

Accounting Alert

Staying on top of developments



In this issue:

- Deloitte Financial Reporting Survey Series
- Back to One Income Statement
- Financial Liabilities and Own Credit Risk
- Goodbye to the Corridor Approach for Defined Benefit Plans
- Discussion Paper on Extractive Activities
- Improvements to IFRSs
- Securities Commission Cycle 11 Results
- Other Topics of Interest

Since the introduction of the New Zealand equivalents to International Financial Reporting Standards (NZ IFRS), entities have had to work through the ever changing, and often complex, requirements of financial reporting. In order to understand how entities apply the financial reporting requirements in practice, we have commenced the Deloitte Financial Reporting Survey Series where we consider a series of questions regarding the financial reports of a sample of New Zealand entities. The first four publications in the series are summarised below.

This Accounting Alert also provides you with information about a number of recent developments in financial reporting, including exposure drafts issued by the International Accounting Standards Board (IASB) and Financial Reporting Standards Board (FRSB). We will continue to keep you apprised of developments as they occur, so watch this space...

Deloitte Financial Reporting Survey Series

Decisions on policies and presentations in the financial statements are influenced by rules, recommendations, regulators and the reality of what is happening in practice.

In order to understand how entities apply the financial reporting requirements in practice, we have commenced the Deloitte Financial Reporting Survey Series where we consider a series of questions regarding the financial reports of a sample of New Zealand entities such as:

- What decisions are made by the first adopters of new financial reporting requirements?
- What trends are emerging in financial reporting?
- Where are the challenges?

Current publications in the survey series as listed below are available at: <http://www.deloitte.com/nz/financialreportingsurvey>



Issue 1: Focus on financial reporting in practice

This issue provides an overview of the financial statements of a sample of companies with June to September 2009 balance dates. Of particular interest in the 2009 reports was the effect of the volatile economic environment on companies, with a significant increase in the level of impairments, onerous contracts and restructuring costs incurred. In addition, we noted that there was an increase in the number of companies receiving audit reports with an emphasis of matter paragraph relating to fundamental uncertainties around going concern.

As companies prepare for the 2010 reporting season, there are some changes to standards to consider. In particular, companies now need to comply with the revised version of NZ IAS 1: *Presentation of Financial Statements*, which provides two options for presentation of the income statement among other changes. To aid in making this choice we have included an analysis of how 20 companies with a December 2009 balance date implemented the changes to NZ IAS 1.



Issue 2: Focus on financial statements – the top 10 considerations

As a result of our focus on financial reporting in practice, we have identified the top 10 matters to consider when preparing financial statements and provide some suggested solutions for addressing these in practice.



Issue 3: Reporting underlying profit

In this issue we look at the widespread practice of providing an alternative measure of financial performance to that calculated in accordance with applicable accounting standards. We also look at best practice in this area and provide a list of questions Directors should ask when considering the use of an underlying profit figure.



Issue 4: Where are the judgements?

In preparing financial statements, entities have to make decisions about outcomes that are subjective or uncertain. Accounting standards require disclosure of the critical judgements and major sources of estimation uncertainty in order to enable stakeholders to understand the areas of the financial statements that are the most subjective, and which could have a material impact on the financial statements if different judgements or assumptions were made.

This issue considers what critical judgements and major sources of estimation uncertainty are being disclosed by companies, where they are presented in the financial statements, and the extent of sensitivity disclosures provided for estimates. The survey results suggest that this is a challenging disclosure area, so we include some questions for Directors to ask as part of an entity's process to prepare the financial statements.

Back to One Income Statement

The IASB is proposing another limited change to IAS 1, this time requiring the presentation of profit or loss and other comprehensive income as separate components in a single financial statement called a Statement of Profit or Loss and Other Comprehensive Income, although other titles may be used.

The 2007 changes to IAS 1 gave entities the option to present either a single Statement of Comprehensive Income or two separate statements, an Income Statement and a separate Statement of Comprehensive Income. Under the exposure draft ED/2010/5 *Presentation of Items of Other Comprehensive Income*, the latter option of presenting two separate statements would be eliminated with all entities becoming required to present a single continuous statement comprising both profit or loss and other comprehensive income (OCI) for the period.

