

June 2013

International Accounting Standards Board® (IASB®)

Illustrative Guidance

IFRS® for SMEs

A Guide for Micro-sized Entities Applying the IFRS for SMEs (2009)



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This Guide accompanies, but is not part of, the IFRS for SMEs

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Introduction

This Guide accompanies, but is not part of, the IFRS for SMEs.

- IN1 Many requirements of the *International Financial Reporting Standard for Small and Medium-sized Entities (IFRS for SMEs)* will not be relevant to micro-sized entities ('micro entities') as they generally only encounter a narrow range of simple transactions.
- IN2 This Guide is intended to help micro entities that are within the scope of the *IFRS for SMEs*, ie who do not have public accountability (see paragraph G2), and are either required to prepare general purpose financial statements in accordance with the *IFRS for SMEs* as issued in July 2009 (for example, under the law in their jurisdictions) or choose to do so, to identify more easily the requirements of the *IFRS for SMEs* that are relevant to them. It is not a separate Standard for micro entities.
- IN3 This Guide is not intended for micro entities preparing financial statements solely for tax reasons or to comply with local laws (unless local laws require micro entities to use the *IFRS for SMEs*). However, those micro entities may still find this Guide helpful in preparing such financial statements.
- IN4 This Guide does not define a micro entity in quantitative terms. A jurisdiction may choose to define a micro entity in quantitative terms or provide further indicators of typical characteristics in order to indicate when this Guide should be used in that jurisdiction. A micro entity is normally a very small entity with simple transactions that has the following typical characteristics:
- (a) few employees and often owner-managed;
 - (b) low or moderate levels of revenue and gross assets; and
 - (c) does not:
 - (i) have investments in subsidiaries, associates or joint ventures;
 - (ii) hold or issue complex financial instruments; and
 - (iii) issue shares or share options to employees or other parties in exchange for goods or services.
- IN5 This Guide extracts requirements from the *IFRS for SMEs* without modifying any of the principles for recognising and measuring assets, liabilities, income, and expenses, and without changing any of the presentation or disclosure requirements. This Guide includes only those requirements of the *IFRS for SMEs* that are likely to be necessary for a typical micro entity. If an entity encounters a transaction in the current period or any comparative period presented in the financial statements (or that occurred in an earlier period but still affects those periods) that is not dealt with in this Guide, the entity is required, by the Guide, to refer to the applicable requirements in the *IFRS for SMEs*.
- IN6 Compliance with this Guide will result in compliance with the *IFRS for SMEs*. If an entity applies this Guide, the basis of preparation note and audit report can still refer to conformity with the *IFRS for SMEs* because this Guide does not modify the *IFRS for SMEs*.

- IN7 If a transaction, other event or condition covered in the *IFRS for SMEs* is not included in this Guide, it is identified in a ‘box’ at the beginning of the relevant section in this Guide, with a requirement that an entity having such a transaction, other event or condition must refer to the *IFRS for SMEs*. If an entity encounters one or two of the transactions, other events or conditions listed in those boxes (ie not dealt with in this Guide), the Guide may still be useful as a starting point to prepare the entity’s financial statements. However, an entity that is required to refer to the *IFRS for SMEs* in more than one or two circumstances will normally find it easier to use the *IFRS for SMEs* on its own, rather than starting with this Guide.
- IN8 A jurisdiction may wish to use the Guide as a starting point when developing its own similar guide. For example, in a jurisdiction where all or most entities, including micro entities, commonly have defined benefit plans, a jurisdiction may wish to issue its own guide to applying the *IFRS for SMEs* that includes requirements for defined benefit plans, rather than having a reference to the *IFRS for SMEs* in the box at the start of Guide Section 28 *Employee Benefits*.
- IN9 This Guide follows the sequence of the 35 sections in the *IFRS for SMEs* but, in some cases, combines several of the sections in the *IFRS for SMEs* together into one section in the Guide. To avoid confusion, each section of the Guide is referred to as a ‘Guide Section’ and when reference is made to a section in the *IFRS for SMEs* the term ‘*IFRS for SMEs* Section’ is used.
- IN10 While many of the paragraphs in this Guide have been taken from the *IFRS for SMEs*, it has been necessary to make some wording changes to improve the flow of the drafting or for other editorial reasons. Such changes do not modify the underlying requirements of the *IFRS for SMEs* in any way. In a few places the Guide contains guidance and illustrative examples that are not included in the *IFRS for SMEs*. The additional guidance and examples are included to help a micro entity apply the principles taken from the *IFRS for SMEs* and they do not modify the requirements of the *IFRS for SMEs*.
- IN11 Because this Guide does not modify any of the requirements of the *IFRS for SMEs*, when the Guide states “this Guide requires ...” or “this Guide permits ...” it is equivalent to saying “the *IFRS for SMEs* requires ...” or “the *IFRS for SMEs* permits ...”.
- IN12 This Guide does not contain a glossary. Key terms have been defined when they arise in this Guide. However, should additional clarity of terms be helpful, there is a comprehensive glossary within the *IFRS for SMEs*.
- IN13 Should an entity need to refer to the *IFRS for SMEs* for transactions not covered in this Guide or to look up a term in the comprehensive glossary, the *IFRS for SMEs* can be downloaded from <http://go.ifrs.org/IFRSforSMEs>.
- IN14 Further guidance and illustrative examples of applying the requirements of the *IFRS for SMEs* can be accessed in the comprehensive training material developed by the IFRS Foundation Education Initiative. There is one module for each section of the *IFRS for SMEs*. The training material can be downloaded from <http://go.ifrs.org/smetraining>.

A Guide for Micro-sized Entities Applying the *IFRS for SMEs* (2009)

Guide Section 1 ***Intended Scope of this Guide***

Use of the Guide

- G1 This Guide is intended to help a micro entity apply the requirements of the *IFRS for SMEs* when preparing its general purpose financial statements. This Guide includes only those requirements of the *IFRS for SMEs* that are likely to be necessary for a typical micro entity. If an entity encounters a transaction in the current period or any comparative period presented in the financial statements (or that occurred in an earlier period but still affects those periods) that is not dealt with in this Guide, the entity should refer to the applicable requirements of the *IFRS for SMEs*. Consequently, compliance with this Guide will result in compliance with the *IFRS for SMEs*.
- G2 This Guide is intended for use by a micro entity that is within the scope of the *IFRS for SMEs* (ie that does not have public accountability and that publishes general purpose financial statements in accordance with the *IFRS for SMEs*). An entity has public accountability, and should therefore be using full IFRSs, if its debt or equity instruments are traded in a public market (or it is in the process of issuing such instruments for trading in a public market) or it holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses.
- G3 This Guide does not define a micro entity in quantitative terms. A micro entity is normally a very small entity with simple transactions and normally:
- (a) has few employees and is often owner managed;
 - (b) has low or moderate levels of revenue and gross assets; and
 - (c) does not:
 - (i) have investments in subsidiaries, associates or joint ventures;
 - (ii) hold or issue complex financial instruments; or
 - (iii) issue shares or share options to employees or other parties in exchange for goods or services.

General purpose financial statements

- G4 General purpose financial statements are financial statements directed to the general financial information needs of a wide range of users who are not in a position to demand reports that are tailored to meet their particular information needs. Micro entities often produce financial statements only for the use of owner-managers or only for the use of tax authorities or other governmental authorities. Financial statements produced solely for those purposes are not general purpose financial statements.

Guide Section 2 ***Concepts and Pervasive Principles***

Objective of financial statements of a micro entity applying the IFRS for SMEs

- G5 The objective of financial statements of a micro entity applying the *IFRS for SMEs* is to provide information about the financial position, performance and cash flows of the entity that is useful for economic decision-making by a broad range of users who are not in a position to demand reports tailored to meet their particular information needs.

Financial position

- G6 The financial position of an entity is the relationship of its assets, liabilities and equity as of a specific date. These are defined as follows:
- (a) an asset is a resource controlled by the entity as a result of past events and from which future economic benefits are expected to flow to the entity;
 - (b) a liability is a present obligation of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits; and
 - (c) equity is the residual interest in the assets of the entity after deducting all its liabilities.

Performance

- G7 Performance is the relationship of the income and expenses of an entity during a reporting period. Income and expenses are defined as follows:
- (a) income is increases in economic benefits during the reporting period in the form of inflows or enhancements of assets or decreases of liabilities that result in increases in equity, other than those relating to contributions from equity investors; and
 - (b) expenses are decreases in economic benefits during the reporting period in the form of outflows or depletions of assets or incurrences of liabilities that result in decreases in equity, other than those relating to distributions to equity investors.

Cash flows

- G8 Cash flow information shows how an entity generates and uses cash and cash equivalents. Entities need cash to conduct their operations, to pay their obligations, to make investments in income-producing assets, and to provide returns to their investors. Information about the performance of an entity shows the income, expenses, and profit or loss of the entity on an accrual basis. However the actual inflows and outflows of cash from an entity's operations generally differ – often significantly – from its income and expenses on an

accrual basis. Moreover, reporting performance on an accrual basis gives no insight into the cash used by an entity in its investing activities or the cash generated by the entity through its financing activities.

- G9 Cash flows are classified as cash flows from operating, investing and financing activities. Classification by activity provides information on how those activities affect the financial position of the entity (including its liquidity and solvency) and the amount of its cash and cash equivalents.

Recognition of assets, liabilities, income and expenses

- G10 An item shall be recognised (ie, incorporated in the financial statements) if it meets the definition of an asset, liability, income or expense and satisfies the following criteria:
- (a) it is probable (ie, more likely than not) that any future economic benefit associated with the item will flow to or from the entity; and
 - (b) the item has a cost or value that can be measured reliably.
- G11 In many cases, the cost or value of an item is known. In other cases it must be estimated. The use of reasonable estimates is an essential part of the preparation of financial statements and does not undermine their reliability.

Accrual basis

- G12 An entity shall prepare its financial statements, except for cash flow information, using the accrual basis of accounting. On the accrual basis, items are recognised as assets, liabilities, equity, income or expenses when they satisfy the definitions and recognition criteria for those items.

Fair value of an asset

- G13 Measurement requirements are generally set out in the individual sections of this Guide. However the following guidance on fair value measurement is relevant to several sections and so has been included here.
- G14 Most of the requirements under this Guide require a cost-based measurement. However, in a few circumstances, fair value measurement is required under this Guide, for example measurement of investments in ordinary shares (Guide Section 11–12 *Financial Instruments*), measurement of owners' contributions of non-cash assets (Guide Section 22 *Equity*) and measurement of impairment of assets (Guide Section 27 *Impairment of Assets*). The fair value of an asset is the amount for which the asset could be exchanged between knowledgeable, willing parties in an arm's length transaction. An entity shall use the following hierarchy to estimate the fair value of an asset:
- (a) the best evidence of fair value is a price in a binding sale agreement in an arm's length transaction or a quoted price for an identical asset in an active market (the latter is usually the current bid price).

- (b) if there is no binding sale agreement or active market for an asset, the price of a recent transaction for an identical asset provides evidence of fair value as long as there has not been a significant change in economic circumstances or a significant lapse of time since the transaction took place. If the entity can demonstrate that the last transaction price is not a good estimate of fair value (for example, because it reflects the amount that an entity would receive or pay in a forced transaction, involuntary liquidation or distress sale), that price is adjusted.
 - (c) if there is no binding sale agreement or active market for an asset and recent transactions of an identical asset on their own are not a good estimate of fair value, an entity estimates the fair value by using another valuation technique. The objective of using a valuation technique is to estimate what the transaction price would have been on the measurement date in an arm's length exchange motivated by normal business considerations.
- G15 Valuation techniques include using recent arm's length market transactions for an identical asset between knowledgeable, willing parties, reference to the current fair value of another asset that is substantially the same as the asset being measured, and discounted cash flow analysis. If there is a valuation technique commonly used by market participants to price the asset and that technique has been demonstrated to provide reliable estimates of prices obtained in actual market transactions, the entity uses that technique.
- G16 The objective of using a valuation technique is to establish what the transaction price would have been on the measurement date in an arm's length exchange motivated by normal business considerations. Fair value is estimated on the basis of the results of a valuation technique that makes maximum use of market inputs, and relies as little as possible on entity-determined inputs. A valuation technique would be expected to arrive at a reliable estimate of the fair value if:
 - (a) it reasonably reflects how the market could be expected to price the asset; and
 - (b) the inputs to the valuation technique reasonably represent market expectations and measures of the risk return factors inherent in the asset.

Offsetting

- G17 An entity shall not offset assets and liabilities, or income and expenses, unless required or permitted by this Guide.
 - (a) Measuring assets net of valuation allowances—for example, allowances for inventory obsolescence and allowances for uncollectible receivables—is not offsetting.
 - (b) If an entity's normal operating activities do not include buying and selling non-current assets, including investments and operating assets, then the entity reports gains and losses on disposal of such assets by deducting from the proceeds on disposal the carrying amount of the asset and related selling expenses.

Guide Section 3–8 **Financial Statement Presentation**

Situations not addressed by this Guide

An entity shall refer to the *IFRS for SMEs*:

- (a) if management is aware, in making its assessment under paragraph G20, of material uncertainties related to events or conditions that cast significant doubt upon the entity's ability to continue as a going concern (see *IFRS for SMEs* paragraph 3.9).
- (b) if presenting assets and liabilities in the statement of financial position in order of liquidity would provide reliable and more relevant information than the current/non-current presentation required by paragraph G45 (see *IFRS for SMEs* paragraph 4.4).
- (c) if the entity has items of other comprehensive income in the current period or any comparative period presented in the financial statements (see *IFRS for SMEs* Section 5 and paragraphs 3.17(b), 4.11(f), 6.3(c), 29.7, 29.14(b), 29.17, 29.22, 29.27 and 29.32(a)).

Note: an entity could only have items of other comprehensive income if it has the following transactions/items: any foreign operations (*IFRS for SMEs* Section 30), any defined benefit post-employment benefit plans (*IFRS for SMEs* Section 28), or investments in associates/joint ventures (*IFRS for SMEs* Sections 14 and 15) or if it applies hedge accounting (*IFRS for SMEs* Section 12). These transactions/items are not addressed by this Guide.

- (d) if the entity is selling a major line of business or geographical area of operations it will need to present discontinued operations separately (see *IFRS for SMEs* paragraphs 5.5(e) and 29.27).

Note: paragraphs G32–G44 of this Guide include illustrative financial statements. Those statements reflect the transactions covered by this Guide. If an entity encounters transactions for which it must refer back to the *IFRS for SMEs* (ie those listed in the boxes at the start of Guide Sections 9–34), it may also have to add additional line items that are not illustrated in the illustrative financial statements (see *IFRS for SMEs* Sections 4–7).

Fair presentation

- G18 Financial statements shall present fairly the financial position, financial performance and cash flows of an entity.

Compliance with the *IFRS for SMEs*

- G19 An entity that meets the requirements of this Guide and whose financial statements comply with this Guide (with reference to the *IFRS for SMEs* if required by the boxes in this Guide), shall make an explicit and unreserved statement of compliance with the *IFRS for SMEs* in the notes to the financial statements.

Going concern

- G20 The principles of financial reporting in this Guide are intended for an entity that is a going concern. An entity is a going concern unless management either intends to liquidate the entity or to cease operations, or has no realistic alternative but to do so. In assessing whether the going concern assumption is appropriate, management takes into account all available information about the future, which is at least, but is not limited to, twelve months from the reporting date.

Frequency of reporting

- G21 An entity shall present a complete set of financial statements (including comparative information—see paragraph G23) at least annually. When the end of an entity's reporting period changes and the annual financial statements are presented for a period longer or shorter than one year, the entity shall disclose the following:
- (a) that fact;
 - (b) the reason for using a longer or shorter period; and
 - (c) the fact that comparative amounts presented in the financial statements (including the related notes) are not entirely comparable.

Consistency of presentation

- G22 An entity shall retain the presentation and classification of items in the financial statements from one period to the next unless it is apparent, following a significant change in the nature of the entity's operations or a review of its financial statements, that another presentation or classification would be more appropriate. If the entity changes the presentation or classification of an item in the financial statements this is a voluntary change in accounting policy (see Guide Section 10 *Accounting Policies, Estimates and Errors*).

Comparative information

- G23 Except when this Guide permits or requires otherwise, an entity shall disclose comparative information in respect of the previous comparable period for all amounts presented in the current period's financial statements. An entity shall include comparative information for narrative and descriptive information when it is relevant to an understanding of the current period's financial statements.

Materiality and aggregation

- G24 Information is material if its omission or misstatement could, individually or collectively, influence the economic decisions of users made on the basis of the financial statements. Materiality depends on the size and nature of the item or error judged in the particular circumstances of its omission or misstatement.

The size or nature of the item, or a combination of both, could be the determining factor. However, it is inappropriate to make, or leave uncorrected, immaterial departures to achieve a particular presentation of an entity's financial position, financial performance or cash flows.

- G25 An entity shall present separately each material class of similar items. An entity shall present separately items of a dissimilar nature or function unless they are immaterial.

Complete set of financial statements

- G26 A complete set of financial statements of an entity shall include all of the following:
- (a) a statement of financial position (sometimes called the balance sheet), showing the entity's assets, liabilities and equity as at the reporting date.
 - (b) a statement of income for the reporting period, displaying all items of income and expense recognised during the period and a 'bottom line', that may be called 'profit or loss' or 'total comprehensive income'.
 - (c) a statement of changes in equity for the reporting period. The statement of changes in equity presents a reconciliation between the carrying amount at the beginning and end of the period for each component of equity. However, if the only changes to equity in the current period or any comparative period presented in the financial statements arise from profit or loss, payment of dividends, corrections of prior period errors, and changes in accounting policy, the entity may present a single statement of income and retained earnings in place of the statement of income and statement of changes in equity.
 - (d) a statement of cash flows for the reporting period. The statement of cash flows provides information about the changes in cash and cash equivalents of an entity for a reporting period, showing separately, changes from operating activities, investing activities and financing activities.
 - (e) notes, comprising a summary of significant accounting policies and other explanatory information. Notes contain information in addition to that presented in the statements in (a)–(d) above. Notes provide narrative descriptions or disaggregations of items presented in those statements and information about items that do not qualify for recognition in those statements.
- G27 Because paragraph G23 requires comparative amounts in respect of the previous period for all amounts presented in the financial statements, a complete set of financial statements means that an entity shall present, as a minimum, two of each of the required financial statements, and the notes shall include comparative information for all amounts presented.
- G28 In a complete set of financial statements, an entity shall present each financial statement with equal prominence.

- G29 An entity may use titles for the financial statements other than those used in this Guide as long as they are not misleading.

