UNIT V –INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)

Understanding International Financial Reporting Standards (IFRS)

IFRS standards are International Financial Reporting Standards that consist of a set of accounting rules that determine how transactions and other accounting events are required to be reported in financial statements. They are designed to maintain credibility and transparency in the financial world, which enables investors and business operators to make informed decisions.

IFRS standards are issued and maintained by the International Accounting Standards Board (IASB) and were created to establish a common language so that financial statements can easily be interpreted from company to company and country to country.

About IASB

The International Accounting Standards Board (IASB) is an independent body formed in 2001 with the sole responsibility of establishing the International Financial Reporting Standards (IFRS). It succeeded the International Accounting Standards Committee (IASC), which was earlier given the responsibility of establishing the international accounting standards. IASB is based in London. It has also provided the 'Conceptual Framework for Financial Reporting' issued in September 2010 which provides a conceptual understanding and the basis of the accounting practices under IFRS.

Definition: The International Accounting Standards Board, typically abbreviated IASB, is the organization that establishes international financial reporting standards or IFRS that are accepted throughout the world.

The IASB consists of 14 members from various countries with different backgrounds in accounting, finance, and auditing. These members are selected as a group of experts with a blend of experience of standard-setting, preparing and using accounts, and academic work.

Meaning of IFRS

International Financial Reporting Standards (IFRS) set common rules so that financial statements can be consistent, transparent and comparable around the world. IFRS are issued by the International Accounting Standards Board (IASB). They specify how companies must maintain and report their accounts, defining types of transactions and other events with financial impact. IFRS were established to create a common accounting language, so that businesses and their financial statements can be consistent and reliable from company to company and country to country.

Objective of Financial Statements

The objective of financial statements is to provide information about the financial position (statement of financial position), performance (statement of comprehensive income), and changes in financial position (statement of cash flows) of an entity that is useful to a wide range of users in making economic decisions. Users of financial information include present and potential capital providers, employees, lenders, suppliers, customers, and the government.

Financial statements also show the results of management's stewardship of the resources entrusted to it. This information, along with other information in the notes to the financial statements, provides users of financial statements with information about the amount, timing, and uncertainty of the entity's future cash flows in order that they can make economic decisions. In order to meet this objective, financial statements contain information about

- assets;
- liabilities;
- equity;
- income and expenses, including gains and losses;
- contributions by and distributions to owners in their capacity as owners; and
- Cash flows.

1. Fair presentation: The objective of financial statements is to achieve fair presentation.

2. Materiality: IFRS only applies to material information. An item is material if its omission or misstatement would change the decisions taken by the users of the financial statements.

Underlying assumptions

3. Accrual basis of accounting: Financial statements are prepared based on the accrual basis of accounting. Under this basis transactions are recorded when they occur and not as the cash flows take place.

4. Going concern: Financial statements are prepared on the assumption that an entity is a going concern and will be in operation for the foreseeable future. Hence it is assumed that the entity has neither the intention nor the need to liquidate or materially curtail the scale of its operations.

Need for IFRS

1. For accounting standards to garner worldwide acceptance they must be universally applied. Comparability is essential if "in accordance with IFRS" means that the same or similar transactions are accounted for the same way everywhere, producing financial statements in accordance with IFRS will add value. Investors would no longer need to waste time and effort to reconcile financial information as they compare similar companies from different countries. Capital would flow more efficiently, at less cost to more companies in more places.
2. A single system of financial reporting would benefit a host of constituents. With quality standards, consistently applied, investor understanding and confidence rises. That translates to strong, stable, liquid markets. With quality reporting, investors wouldn't need to compensate for a lack of understanding by demanding a risk premium. With consistent application and the resulting comparability investors and analysts have an easier time knowing how to best allocate capital. Having one financial language reduces preparation and audit costs. No longer is there a need to learn different standards or keep current in them, at the expense of more fruitful pursuits. Regulation can be easier if properly coordinated. Education and training become easier and more focused.
3. Convergence of accounting standards has played a major role in the growing acceptance of IFRS. As the differences narrow between IFRS and other widely-accepted accounting systems, resistance to IFRS is beginning to fall away.