The exposure draft also proposes presentation of components of OCI in two classes:

- items that might be reclassified to profit or loss in subsequent periods (such as cash flow hedging items), and
- items that will not be reclassified to profit or loss in subsequent periods (such as revaluations of property, plant and equipment).

More detail on the proposals and illustrative examples are available in the June 2010 Deloitte Global publication **IFRS in Focus**.

The **Exposure Draft** is available on the NZICA Website. Comments are due to the FRSB by 17 September 2010 and to the IASB by 30 September 2010.

Financial Liabilities and Own Credit Risk

The IASB has released an exposure draft addressing the accounting for financial liabilities, previously excluded from IFRS 9: *Financial Instruments* as part of the IASB's project to simplify the accounting for financial instruments. The exposure draft proposes:

- changes to the presentation of the effects of changes in an entity's own credit risk, and

- the elimination of the cost exception for derivative liabilities to be settled by delivery of unquoted equity instruments (consistent with IFRS 9's elimination of the cost exception for financial assets that were unquoted equity instruments).

The basic accounting model for financial liabilities under IAS 39: *Financial Instruments: Recognition and Measurement* would remain unchanged. Financial liabilities held for trading would continue to be measured at fair value through profit or loss (FVTPL), and all other financial liabilities would be measured at amortised cost unless the fair value option is applied, using the existing criteria in IAS 39. However, where an entity designates financial liabilities at FVTPL under the fair value option, any changes resulting from a change in own credit risk will be presented in OCI instead of in profit or loss.

Example

An entity designated a financial liability at FVTPL. At the beginning of 2011, the liability's carrying amount was \$100 and at the end of 2011 it was \$110. The change in fair value of \$10 is comprised of a change of \$2 due to a strengthening in the entity's own credit risk, with the rest due to changes in other risk factors such as a decline in interest rates. Under current requirements the total change in fair value of \$10 would go through profit or loss. Under the exposure draft the following journal entries would be recorded to reflect the two-step approach:

Dr: Loss on remeasurement (profit or loss)	10	
		Cr: Financial liability designated at FVTPL
		10
Dr: Other comprehensive income	2	
		Cr: Fair value change attributable to own credit risk (profit or loss)
		2

Any final guidance would be incorporated into IFRS 9.

The **Exposure Draft** is available on the NZICA Website. Comments are due to the FRSB by 7 July 2010 and to the IASB by 16 July 2010.

For more information please read the Deloitte Global May 2010 IAS Plus Newsletter **IASB issues proposals on the fair value option for financial liabilities**.

Goodbye to the Corridor Approach for Defined Benefit Plans

The exposure draft ED/2010/3 *Defined Benefit Plans – Proposed amendments to IAS 19* proposes several significant changes to the current requirements of IAS 19: *Employee Benefits* in regards to defined benefit plans.

Elimination of the corridor method

IAS 19 currently allows entities to defer a portion of actuarial gains and losses that fall outside a specified corridor (being the greater of 10% of the defined benefit obligation or 10% of the fair value of plan assets). The exposure draft proposes eliminating this option with all actuarial gains and losses instead being recognised immediately through OCI. The net pension asset or liability would be recognised in the statement of financial position reflecting the full amount of the overfunded or underfunded status of the benefit plan.

Change in presentation approach

The ED proposes segregating changes in the defined benefit obligation and the fair value of plan assets into those associated with service costs, finance costs and remeasurements with recognition as follows:

Changes in the defined benefit obligation	Recorded as
Service costs	Employment expense (profit or loss)
Finance costs	Finance costs (profit or loss)
Remeasurements	Other comprehensive income

Disclosure

To improve the clarity of information disclosed the following objectives for disclosure are proposed:

- explain the characteristics of an entity's defined benefit plans,
- identify and explain the amounts in the financial statements resulting from those plans, and
- describe how future cash flows (amount, timing and uncertainty) may be affected by the defined benefit plans offered by the entity.

These principles and supporting detail would result in increased disclosures by entities involved in multi-employer plans and around sensitivity analysis.

There are a number of other less significant changes proposed, which are summarised in the Deloitte IAS Plus Newsletter [Closing the Corridor – IASB proposes significant changes to pension accounting](#) available at www.iasplus.com.