Identification of the financial statements

- G30 An entity shall clearly identify each of the financial statements and the notes and distinguish them from other information in the same document. In addition, an entity shall display the following information prominently, and repeat it when necessary for an understanding of the information presented:
- (a) the name of the reporting entity and any change in its name since the end of the preceding reporting period;
 - (b) the fact that the financial statements cover an individual entity [this Guide does not cover consolidated financial statements—see box at the start of Guide Section 9 *Consolidated and Separate Financial Statements*];
 - (c) the date of the end of the reporting period and the period covered by the financial statements;
 - (d) the currency in which the financial statements are presented; and
 - (e) the level of rounding, if any, used in presenting amounts in the financial statements.
- G31 An entity shall disclose the following in the notes:
- (a) the domicile and legal form of the entity, its country of incorporation and the address of its registered office (or principal place of business, if different from the registered office); and
 - (b) a description of the nature of the entity's operations and its principal activities.

Illustrative formats

- G32 Paragraph G26 defines a complete set of financial statements. The statements set out in paragraphs G33–G44 illustrate suitable formats for a typical micro entity for the presentation of the statement of financial position, statement of income and retained earnings, statement of income, statement of changes in equity and the two ways of preparing the statement of cash flows. However, each entity will need to consider the format of presentation and the descriptions used for line items to achieve a fair presentation in that entity's particular circumstances. The entity will also need to consider whether the financial statements comply with local laws or regulations.

Statement of financial position

- G33 The illustrative statement of financial position presents current assets followed by non-current assets, and presents current liabilities followed by non-current liabilities and then presents equity. In some jurisdictions, the sequencing is typically reversed, and that is also permitted.
- G34 The illustrative statement of financial position shows the minimum line items that are required to be presented in the statement of financial position if the

entity encounters only transactions and events addressed by this Guide. (Note: if an entity has current and/or deferred tax assets, these are also required to be presented in the statement of financial position.) If an entity encounters transactions and events not addressed in this Guide additional line items may be required [see the box at the start of Guide Section 3–7]. Furthermore, an entity shall present additional line items, headings and subtotals in the statement of financial position when such presentation is relevant to an understanding of the entity's financial position.

G35 Paragraphs G51–G54 require other items to be presented in the statement of financial position or in the notes. If only the minimum line items are presented in the statement of financial position, as in the example below, those other items shall be disclosed in the notes.

Statement of financial position at 31 December 20X2

	20X2 CU	20X1 CU
ASSETS		
Current assets		
Cash and cash equivalents	X	X
Trade and other receivables	X	X
Investments in shares	X	X
Inventories	X	X
	<hr/>	<hr/>
	X	X
Non-current assets		
Property, plant and equipment	X	X
	<hr/>	<hr/>
Total assets	<hr/> <hr/>	<hr/> <hr/>
LIABILITIES AND EQUITY		
Current liabilities		
Trade and other payables	X	X
Current tax liability	X	X
Provisions	X	X
	<hr/>	<hr/>
	X	X
Non-current liabilities		
Bank loan	X	X
Provisions	X	X
Obligations under finance leases	X	X
Deferred tax liability	X	X
	<hr/>	<hr/>
	X	X
Total liabilities	<hr/> <hr/>	<hr/> <hr/>

continued...

...continued

Statement of financial position at 31 December 20X2

	20X2 CU	20X1 CU
Equity^(a)		
Share capital	X	X
Retained earnings	X	X
Total equity	<u>X</u>	<u>X</u>
Total liabilities and equity	<u>X</u>	<u>X</u>

(a) The categories of equity will differ depending on the nature of the organisation, for example if the entity is a sole proprietorship, partnership or company. For example, for an unincorporated business, instead of share capital the owner's paid-in capital may be called proprietor's capital invested in the business. The retained earnings may or may not be combined into this amount depending on legal requirements or clarity of presentation. The categories may also differ depending on legal and other requirements of different jurisdictions.

Alternative 1: statement of income and retained earnings

- G36 A statement of income and retained earnings is illustrated below. Most micro entities will meet the condition in paragraph G26(c) to present a single statement of income and retained earnings in place of both a statement of income and a statement of changes in equity. The statement of income and retained earnings below illustrates classification of expenses by nature (see paragraph G56(a)). The illustration shows the minimum line items that are required to be presented in the statement of income and retained earnings (these are the non-italicised line items). An entity shall present additional line items, headings and subtotals in the statement of income when such presentation is relevant to an understanding of the entity's financial performance.
- G37 Profit before tax is not a required line item. The other line items that are in italics (the analysis of expenses) may be presented in the notes or in the statement of income and retained earnings (see paragraph G56). The line items have been illustrated in this statement as this is a common presentation in practice.
- G38 Where an entity does not have prior period errors or changes in accounting policy (see Guide Section 10), the line items relating to the restatement of retained earnings for these items would be omitted.

**Statement of income and retained earnings for the year ended
31 December 20X2 (by nature presentation)**

(optional line items are shown in italics)	20X2	20X1
	CU	CU
Revenue	X	X
<i>Other income</i>	X	X
<i>Changes in inventories of finished goods and work in progress</i>	X	X
<i>Raw material and consumables used</i>	X	X
<i>Employee salaries and benefits</i>	X	X
<i>Depreciation expense</i>	X	X
<i>Impairment of property, plant and equipment</i>	X	X
<i>Other expenses</i>	X	X
Finance costs	X	X
<i>Profit before tax</i>	X	X
Income tax expense	X	X
Profit for the year	X	X
Retained earnings at start of year	X	X
Restatement of retained earnings for corrections of prior period errors	X	X
Restatement of retained earnings for changes in accounting policy	X	X
Dividends paid during the year	X	X
Retained earnings at end of year	X	X

Alternative 2: both a statement of income and a statement of changes in equity

- G39 A statement of income is illustrated below. If an entity presents a statement of income it will also need to present a separate statement of changes in equity. The statement of income below illustrates the classification of expenses by function (see paragraph G56(b)). The illustration shows the minimum line items that are required to be presented in the statement of income (these are the non-italicised line items). An entity shall present additional line items, headings and subtotals in the statement of income when such presentation is relevant to an understanding of the entity's financial performance.
- G40 Profit before tax is not a required line item. The other line items that are in italics (the analysis of expenses) may be presented in the notes or in the statement of income (see paragraph G56). The line items in italics have been shown in this statement as this is a common presentation in practice.

Statement of income for the year ended 31 December 20X2 (by function presentation)

(optional line items are shown in italics)

	20X2	20X1
	CU	CU
Revenue	X	X
<i>Cost of sales</i>	X	X
<i>Gross profit</i>	X	X
<i>Other income</i>	X	X
<i>Distribution costs</i>	X	X
<i>Administrative expenses</i>	X	X
<i>Other expenses</i>	X	X
Finance costs	X	X
<i>Profit before tax</i>	X	X
Income tax expense	X	X
Profit for the year	X	X

G41 An statement of changes in equity is illustrated below. An entity shall show the following line items in the statement of changes in equity:

- (a) profit or loss for the period (or total comprehensive income);
- (b) for each component of equity, the effects of retrospective application or retrospective restatement recognised in accordance with Guide Section 10; and
- (c) for each component of equity, a reconciliation between the carrying amount at the beginning and the end of the period, separately disclosing changes resulting from:
 - (i) profit or loss; and
 - (ii) the amounts of investments by, and dividends and other distributions to, owners, showing separately issues of shares, dividends and other distributions to owners.

An unincorporated business may only have one component of equity, for example, the proprietor's capital invested in the business.

G42 Where an entity does not have prior period errors or changes in accounting policy (see Guide Section 10) the line items in paragraph G41(b) relating to the restatement of retained earnings for these items would be omitted.

Statement of changes in equity for the year ended 31 December 20X2

	Share capital	Retained earnings
	CU	CU
Balance at 1 January 20X1 (as originally reported)	X	X
Corrections of prior period errors	X	X
Changes in accounting policy	X	X
	<hr/>	<hr/>
Restated balance at 1 January 20X1	X	X
Profit or loss for the year	X	X
Dividends paid during the year	X	X
Issue of shares	X	X
	<hr/>	<hr/>
Restated balance at 31 December 20X1	X	X
	<hr/>	<hr/>
Profit or loss for the year	X	X
Dividends paid during the year	X	X
	<hr/>	<hr/>
Balance at 31 December 20X2	<u>X</u>	<u>X</u>

Statement of cash flows

- G43 A statement of cash flows shall present cash flows for a reporting period classified by operating activities, investing activities and financing activities. Two statements of cash flows are illustrated below to show the two different methods of reporting cash flows from operating activities (see paragraph G59).
- G44 Guide Section 3-8 does not prescribe specific minimum line items for the statement of cash flows. The illustrative cash flow statements below show the types of cash flows that micro entities typically encounter.

Alternative 1: statement of cash flows for the year ended 31 December 20X2 (illustrates indirect method in paragraph G60)

	20X2	20X1
	CU	CU
Cash flows from operating activities		
Profit for the year	X	X
Adjustments for non-cash income and expenses:		
Non-cash finance costs	X	X
Non-cash income tax expense	X	X
Gain on sale of equipment	X	X
Depreciation of property, plant and equipment	X	X
Impairment loss on property, plant and equipment	X	X
Changes in operating assets and liabilities:		
Decrease (increase) in trade and other receivables	X	X
Decrease (increase) in inventories	X	X
Increase (decrease) in trade payables	X	X
Net cash from (used in) operating activities	<u>X</u>	<u>X</u>
Cash flows from investing activities		
Proceeds from sale of equipment	X	X
Purchases of equipment	X	X
Net cash from (used in) investing activities	<u>X</u>	<u>X</u>
Cash flows from financing activities		
Repayment of borrowings	X	X
Payment of finance lease obligations	X	X
Dividends paid	X	X
Net cash from (used in) financing activities	<u>X</u>	<u>X</u>
Net increase (decrease) in cash and cash equivalents	X	X
Cash and cash equivalents at beginning of year	<u>X</u>	<u>X</u>
Cash and cash equivalents at end of year	<u><u>X</u></u>	<u><u>X</u></u>

Alternative 2: statement of cash flows for the year ended 31 December 20X2 (illustrates direct method in paragraph G61)

	20X2 CU	20X1 CU
Cash flows from operating activities		
Cash receipts from customers	X	X
Cash paid to suppliers and employees	X	X
Interest paid	X	X
Income taxes paid	X	X
	<hr/>	<hr/>
Net cash from (used in) operating activities	X	X
Cash flows from investing activities		
Proceeds from sale of equipment	X	X
Purchases of equipment	X	X
	<hr/>	<hr/>
Net cash from (used in) investing activities	X	X
Cash flows from financing activities		
Repayment of borrowings	X	X
Payment of finance lease obligations	X	X
Dividends paid	X	X
	<hr/>	<hr/>
Net cash from (used in) financing activities	X	X
	<hr/>	<hr/>
Net increase (decrease) in cash and cash equivalents	X	X
Cash and cash equivalents at beginning of year	X	X
	<hr/>	<hr/>
Cash and cash equivalents at end of year	X	X
	<hr/> <hr/>	<hr/> <hr/>

Statement of financial position and accompanying notes

Current/non-current distinction

- G45 An entity shall present current and non-current assets, and current and non-current liabilities, as separate classifications in its statement of financial position in accordance with paragraphs G46–G49.
- G46 An entity shall classify an asset as current when:
- (a) it expects to realise the asset, or intends to sell or consume it, in the entity's normal operating cycle;
 - (b) it holds the asset primarily for the purpose of trading;
 - (c) it expects to realise the asset within twelve months after the reporting date; or
 - (d) the asset is cash or a cash equivalent, unless it is restricted from being exchanged or used to settle a liability for at least twelve months after the reporting date.

G47 An entity shall classify all other assets as non-current. When the entity's normal operating cycle is not clearly identifiable, its duration is assumed to be twelve months.

G48 An entity shall classify a liability as current when:

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

G49 An entity shall classify all other liabilities as non-current.

Sequencing of items and format of items in the statement of financial position

G50 The Guide does not prescribe the sequence or format in which items are to be presented. Paragraph G34 simply requires minimum line items that are sufficiently different in nature or function to warrant separate presentation in the statement of financial position. In addition:

- (a) line items are included when the size, nature or function of an item or aggregation of similar items is such that separate presentation is relevant to an understanding of the entity's financial position; and
- (b) the descriptions used and the sequencing of items or aggregation of similar items may be amended according to the nature of the entity and its transactions, to provide information that is relevant to an understanding of the entity's financial position.

Information to be presented either in the statement of financial position or in the notes

G51 An entity shall disclose, either in the statement of financial position or in the notes, the following subclassifications of the line items presented:

- (a) property, plant and equipment in classifications appropriate to the entity;
- (b) trade and other receivables showing separately amounts due from related parties, amounts due from other parties, and receivables arising from accrued income not yet billed;
- (c) inventories, showing separately amounts of inventories:
 - (i) held for sale in the ordinary course of business (for example, inventories held by retailers and the finished goods of a manufacturer);
 - (ii) in the process of production for such sale (for example, the work in progress of a manufacturer);

- (iii) in the form of materials or supplies to be consumed in the production process or in the rendering of services (for example, raw materials); and
 - (d) trade and other payables, showing separately amounts payable to trade suppliers, payable to related parties, deferred income and accruals;
 - (e) provisions for employee benefits and other provisions; and
 - (f) classes of equity, such as paid-in capital, share premium, and retained earnings.
- G52 An entity with share capital shall disclose the following, either in the statement of financial position or in the notes:
 - (a) for each class of share capital:
 - (i) the number of shares authorised;
 - (ii) the number of shares issued and fully paid, and issued but not fully paid;
 - (iii) par value per share, or that the shares have no par value;
 - (iv) a reconciliation of the number of shares outstanding at the beginning and at the end of the period;
 - (v) the rights, preferences and restrictions attaching to that class including restrictions on the distribution of dividends and the repayment of capital; and
 - (vi) shares reserved for issue under options and contracts for the sale of shares, including the terms and amounts; and
 - (b) a description of each reserve within equity.
- G53 An entity without share capital, such as a partnership or trust, shall disclose information equivalent to that required by paragraph G52(a), showing changes during the period in each category of equity, and the rights, preferences and restrictions attaching to each category of equity.
- G54 If, at the reporting date, an entity has a binding sale agreement for a major disposal of assets, or a group of assets and liabilities, the entity shall disclose the following information:
 - (a) a description of the asset(s) or the group of assets and liabilities;
 - (b) a description of the facts and circumstances of the sale or plan; and
 - (c) the carrying amount of the assets or, if the disposal involves a group of assets and liabilities, the carrying amounts of those assets and liabilities.

Statement of income and accompanying notes

- G55 An entity shall not present or describe any items of income and expense as 'extraordinary items' in the statement of income or in the notes.

Analysis of expenses

- G56 An entity shall present an analysis of expenses using a classification based on either the nature of expenses or the function of expenses within the entity, whichever provides information that is reliable and more relevant.

Analysis by nature of expense

- (a) Under this method of classification, expenses are aggregated in the statement of income according to their nature (for example, depreciation, purchases of materials, transport costs, employee benefits and advertising costs), and are not reallocated among various functions within the entity.

Analysis by function of expense

- (b) Under this method of classification, expenses are aggregated according to their function as part of cost of sales or, for example, the costs of distribution or administrative activities. At a minimum, an entity discloses its cost of sales under this method separately from other expenses.

Statement of cash flows and accompanying notes

Cash equivalents

- G57 Cash is cash on hand and demand deposits. Cash equivalents are short-term, highly liquid investments held to meet short-term cash commitments rather than for investment or other purposes. Therefore, an investment normally qualifies as a cash equivalent only when it has a short maturity of, say, three months or less from the date of acquisition. Bank overdrafts are normally considered financing activities similar to borrowings. However, if they are repayable on demand and form an integral part of an entity's cash management, bank overdrafts are a component of cash and cash equivalents.

Operating activities

- G58 Operating activities are the principal revenue-producing activities of the entity. Therefore, cash flows from operating activities generally result from the transactions and other events and conditions that enter into the determination of profit or loss. Examples of cash flows from operating activities are:

- (a) cash receipts from the sale of goods and the rendering of services;
- (b) cash payments to suppliers for goods and services;
- (c) cash payments to and on behalf of employees; and
- (d) cash payments or refunds of income tax, unless they can be specifically identified with financing and investing activities.

Some transactions, such as the sale of an item of plant by a manufacturing entity, may give rise to a gain or loss that is included in profit or loss. However, the cash flows relating to such transactions are cash flows from investing activities.

- G59 An entity shall present cash flows from operating activities using either:
- (a) the indirect method, whereby profit or loss is adjusted for the effects of non-cash transactions, any deferrals or accruals of past or future operating cash receipts or payments, and items of income or expense associated with investing or financing cash flows; or
 - (b) the direct method, whereby major classes of gross cash receipts and gross cash payments are disclosed.

Indirect method

- G60 Under the indirect method, the net cash flow from operating activities is determined by adjusting profit or loss for the effects of:
- (a) changes during the period in inventories and operating receivables and payables;
 - (b) non-cash items such as depreciation, provisions, deferred tax, accrued income (expenses) not yet received (paid) in cash, unrealised foreign currency gains and losses; and
 - (c) all other items for which the cash effects relate to investing or financing.

Direct method

- G61 Under the direct method, net cash flow from operating activities is presented by disclosing information about major classes of gross cash receipts and gross cash payments. Such information may be obtained either:
- (a) from the accounting records of the entity; or
 - (b) by adjusting sales, cost of sales and other items in the statement of income for:
 - (i) changes during the period in inventories and operating receivables and payables;
 - (ii) other non-cash items; and
 - (iii) other items for which the cash effects are investing or financing cash flows.

Investing activities

- G62 Investing activities are the acquisition and disposal of long-term assets and other investments not included in cash equivalents. Examples of cash flows arising from investing activities are:
- (a) cash payments to acquire property, plant and equipment (including self-constructed property, plant and equipment);
 - (b) cash receipts from sales of property, plant and equipment;
 - (c) cash advances and loans made to other parties, for example, employees; and
 - (d) cash receipts from the repayment of advances and loans made to other parties.

Financing activities

- G63 Financing activities are activities that result in changes in the size and composition of the contributed equity and borrowings of an entity. Examples of cash flows arising from financing activities are:
- (a) cash proceeds from owner contributions, issuing shares or other equity instruments;
 - (b) cash payments to owners to acquire or redeem the entity's shares;
 - (c) cash proceeds from loans payable and other borrowings;
 - (d) cash repayments of amounts borrowed; and
 - (e) cash payments by a lessee for the reduction of the outstanding liability relating to a finance lease.

Reporting cash flows from investing and financing activities

- G64 An entity shall present separately major classes of gross cash receipts and gross cash payments arising from investing and financing activities.