Main features of IFRS

IFRS financial statements come in various shapes and sizes, but they all have certain features in common. Information in IFRS financial statements has these characteristics:

1. **Understandability**: Information should be readily understandable by users who have a basic knowledge of business, economic activities, and accounting, and who have a willingness to study the information with reasonable diligence.

2. **Relevance**: Relevant information influences the economic decisions of users, helping them to evaluate past, present, and future events or to confirm or correct their past evaluations. The relevance of information is affected by its nature and materiality. Information is considered to be material if its omission or misstatement could influence the economic decisions of users taken on the basis of the financial statements.

3. **Reliability**: Reliable information is free from material error and bias and can be depended upon by users to represent faithfully that which it either purports to represent or could reasonably be expected to represent. The following factors contribute to reliability:

    • Faithful representation;

    • Substance over form;

    • Neutrality;

    • Prudence; and

    • Completeness.

4. **Comparability**: Information should be presented in a consistent manner over time and in a consistent manner between entities to enable users to make significant comparisons.

5. **Verifiability:** Different people could reach the same decision based on the information, but not necessarily reach complete agreement.

6. **Timeliness:** You make information available to users in good time. Historical information quickly becomes out of date.

Objectives of IFRS

- To develop, in the public interest, a single set of high quality, understandable, enforceable and globally accepted financial reporting standards based upon clearly articulated principles.
- To ensure high quality, transparent and comparable information in financial statements and other financial reporting to help investors, other participants in the world's capital markets and other users of financial information make economic decisions.
- To promote the use and rigorous application of those standards.

- To promote and facilitate adoption of the IFRS Standards, being the standards and interpretations issued by the IASB, through the convergence of national accounting standards and IFRS Standards to high quality solutions.
- To make a common platform for better understanding of accounting, internationally.
- Synchronization of accounting standards across the globe.
- To create comparable, reliable and transparent financial statements.
- To facilitate greater cross-border capital raising and trade.
- To have company-wide one accounting language which has subsidiaries in different countries.
- To take account of, as appropriate, the special needs of small and medium-sized entities and emerging economies.

Benefits of IFRS

The advantages of achieving convergence with IFRS are numerous.

1. It benefits the economy by increasing the growth of its international business.

2. By encouraging the international investors to invest, it leads to more foreign capital flows to the country.

3. Financial statements prepared using a common set of accounting standards help investors better understand investment opportunities as opposed to financial statements prepared using a different set of national accounting standards.

4. The industry is able to raise capital from foreign markets at lower cost if it can create confidence in the minds of foreign investors that their financial statements comply with globally accepted accounting standards.

5. It offers accounting professionals more opportunities in any part of the world if same accounting practices prevail throughout the world.

List of International Financial Reporting Standards (IFRS) Issued By IASB

1.IFRS 1 - First time adoption of International Financial Reporting Standards
It sets out the procedures that an entity must follow when it adopts IFRSs for the first time as the basis for preparing its general purpose financial statements. This IFRS grants limited exemptions from the general requirement to comply with each IFRS effective at the end of its first IFRS reporting period.

2. IFRS 2 - Share-based Payment

It requires an entity to recognise share-based payment transactions (example: granted shares, share options, or share appreciation rights) in its financial statements, also including transactions with employees or other parties to be settled in cash, other assets, or equity instruments of the entity. Specific requirements are included for equity-settled and cash-settled share-based payment transactions, as well as those where the entity or supplier has a choice of cash or equity instruments.

3. IFRS 3 - Business Combinations

It outlines the accounting when an acquirer obtains control of a business (example: an acquisition or merger). Such business combinations are accounted for using the 'acquisition method', which generally requires assets acquired and liabilities assumed to be measured at their fair values at the acquisition date.

4. IFRS 4 - Insurance Contracts

It applies, with limited exceptions, to all insurance contracts (including reinsurance contracts) that an entity issues and to reinsurance contracts that it holds. In light of the International Accounting Standard Board's comprehensive project on insurance contracts, the standard provides a temporary exemption from the requirements of some other IFRSs, including the requirement to consider International Accounting Standard- 8 Accounting Policies, Changes in Accounting Estimates and Errors when selecting accounting policies for insurance contracts.