Comments are due to the FRSB by 14 August 2010 and to the IASB by 6 September 2010. The [Exposure Draft](#) is available on the NZICA website.

Discussion Paper on Extractive Activities

The IASB has issued a discussion paper on the accounting for extractive activities proposing a single accounting and disclosure model. The discussion paper proposes:

- a common basis for defining 'reserves and resources' to be used,
- the initial focus for accounting for minerals or oil and gas properties should be the legal rights to that property. These rights could be exploration rights or extraction rights with property recognised as an asset when the legal rights are acquired,
- minerals or oil and gas properties to be measured at historical cost, supplemented with detailed disclosure, and
- disclosure requirements would help users to assess the nature and extent of the risks involved in the extractive activities.

The discussion paper only contains the views of the project team. After considering the responses received on the discussion paper, the IASB will decide whether to add the project to its active agenda.

The [discussion paper](#) is available on the NZICA website. Comments are due to the FRSB by 15 July 2010 and to the IASB by 30 July 2010.

Improvements to IFRSs

The IASB has issued the latest round of minor tweaks and clarifications to IFRS. Two of the more significant changes are as follows:

Measurement of non-controlling interests in a business combination

The choice of how non-controlling interests are measured in a business combination has been limited to when ownership interests entitle their holders to a proportionate share of the entity's net assets in the event of liquidation. All other components of non-controlling interest should be measured at their acquisition date fair value, unless another measurement basis is required by IFRS.

Interim financial reporting

The amendments clarify the requirement to provide disclosure that updates information presented in the most recent annual financial statements with the following examples:

- changes in the business or economic circumstances that affect the fair value of the entity's financial assets and financial liabilities, whether they are recorded at fair value or amortised cost,
- transfers of financial instruments measured at fair value between levels of the fair value hierarchy, and
- changes in the classification of financial assets as a result of a change in the purpose or use of those assets.

For a full list of the improvements refer to the Deloitte IAS Plus Update [Improvements to IFRSs 2010](#) available at www.iasplus.com.

Securities Commission Cycle 11 Results

The Securities Commission *“urges issuers and their directors to take up the challenge of correctly applying the principles underlying NZ IFRS and to assume full responsibility for the transparency of their financial statements.”*

These comments were the result of the Securities Commission’s ongoing financial reporting surveillance programme, where a mix of listed and unlisted issuer financial reports are reviewed for compliance with NZ GAAP. The Cycle 11 review covered financial reports published by issuers for periods ending 31 March 2009 – 30 June 2009 and resulted in the Commission writing to 20 of the 24 issuers reviewed.

The following specific issues were raised, in addition to some other less widespread matters:

- financial instrument disclosures, particularly in relation to errors or insufficient disclosure around credit risk and interest rate sensitivity,
- failure to provide an explicit and unreserved statement of compliance with IFRS,
- impairment of non-financial assets with poor disclosure of assumptions underlying goodwill impairment testing,
- related party information, with omissions in key management personnel compensation disclosures and non-disclosure of the consideration used to settle related party transactions,
- valuation of property, plant and equipment disclosures – in particular assumptions underlying the valuation of such assets, and
- failure to describe the nature of non-audit services provided.

As a number of issues are continually being raised, the Commission is proposing to provide workshops as part of an education programme.

The Securities Commission’s **Cycle 11 Report** is available on their website (www.sec-com.govt.nz).

Other Topics of Interest

International Public Sector Accounting Standards Board Activity

The International Public Sector Accounting Standards Board (IPSASB) has issued an exposure draft on accounting for service concession arrangements by the grantor (IPSASB ED 43). It is adapted from IFRIC 12: *Service Concession Arrangements* which sets out the accounting requirements for the operator in a service concession arrangement.

The IPSASB has also issued an exposure draft on improvements to IPSASs (IPSASB ED 44) primarily to maintain alignment with IFRSs where the standards are equivalent.

Conceptual Framework

The IASB in conjunction with the US Financial Reporting Standards Board (FASB) continues to work on the conceptual framework which provides the basis for developing future accounting standards. In March they published an exposure draft on the reporting entity concept.