Interest and dividends

- G65 An entity shall present separately cash flows from interest and dividends received and paid. The entity shall classify cash flows consistently from period to period as operating, investing or financing activities.
- G66 An entity may classify interest paid and interest and dividends received as operating cash flows because they are included in profit or loss. Alternatively, the entity may classify interest paid and interest and dividends received as financing cash flows and investing cash flows respectively, because they are costs of obtaining financial resources or returns on investments.
- G67 An entity may classify dividends paid as a financing cash flow because they are a cost of obtaining financial resources. Alternatively, the entity may classify dividends paid as a component of cash flows from operating activities because they are paid out of operating cash flows.

Income tax

- G68 An entity shall present separately cash flows arising from income tax and shall classify them as cash flows from operating activities unless they can be specifically identified with financing and investing activities. When tax cash flows are allocated over more than one class of activity, the entity shall disclose the total amount of taxes paid.

Non-cash transactions

- G69 An entity shall exclude from the statement of cash flows investing and financing transactions that do not require the use of cash or cash equivalents. An entity shall disclose such transactions elsewhere in the financial statements in a way that provides all the relevant information about those investing and financing activities. Examples of non-cash transactions are:

- (a) the acquisition of assets either by assuming directly related liabilities or by means of a finance lease; and
- (b) the contribution of a non-cash asset, for example, an item of property, plant and equipment, by the owner.

Components of cash and cash equivalents

- G70 An entity shall present the components of cash and cash equivalents and shall present a reconciliation of the amounts presented in the statement of cash flows to the equivalent items presented in the statement of financial position. However, an entity is not required to present this reconciliation if the amount of cash and cash equivalents presented in the statement of cash flows is identical to the amount similarly described in the statement of financial position.

Other disclosures

- G71 An entity shall disclose, together with a commentary by management, the amount of significant cash and cash equivalent balances held by the entity that are not available for use by the entity. For example, cash and cash equivalents held by an entity may not be available for use by the entity because of legal restrictions.

Notes to the financial statements

- G72 The notes shall:
- (a) present information about the basis of preparation of the financial statements and the specific accounting policies used, in accordance with paragraphs G76–G78;
 - (b) disclose the information required by this Guide that is not presented elsewhere in the financial statements; and
 - (c) provide information that is not presented elsewhere in the financial statements but is relevant to an understanding of any of them.
- G73 Additional disclosures may be necessary in the notes if management feels that compliance with the specific requirements in this Guide is insufficient to enable users to understand the effect of particular transactions, other events and conditions on the entity's financial position and financial performance.
- G74 An entity shall, as far as practicable, present the notes in a systematic manner. An entity shall cross-reference each item in the financial statements to any related information in the notes.
- G75 An entity normally presents the notes in the following order:
- (a) a statement that the financial statements have been prepared in compliance with the *IFRS for SMEs* (see paragraph G19);
 - (b) a summary of significant accounting policies applied (see paragraph G76);

- (c) supporting information for items presented in the financial statements, in the sequence in which each statement and each line item is presented; and
- (d) any other disclosures.

Disclosure of accounting policies

G76 An entity shall disclose the following in the summary of significant accounting policies:

- (a) the measurement basis (or bases) used in preparing the financial statements (for example, historical cost, fair value, etc); and
- (b) the other accounting policies used that are relevant to an understanding of the financial statements.

Information about judgements

G77 An entity shall disclose, in the summary of significant accounting policies or other notes, the judgements, apart from those involving estimations (see paragraph G78), that management has made in the process of applying the entity's accounting policies and that have the most significant effect on the amounts recognised in the financial statements.

Information about key sources of estimation uncertainty

G78 An entity shall disclose in the notes information about the key assumptions concerning the future, and other key sources of estimation uncertainty at the reporting date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year. In respect of those assets and liabilities, the notes shall include details of:

- (a) their nature; and
- (b) their carrying amount as at the end of the reporting period.

Guide Section 9 Consolidated and Separate Financial Statements

Situations not addressed by this Guide	
An entity shall refer to the <i>IFRS for SMEs</i> :	
(a)	if the entity has control over one or more other entities (known as subsidiaries), including any that were acquired exclusively with a view to resale (see <i>IFRS for SMEs</i> Section 9 and paragraphs 5.5(e), 22.2(a), 22.19, 29.1, 29.27, 32.11(b), 33.10(b) and 33.12(j)).
(b)	if the entity prepares combined financial statements, ie, financial statements incorporating two or more entities controlled by a single investor (see <i>IFRS for SMEs</i> paragraphs 9.28–9.30).

Guide Section 10

Accounting Policies, Estimates and Errors

Situations not addressed by this Guide

If this Guide does not specifically address a situation (for example, a transaction, other event or condition) and that situation is also not identified in a 'box' at the beginning of one of the sections in this Guide, an entity shall refer to *IFRS for SMEs* Section 10 in developing an appropriate accounting policy for that particular event or transaction. *IFRS for SMEs* paragraphs 10.4–10.6 provide guidance for those rare cases when an entity encounters a situation that is not specifically covered by the *IFRS for SMEs* (and would therefore also not be specifically covered in this Guide).

Selection and application of accounting policies

- G79 Accounting policies are the specific principles, bases, conventions, rules and practices applied by an entity in preparing and presenting financial statements. An entity shall select and apply its accounting policies consistently for similar transactions, other events and conditions.
- G80 An entity need not follow a requirement in this Guide if the effect of doing so would not be material.

Changes in accounting policies

- G81 An entity shall change an accounting policy only if the change results in the financial statements providing reliable and more relevant information about the effects of transactions, other events or conditions on the entity's financial position, financial performance or cash flows. Therefore, changes in accounting policies are generally rare.
- G82 Examples of changes in accounting policies that would be appropriate if the new policy provides reliable and more relevant information are:
- (a) in the statement of income, a change from presenting an analysis of expenses based on the nature of expenses to presenting it based on the function of expenses;
 - (b) changing the cost formula used to measure inventories from first-in first-out to weighted average; and
 - (c) a change from presenting a single statement of income and retained earnings to preparing both a separate statement of income and a separate statement of changes in equity (except for the change in paragraph G83(b)).
- G83 The following are not changes in accounting policies:
- (a) the application of a new accounting policy for transactions, other events or conditions that did not occur previously or were not material; and

- (b) a change from presenting a single statement of income and retained earnings to preparing both a separate statement of income and a separate statement of changes in equity because the entity no longer complies with the conditions to present a single statement of income and retained earnings under paragraph G26(c).

Applying changes in accounting policies

- G84 An entity shall account for changes in an accounting policy under paragraph G81 retrospectively. This means the entity shall apply the new accounting policy to comparative information for prior periods at the earliest date for which it is practicable, as if the new accounting policy had always been applied.
- G85 When it is impracticable to determine the individual-period effects of a change in accounting policy on comparative information for one or more prior periods presented (ie, the entity cannot determine it after making every reasonable effort to do so), the entity shall apply the new accounting policy to the carrying amounts of assets and liabilities as at the beginning of the earliest period for which retrospective application is practicable, which may be the current period, and shall make a corresponding adjustment to the opening balance of each affected component of equity for that period.

Changes in accounting estimates

- G86 A change in accounting estimate is an adjustment of the carrying amount of an asset or a liability, or the amount of the periodic consumption of an asset, that results from the assessment of the present status of, and expected future benefits and obligations associated with, assets and liabilities. Changes in accounting estimates result from new information or new developments and, accordingly, are not corrections of errors. When it is difficult to distinguish a change in an accounting policy from a change in an accounting estimate, the change is treated as a change in an accounting estimate.
- G87 Examples of changes in accounting estimate include:
 - (a) a change in the method of depreciating an item of property, plant and equipment from a reducing balance method to a straight line method to reflect a revised assessment of the pattern of consumption of benefits of the asset; and
 - (b) the re-estimate of useful life of an item of property, plant and equipment.
- G88 An entity shall recognise the effect of a change in an accounting estimate, other than a change to which paragraph G89 applies, prospectively by including it in profit or loss in:
 - (a) the period of the change, if the change affects that period only; or
 - (b) the period of the change and future periods, if the change affects both.

- G89 To the extent that a change in an accounting estimate gives rise to changes in assets and liabilities, or relates to an item of equity, the entity shall recognise it by adjusting the carrying amount of the related asset, liability or equity item in the period of the change.

Corrections of prior period errors

- G90 Prior period errors are omissions from, and misstatements in, the entity's financial statements for one or more prior periods arising from a failure to use, or misuse of, reliable information that:
- (a) was available when financial statements for those periods were authorised for issue; and
 - (b) could reasonably be expected to have been obtained and taken into account in the preparation and presentation of those financial statements.
- G91 Such errors include the effects of mathematical mistakes, mistakes in applying accounting policies, oversights or misinterpretations of facts, and fraud.
- G92 To the extent practicable, an entity shall correct a material prior period error retrospectively (ie restating the financial statements as if that error had never occurred) in the first financial statements authorised for issue after its discovery by:
- (a) restating the comparative amounts for the prior period(s) presented in which the error occurred; or
 - (b) if the error occurred before the earliest prior period presented, restating the opening balances of assets, liabilities and equity for the earliest prior period presented.
- G93 When it is impracticable to determine the period-specific effects of an error on comparative information for one or more prior periods presented (ie, the entity cannot determine it after making every reasonable effort to do so), the entity shall restate the opening balances of assets, liabilities and equity for the earliest period for which retrospective restatement is practicable (which may be the current period).

Disclosures

Disclosure of a change in accounting policy

- G94 When a change in accounting policy has an effect on the current period or any prior period, an entity shall disclose the following:
- (a) the nature of the change in accounting policy;
 - (b) the reasons why applying the new accounting policy provides reliable and more relevant information;
 - (c) to the extent practicable, the amount of the adjustment for each financial statement line item affected, shown separately:
 - (i) for the current period;

- (ii) for each prior period presented; and
- (iii) in the aggregate for periods before those presented; and
- (d) an explanation if it is impracticable to determine the amounts to be disclosed in (c) above.

Financial statements of subsequent periods need not repeat these disclosures.

Disclosure of a change in estimate

- G95 An entity shall disclose the nature of any change in an accounting estimate and the effect of the change on assets, liabilities, income and expense for the current period. If it is practicable for the entity to estimate the effect of the change in one or more future periods, the entity shall disclose those estimates.

Disclosure of prior period errors

- G96 An entity shall disclose the following about prior period errors:
- (a) the nature of the prior period error;
 - (b) for each prior period presented, to the extent practicable, the amount of the correction for each financial statement line item affected;
 - (c) to the extent practicable, the amount of the correction at the beginning of the earliest prior period presented; and
 - (d) an explanation if it is not practicable to determine the amounts to be disclosed in (b) or (c) above.

Financial statements of subsequent periods need not repeat these disclosures.

Guide Section 11–12 Financial Instruments

Situations not addressed by this Guide	
An entity shall refer to the <i>IFRS for SMEs</i> :	
(a)	if the entity has any financial instruments other than those listed in paragraphs G98–G100 below, for example, investments in ordinary shares that do not have a quoted price in an active market; investments in preference shares; derivatives (such as option, forward and swap contracts); convertible instruments; instruments containing put or call options; and commitments to make or receive a loan (see <i>IFRS for SMEs</i> Sections 11 and 12).
(b)	if the entity transfers receivables to another party (for example, a bank), but retains some risks and rewards of ownership, for example, enters into a recourse factoring transaction with a bank (see <i>IFRS for SMEs</i> paragraphs 11.33(c), 11.34 and 11.45).

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Situations not addressed by this Guide	
(c)	if the entity provides a financial instrument as collateral to another party (for example, providing a receivable as security for a loan), or the entity receives a financial instrument as collateral from another party (see <i>IFRS for SMEs</i> paragraphs 11.35 and 11.45–11.46).
(d)	<u>omitted option</u> : instead of applying the recognition and measurement requirements for financial instruments in Guide Section 11–12, management may apply the recognition and measurement provisions of IAS 39 <i>Financial Instruments: Recognition and Measurement</i> (see <i>IFRS for SMEs</i> paragraph 11.2).
(e)	<u>omitted option</u> : hedge accounting has been omitted as financial instruments used for hedging purposes are outside the scope of this Guide (see <i>IFRS for SMEs</i> Section 12).

Scope of Guide Section 11–12

- G97 A financial instrument is a contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity.
- G98 An entity shall account for the following financial instruments, unless they are excluded by paragraph G100, in accordance with Guide Section 11–12:
- (a) cash;
 - (b) the following receivables and payables provided they meet the requirements in paragraph G99:
 - (i) bank deposits;
 - (ii) trade receivables and payables;
 - (iii) loans receivable and payable;
 - (iv) notes receivable and payable; and
 - (c) investments in non-puttable ordinary shares that have a quoted price in an active market. Non-puttable shares in an entity are shares that cannot be sold back to the entity at the option of the holder.
- All other financial instruments are outside the scope of Guide Section 11–12.
- G99 A financial instrument that is a debt instrument, receivable or payable, shall be accounted for in accordance with Guide Section 11–12 if it satisfies all of the conditions in (a)–(d) below:
- (a) Returns to the holder are
 - (i) a fixed amount;
 - (ii) a fixed rate of return over the life of the instrument;

- (iii) a variable return that, throughout the life of the instrument, is equal to a single referenced quoted or observable interest rate (such as LIBOR); or
 - (iv) some combination of such fixed rate and variable rates (such as LIBOR plus 200 basis points), provided that both the fixed and variable rates are positive.
- (b) There is no contractual provision that could, by its terms, result in the holder losing the principal amount or any interest attributable to the current period or prior periods. The fact that a debt instrument is subordinated to other debt instruments is not an example of such a contractual provision.
- (c) Contractual provisions that permit the debtor to prepay a debt instrument or permit the creditor to require the debtor to repay the debt before maturity are not contingent on future events.
- (d) There are no conditional returns or repayment provisions except for the variable rate return described in (a) and prepayment provisions described in (b).
- G100 The following financial instruments are not accounted for in accordance with this section and are covered by other sections of this Guide:
- (a) financial instruments that meet the definition of an entity's own equity covered by Guide Section 22 *Equity*;
 - (b) leases covered by Guide Section 20 *Leases*. However, the derecognition requirements in paragraphs G117–G119 apply to lease payables recognised by a lessee; and
 - (c) employers' rights and obligations under employee benefit plans covered by Guide Section 28 *Employee Benefits*.

Initial recognition of financial assets and liabilities

- G101 An entity shall recognise a financial asset or a financial liability only when the entity becomes a party to the contractual provisions of the instrument.

Initial measurement

- G102 When a financial asset or financial liability is recognised initially, an entity shall measure it at the transaction price (including transaction costs) unless the arrangement constitutes, in effect, a financing transaction. A financing transaction may take place in connection with the sale of goods or services, for example, if payment is deferred beyond normal business terms or is financed at a rate of interest that is not a market rate. If the arrangement constitutes a financing transaction, the entity shall measure the financial asset or financial liability at the present value of the future payments discounted at a market rate of interest for a similar debt instrument.

Example—financial assets	
1	For a long-term loan made to another entity, a receivable is recognised at the present value of cash receivable (including interest payments and repayment of principal) from that entity.
2	For goods sold to a customer on short-term credit, a receivable is recognised at the undiscounted amount of cash receivable from that entity, which is normally the invoice price.
3	For an item sold to a customer on two-year interest-free credit, a receivable is recognised at the current cash sale price for that item. If the current cash sale price is not known, it may be estimated as the present value of the cash receivable discounted using the prevailing market rate(s) of interest for a similar receivable.
4	For a cash purchase of another entity's ordinary shares, the investment is recognised at the amount of cash paid to acquire the shares.

Example—financial liabilities	
1	For a loan received from a bank, a payable is recognised initially at the present value of cash payable to the bank (for example, including interest payments and repayment of principal).
2	For goods purchased from a supplier on short-term credit, a payable is recognised at the undiscounted amount owed to the supplier, which is normally the invoice price.

Subsequent measurement

- G103 At the end of each reporting period, an entity shall measure financial instruments as follows, without any deduction for transaction costs the entity may incur on sale or other disposal:
- (a) Debt instruments that meet the conditions in paragraph G99 shall be measured at amortised cost using the effective interest method (see paragraphs G104–G109). Cash and debt instruments that are classified as current assets or current liabilities shall be measured at the undiscounted amount of the cash or other consideration expected to be paid or received (ie, net of impairment) unless the arrangement constitutes, in effect, a financing transaction (see paragraph G102). If the arrangement constitutes a financing transaction, the entity shall measure the debt instrument at the present value of the future payments discounted at a market rate of interest for a similar debt instrument. Paragraphs G110–G115 provide guidance on impairment or uncollectibility.

- (b) Investments in shares shall be measured at fair value with changes in fair value recognised in profit or loss. For shares traded in an active market the best evidence of fair value is the quoted price for those shares in that active market.

Amortised cost and effective interest method

G104 The amortised cost of a financial asset or financial liability at each reporting date is the net of the following amounts:

- (a) the amount at which the financial asset or financial liability is measured at initial recognition;
- (b) minus any repayments of the principal;
- (c) plus or minus the cumulative amortisation using the effective interest method of any difference between the amount at initial recognition and the maturity amount; and
- (d) minus, in the case of a financial asset, any reduction (directly or through the use of an allowance account) for impairment or uncollectibility.

Financial assets and financial liabilities that have no stated interest rate and are classified as current assets or current liabilities are initially measured at an undiscounted amount in accordance with paragraph G103(a). Therefore, (c) above does not apply to them.

G105 The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability (or a group of financial assets or financial liabilities) and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period, to the carrying amount of the financial asset or financial liability. The effective interest rate is determined on the basis of the carrying amount of the financial asset or liability at initial recognition. Under the effective interest method:

- (a) the amortised cost of a financial asset (liability) is the present value of future cash receipts (payments) discounted at the effective interest rate; and
- (b) the interest expense (income) in a period equals the carrying amount of the financial liability (asset) at the beginning of a period multiplied by the effective interest rate for the period.

Appendix to Guide Section 11–12 provides an example of using the Internal Rate of Return function in Microsoft Excel to determine the effective interest rate of a loan.

G106 When calculating the effective interest rate, an entity shall estimate cash flows considering all contractual terms of the financial instrument (for example, prepayment and other options) and known credit losses that have been incurred, but it shall not consider possible future credit losses not yet incurred.

G107 When calculating the effective interest rate, an entity shall amortise any related fees, finance charges paid or received, and transaction costs over the expected

life of the instrument, except as follows. The entity shall use a shorter period if that is the period to which the fees, finance charges paid or received, or transaction costs relate. This will be the case when the variable to which the fees, finance charges paid or received, and transaction costs is repriced to market rates before the expected maturity of the instrument. In such a case, the appropriate amortisation period is the period to the next such repricing date.