5. IFRS 5 - Non-current Assets Held for Sale and Discontinued Operations

It outlines how to account for non-current assets held for sale (or for distribution to owners). In general terms, assets held for sale are not depreciated, are measured at the lower of carrying amount and fair value less costs to sell, and are presented separately in the statement of financial position. Specific disclosures are also required for discontinued operations and disposals of non-current assets.

6. IFRS 6 - Exploration for and Evaluation of Mineral Resources

It has the effect of allowing entities adopting the standard for the first time to use accounting policies for exploration and evaluation assets that were applied before adopting IFRSs. It also modifies impairment testing of exploration and evaluation assets by introducing different impairment indicators and allowing the carrying amount to be tested at an aggregate level (not greater than a segment).

7. IFRS 7 - Financial Instruments: Disclosures

It requires disclosure of information about the significance of financial instruments to an entity, and the nature and extent of risks arising from those financial instruments, both in qualitative and quantitative terms. Specific disclosures are required in relation to transferred financial assets and a number of other matters.

8. IFRS 8 - Operating Segments

It requires particular classes of entities (essentially those with publicly traded securities) to disclose information about their operating segments, products and services, the geographical areas in which they operate, and their major customers. Information is based on internal management reports, both in the identification of operating segments and measurement of disclosed segment information.

9. IFRS 9 - Financial Instruments

It is the International Accounting Standard Board's replacement of International Accounting Standard 39 Financial Instruments: Recognition and Measurement. It includes requirements for recognition and measurement, impairment, derecognition and general hedge accounting.

10. IFRS 10 – Consolidated Financial Statements

It outlines the requirements for the preparation and presentation of consolidated financial statements, requiring entities to consolidate entities it controls. Control requires exposure or rights to variable returns and the ability to affect those returns through power over an investee.

11. IFRS 11 – Joint Arrangements

It outlines the accounting by entities that jointly control an arrangement. Joint control involves the contractually agreed sharing of control and arrangements subject to joint control are classified as either a joint venture; representing a share of net assets and equity accounted or a joint operation; representing rights to assets and obligations for liabilities, accounted for accordingly.

12. IFRS 12 - Disclosure of Interests in Other Entities

It is a consolidated disclosure standard requiring a wide range of disclosures about an entity's interests in subsidiaries, joint arrangements, associates and unconsolidated 'structured entities'. Disclosures are presented as a series of objectives, with detailed guidance on satisfying those objectives.

13. IFRS 13 - Fair Value Measurement

It applies to IFRSs that require or permit fair value measurements or disclosures and provides a single IFRS framework for measuring fair value and requires disclosures about fair value measurement. The Standard defines fair value on the basis of an exit price notion and uses a fair value hierarchy, which results in a market-based rather than entity-specific measurement.

14. IFRS 14 - Regulatory Deferral Accounts

It permits an entity which is a first-time adopter of International Financial Reporting Standards to continue to account, with some limited changes, for ‘regulatory deferral account balances’ in accordance with its previous GAAP, both on initial adoption of IFRS and in subsequent financial statements. Regulatory deferral account balances, and movements in them, are presented separately in the statement of financial position and statement of profit or loss and other comprehensive income, and specific disclosures are required.

15. IFRS 15 - Revenue from contracts with customers

It specifies how and when an IFRS reporter will recognise revenue as well as requiring such entities to provide users of financial statements with more informative, relevant disclosures. The standard provides a single, principles based five-step model to be applied to all contracts with customers. It applies to an annual reporting period beginning on or after 1 January 2018.

16. IFRS 16 - Leases

It specifies how an IFRS reporter will recognise, measure, present and discloses leases. The standard provides a single lessee accounting model, requiring lessees to recognise assets and liabilities for all leases unless the lease term is 12 months or less or the underlying asset has a low value. Lessors continue to classify leases as operating or finance, with IFRS 16’s approach to lessor accounting substantially unchanged from its predecessor.