The exposure draft proposes that a reporting entity is *“a circumscribed area of economic activities whose financial information has the potential to be useful to existing and potential equity investors, lenders and other creditors who cannot directly obtain the information they need in making decisions about providing resources to the entity and in assessing whether the management and the governing board of that entity have made efficient and effective use of the resources provided.”*

The exposure draft also suggests that consolidated financial statements may be required when an entity controls another entity, and considers whether a portion of an entity could qualify as a reporting entity where the economic activities of that portion can be distinguished objectively from the rest of the entity.

Comments to the IASB are open until 16 July 2010. The **Exposure Draft** is available on the NZICA website.

Insurance Accounting Monthly Newsletter

Deloitte (United Kingdom) continues to issue a monthly newsletter focusing on the joint IASB and FASB project to develop a new global financial reporting standard for insurance. With an exposure draft scheduled to come out this month (according to the IASB's work plan) there have been a number of meetings held recently regarding this project. All issues of this newsletter are available on the [IAS Plus Insurance Project Page](#).

Kind Regards,

Denise Hodgkins

National Technical Partner

Ph: +64 (0) 9 303 0918

Email: dhodgkins@deloitte.co.nz

New Zealand Directory

Auckland Private Bag 115-033, Shortland Street, Auckland 1140, Ph +64 (0) 9 309 4944, Fax +64 (0) 9 309 4947

Hamilton PO Box 17, Hamilton 3240, Ph +64 (0) 7 838 4800, Fax +64 (0) 7 838 4810

Wellington PO Box 1990, Wellington 6140, Ph +64 (0) 4 472 1677, Fax +64 (0) 4 472 8023

Christchurch PO Box 248, Christchurch 8140, Ph +64 (0) 3 379 7010, Fax +64 (0) 3 366 6539

Dunedin PO Box 1245, Dunedin 9054, Ph +64 (0) 3 474 8630, Fax +64 (0) 3 474 8650

Internet address <http://www.deloitte.co.nz>

Deloitte New Zealand brings together more than 900 specialists providing audit, tax, technology and systems, strategy and performance improvement, risk management, corporate finance, business recovery, forensic and accounting services. Our people are based in Auckland, Hamilton, Wellington, Christchurch and Dunedin, serving clients that range from New Zealand's largest companies and public sector organisations to smaller businesses with ambition to grow.

Deloitte provides audit, tax, consulting, and financial advisory services to public and private clients spanning multiple industries. With a globally connected network of member firms in more than 140 countries, Deloitte brings world-class capabilities and deep local expertise to help clients succeed wherever they operate. Deloitte's more than 168,000 professionals are committed to becoming the standard of excellence.

Deloitte's professionals are unified by a collaborative culture that fosters integrity, outstanding value to markets and clients, commitment to each other, and strength from cultural diversity. They enjoy an environment of continuous learning, challenging experiences, and enriching career opportunities. Deloitte's professionals are dedicated to strengthening corporate responsibility, building public trust, and making a positive impact in their communities.

This publication contains general information only, and none of Deloitte Touche Tohmatsu, its member firms, or its and their affiliates are, by means of this publication, rendering accounting, business, financial, investment, legal, tax, or other professional advice or services. This publication is not a substitute for such professional advice or services, nor should it be used as a basis for any decision or action that may affect your finances or your business. Before making any decision or taking any action that may affect your finances or your business, you should consult a qualified professional adviser.

None of Deloitte Touche Tohmatsu, its member firms, or its and their respective affiliates shall be responsible for any loss whatsoever sustained by any person who relies on this publication.

Deloitte refers to one or more of Deloitte Touche Tohmatsu, a Swiss Verein, and its network of member firms, each of which is a legally separate and independent entity. Please see www.deloitte.com/nz/about for a detailed description of the legal structure of Deloitte Touche Tohmatsu and its Member Firms.

This publication is intended for the use of clients and personnel of Deloitte. It is also made available to other selected recipients. Those wishing to receive this publication regularly are asked to communicate with:

The Editor,
Accounting Alert
PO Box 33, Auckland.
Ph +64 (0) 9 309 4944
Fax +64 (0) 9 309 4947