- G108 For variable rate financial assets and variable rate financial liabilities, periodic re-estimation of cash flows to reflect changes in market rates of interest alters the effective interest rate. If a variable rate financial asset or variable rate financial liability is recognised initially at an amount equal to the principal receivable or payable at maturity, re-estimating the future interest payments normally has no significant effect on the carrying amount of the asset or liability.
- G109 If an entity revises its estimates of payments or receipts, the entity shall adjust the carrying amount of the financial asset or financial liability (or group of financial instruments) to reflect actual and revised estimated cash flows. The entity shall recalculate the carrying amount by computing the present value of estimated future cash flows at the financial instrument's original effective interest rate. The entity shall recognise the adjustment as income or expense in profit or loss at the date of the revision.

Example—determining amortised cost for a five-year loan using the effective interest method				
On 1 January 20X1, an entity obtains a five-year CU1,000 loan from a bank, paying bank administration fees of CU50, so that the net cash received is CU950. The entity is required to pay cash interest of 4 per cent annually in arrears (= 4% × CU1,000 = CU40). The entity is required to repay the loan of CU1,000 to the bank on 31 December 20X5.				
Year	Carrying amount at beginning of period	Interest payable at 5.15999%^(a)	Cash outflow	Carrying amount at end of period
	CU	CU	CU	CU
20X1	950.00	49.02	(40)	959.02
20X2	959.02	49.49	(40)	968.51
20X3	968.51	49.97	(40)	978.48
20X4	978.48	50.49	(40)	988.97
20X5	988.97	51.03	(1,040)	—

Appendix to Guide Section 11–12 shows how to determine the effective interest rate using Microsoft Excel.

(a) The effective interest rate of 5.15999 per cent is the rate that discounts the expected cash flows on the loan to the initial carrying amount:
 $40/(1.0515999)^1 + 40/(1.0515999)^2 + 40/(1.0515999)^3 + 40/(1.0515999)^4 + 1,040/(1.0515999)^5 = 950$

Impairment of financial assets measured at cost or amortised cost

Recognition

- G110 At the end of each reporting period, an entity shall assess whether there is objective evidence of impairment of any financial assets that are measured at cost or amortised cost. If there is objective evidence of impairment, the entity shall recognise an impairment loss in profit or loss immediately.
- G111 Objective evidence that a financial asset or group of assets is impaired includes observable data that come to the attention of the entity about the following loss events:
- (a) a breach of contract by the debtor, such as a default or delinquency in interest or principal payments;
 - (b) the entity, for economic or legal reasons relating to the debtor's financial difficulty, granting to the debtor a concession that the entity would not otherwise consider; or
 - (c) significant financial difficulty of the debtor or it has become probable that the debtor will enter bankruptcy or other financial reorganisation.
- G112 Other factors may also be evidence of impairment, including significant changes with an adverse effect that have taken place in the technological, market, economic or legal environment in which the debtor operates.
- G113 An entity shall assess financial assets that are individually significant for impairment separately. An entity shall assess other financial assets for impairment either individually or grouped on the basis of similar credit risk characteristics.

Measurement

- G114 An entity shall measure an impairment loss on financial assets measured at cost or amortised cost as the difference between the asset's carrying amount and the present value of estimated cash flows discounted at the asset's original effective interest rate. If such a financial asset has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract.

Reversal

- G115 If, in a subsequent period, the amount of an impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the entity shall reverse the previously recognised impairment loss either directly or by adjusting an allowance account. The reversal shall not result in a carrying amount of the financial asset (net of any allowance account) that exceeds what the carrying amount would have been had the impairment not previously been recognised. The entity shall recognise the amount of the reversal in profit or loss immediately.

Derecognition of a financial asset

- G116 An entity shall derecognise a financial asset when:
- (a) the contractual rights to the cash flows from the financial asset expire or are settled; or
 - (b) the entity transfers to another party substantially all of the risks and rewards of ownership of the financial asset.

Derecognition of a financial liability

- G117 An entity shall derecognise a financial liability (or a part of a financial liability) only when it is extinguished—ie, when the obligation specified in the contract is discharged, is cancelled or expires.
- G118 If an existing borrower and lender exchange financial instruments with substantially different terms, the entities shall account for the transaction as an extinguishment of the original financial liability and the recognition of a new financial liability. Similarly, an entity shall account for a substantial modification of the terms of an existing financial liability or a part of it (whether or not attributable to the financial difficulty of the debtor) as an extinguishment of the original financial liability and the recognition of a new financial liability.
- G119 The entity shall recognise in profit or loss any difference between the carrying amount of the financial liability (or part of a financial liability) extinguished or transferred to another party and the consideration paid, including any non-cash assets transferred or liabilities assumed.

Disclosures

Disclosure of accounting policies for financial instruments

- G120 In accordance with paragraph G76, an entity shall disclose, in the summary of significant accounting policies, the measurement basis (or bases) used for financial instruments and the other accounting policies used for financial instruments that are relevant to an understanding of the financial statements.

Statement of financial position—categories of financial assets and financial liabilities

- G121 An entity shall disclose the carrying amounts of each of the following categories of financial assets and financial liabilities at the reporting date, in total, either in the statement of financial position or in the notes:
- (a) financial assets measured at cost/amortised cost;
 - (b) financial liabilities measured at cost/amortised cost; and
 - (c) investments in shares.
- G122 An entity shall disclose information that enables users of its financial statements to evaluate the significance of financial instruments for its financial position and performance. For example, for long-term debt such information would

normally include the terms and conditions of the debt instrument (such as interest rate, maturity, repayment schedule, and restrictions that the debt instrument imposes on the entity).

- G123 For investments in shares, the entity shall disclose the basis for determining fair value. For investments in shares in paragraph G98(c) that basis will be the quoted market price in an active market.

Defaults and breaches on loans payable

- G124 For loans payable recognised at the reporting date for which there is a breach of terms or default of principal, interest, sinking fund, or redemption terms that has not been remedied by the reporting date, an entity shall disclose the following:

- (a) details of that breach or default;
- (b) the carrying amount of the related loans payable at the reporting date; and
- (c) whether the breach or default was remedied, or the terms of the loans payable were renegotiated, before the financial statements were authorised for issue.

Items of income, expense, gains or losses

- G125 An entity shall disclose the following items of income, expense, gains or losses:

- (a) income, expense, gains or losses, including changes in fair value, recognised on:
 - (i) investments in shares;
 - (ii) financial assets measured at cost/amortised cost; and
 - (iii) financial liabilities measured at cost/amortised cost;
- (b) total interest income and total interest expense (calculated using the effective interest method) for financial assets or financial liabilities measured at cost/amortised cost; and
- (c) the amount of any impairment loss for each class of financial asset.

Appendix to Guide Section 11–12 Guidance on determining the effective interest rate using Microsoft Excel

Example—using the ‘Internal Rate of Return’ function in Microsoft Excel to calculate the effective interest rate of a loan.

The effective interest rate (see paragraph G105) can be determined using the ‘Internal Rate of Return’ function in an Excel spreadsheet. This is illustrated below using the example of a five-year bank loan. Additional help can be found using the help function in Excel.

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Example—using the ‘Internal Rate of Return’ function in Microsoft Excel to calculate the effective interest rate of a loan.

On 1 January 20X1, an entity obtains a five-year CU1,000 loan from a bank, paying bank administration fees of CU50, so that the net cash received is CU950. The entity is required to pay cash interest of 4 per cent annually in arrears (= 4% × CU1,000 = CU40). The entity is required to repay the loan of CU1,000 to the bank on 31 December 20X5.

The carrying amount of the liability on initial recognition (1 January 20X1) is CU950 (= cash loaned of CU1,000 less bank administration fees paid of CU50). The bank administration fees are not accounted for as an upfront expense but, rather, as an adjustment of interest expense over the life of the loan. The total interest must be recognised by the effective interest method as described in Guide Section 11–12.

The entity could prepare a schedule similar to the following:

Year	Carrying amount at beginning of year	Interest expense paid at ??%	Cash outflow	Carrying amount at end of year
	CU	CU	CU	CU
20X1	950.00		(40)	
20X2			(40)	
20X3			(40)	
20X4			(40)	
20X5			(1,040)	—

In order to fill in the missing gaps it is necessary to calculate the effective interest rate. The effective interest rate paid by the entity is 5.16%. That is the interest rate that exactly discounts the cash outflows of CU40 per year for five years plus CU1,000 at the end of the fifth year to the initial carrying amount of CU950.00.

How is the effective interest rate calculated? One way to do it is with an Excel spreadsheet using Excel’s built-in ‘Internal Rate of Return’ function. For this simple example, the spreadsheet would need only two columns and seven rows, with data input as follows:

	Column A—Dates	Column B—Cash Inflows (Outflows)
		CU
Row 1	1 January 20X1	950
Row 2	31 December 20X1	(40)
Row 3	31 December 20X2	(40)
Row 4	31 December 20X3	(40)
Row 5	31 December 20X4	(40)
Row 6	31 December 20X5	(1,040)
Row 7		=IRR(B1:B6)

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Example—using the ‘Internal Rate of Return’ function in Microsoft Excel to calculate the effective interest rate of a loan.

Cell B7 is used to calculate the effective interest rate. The calculation is accomplished by typing the following formula into cell B7: =IRR(B1:B6)

The equal sign in cell B7 tells Excel to calculate an amount based on a formula. The IRR in cell B7 is a built-in function in Excel to calculate the internal rate of return from a series of cash flows. The cash flows are set out in cells B1–B6, with cash outflows as negative numbers and cash inflows as positive numbers. The (B1:B6) in cell B7 tells Excel to look in cells B1 through to, and including, B6 to find the cash flow data. (Alternatively, you could have typed (B1, B2, B3, B4, B5, B6 to tell Excel which cells have the cash flows.) When you type =IRR(B1:B6) in cell B7, what Excel will show in cell B7 is 5, 5.2, 5.16, 5.160, 5.15999, etc. depending how many decimal places are showing. The number of decimal places shown will depend on how you have formatted cell B7. To change formatting, right-click on the cell and then click on Format Cells.

The schedule can now be completed:

Year	Carrying amount at beginning of year	Interest expense paid at 5.16%	Cash outflow	Carrying amount at end of year
	CU	CU	CU	CU
20X1	950.00	49.02	(40)	959.02
20X2	959.02	49.49	(40)	968.51
20X3	968.51	49.97	(40)	978.48
20X4	978.48	50.49	(40)	988.97
20X5	988.97	51.03	(1,040)	—

This is the journal entry the entity would make on 1 January 20X1 when it enters into the loan:

	Debit	Credit
	CU	CU
Cash	950.00	
Loan payable		950.00

And this is the journal entry the entity would make at 31 December 20X1:

	Debit	Credit
	CU	CU
Interest expense	49.02	
Cash		40.00
Loan payable		9.02

Guide Section 13 *Inventories*

Situations not addressed by this Guide
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An entity shall refer to the <i>IFRS for SMEs</i> if the entity holds inventories of commodities as a commodity broker/dealer (see <i>IFRS for SMEs</i> paragraph 13.3(b)).

Scope of Guide Section 13

- G126 Inventories are assets:
- (a) held for sale in the ordinary course of business;
 - (b) in the process of production for such sale; or
 - (c) in the form of materials or supplies to be consumed in the production process or in the rendering of services.
- G127 Guide Section 13 does not apply to:
- (a) work in progress arising under construction contracts, including directly related service contracts (see Guide Section 23 *Revenue*); and
 - (b) financial instruments (see Guide Section 11–12 *Financial Instruments*).

Measurement of inventories

- G128 An entity shall measure inventories at the lower of cost and estimated selling price less costs to complete and sell. Guide Section 27 *Impairment of Assets* covers impairment requirements for inventories.

Cost of inventories

- G129 An entity shall include in the cost of inventories all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

Costs of purchase

- G130 The costs of purchase of inventories comprise the purchase price, import duties and other taxes (other than those subsequently recoverable by the entity from the taxing authorities), and transport, handling and other costs directly attributable to the acquisition of finished goods, materials and services. Trade discounts, rebates and other similar items are deducted in determining the costs of purchase.

- G131 An entity may purchase inventories on deferred settlement terms. In some cases, the arrangement effectively contains an unstated financing element, for example, a difference between the purchase price for normal credit terms and the deferred settlement amount. In these cases, the difference is recognised as interest expense over the period of the financing and is not added to the cost of the inventories.

Costs of conversion

- G132 The costs of conversion of inventories include costs directly related to the units of production, such as direct labour. They also include a systematic allocation of fixed and variable production overheads that are incurred in converting materials into finished goods. Fixed production overheads are those indirect costs of production that remain relatively constant regardless of the volume of production, such as depreciation and maintenance of factory buildings and equipment, and the cost of factory management and administration. Variable production overheads are those indirect costs of production that vary directly, or nearly directly, with the volume of production, such as indirect materials and indirect labour.

Allocation of production overheads

- G133 An entity shall allocate fixed production overheads to the costs of conversion on the basis of the normal capacity of the production facilities. Normal capacity is the production expected to be achieved on average over a number of periods or seasons under normal circumstances, taking into account the loss of capacity resulting from planned maintenance. The actual level of production may be used if it approximates normal capacity. The amount of fixed overhead allocated to each unit of production is not increased as a consequence of low production or idle plant. Unallocated overheads are recognised as an expense in the period in which they are incurred. In periods of abnormally high production, the amount of fixed overhead allocated to each unit of production is decreased so that inventories are not measured above cost. Variable production overheads are allocated to each unit of production on the basis of the actual use of the production facilities.

Joint products and by-products

- G134 A production process may result in more than one product being produced simultaneously. This is the case, for example, when joint products are produced or when there is a main product and a by-product. When the costs of raw materials or conversion of each product are not separately identifiable, an entity shall allocate them between the products on a rational and consistent basis. The allocation may be based, for example, on the relative sales value of each product either at the stage in the production process when the products become separately identifiable, or at the completion of production. Most by-products, by their nature, are immaterial. When this is the case, the entity shall measure them at selling price less costs to complete and sell and deduct this amount

from the cost of the main product. As a result, the carrying amount of the main product is not materially different from its cost.

Other costs included in inventories

G135 An entity shall include other costs in the cost of inventories only to the extent that they are incurred in bringing the inventories to their present location and condition.

Costs excluded from inventories

G136 Examples of costs excluded from the cost of inventories and recognised as expenses in the period in which they are incurred are:

- (a) abnormal amounts of wasted materials, labour or other production costs;
- (b) storage costs, unless those costs are necessary during the production process before a further production stage;
- (c) administrative overheads that do not contribute to bringing inventories to their present location and condition; and
- (d) selling costs.

Cost of inventories of a service provider

G137 To the extent that service providers have inventories, they measure them at the costs of their production. These costs consist primarily of the labour and other costs of personnel directly engaged in providing the service, including supervisory personnel, and attributable overheads. Labour and other costs relating to sales and general administrative personnel are not included but are recognised as expenses in the period in which they are incurred. The cost of inventories of a service provider does not include profit margins or non-attributable overheads that are often factored into prices charged by service providers.

Techniques for measuring cost, such as standard costing, retail method and most recent purchase price

G138 An entity may use techniques such as the standard cost method, the retail method or most recent purchase price for measuring the cost of inventories if the result approximates cost. Standard costs take into account normal levels of materials and supplies, labour, efficiency and capacity utilisation. They are regularly reviewed and, if necessary, revised in the light of current conditions. The retail method measures cost by reducing the sales value of the inventory by the appropriate percentage gross margin.

Cost formulas

- G139 An entity shall measure the cost of inventories of items that are not ordinarily interchangeable and goods or services produced and segregated for specific projects by using specific identification of their individual costs.
- G140 An entity shall measure the cost of inventories, other than those dealt with in paragraph G139, by using the first-in, first-out (FIFO) or weighted average cost formula. An entity shall use the same cost formula for all inventories having a similar nature and use to the entity. For inventories with a different nature or use, different cost formulas may be justified. The last-in, first-out method (LIFO) is not permitted.

Recognition as an expense

- G141 When inventories are sold, the entity shall recognise the carrying amount of those inventories as an expense (often referred to as cost of goods sold) in the period in which the related revenue is recognised.
- G142 Some inventories may be allocated to other asset accounts, for example, inventory used as a component of self-constructed property, plant or equipment. Inventories allocated to another asset in this way are accounted for subsequently in accordance with the section of this Guide relevant to that type of asset.

Disclosures

- G143 An entity shall disclose the following:
- (a) the accounting policies adopted in measuring inventories, including the cost formula used;
 - (b) the total carrying amount of inventories and the carrying amount in classifications appropriate to the entity;
 - (c) the amount of inventories recognised as an expense during the period;
 - (d) impairment losses recognised or reversed in profit or loss in accordance with Guide Section 27 *Impairment of Assets*; and
 - (e) the total carrying amount of inventories pledged as security for liabilities.

Guide Section 14–15 *Investments in Associates and Joint Ventures*

Situations not addressed by this Guide

An entity shall refer to the *IFRS for SMEs* if the entity has any investments in associates or joint ventures, ie it either has significant influence or joint control over another entity, including an unincorporated entity such as a partnership, and/or the entity is party to a contractual arrangement whereby two or more parties undertake an economic activity that is subject to joint control (see *IFRS for SMEs* Section 14, Section 15 and paragraphs 9.24–9.27, 22.2(a), 23.2(b), 27.33, 29.1, 33.4(b) and 33.10(b)).

Guide Section 16 *Investment Property*

Situations not addressed by this Guide

An entity shall refer to the *IFRS for SMEs* if the entity holds (either as owner or lessee) any investment property, ie property (land or a building, or part of a building, or both) to earn rentals or for capital appreciation or both (see *IFRS for SMEs* Section 16 and paragraphs 17.1, 17.31(e), 20.1(c), 23.2(d), 27.1(d) and 27.33(b)).

Note: Investment property is not property held for the entity's own use (this would be property, plant and equipment under Guide Section 17) or for sale in the ordinary course of business (this would be inventory under Guide Section 13).

Guide Section 17 *Property, Plant and Equipment (PPE)*

Situations not addressed by this Guide

An entity shall refer to the *IFRS for SMEs*:

- (a) if the entity has an item of PPE comprising one or more major components with a significantly different useful life or pattern of consumption of economic benefits than the rest of the item, for example, if a building includes elevators that have significantly shorter lives than the building structure (see *IFRS for SMEs* paragraphs 17.6 and 17.16).
- (b) if the entity is required to perform regular major inspections for faults on an item of PPE as a condition of operating the asset, for example, if an entity runs a public bus service it may have to perform checks on its fleet when they have completed a certain mileage (see *IFRS for SMEs* paragraph 17.7).
- (c) if the entity has an obligation to dismantle and remove an item of PPE or restore the site on which it is located, for example, rectifying environmental damage (see *IFRS for SMEs* paragraph 17.10(c)).
- (d) if the entity acquires an item of PPE in exchange for non-monetary assets, for example, acquires a machine in exchange for inventories (see *IFRS for SMEs* paragraph 17.14).

