estimated point-of-sale costs of agricultural produce harvested during the period, determined at the point of harvest.***

49. ***An enterprise should disclose:***

(a) ***the existence and carrying amounts of biological assets whose title is restricted, and the carrying amounts of biological assets pledged as security for liabilities;***

(b) ***the amount of commitments for the development or acquisition of biological assets; and***

(c) ***financial risk management strategies related to agricultural activity.***

50. ***An enterprise should present a reconciliation of changes in the carrying amount of biological assets between the beginning and the end of the current period. Comparative information is not required. The reconciliation should include:***

(a) ***the gain or loss arising from changes in fair value less estimated point-of-sale costs;***

(b) ***increases due to purchases;***

(c) ***decreases due to sales;***

(d) ***decreases due to harvest;***

(e) ***increases resulting from business combinations;***

(f) ***net exchange differences arising on the translation of financial statements of a foreign entity; and***

(g) ***other changes.***

51. The fair value less estimated point-of-sale costs of a biological asset can change due to both physical changes and price changes in the market. Separate disclosure of physical and price changes is useful in appraising current period performance and future prospects, particularly when there is a production cycle of more than one year. In such cases, an enterprise is encouraged to disclose, by group or otherwise, the amount of change in fair value less estimated point-of-sale costs included in net profit or loss due to physical changes and due to price changes. This information is generally less useful when the production cycle is less than one year (for example, when raising chickens or growing cereal crops).

52. Biological transformation results in a number of types of physical change — growth, degeneration, production, and procreation, each of which is observable and measurable. Each of those physical changes has a direct relationship to future economic benefits. A change in fair value of a biological asset due to harvesting is also a physical change.

53. Agricultural activity is often exposed to climatic, disease, and other natural risks. If an event occurs that because of its size, nature, or incidence is relevant to understanding the enterprise's performance for the period, the nature and amount of related items of income and expense are disclosed under IAS 8, net profit or loss for the period, fundamental errors and changes in accounting policies. Examples include an outbreak of a virulent disease, a flood, severe droughts or frosts, and a plague of insects.

Additional disclosures for biological assets where fair value cannot be measured reliably

54. ***If an enterprise measures biological assets at their cost less any accumulated depreciation and any accumulated impairment losses (see paragraph 30) at the end of the period, the enterprise should disclose for such biological assets:***

(a) ***a description of the biological assets;***

(b) ***an explanation of why fair value cannot be measured reliably;***

(c) ***if possible, the range of estimates within which fair value is highly likely to lie;***

(d) ***the depreciation method used;***

(e) ***the useful lives or the depreciation rates used; and***

(f) ***the gross carrying amount and the accumulated depreciation (aggregated with accumulated impairment losses) at the beginning and end of the period.***

55. ***If, during the current period, an enterprise measures biological assets at their cost less any accumulated depreciation and any accumulated impairment losses (see paragraph 30), an enterprise should disclose any gain or loss recognised on disposal of such biological assets and the reconciliation required by paragraph 50 should disclose amounts related to such biological assets separately. In addition, the reconciliation should include the following amounts included in net profit or loss related to those biological assets:***

(a) ***impairment losses;***

(b) ***reversals of impairment losses; and***

(c) ***depreciation.***

56. ***If the fair value of biological assets previously measured at their cost less any accumulated depreciation and any accumulated impairment losses becomes reliably measurable during the current period, an enterprise should disclose for those biological assets:***

(a) ***a description of the biological assets;***

(b) ***an explanation of why fair value has become reliably measurable; and***

(c) ***the effect of the change.***

Government grants

57. ***An enterprise should disclose the following related to agricultural activity covered by this Standard:***

(a) ***the nature and extent of government grants recognised in the financial statements;***

(b) ***unfulfilled conditions and other contingencies attaching to government grants; and***

(c) ***significant decreases expected in the level of government grants.***

EFFECTIVE DATE AND TRANSITION

58. ***This International Accounting Standard becomes operative for annual financial statements covering periods beginning on or after 1 January 2003. Earlier application is encouraged. If an enterprise applies this Standard for periods beginning before 1 January 2003, it should disclose that fact.***

59. This Standard does not establish any specific transitional provisions. The adoption of this Standard is accounted for in accordance with IAS 8, net profit or loss for the period, fundamental errors and changes in accounting policies.