Scope of Guide Section 17

- G144 Property, plant and equipment accounted for under Guide Section 17 are tangible assets that:
- (a) are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes; and
 - (b) are expected to be used during more than one period.

Recognition

- G145 Items such as spare parts, stand-by equipment and servicing equipment are property, plant and equipment if the entity expects to use them during more than one period or if they can be used only in connection with an item of property, plant and equipment. Otherwise, such items are classified as inventories.
- G146 Land and buildings are separable assets, and an entity shall account for them separately, even when they are acquired together.

Measurement at recognition

- G147 An entity shall measure an item of property, plant and equipment at initial recognition at its cost.

Elements of cost

- G148 The cost of an item of property, plant and equipment comprises all of the following:
- (a) its purchase price, including legal and brokerage fees, import duties and non-refundable purchase taxes, after deducting trade discounts and rebates; and
 - (b) any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management. These can include the costs of site preparation, initial delivery and handling, installation and assembly, and testing of functionality.

If payment is deferred beyond normal credit terms, the cost is the present value of all future payments.

- G149 The following costs are not costs of an item of property, plant and equipment, and an entity shall recognise them as an expense when they are incurred:
- (a) costs of opening a new facility;
 - (b) costs of introducing a new product or service (including costs of advertising and promotional activities);
 - (c) costs of conducting business in a new location or with a new class of customer (including costs of staff training);
 - (d) administration and other general overhead costs; and

(e) borrowing costs.

G150 The income and related expenses of incidental operations during construction or development of an item of property, plant and equipment are recognised in profit or loss if those operations are not necessary to bring the item to its intended location and operating condition.

Measurement after initial recognition

G151 An entity shall measure all items of property, plant and equipment after initial recognition at cost less any accumulated depreciation and any accumulated impairment losses. An entity shall recognise the costs of day-to-day servicing of an item of property, plant and equipment in profit or loss in the period in which the costs are incurred. Guide Section 27 *Impairment of Assets* covers impairment requirements for property, plant and equipment.

Depreciable amount and depreciation period

G152 An entity shall allocate the depreciable amount of an asset on a systematic basis over its useful life. Paragraphs G157–G158 provide guidance for selecting a depreciation method. The depreciable amount is cost minus accumulated depreciation and accumulated impairment losses, and minus residual value. The residual value of an asset is the estimated amount that an entity would currently obtain from disposal of an asset, after deducting the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life.

G153 The depreciation charge for each period shall be recognised in profit or loss unless another section of this Guide requires the cost to be recognised as part of the cost of an asset. For example, the depreciation of manufacturing property, plant and equipment is included in the costs of inventories (see Guide Section 13 *Inventories*).

G154 Factors such as a change in how an asset is used, significant unexpected wear and tear, technological advancement, and changes in market prices may indicate that the residual value or useful life of an asset has changed since the most recent annual reporting date. If such indicators are present, an entity shall review its previous estimates and, if current expectations differ, amend the residual value, depreciation method or useful life. The entity shall account for the change in residual value, depreciation method or useful life as a change in an accounting estimate in accordance with paragraphs G86–G89 and G95.

G155 Depreciation of an asset begins when it is available for use, ie, when it is in the location and condition necessary for it to be capable of operating in the manner intended by management. Depreciation of an asset ceases when the asset is derecognised. Depreciation does not cease when the asset becomes idle or is retired from active use unless the asset is fully depreciated. However, under usage methods of depreciation the depreciation charge can be zero while there is no production.

- G156 The useful life of an asset is the period over which the asset is expected to be available for use by the entity or the number of production or similar units expected to be obtained from the asset by the entity. An entity shall consider all of the following factors in determining the useful life of an asset:
- (a) the expected usage of the asset. Usage is assessed by reference to the asset's expected capacity or physical output;
 - (b) expected physical wear and tear, which depends on operational factors such as the number of shifts for which the asset is to be used and the repair and maintenance programme, and the care and maintenance of the asset while idle;
 - (c) technical or commercial obsolescence arising from changes or improvements in production, or from a change in the market demand for the product or service output of the asset; and
 - (d) legal or similar limits on the use of the asset, such as the expiry dates of related leases.

With some exceptions, such as quarries and sites used for landfill, land has an unlimited useful life and therefore is not depreciated.

Depreciation method

- G157 An entity shall select a depreciation method that reflects the pattern in which it expects to consume the asset's future economic benefits. The possible depreciation methods include the straight-line method, the diminishing balance method and a method based on usage such as the units of production method.
- G158 Usually, an asset is depreciated using the same method from period to period. However, if there is an indication that there has been a significant change since the last annual reporting date in the pattern by which an entity expects to consume an asset's future economic benefits, the entity shall review its present depreciation method and, if current expectations differ, change the depreciation method to reflect the new pattern. The entity shall account for the change as a change in an accounting estimate in accordance with paragraphs G86–G89 and G95.

Derecognition

- G159 An entity shall derecognise an item of property, plant and equipment:
- (a) on disposal; or
 - (b) when no future economic benefits are expected from its use or disposal.
- G160 An entity shall recognise the gain or loss on the derecognition of an item of property, plant and equipment in profit or loss when the item is derecognised. The entity shall not classify such gains as revenue.
- G161 For a straightforward disposal of an item of property, plant and equipment for cash, the date of disposal is usually the date when the risks and rewards of ownership of the asset have passed. For more complex scenarios, an entity

determines the date of disposal by applying the criteria in Guide Section 23 *Revenue* for recognising revenue from the sale of goods.

- G162 An entity shall determine the gain or loss arising from the derecognition of an item of property, plant and equipment as the difference between the net disposal proceeds, if any, and the carrying amount of the item.

Disclosures

- G163 An entity shall disclose the following for each class of property, plant and equipment that was deemed appropriate in accordance with paragraph G51(a):
- (a) the measurement bases used for determining the gross carrying amount;
 - (b) the depreciation methods used;
 - (c) the useful lives or the depreciation rates used;
 - (d) the gross carrying amount and the accumulated depreciation (aggregated with accumulated impairment losses) at the beginning and end of the reporting period; and
 - (e) a reconciliation of the carrying amount at the beginning and the end of the reporting period showing separately:
 - (i) additions;
 - (ii) disposals;
 - (iii) impairment losses recognised or reversed in profit or loss in accordance with Guide Section 27;
 - (iv) depreciation; and
 - (v) other changes.

This reconciliation need not be presented for prior periods.

- G164 The entity shall also disclose the following:
- (a) the existence and carrying amounts of property, plant and equipment to which the entity has restricted title or that is pledged as security for liabilities; and
 - (b) the amount of contractual commitments for the acquisition of property, plant and equipment.

Guide Section 18 *Intangible Assets Other than Goodwill*

Situations not addressed by this Guide

An entity shall refer to the *IFRS for SMEs* if the entity holds or leases intangible assets, other than those developed internally or those held for sale in the ordinary course of business (see *IFRS for SMEs* Section 18 and paragraphs 20.1(b), 27.10 and 27.33(d)).

Note: An intangible asset is an identifiable non-monetary asset without physical substance, for example, patents, copyrights, broadcasting licences, fishing licences, etc. Such an asset is identifiable when it is separable from the entity or arises from contractual or other legal rights (regardless of whether those rights are transferable or separable).

Scope of Guide Section 18

G165 If an entity has intangible assets held for sale in the ordinary course of business Guide Section 13 *Inventories* and Guide Section 23 *Revenue* apply.

Internally generated intangible items

G166 An entity shall recognise expenditure incurred internally on an intangible item, including all expenditure for both research and development activities, as an expense when it is incurred unless it forms part of the cost of another asset that meets the recognition criteria under another section of this Guide, for example, Guide Section 13 *Inventories*.

G167 As examples of applying paragraph G166, an entity shall recognise expenditure on the following items as an expense and shall not recognise such expenditure as intangible assets:

- (a) internally generated brands, customer lists and items similar in substance;
- (b) start-up activities (ie start-up costs), which include establishment costs such as legal and secretarial costs incurred in establishing a legal entity, expenditure to open a new facility or business (ie pre-opening costs) and expenditure for starting new operations or launching new products or processes (ie pre-operating costs);
- (c) training activities;
- (d) advertising and promotional activities;
- (e) internally generated software; and
- (f) internally generated goodwill.

G168 Paragraph G167 does not preclude recognising a prepayment as an asset when payment for goods or services has been made in advance of the delivery of the goods or the rendering of the services.

Disclosures

- G169 An entity shall disclose the aggregate amount of research and development expenditure recognised as an expense during the period (ie, the amount of expenditure incurred internally on research and development that has not been capitalised as part of the cost of another asset that meets the recognition criteria in this Guide).

Guide Section 19 *Business Combinations and Goodwill*

Situations not addressed by this Guide

An entity shall refer to the *IFRS for SMEs* if the entity has entered into a business combination (see *IFRS for SMEs* Section 19 and paragraphs 17.31(e), 21.12, 22.2(c) and 29.16(b)).

Note: a business combination is the bringing together of separate entities or businesses into one reporting entity, for example, where one entity obtains control of one or more other businesses. A business combination occurring many years ago may still affect the current period or a comparative period presented in the financial statements.

Guide Section 20 *Leases*

Situations not addressed by this Guide

An entity shall refer to the *IFRS for SMEs*:

- (a) if the entity is a lessor (see *IFRS for SMEs* Section 17).
- (b) if the entity sells an asset and then leases back the same asset (see *IFRS for SMEs* paragraphs 17.28–17.29 and 20.32–20.35).
- (c) if the entity is party to a lease that could result in a loss to the lessee or the lessor because of contractual terms that are unrelated to changes in the price of the leased asset, changes in foreign exchange rates or a default by one of the counterparties (such a lease shall be accounted for under *IFRS for SMEs* Section 12 and paragraph 11.7(c)).

Scope of Guide Section 20

- G170 A lease is an agreement whereby the lessor conveys to the lessee in return for a payment or series of payments the right to use an asset for an agreed period of time. Guide Section 20 does not cover operating leases that are onerous (see Guide Section 21 *Provisions and Contingencies*).
- G171 Guide Section 20 applies to agreements that transfer the right to use assets even though substantial services by the lessor may be called for in connection with the operation or maintenance of such assets. Guide Section 20 does not apply to

agreements that are contracts for services that do not transfer the right to use assets from one contracting party to the other.

- G172 Some arrangements do not take the legal form of a lease but convey rights to use assets in return for payments. Such arrangements are in substance leases of assets, and they should be accounted for under Guide Section 20.

Classification of leases

- G173 A lease is classified as a finance lease if it transfers substantially all the risks and rewards incidental to ownership. A lease is classified as an operating lease if it does not transfer substantially all the risks and rewards incidental to ownership.

- G174 Whether a lease is a finance lease or an operating lease depends on the substance of the transaction rather than the form of the contract. Examples of situations that individually or in combination would normally lead to a lease being classified as a finance lease are:

- (a) the lease transfers ownership of the asset to the lessee by the end of the lease term.
- (b) the lessee has the option to purchase the asset at a price that is expected to be sufficiently lower than the fair value at the date the option becomes exercisable for it to be reasonably certain, at the inception of the lease, that the option will be exercised.
- (c) the lease term is for the major part of the economic life of the asset even if title is not transferred.
- (d) at the inception of the lease the present value of the minimum lease payments amounts to at least substantially all of the fair value of the leased asset.
- (e) the leased assets are of such a specialised nature that only the lessee can use them without major modifications.

- G175 Indicators of situations that individually or in combination could also lead to a lease being classified as a finance lease are:

- (a) if the lessee can cancel the lease but the lessee must compensate the lessor for losses associated with the cancellation;
- (b) gains or losses from the fluctuation in the residual value of the leased asset accrue to the lessee (for example, in the form of a payment at the end of the lease); and
- (c) the lessee has the ability to continue the lease for a renewal period at a rent that is substantially lower than market rent.

- G176 The examples and indicators in paragraphs G174–G175 are not always conclusive. If it is clear from other features that the lease does not transfer substantially all risks and rewards incidental to ownership, the lease is classified as an operating lease.

- G177 Lease classification is made at the inception of the lease and is not changed during the term of the lease unless the lessee and the lessor agree to change the

provisions of the lease (other than simply by renewing the lease), in which case the lease classification shall be re-evaluated.

Financial statements of lessees—finance leases

Initial recognition

- G178 At the commencement of the lease term, a lessee shall recognise its rights of use and obligations under finance leases as assets and liabilities in its statement of financial position at amounts equal to the fair value of the leased property (normally the retail selling price of the asset) or, if lower, the present value of the minimum lease payments, determined at the inception of the lease. Any initial direct costs of the lessee (incremental costs that are directly attributable to negotiating and arranging a lease) are added to the amount recognised as an asset.
- G179 The present value of the minimum lease payments should be calculated using the interest rate implicit in the lease, ie the discount rate that, at the inception of the lease, causes the aggregate present value of (a) the minimum lease payments and (b) the unguaranteed residual value to be equal to the sum of (i) the fair value of the leased asset and (ii) any initial direct costs of the lessor.
- G180 If this cannot be determined, the lessee's incremental borrowing rate shall be used. This is the rate of interest the lessee would have to pay on a similar lease or, if that is not determinable, the rate that, at the inception of the lease, the lessee would incur to borrow over a similar term, and with a similar security, the funds necessary to purchase the asset.

Subsequent measurement

- G181 A lessee shall apportion minimum lease payments between the finance charge and the reduction of the outstanding liability using the effective interest method (see paragraphs G104–G109). The lessee shall allocate the finance charge to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability. A lessee shall charge contingent rents as expenses in the periods in which they are incurred.
- G182 A lessee shall depreciate an asset leased under a finance lease in accordance with the relevant section of this Guide for that type of asset, for example, Guide Section 17 *Property, Plant and Equipment*. If there is no reasonable certainty that the lessee will obtain ownership by the end of the lease term, the asset shall be fully depreciated over the shorter of the lease term and its useful life. A lessee shall also assess at each reporting date whether an asset leased under a finance lease is impaired (see Guide Section 27 *Impairment of Assets*).

Financial statements of lessees—operating leases

Recognition and measurement

- G183 A lessee shall recognise lease payments under operating leases (excluding costs for services such as insurance and maintenance) as an expense on a straight-line basis unless either:

- (a) another systematic basis is representative of the time pattern of the user's benefit, even if the payments are not on that basis; or
- (b) the payments to the lessor are structured to increase in line with expected general inflation (based on published indexes or statistics) to compensate for the lessor's expected inflationary cost increases. If payments to the lessor vary because of factors other than general inflation, then this condition (b) is not met.

Disclosures

Disclosures for lessees—finance leases

- G184 A lessee shall make the following disclosures for finance leases:
- (a) for each class of asset, the net carrying amount at the end of the reporting period;
 - (b) the total of future minimum lease payments at the end of the reporting period, for each of the following periods:
 - (i) not later than one year;
 - (ii) later than one year and not later than five years; and
 - (iii) later than five years; and
 - (c) a general description of the lessee's significant leasing arrangements including, for example, information about contingent rent, renewal or purchase options, subleases, and restrictions imposed by lease arrangements.
- G185 In addition, the requirements for disclosure about assets in accordance with other sections of the Guide apply to lessees for assets leased under finance leases (for example, Guide Sections 17 and 27).

Disclosures for lessees—operating leases

- G186 A lessee shall make the following disclosures for operating leases:
- (a) the total of future minimum lease payments under non-cancellable operating leases for each of the following periods:
 - (i) not later than one year;
 - (ii) later than one year and not later than five years; and
 - (iii) later than five years;
 - (b) lease payments recognised as an expense; and
 - (c) a general description of the lessee's significant leasing arrangements including, for example, information about contingent rent, renewal or purchase options, subleases, and restrictions imposed by lease arrangements.

Guide Section 21 ***Provisions and Contingencies***

Scope of Guide Section 21

- G187 Guide Section 21 applies to all provisions (ie liabilities of uncertain timing or amount), contingent liabilities and contingent assets except those provisions covered by other sections of this Guide. These include provisions relating to:
- (a) leases (Guide Section 20 *Leases*). However, Guide Section 21 deals with operating leases that have become onerous. If an entity has a contract that is onerous, the entity recognises and measures the present obligation under the contract as a provision;
 - (b) construction contracts (Guide Section 23 *Revenue*);
 - (c) employee benefit obligations (Guide Section 28 *Employee Benefits*); and
 - (d) income tax (Guide Section 29 *Income Tax*).
- G188 The requirements in Guide Section 21 do not apply to executory contracts unless they are onerous contracts (ie the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it). 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.
- G189 The word 'provision' is sometimes used in the context of such items as depreciation, impairment of assets, and uncollectible receivables. Those are adjustments of the carrying amounts of assets, rather than recognition of liabilities, and therefore are not covered by Guide Section 21.

Initial recognition

- G190 An entity shall recognise a provision only when:
- (a) the entity has an obligation at the reporting date as a result of a past event;
 - (b) it is probable (ie more likely than not) that the entity will be required to transfer economic benefits in settlement; and
 - (c) the amount of the obligation can be estimated reliably.
- G191 The entity shall recognise the provision as a liability in the statement of financial position and shall recognise the amount of the provision as an expense, unless another section of this Guide requires the cost to be recognised as part of the cost of an asset such as inventories or property, plant and equipment.
- G192 The condition in paragraph G190(a) (obligation at the reporting date as a result of a past event) means that a loss event has already occurred and the entity has no realistic alternative to settling the obligation. This can happen either when the entity has a legal obligation that can be enforced by law or when a past event (for example, a history of settling similar obligations in the past) has resulted in

other parties having a valid expectation that the entity will settle the obligation. Obligations that will arise from the entity's future actions (ie the future conduct of its business) do not satisfy the condition in paragraph G190(a), no matter how likely they are to occur and even if they are contractual. To illustrate, because of commercial pressures or legal requirements, an entity 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 particular type of factory). Because the entity can avoid the future expenditure by its future actions, for example by changing its method of operation or selling the factory, it has no present obligation for that future expenditure, and no provision is recognised.

- G193 An entity shall not recognise a provision for future operating losses. Expected future losses do not meet the definition of a liability. The expectation of future operating losses may be an indicator that one or more assets are impaired.

Initial measurement

- G194 An entity shall measure a provision at the best estimate of the amount required to settle the obligation at the reporting date. The best estimate is the amount an entity would rationally pay to settle the obligation at the end of the reporting period or to transfer it to a third party at that time.
- (a) When the provision involves a large population of items, the estimate of the amount reflects the weighting of all possible outcomes by their associated probabilities. 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—measuring a provision for a large population of items

Just before its year end, an entity sells 1,000 units of a product with warranties under which the entity will repair any manufacturing defects that become apparent within the first six months after purchase. If a minor defect is detected in a product, estimated repair costs of CU100 will result. If a major defect is detected in a product, estimated repair costs of CU400 will result. The entity's experience indicates that 75 per cent of the goods sold have no defects, 20 per cent of the goods sold have minor defects and 5 per cent of the goods sold have major defects. The entity expects that the level of defects will remain the same in the next year.

The expected cost of repairs is:

$$(75\% \times 1,000 \text{ units sold} \times \text{nil}) + (20\% \times 1,000 \text{ units} \times \text{CU100}) \\ + (5\% \times 1,000 \text{ units} \times \text{CU400}) = \text{CU40,000}.$$

Consequently, a provision of CU40,000 would be appropriate at the year end for those 1,000 units. This is not a provision for an expected future loss but, rather, a provision for a loss that has already been incurred because, before the year end, the entity sold defective goods with a warranty to repair the defects.

- (b) When the provision arises from a single obligation, the individual most likely outcome may be the best estimate of the amount required to settle the obligation. However, even in such a case, the entity considers other possible outcomes. When 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 than the single most likely outcome.
- G195 When the effect of the time value of money is material, the amount of a provision shall be the present value of the amount expected to be required to settle the obligation. The discount rate (or rates) shall be a pre-tax rate (or rates) that reflect(s) current market assessments of the time value of money. The risks specific to the liability should be reflected either in the discount rate or in the estimation of the amounts required to settle the obligation, but not both.
- G196 An entity shall exclude gains from the expected disposal of assets from the measurement of a provision.
- G197 When some or all of the amount required to settle a provision may be reimbursed by another party (for example, through an insurance claim), the entity shall recognise the reimbursement as a separate asset only when it is virtually certain that the entity will receive the reimbursement on settlement of the obligation. The amount recognised for the reimbursement shall not exceed the amount of the provision. The reimbursement receivable shall be presented in the statement of financial position as an asset and shall not be offset against the provision. In the statement of income, the entity may offset any reimbursement from another party against the expense relating to the provision.

Subsequent measurement

- G198 An entity shall charge against a provision only those expenditures for which the provision was originally recognised.
- G199 An entity shall review provisions at each reporting date and adjust them to reflect the current best estimate of the amount that would be required to settle the obligation at that reporting date. Any adjustments to the amounts previously recognised shall be recognised in profit or loss unless the provision was originally recognised as part of the cost of an asset (see paragraph G191). When a provision is measured at the present value of the amount expected to be required to settle the obligation, the subsequent reduction in the present value that results from the passing of time shall be recognised as a finance cost in profit or loss in the period it arises.

Contingent liabilities

- G200 A contingent liability is either a possible but uncertain obligation or a present obligation that is not recognised because it fails to meet one or both of the conditions (b) and (c) in paragraph G190. An entity shall not recognise a contingent liability as a liability. When an entity 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.

Contingent assets

- G201 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 entity. An entity shall not recognise a contingent asset as an asset. When the flow of future economic benefits to the entity is virtually certain, then the related asset is not a contingent asset, and its recognition is appropriate.

Disclosures

Disclosures about provisions

- G202 For each class of provision, an entity shall disclose all of the following:
- (a) a reconciliation showing:
 - (i) the carrying amount at the beginning and end of the period;
 - (ii) additions during the period, including adjustments that result from changes in measuring the discounted amount;
 - (iii) amounts charged against the provision during the period; and
 - (iv) unused amounts reversed during the period;
 - (b) a brief description of the nature of the obligation and the expected amount and timing of any resulting payments;
 - (c) an indication of the uncertainties about the amount or timing of those outflows; and
 - (d) the amount of any expected reimbursement, stating the amount of any asset that has been recognised for that expected reimbursement.

Comparative information for prior periods is not required.

Disclosures about contingent liabilities

- G203 Unless the possibility of any outflow of resources in settlement is remote, an entity shall disclose, for each class of contingent liability at the reporting date, a brief description of the nature of the contingent liability and, when practicable:
- (a) an estimate of its financial effect, measured in accordance with paragraphs G194–G199;
 - (b) an indication of the uncertainties relating to the amount or timing of any outflow; and
 - (c) the possibility of any reimbursement.

If after making every reasonable effort to do so, an entity cannot make one or more of these disclosures, that fact shall be stated.

Disclosures about contingent assets

- G204 If an inflow of economic benefits is probable (more likely than not) but not virtually certain, an entity shall disclose a description of the nature of the contingent assets at the end of the reporting period, and, when practicable

without undue cost or effort, an estimate of their financial effect, measured using the principles set out in paragraphs G194–G199. If after making every reasonable effort to do so, an entity cannot make this disclosure, that fact shall be stated.

Prejudicial disclosures

- G205 In extremely rare cases, disclosure of some or all of the information required by paragraphs G202–G204 can be expected to prejudice seriously the position of the entity in a dispute with other parties on the subject matter of the provision, contingent liability or contingent asset. In such cases, an entity need not disclose the information, but shall disclose the general nature of the dispute, together with the fact that, and reason why, the information has not been disclosed.

Guide Section 22 Equity

Situations not addressed by this Guide	
An entity shall refer to the <i>IFRS for SMEs</i> :	
(a)	if the entity issues any of the following instruments: <ul style="list-style-type: none"> (i) puttable financial instruments, ie an instrument that gives the holder the right to sell the instrument back to the entity or that is automatically redeemed or repurchased by the issuer on the occurrence of a specified event (see <i>IFRS for SMEs</i> paragraphs 22.4(a) and 22.5). (ii) financial instruments that require the entity to pay out a pro rata share of its net assets on liquidation of the entity (see <i>IFRS for SMEs</i> paragraphs 22.4(b) and 22.5). (iii) equity that is issued by means of options, rights, warrants and similar equity instruments (see <i>IFRS for SMEs</i> paragraph 22.11). (iv) convertible debt (ie a loan that can be converted into equity) or other compound financial instruments, such as instruments with both debt and equity components (see <i>IFRS for SMEs</i> paragraphs 22.13–22.15).
(b)	if any shares in the entity are held by the entity itself or by its subsidiaries (known as treasury shares) or by any associates (see <i>IFRS for SMEs</i> paragraphs 4.12(a) and 22.16).
(c)	if the entity has made a capitalisation or bonus issue (sometimes referred to as a 'stock dividend'), ie the issue of new shares to shareholders in proportion to their existing shareholdings, or has made a share split (sometimes referred to as a 'stock split'), ie the dividing of existing shares into multiple shares (see <i>IFRS for SMEs</i> paragraph 22.12).

Classification

- G206 Equity is the residual interest in the assets of an entity after deducting all its liabilities. A liability is a present obligation of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of cash or other resources (for example, an instrument that obligates the entity to pay cash to another party or gives another party the right to demand cash from the entity is a liability of the entity even if it has a different status under local laws). Equity includes investments by the owners of the entity, plus additions to those investments earned through profitable operations and retained for use in the entity's operations, minus reductions to owners' investments as a result of unprofitable operations and distributions to owners.
- G207 Members' shares in co-operative entities and similar instruments are equity if:
- (a) the co-operative entity has an unconditional right to refuse redemption of the members' shares; or
 - (b) redemption is unconditionally prohibited by local law, regulation or the entity's governing charter.

Original issue of shares or other equity instruments

- G208 An entity shall recognise the issue of shares or other equity instruments as equity when it issues those instruments and when another party is obliged to provide cash or other resources to the entity in exchange for the instruments:
- (a) if the equity instruments are issued before the entity receives the cash or other resources, the entity shall present the amount receivable as an offset to equity in its statement of financial position, not as an asset.
 - (b) if the entity receives the cash or other resources before the equity instruments are issued, and the entity cannot be required to repay the cash or other resources received, the entity shall recognise the corresponding increase in equity to the extent of consideration received.
 - (c) to the extent that the equity instruments have been subscribed for but not issued, and the entity has not yet received the cash or other resources, the entity shall not recognise an increase in equity.
- G209 An entity shall measure the equity instruments at the amount of cash received. If payment is deferred and the time value of money is material, the initial measurement shall be on a present value basis. If the equity instruments are exchanged for resources other than cash, the equity instruments shall be recognised at the fair value of those resources (paragraphs G13–G16 provide guidance on determining fair value).
- G210 An entity shall account for the transaction costs (ie incremental costs that are directly attributable to the issue) of an equity transaction as a deduction from equity, net of any related income tax benefit.
- G211 How the increase in equity arising on the issue of shares or other equity instruments is presented in the statement of financial position is determined by

applicable laws. For example, the par value (or other nominal value) of shares and the amount paid in excess of par value may be required to be presented separately.

Distributions to owners

- G212 An entity shall reduce equity for the amount of distributions to its owners (holders of its equity instruments), net of any related income tax benefits.
- G213 Sometimes an entity distributes assets other than cash as dividends to its owners. When an entity declares such a distribution and has an obligation to distribute non-cash assets to its owners, it shall recognise a liability. It shall measure the liability at the fair value of the assets to be distributed. At the end of each reporting period and at the date of settlement, the entity shall review and adjust the carrying amount of the dividend payable to reflect changes in the fair value of the assets to be distributed, with any changes recognised in equity as adjustments to the amount of the distribution.

Guide Section 23 Revenue

Situations not addressed by this Guide	
An entity shall refer to the <i>IFRS for SMEs</i> :	
(a)	if the entity has any revenue in the form of royalties or dividends arising from other parties using the entity's assets (see <i>IFRS for SMEs</i> paragraphs 23.1(d), 23.2(b) and 23.28–23.30).
(b)	if the entity exchanges goods and services for other goods and services (see <i>IFRS for SMEs</i> paragraphs 23.6–23.7).
(c)	if the entity grants customers loyalty awards, for example, points that the customer may redeem in the future for free or discounted goods or services (see <i>IFRS for SMEs</i> paragraph 23.9).
(d)	if the entity has two or more construction contracts that it negotiated together as a single package, or the entity has a single construction contract covering several assets and those assets were negotiated separately (see <i>IFRS for SMEs</i> paragraphs 23.8 and 23.18–23.20).

Scope of Guide Section 23

- G214 Revenue is the gross inflow of economic benefits during the period arising in the course of the ordinary activities of an entity when those inflows result in increases in equity, other than increases relating to contributions from equity participants. Guide Section 23 shall be applied in accounting for revenue arising from the following transactions and events:
- (a) the sale of goods (whether produced by the entity for the purpose of sale or purchased for resale);

- (b) the rendering of services;
- (c) construction contracts in which the entity is the contractor. A construction contract is a contract specifically negotiated for the construction of an asset or a combination of assets that are closely interrelated or interdependent in terms of their design, technology and function or their ultimate purpose or use; and
- (d) deposits or receivables yielding interest.

Measurement of revenue

G215 An entity shall measure revenue at the fair value of the consideration received or receivable. The fair value of the consideration received or receivable is after deducting the amount of any trade discounts, prompt settlement discounts and volume rebates allowed by the entity. The fair value also takes into account the time value of money.

G216 An entity shall include in revenue only the gross inflows of economic benefits received and receivable by the entity on its own account. An entity shall exclude from revenue all amounts collected on behalf of third parties, for example sales taxes, goods and services taxes and value added taxes collected on behalf of a government. In an agency relationship, an entity shall include in revenue only the amount of its commission. The amounts collected on behalf of the principal are not revenue of the entity.

Deferred payment

G217 When the inflow of cash or cash equivalents is deferred, and the arrangement constitutes in effect a financing transaction, the fair value of the consideration is the present value of all future receipts determined using an imputed rate of interest. A financing transaction arises when, for example, an entity provides interest-free credit to the buyer or accepts a note receivable bearing a below-market interest rate from the buyer as consideration for the sale of goods. The imputed rate of interest is the more clearly determinable of either:

- (a) the prevailing rate for a similar instrument of an issuer with a similar credit rating; or
- (b) a rate of interest that discounts the nominal amount of the instrument to the current cash sales price of the goods or services.

An entity shall recognise the difference between the present value of all future receipts and the nominal amount of the consideration as interest revenue in accordance with paragraph G232 and Guide Section 11–12 *Financial Instruments*.

Example—deferred payment
<p>On 1 January 20X1 an entity sold inventories for CU2,000 receivable in two years' time. The cash sales price of the goods on 1 January 20X1 was CU1,653.</p> <p>Since there is a CU347 difference between the cash price of CU1,653 and the amount due under the two year credit arrangement, the arrangement is in effect a financing transaction as well as the sale of goods. The entity recognises revenue from the sale of goods on 1 January 20X1 of CU1,653. Furthermore, the entity must recognise interest revenue of CU165 and CU182 in the reporting periods ending 31 December 20X1 and 20X2 respectively.</p> <p>Using a spreadsheet or a financial calculator, the imputed rate of interest is calculated at 10 per cent per year (ie the rate that discounts the nominal amount (CU2,000) payable in two years' time to the current cash sales price (CU1,653)).</p> <p>Revenue arising from the sale of goods is CU1,653 (ie the present value of the future payment).</p> <p>Interest revenue for 20X1 is CU165 (= CU1,653 × 10%).</p> <p>Interest revenue for 20X2 is CU182 (= (CU1,653 + CU165 interest accrued) × 10%).</p>

Identification of the revenue transaction

- G218 An entity usually applies the revenue recognition criteria in this Guide Section 23 separately to each transaction. However, an entity applies the recognition criteria to the separately identifiable components of a single transaction when necessary to reflect the substance of the transaction. For example, an entity applies the recognition criteria to the separately identifiable components of a single transaction when the selling price of a product includes an identifiable amount for subsequent servicing. Conversely, an entity applies the recognition criteria to two or more transactions together when they are linked in such a way that the commercial effect cannot be understood without reference to the series of transactions as a whole. For example, an entity applies the recognition criteria to two or more transactions together when it sells goods and, at the same time, enters into a separate agreement to repurchase the goods at a later date, thus negating the substantive effect of the transaction.

Sale of goods

- G219 An entity shall recognise revenue from the sale of goods when all the following conditions are satisfied:
- (a) the entity has transferred to the buyer the significant risks and rewards of ownership of the goods;

- (b) the entity retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold;
- (c) the amount of revenue can be measured reliably;
- (d) it is probable (ie more likely than not) that the economic benefits associated with the transaction will flow to the entity; and
- (e) the costs incurred or to be incurred in respect of the transaction can be measured reliably.

For a straightforward sale of goods for cash or on credit, revenue is generally recognised on the date when the goods are delivered to the customer.

G220 The assessment of when an entity has transferred the significant risks and rewards of ownership to the buyer requires an examination of the circumstances of the transaction. In most cases, the transfer of the risks and rewards of ownership coincides with the transfer of the legal title or the passing of possession to the buyer. This is the case for most retail sales. An entity does not recognise revenue if it retains significant risks and rewards of ownership, for example, if the receipt of the revenue from a particular sale is contingent on the buyer selling the goods. If an entity retains only an insignificant risk of ownership, the transaction is a sale and the entity recognises the revenue. For example, an entity recognises revenue on the sale of goods if it offers a refund if the customer finds the goods faulty or is not satisfied for other reasons, and the entity can estimate the returns reliably. In such cases, the entity recognises a provision for returns in accordance with Guide Section 21 *Provisions and Contingencies*.

Rendering of services

G221 When the outcome of a transaction involving the rendering of services can be estimated reliably, an entity shall recognise revenue associated with the transaction by reference to the stage of completion of the transaction at the end of the reporting period (sometimes referred to as the percentage of completion method). The outcome of a transaction can be estimated reliably when all the following conditions are satisfied:

- (a) the amount of revenue can be measured reliably;
- (b) it is probable that the economic benefits associated with the transaction will flow to the entity;
- (c) the stage of completion of the transaction at the end of the reporting period can be measured reliably; and
- (d) the costs incurred for the transaction and the costs to complete the transaction can be measured reliably.

Paragraphs G225–G231 provide guidance for applying the percentage of completion method.

G222 When services are performed by an indeterminate number of acts over a specified period of time, an entity recognises revenue on a straight-line basis

over the specified period unless there is evidence that some other method better represents the stage of completion. When a specific act is much more significant than any other act, the entity postpones recognition of revenue until the significant act is executed.

- G223 When the outcome of the transaction involving the rendering of services cannot be estimated reliably, an entity shall recognise revenue only to the extent of the expenses recognised that are recoverable.

Construction contracts

- G224 When the outcome of a construction contract can be estimated reliably, an entity shall recognise contract revenue and contract costs associated with the construction contract as revenue and expenses respectively by reference to the stage of completion of the contract activity at the end of the reporting period (often referred to as the percentage of completion method). Reliable estimation of the outcome requires reliable estimates of the stage of completion, future costs and collectability of billings. Paragraphs G225–G231 provide guidance for applying the percentage of completion method.

Percentage of completion method

- G225 This method is used to recognise revenue from rendering services (see paragraphs G221–G223) and from construction contracts (see paragraph G224). An entity shall review and, when necessary, revise the estimates of revenue and costs as the service transaction or construction contract progresses.

- G226 An entity shall determine the stage of completion of a transaction or contract using the method that measures most reliably the work performed. Possible methods include:

- (a) the proportion that costs incurred for work performed to date bear to the estimated total costs. Costs incurred for work performed to date do not include costs relating to future activity, such as for materials or prepayments;
- (b) surveys of work performed; and
- (c) completion of a physical proportion of the service transaction or contract work.

Progress payments and advances received from customers often do not reflect the work performed.

Example—percentage of completion method

A construction contractor has a fixed-price contract for CU2,000 to construct a building. The contractor's initial estimate of total contract costs is CU1,200. It is expected to take two years to construct the building.

At the end of the first year of the project (31 December 20X1) the contractor had incurred costs of CU800 on the contract and the entity's estimate of the total contract costs stayed the same.

The contract finishes in the middle of 20X2. Total costs actually incurred are CU1,250. The additional costs were incurred at the end of the contract and could not be foreseen at the time of preparing the financial statements for 20X1.

The contractor determines the stage of completion of the construction contract by reference to the proportion that costs incurred for work performed to date bear to the estimated total costs.

At 31 December 20X1 the contract is 66.7 per cent complete: $CU800 \text{ costs incurred} \div CU1,200 \text{ estimated total contract costs} = 66.7\%$.

In 20X1 the contractor recognises revenue and expenses of respectively CU1,333 (ie $66.7\% \times CU2,000$ total expected contract revenue) and CU800. This means that the profit in 20X1 is CU533.

In 20X2 the contractor recognises revenue and expenses of respectively CU667 and CU450 (ie $CU1,250 - CU800$). This means that the profit in 20X2 is CU217.

- G227 An entity shall recognise costs that relate to future activity on the transaction or contract, such as for materials or prepayments, as an asset if it is probable that the costs will be recovered.
- G228 An entity shall recognise as an expense immediately any costs whose recovery is not probable.
- G229 When the outcome of a construction contract cannot be estimated reliably:
- (a) an entity shall recognise revenue only to the extent of contract costs incurred that it is probable will be recoverable; and
 - (b) the entity shall recognise contract costs as an expense in the period in which they are incurred.
- G230 When it is probable that total contract costs will exceed total contract revenue on a construction contract, the expected loss shall be recognised as an expense immediately, with a corresponding provision for an onerous contract (see Guide Section 21).
- G231 If the collectibility of an amount already recognised as contract revenue is no longer probable, the entity shall recognise the uncollectible amount as an expense rather than as an adjustment of the amount of contract revenue.

Interest

G232 Interest shall be recognised using the effective interest method as described in paragraphs G104–G109.

Disclosures

General disclosures about revenue

G233 An entity shall disclose:

- (a) the accounting policies adopted for the recognition of revenue, including the methods adopted to determine the stage of completion of transactions involving the rendering of services; and
- (b) the amount of each category of revenue recognised during the period, showing separately, at a minimum, revenue arising from:
 - (i) the sale of goods;
 - (ii) the rendering of services;
 - (iii) interest;
 - (iv) commissions; and
 - (v) any other significant types of revenue.

Disclosures relating to revenue from construction contracts

G234 An entity shall disclose the following:

- (a) the amount of contract revenue recognised as revenue in the period;
- (b) the methods used to determine the contract revenue recognised in the period; and
- (c) the methods used to determine the stage of completion of contracts in progress.

G235 An entity shall present:

- (a) the gross amount due from customers for contract work, as an asset; and
- (b) the gross amount due to customers for contract work, as a liability.

Guide Section 24 Government Grants

Situations not addressed by this Guide
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An entity shall refer to the <i>IFRS for SMEs</i> if the entity receives any government grants, ie assistance by government in the form of a transfer of resources to the entity in return for past or future compliance with specified conditions relating to the operating activities of the entity (see <i>IFRS for SMEs</i> Section 24 and paragraph 23.30(b)).

Scope of Guide Section 24

G236 Guide Section 24 does not cover government assistance that is provided for an entity in the form of benefits that are available in determining taxable profit or tax loss, or are determined or limited on the basis of income tax liability. Examples of such benefits are income tax holidays, investment tax credits, accelerated depreciation allowances and reduced income tax rates. Guide Section 29 *Income Tax* covers accounting for taxes based on income.

Disclosure

G237 If an entity receives any government assistance other than government grants [see box at the start of Guide Section 24] the entity shall disclose a description of any such government assistance from which the entity has directly benefited. Government assistance is action by government designed to provide an economic benefit specific to an entity or range of entities qualifying under specified criteria. Examples include free technical or marketing advice and the provision of guarantees.

Guide Section 25 *Borrowing Costs*

Scope of Guide Section 25

G238 Borrowing costs are interest and other costs that an entity incurs in connection with the borrowing of funds. Borrowing costs include:

- (a) interest expense calculated using the effective interest method as described in Guide Section 11–12 *Financial Instruments*; and
- (b) finance charges in respect of finance leases recognised in accordance with Guide Section 20 *Leases*.

Recognition

G239 An entity shall recognise all borrowing costs as an expense in profit or loss in the period in which they are incurred.

Guide Section 26 *Share-based Payment*

Situations not addressed by this Guide

An entity shall refer to the *IFRS for SMEs* if the entity has any share-based payment transactions, ie it receives goods or services (including services from employees) as consideration for its equity instruments or by incurring liabilities for amounts that are based on the price of the entity's equity instruments (see *IFRS for SMEs* Section 26 and paragraphs 22.2(b), 28.1–28.2 and 33.6).

Guide Section 27 *Impairment of Assets*

Situations not addressed by this Guide	
An entity shall refer to the <i>IFRS for SMEs</i> :	
(a)	if the entity has goodwill (see <i>IFRS for SMEs</i> paragraphs 27.21, 27.24–27.28 and 27.33(c)).
(b)	if there is any indication that an impairment loss recognised in prior periods for non-financial assets other than inventories may no longer exist or may have reduced (see <i>IFRS for SMEs</i> paragraphs 27.29–27.33).

Scope of Guide Section 27

- G240 An impairment loss occurs when the carrying amount of an asset exceeds its recoverable amount. Guide Section 27 shall be applied in accounting for the impairment of all assets other than the following, for which other sections of this Guide establish impairment requirements:
- (a) deferred tax assets (see Guide Section 29 *Income Tax*);
 - (b) assets arising from employee benefits (see Guide Section 28 *Employee Benefits*); and
 - (c) financial assets within the scope of Guide Section 11–12 *Financial Instruments*.

Impairment of inventories

Selling price less costs to complete and sell

- G241 An entity shall assess at each reporting date whether any inventories are impaired. The entity shall make the assessment by comparing the carrying amount of each item of inventory (or group of similar items—see paragraph G242) with its selling price less costs to complete and sell. If an item of inventory (or group of similar items) is impaired, the entity shall reduce the carrying amount of the inventory (or the group) to its selling price less costs to complete and sell. That reduction is an impairment loss and it is recognised immediately in profit or loss.
- G242 If, after making every reasonable effort to do so, an entity is unable to determine the selling price less costs to complete and sell for inventories item by item, the entity may group items of inventory relating to the same product line that have similar purposes or end uses and are produced and marketed in the same geographical area for the purpose of assessing impairment.

Reversal of impairment

- G243 An entity shall make a new assessment of selling price less costs to complete and sell at each subsequent reporting date. When the circumstances that previously caused inventories to be impaired no longer exist, or when there is clear

evidence of an increase in selling price less costs to complete and sell because of changed economic circumstances, the entity shall reverse the amount of the impairment (ie the reversal is limited to the amount of the original impairment loss) so that the new carrying amount is the lower of the cost and the revised selling price less costs to complete and sell.

Impairment of assets other than inventories

General principles

- G244 If, and only if, the recoverable amount of an asset is less than its carrying amount, the entity shall reduce the carrying amount of the asset to its recoverable amount. That reduction is an impairment loss. Paragraphs G250–G259 provide guidance on measuring recoverable amount.
- G245 An entity shall recognise an impairment loss immediately in profit or loss.

Indicators of impairment

- G246 An entity shall assess at each reporting date whether there is any indication that an asset may be impaired. If any such indication exists, the entity shall estimate the recoverable amount of the asset. If there is no indication of impairment, it is not necessary to estimate the recoverable amount.
- G247 If it is not possible to estimate the recoverable amount of the individual asset, an entity shall estimate the recoverable amount of the cash-generating unit to which the asset belongs. This may be the case because measuring recoverable amount requires forecasting cash flows, and sometimes individual assets do not generate cash flows by themselves. An asset's cash-generating unit is the smallest identifiable group of assets that includes the asset and generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets.
- G248 In assessing whether there is any indication that an asset may be impaired, an entity shall 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 entity 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 entity 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 materially the discount rate used in calculating an asset's value in use and decrease the asset's fair value less costs to sell.

- (d) The carrying amount of the net assets of the entity is more than the estimated fair value of the entity as a whole (such an estimate may have been made, for example, in relation to the potential sale of part or all of the entity).

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 entity 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 the asset becoming idle, plans to discontinue or restructure the operation to which an asset belongs, and plans to dispose of an asset before the previously expected date.
- (g) Evidence is available from internal reporting that indicates that the economic performance of an asset is, or will be, worse than expected. In this context economic performance includes operating results and cash flows.

- G249 If there is an indication that an asset may be impaired, this may indicate that the entity should review the remaining useful life, the depreciation method or the residual value for the asset and adjust it in accordance with the section of this Guide applicable to the asset (for example, Guide Section 17 *Property, Plant and Equipment*), even if no impairment loss is recognised for the asset.

Measuring recoverable amount

- G250 The recoverable amount of an asset or a cash-generating unit is the higher of its fair value less costs to sell and its value in use. If it is not possible to estimate the recoverable amount of an individual asset, references in paragraphs G251–G259 to an asset should be read as references also to an asset’s cash-generating unit.
- G251 It is not always necessary to determine both an asset’s fair value less costs to sell and its value in use. 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.
- G252 If there is no reason to believe that an asset’s value in use materially exceeds its fair value less costs to sell, the asset’s fair value less costs to sell may be used as its recoverable amount. This will often be the case for an asset that is held for disposal.

Fair value less costs to sell

- G253 Fair value less costs to sell 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. (See guidance in paragraphs G13–G16).

Value in use

- G254 Value in use is the present value of the future cash flows expected to be derived from an asset (or cash-generating unit). This present value calculation 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 those future cash flows.
- G255 The following elements shall be reflected in the calculation of an asset's value in use:
- (a) an estimate of the future cash flows the entity expects to derive from the asset;
 - (b) expectations about possible variations in the amount or timing of those future cash flows;
 - (c) the time value of money, represented by the current market risk-free rate of interest;
 - (d) the price for bearing the uncertainty inherent in the asset; and
 - (e) other factors, such as illiquidity, that market participants would reflect in pricing the future cash flows the entity expects to derive from the asset.
- G256 In measuring value in use, estimates of future cash flows shall 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 can be directly attributed, or allocated on a reasonable and consistent basis, to the asset; and
 - (c) net cash flows, if any, expected to be received (or paid) for the disposal of the asset at the end of its useful life in an arm's length transaction between knowledgeable, willing parties.
- The entity may wish to use any recent financial budgets or forecasts to estimate the cash flows, if available. To estimate cash flow projections beyond the period covered by the most recent budgets or forecasts an entity may wish to extrapolate the projections based on the budgets or forecasts using a steady or declining growth rate for subsequent years, unless an increasing rate can be justified.
- G257 Estimates of future cash flows shall not include:
- (a) cash inflows or outflows from financing activities; or
 - (b) income tax receipts or payments.
- G258 Future cash flows shall be estimated for the asset in its current condition. Estimates of future cash flows shall not include estimated future cash inflows or outflows that are expected to arise from:
- (a) a future restructuring to which an entity is not yet committed; or
 - (b) improving or enhancing the asset's performance.
- G259 The discount rate (rates) used in the present value calculation shall be a pre-tax rate (rates) that reflect(s) current market assessments of:

- (a) the time value of money; and
- (b) the risks specific to the asset for which the future cash flow estimates have not been adjusted.

The discount rate (rates) used to measure an asset's value in use shall not reflect risks for which the future cash flow estimates have been adjusted, to avoid double-counting.

Example—value in use calculation			
<p>At the end of 20X0 an entity tests a machine for impairment. The machine was bought five years earlier for CU300,000, when its useful life was estimated to be 15 years and the estimated residual value was nil. At 31 December 20X0, after recognising the depreciation charge for 20X0, the machine's carrying amount was CU200,000 and its remaining useful life was estimated at 10 years.</p> <p>The machine's value in use is calculated using a pre-tax discount rate of 14 per cent per year. Budgets approved by management reflect expected cash inflows net of the estimated costs that are necessary to maintain the level of economic benefit that is expected to arise from the machine in its current condition. Assume, for simplicity, that the expected future cash flows occur at the end of each reporting period.</p> <p>An estimate of the value in use of the machine at the end of 20X0 is:</p>			
<i>Year</i>	<i>Expected future cash flow</i>	<i>Present value factor 14%^(a)</i>	<i>Discounted cash flow</i>
	<i>CU</i>	<i>CU</i>	<i>CU</i>
20X1	22,742	0.877193	19,949
20X2	25,090	0.769468	19,306
20X3	26,794	0.674972	18,085
20X4	35,497	0.592080	21,017
20X5	39,985	0.519369	20,767
20X6	41,959	0.455587	19,116
20X7	43,462	0.399637	17,369
20X8	47,344	0.350559	16,597
20X9	47,287	0.307508	14,541
20Y0 ^(b)	46,574	0.269744	12,563
Value in use			179,310

Assume that the fair value less cost to sell is lower than the value in use.^(c)

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Example—value in use calculation		
The calculation of the impairment loss at the end of 20X0 is as follows:		
		CU
Carrying amount before impairment loss		200,000
less recoverable amount		(179,310)
Impairment loss		20,690
Carrying amount after impairment loss (ie recoverable amount)		179,310
The entity recognises the impairment loss on the machine at 31 December 20X0 as follows:		
	Debit	Credit
	CU	CU
Profit or loss (impairment loss)	20,690	
Asset—Accumulated impairment (machine)		20,690
As a consequence of the impairment loss recognised at 31 December 20X0, the carrying amount of the machine immediately after the impairment recognition is equal to the machine's recoverable amount (ie CU179,310). In this case, in subsequent periods (ie 20X1–20Y0), assuming all variables remain the same as at the end of 20X0, the depreciable amount will be CU179,310 (see paragraph G152), so the depreciation charge will be CU17,931 per year (ie CU179,310 ÷ 10 years).		
(a) The present value factor is calculated as $k = 1 \div (1 + i)^n$, where <i>i</i> is the discount rate and <i>n</i> is the number of periods of discount (for example, for 20Y0 the present value factor (k_{20Y0}) is calculated as follows: $1 \div (1 + 0.14)^{10} = 1 \div (1.14)^{10} = 1 \div 3.707221 = 0.269744$).		
(b) The expected future cash flow for year 20Y0 includes CU1,000 expected to be paid to dispose of the asset at the end of its useful life. The residual value is nil because it is expected that the machine will be scrapped at the end of 20Y0.		
(c) Assuming that the machine's fair value less costs to sell is lower than its value in use, the value in use is the recoverable amount.		

Recognising and measuring an impairment loss for a cash-generating unit

- G260 An impairment loss shall be recognised for a cash-generating unit if, and only if, the recoverable amount of the unit is less than the carrying amount of the unit. The impairment loss shall be allocated to the assets of the unit pro rata on the basis of the carrying amount of each asset in the cash-generating unit.
- G261 However, an entity shall not reduce the carrying amount of any asset in the cash-generating unit below the highest of:
- its fair value less costs to sell (if determinable);
 - its value in use (if determinable); and

(c) zero.

G262 Any excess amount of the impairment loss that cannot be allocated to an asset because of the restriction in paragraph G261 shall be allocated to the other assets of the unit pro rata on the basis of the carrying amount of those other assets.

Reversal of an impairment loss

G263 An entity shall assess at each reporting date whether there is any indication that an impairment loss recognised in prior periods may no longer exist or may have decreased. Indications that an impairment loss may have decreased or may no longer exist are generally the opposite of those set out in paragraph G248. If any such indication exists, the entity shall determine whether all or part of the prior impairment loss should be reversed [See box at the start of Guide Section 27].

Compensation for impairment

G264 An entity shall include in profit or loss compensation from third parties for assets that were impaired, lost or given up only when the compensation becomes receivable.

Disclosures

G265 An entity shall disclose separately for inventories and for property, plant and equipment the amount of impairment losses recognised in profit or loss during the period and the line item(s) in the income statement in which those impairment losses are included.

Guide Section 28 Employee Benefits

Situations not addressed by this Guide	
An entity shall refer to the <i>IFRS for SMEs</i> :	
(a)	if the entity has a post-employment benefit plan that does not meet the description in paragraph G272, ie if the entity has an obligation other than to make fixed contributions into a plan in exchange for employee service (see <i>IFRS for SMEs</i> paragraphs 22.2(b), 28.9–28.28 and 28.40–28.41).
(b)	if the entity developed a formal plan to terminate the employment of one or more employees in advance of the termination and cannot realistically withdraw from that plan (see <i>IFRS for SMEs</i> paragraphs 28.34–28.37, 28.43–28.44 and 21A.3).

General recognition principle for all employee benefits

G266 Employee benefits are all forms of consideration given by an entity in exchange for service rendered by employees, including directors and management. An entity shall recognise the cost of all employee benefits to which its employees have become entitled as a result of service rendered to the entity during the reporting period:

- (a) as a liability, after deducting amounts that have been paid either directly to the employees or as a contribution to an employee benefit fund. If the amount paid exceeds the obligation arising from service before the reporting date, an entity shall recognise that excess as an asset to the extent that the prepayment will lead to a reduction in future payments or a cash refund.
- (b) as an expense, unless another section of this Guide requires the cost to be recognised as part of the cost of an asset such as inventories or property, plant and equipment.

In other words, employee benefits are recognised when the employee earns those benefits, not when those benefits are paid in cash.

Short-term employee benefits

- G267 Short-term employee benefits are employee benefits (other than termination benefits) that are wholly due within twelve months after the end of the period in which the employees render the related service, for example, wages, salaries, annual bonus payable, social security contributions and non-monetary benefits such as cars. When an employee has rendered service to an entity during the reporting period, the entity shall measure the amounts recognised in accordance with paragraph G266 at the undiscounted amount of short-term employee benefits expected to be paid in exchange for that service.
- G268 An entity may compensate employees for absence for various reasons including annual vacation leave and sick leave. Some short-term compensated absences accumulate—they can be carried forward and used in future periods if the employee does not use the current period's entitlement in full. An entity shall recognise the expected cost of accumulating compensated absences when the employees render service that increases their entitlement to future compensated absences. The entity shall measure the expected cost of accumulating compensated absences at the undiscounted additional amount that the entity expects to pay as a result of the unused entitlement that has accumulated at the end of the reporting period. The entity shall present this amount as a current liability at the reporting date.
- G269 An entity shall recognise the cost of other (non-accumulating) compensated absences when the absences occur. The entity shall measure the cost of non-accumulating compensated absences at the undiscounted amount of salaries and wages paid or payable for the period of absence.
- G270 An entity shall recognise the expected cost of profit-sharing and bonus payments only when:
- (a) as a result of past events, the entity either has:
 - (i) a present legal obligation; or

- (ii) an obligation arising from the entity's past actions (for example, history of making payments) that has created a valid expectation in other parties that the entity will make such payments (this means the entity has no realistic alternative but to make the payments); and
- (b) a reliable estimate of the obligation can be made.

Post-employment benefit plans

G271 Post-employment benefits are employee benefits (other than termination benefits) that are payable after the completion of employment, for example, retirement benefits, such as pensions. Arrangements whereby an entity provides post-employment benefits are post-employment benefit plans. In some cases, these arrangements are imposed by law rather than by action of the entity.

G272 If an entity has a post-employment benefit plan under which the entity:

- (a) either pays fixed contributions into a separate entity (for example, a fund, a group fund, or a government pension plan) for the employees or pays insurance premiums to fund a post-employment benefit plan; and
- (b) has no legal obligation or obligation arising from a past practice of making payments to pay further contributions or to make direct benefit payments to employees if the fund does not hold sufficient assets to pay (or if the insurer does not pay) all employee benefits relating to employee service in the current and prior periods,

then the entity's obligation to fund the post-employment benefits that will be received by the employees is limited to the amount of the entity's contributions to the post-employment benefit plan and the entity accounts for the post-employment benefit plan in accordance with paragraph G273.

G273 An entity shall recognise the contribution payable for a period:

- (a) as a liability, after deducting any amount already paid. If contribution payments exceed the contribution due for service before the reporting date, an entity shall recognise that excess as an asset; and
- (b) as an expense, unless another section of this Guide requires the cost to be recognised as part of the cost of an asset such as inventories or property, plant and equipment.

Other long-term employee benefits

G274 Other long-term employee benefits are employee benefits (other than post-employment benefits and termination benefits) that are not wholly due within twelve months after the end of the period in which the employees render the related service, for example, long-service benefits, long-term compensated absences such as long service or sabbatical leave, and bonuses payable twelve months or more after the end of the period in which the employees render the related service.

G275 An entity shall recognise a liability for other long-term employee benefits measured at the net total of the following amounts:

- (a) the present value of the benefit obligation at the reporting date; minus
- (b) the fair value at the reporting date of plan assets (if any) out of which the obligations are to be settled directly.

An entity shall recognise the change in the liability in profit or loss as an expense unless another section of this Guide requires the cost to be recognised as part of the cost of an asset such as inventories or property, plant and equipment.

Termination benefits

G276 Termination benefits are employee benefits payable as a result of either an entity's decision to terminate an employee's employment before the normal retirement date, or an employee's decision to accept voluntary redundancy in exchange for those benefits. Because termination benefits do not provide an entity with future economic benefits, an entity shall recognise them as an expense in profit or loss immediately. This will normally be on payment of the benefits unless formal plans are developed in advance [See box at the start of Guide Section 28].

Subsidiaries under group plans

G277 If a parent entity provides benefits to the employees of one or more of its subsidiaries, and the parent presents consolidated financial statements using either the *IFRS for SMEs* or full IFRSs, such subsidiaries are permitted to recognise and measure employee benefit expense on the basis of a reasonable allocation of the expense recognised for the group (ie for the parent and its subsidiaries).

Disclosures

Disclosures about post-employment benefit plans

G278 An entity shall disclose the amount recognised in profit or loss as an expense for post-employment benefit plans.

Disclosures about other long-term benefits

G279 For each category of other long-term benefits that an entity provides to its employees, the entity shall disclose the nature of the benefit, the amount of its obligation and the extent of funding at the reporting date.

Disclosures about termination benefits

G280 For each category of termination benefits that an entity provides to its employees, the entity shall disclose the nature of the benefit and its accounting policy.

Guide Section 29

Income Tax

Situations not addressed by this Guide

An entity shall refer to the *IFRS for SMEs*:

- (a) if the entity has a significant uncertainty about whether the tax authorities will accept the amounts reported to them because the entity has doubt over the appropriate tax treatment for some items in its tax return and the tax involved is material. For example, if the entity is unsure whether certain expenses are tax deductible and the amount of tax on those expenses is material to the financial statements (see *IFRS for SMEs* paragraphs 29.3(f), 29.8, 29.24 and 29.31(e)).
- (b) if there are income tax consequences for the entity if part or all of the profit or retained earnings is paid out as a dividend to shareholders, for example, income tax is payable by, or refundable to, the entity when the dividend is paid (see *IFRS for SMEs* paragraphs 29.25 and 29.32(f)).
- (c) if the entity files a consolidated tax return, ie the tax return covers two or more entities (see *IFRS for SMEs* paragraph 29.11).

Scope of Guide Section 29

- G281 Income tax includes all domestic and foreign taxes that are based on taxable profit (ie the tax is based on a measure of taxable revenue minus deductible expenses established by local legislation or regulation).

Basic principle

- G282 An entity shall recognise the current and future tax consequences of transactions and other events that have been recognised in the financial statements. These recognised tax amounts comprise current tax and deferred tax.
- (a) Current tax is income tax payable (refundable) in respect of the taxable profit (tax loss) for the current period or past periods. Current tax is the amount reported on an entity's income tax return for the period in conformity with tax laws or regulations.
 - (b) Deferred tax is income tax payable (recoverable) in respect of the taxable profit (tax loss) for future reporting periods as a result of past transactions or events. The past transactions or events are those that:
 - (i) have not yet been included in the entity's income tax return although they have been included when measuring profit or loss in conformity with this Guide; or
 - (ii) have been included in the entity's income tax return although they have not yet been included when measuring profit or loss in conformity with this Guide.

These differences between amounts reflected in current tax and amounts reflected in deferred tax are known as temporary differences (explained in more detail in paragraph G295).

- G283 An entity shall recognise a deferred tax liability for all temporary differences that are expected to increase taxable profit in the future (and therefore result in higher future tax payments). An entity shall recognise a deferred tax asset for all temporary differences that are expected to reduce taxable profit in the future (and will therefore benefit the entity by lowering future tax payments).
- G284 Income tax expense for the current period is the sum of:
- (a) the changes in the current tax liability and asset during the period; and
 - (b) the changes in the deferred tax liability and asset during the period.

Requirements for current tax

- G285 An entity shall recognise a current tax liability for tax payable on taxable profit for the current and past periods. If the amount paid for the current and past periods exceeds the amount payable for those periods, the entity shall recognise the excess as a current tax asset. An entity shall recognise a current tax asset for the benefit of a tax loss that can be carried back to recover tax paid in a previous period.
- G286 An entity shall measure its current tax liabilities (assets) using the tax rates and laws that have been enacted or substantively enacted by the reporting date. An entity shall regard tax rates as substantively enacted when future events required by the enactment process historically have not affected the outcome and are unlikely to do so (for example, tax legislation has been enacted by the legislature and is awaiting publication in an official journal).
- G287 An entity shall not discount current tax assets and liabilities.

Requirements for deferred tax

General recognition principle

- G288 An entity shall recognise a deferred tax asset or liability for tax recoverable or payable in future periods as a result of past transactions or events. Such tax arises from the difference between the amounts recognised for the entity's assets and liabilities in the statement of financial position and the recognition of those assets and liabilities by the tax authorities, and the carryforward of currently unused tax losses and tax credits. In most cases, those differences between the amounts in the statement of financial position and the amounts recognised by the tax authorities are accompanied by corresponding differences between profit or loss as measured by this Guide and taxable profit or loss.

Illustrative examples

- G289 The following examples illustrate scenarios that may be encountered by a typical micro entity that give rise to deferred tax. If the only differences between profit or loss (as measured by this Guide) and taxable profit arise because of the types of transactions illustrated by the examples, an entity may find that the examples

below will act as sufficient guidance when applying the requirements in paragraphs G290–G301. When using the examples, the entity shall ensure that the tax treatment of the income and expenses as illustrated in the examples is in line with the rules established by the local taxation authorities in the entity's jurisdiction.

Example—expenses incurred (and therefore recognised when measuring profit or loss by this Guide) but only tax deductible when paid^(a)

On 31 December 20X1, an entity has a warranty provision of CU1,000 for goods sold in 20X1 under a six-month warranty. The amount recognised as a provision is not deductible for tax purposes until it is actually paid or used. The tax rate for 20X2 is 30 per cent.

The entity has a deferred tax asset, ie a future tax saving of CU300 (= CU1,000 × 30%). The related expense of CU1,000 was recognised in accordance with this Guide when the goods were sold in 20X1.

If the entity does not expect to have sufficient taxable profit to realise the tax benefit in 20X2 (or in future periods when a carryforward is permitted), a valuation allowance against the deferred tax asset should be recognised in accordance with paragraphs G300–G301.

Note: expenses incurred that will never be deductible for tax purposes will not result in deferred tax, for example, this may be the case for some fines or entertainment costs.

(a) Depending on the jurisdiction such costs may include warranty costs, salary costs, research and development costs, etc.

Example—income accrued under this Guide when earned but taxed when paid

An entity has a bank deposit on which interest is paid annually on 30 June. On 31 December 20X1, the entity has an asset of CU1,000 for interest receivable for the period 1 July 20X1 to 31 December 20X1. That interest will be taxed when the interest is paid to the entity on 30 June 20X2. The tax rate for 20X2 is 30 per cent.

At 31 December 20X1, the entity recognises a deferred tax liability of CU300 (= CU1,000 × 30%) relating to the CU1,000 interest income that it accrued in 20X1. The tax liability is a deferred tax liability rather than a current tax liability because the CU300 is not owed for taxable income in 20X1 but rather will be paid when the CU1,000 interest income is included on the entity's tax return for 20X2.

Example—accelerated tax depreciation

On 1 January 20X1, an entity purchased an item of machinery for a cost of CU10,000. In accordance with this Guide, the item of machinery is being depreciated on a straight-line basis over 10 years. For tax purposes, the asset is depreciated over 4 years on a straight-line basis (accelerated tax depreciation). Revenue generated by using the machine is taxable. The asset is expected to be used for its full life and then scrapped. The currently enacted tax rate applicable in future years is 30 per cent.

Taxable income arises by using the machinery to generate revenue. Because of accelerated tax depreciation, in years 1–4, tax depreciation will be more than depreciation in accordance with this Guide (thus reducing taxable profit as compared to profit in accordance with this Guide), while in years 5–10, tax depreciation will be less than depreciation in accordance with this Guide (thus increasing taxable profit as compared to profit in accordance with this Guide). At the end of each of the first four years, the entity will recognise a deferred tax liability to reflect the additional tax it will pay in years 5–10. This deferred tax liability will reverse over years 5–10.

Consequently, on 31 December 20X1, the entity has a deferred tax liability of CU450 for the tax payable in the future on the difference between the carrying amount and the tax written down amount ($= 30\% \times (\text{CU}9,000 - \text{CU}7,500)$).

Likewise, on 31 December 20X2, the entity has a deferred tax liability of CU900 for the tax payable in the future on the difference between the carrying amount and the tax written down amount ($= 30\% \times (\text{CU}8,000 - \text{CU}5,000)$).

Note: if the facts in this example were reversed and the asset was depreciated faster for accounting purposes than for tax purposes, then on 31 December 20X1 there would be a deferred tax asset of CU450 for the tax saving in the future on the difference between the tax written down amount and the carrying amount ($= (\text{CU}9,000 - \text{CU}7,500) \times 30\%$).

Example—unused tax losses or tax credits

At 31 December 20X1, an entity has unused tax losses of CU100 that it is permitted to carry forward as a tax deduction in future periods. The tax rate is 30 per cent.

The entity has a deferred tax asset, ie a future tax deduction of CU30 ($= \text{CU}100 \times 30\%$). However, if the entity does not expect to have sufficient taxable profit to realise the tax benefit in the future periods, for example, if the entity is expected to be loss-making in the periods in which the carryforward is deductible, a valuation allowance against the deferred tax asset should be recognised in accordance with paragraphs G300–G301.

Example—calculation of current and deferred tax

An entity's profit for the year under this Guide is CU150,000. The tax rate is 15 per cent. The profit of CU150,000 reflects:

- CU20,000 interest income that is tax exempt.
- A deduction of CU5,000 for entertainment expense that is not deductible under the tax law.
- Bad debt expense of CU2,500, which includes CU2,000 for worthless receivables actually written off plus an additional CU500 estimated allowance for other receivables. A tax deduction is only given when worthless receivables are actually written off.
- Depreciation of CU35,000. However, tax depreciation (accelerated) was CU43,000.

Calculation of current tax expense:

	CU
Accounting profit	150,000
Less non-taxable interest income	(20,000)
Plus non-deductible entertainment	5,000
Plus non-deductible bad debts	500
Less additional tax depreciation	(8,000)
Taxable profit	127,500

Current tax = 15% × CU127,500 = CU19,125

Calculation of deferred tax expense:

Deferred tax asset—non-deductible bad debt:

$$\text{CU}500 \times 15\% = \text{CU}75$$

Deferred tax liability—accelerated depreciation^(a)

$$\text{CU}8,000 \times 15\% = \text{CU}1,200$$

Deferred tax expense = CU1,200 – CU75 = CU1,125

Deferred tax liability = CU1,125

Calculation of total income tax expense:

Total tax expense = CU19,125 + CU1,125 = CU20,250

Journal entry to reflect the above:

	Debit	Credit
	CU	CU
Income tax expense	20,250	
Tax currently payable		19,125
Deferred tax liability		1,125

(a) A full example of determining the deferred tax asset arising on accelerated tax depreciation is shown on the previous page.

Summary of steps in recognising deferred tax

- G290 An entity shall account for deferred tax by following the steps (a)–(f) below:
- (a) identify which assets and liabilities would be expected to affect taxable profit if they were recovered or settled for their present carrying amounts (paragraphs G288 and G291);
 - (b) determine the tax basis of the following at the end of the reporting period:
 - (i) the assets and liabilities in (a) (paragraphs G292–G293); and
 - (ii) other items that have a tax basis (paragraph G294).

The tax basis of an asset, liability, or other item is its measurement under the applicable substantively enacted tax laws or regulations.
 - (c) compute any temporary differences, unused tax losses and unused tax credits (paragraph G295);
 - (d) recognise deferred tax assets and deferred tax liabilities arising from the temporary differences, unused tax losses and unused tax credits (paragraphs G296);
 - (e) measure deferred tax assets and liabilities (paragraphs G297–G299); and
 - (f) recognise a valuation allowance against deferred tax assets to the extent that the gross amount is not expected to be recovered (paragraphs G300–G301).

Assets and liabilities whose recovery or settlement will not affect taxable profit

- G291 If the entity expects to recover the carrying amount of an asset or settle the carrying amount of a liability without affecting taxable profit, no deferred tax arises in respect of the asset or liability. Therefore, paragraphs G292–G301 apply only to assets and liabilities for which the entity expects the recovery or settlement of the carrying amount to affect taxable profit and to other items that have a tax basis. Examples of transactions that will not affect taxable profit include:
- (a) trade receivables for which revenue has already been included in taxable income as well as in profit or loss under this Guide. Associated cash receipt will have no tax consequence;
 - (b) bank loan payable. Repayment of the loan has no tax consequence; and
 - (c) a non-tax deductible fine incurred but not yet paid. The expense and related liability were recognised under this Guide when incurred. The payment of the fine will have no tax consequence.

Tax basis

- G292 An entity shall determine the tax basis of an asset, liability or other item in accordance with enacted or substantively enacted law.

- G293 The tax basis determines the amounts that will be included in taxable profit on recovery or settlement of the carrying amount of an asset or liability. Specifically:
- (a) the tax basis of an asset equals the amount that would have been deductible in arriving at taxable profit if the carrying amount of the asset had been recovered through sale at the end of the reporting period. If the recovery of the asset through sale does not increase taxable profit, the tax basis shall be deemed to be equal to the carrying amount.
 - (b) the tax basis of a liability equals its carrying amount less any amounts deductible in determining taxable profit (or plus any amounts included in taxable profit) that would have arisen if the liability had been settled for its carrying amount at the end of the reporting period. In the case of deferred revenue, the tax base of the resulting liability is its carrying amount, less any amount of revenue that will not be taxable in future periods.
- G294 Some items have a tax basis but are not recognised as assets or liabilities. For example, research costs are recognised as an expense when they are incurred but may not be permitted as a deduction in determining taxable profit until a future period. Thus, the carrying amount of the research costs is nil and the tax basis is the amount that will be deducted in future periods. An equity instrument issued by the entity may also give rise to deductions in a future period. There is no asset or liability in the statement of financial position, but the tax basis is the amount of the future deductions.

Temporary differences

- G295 Temporary differences arise:
- (a) when there is a difference between the carrying amounts and tax bases on the initial recognition of assets and liabilities, or at the time a tax basis is created for those items that have a tax basis but are not recognised as assets and liabilities;
 - (b) when a difference between the carrying amount and tax basis arises after initial recognition because income or expense is recognised in either profit or loss or equity in one reporting period but is recognised in taxable profit in a different period; or
 - (c) when the tax basis of an asset or liability changes and the change will not be recognised in the asset or liability's carrying amount in any period.

Deferred tax liabilities and assets

- G296 An entity shall recognise:
- (a) a deferred tax liability for all temporary differences that are expected to increase taxable profit in the future;
 - (b) a deferred tax asset for all temporary differences that are expected to reduce taxable profit in the future; and

- (c) a deferred tax asset for the carryforward of unused tax losses and unused tax credits.

Measurement of deferred tax

Tax rates

- G297 An entity shall measure its deferred tax liabilities (assets) using the tax rates and laws that have been enacted or substantively enacted by the reporting date. When different tax rates apply to different levels of taxable profit, an entity shall measure deferred tax expense (income) and related deferred tax liabilities (assets) using the average enacted or substantively enacted rates that it expects to be applicable to the taxable profit (tax loss) of the periods in which it expects the deferred tax asset to be realised or the deferred tax liability to be settled.
- G298 The measurement of deferred tax liabilities and deferred tax assets shall reflect the tax consequences that would follow from the manner in which the entity expects, at the reporting date, to recover or settle the carrying amount of the related assets and liabilities. For example, if the temporary difference arises from an item of income that is expected to be taxable as a capital gain in a future period, the deferred tax expense is measured using the capital gain tax rate.
- G299 An entity shall not discount deferred tax assets and liabilities.

Valuation allowance

- G300 An entity shall recognise a valuation allowance against deferred tax assets so that the net carrying amount equals the highest amount that is more likely than not (ie greater than 50 per cent probability) to be recovered based on current or future taxable profit.
- G301 An entity shall review the net carrying amount of a deferred tax asset at each reporting date and shall adjust the valuation allowance to reflect the current assessment of future taxable profits.

Withholding tax on dividends

- G302 When an entity pays dividends to its shareholders, it may be required to pay a portion of the dividends to taxation authorities on behalf of the shareholders. Such an amount paid or payable to taxation authorities is charged to equity as a part of the dividends.

Presentation

Allocation in income and equity

- G303 An entity shall recognise tax expense in income, unless the transaction or other event that resulted in the tax expense, or part of it, was recognised in equity in which case the tax expense, or that part of it, is recognised in equity.

Current/non-current distinction

- G304 An entity shall not classify any deferred tax assets (liabilities) as current assets (liabilities).

Offsetting

- G305 An entity shall offset current tax assets and current tax liabilities, or offset deferred tax assets and deferred tax liabilities, only when it has a legally enforceable right to set off the amounts and it intends either to settle on a net basis or to realise the asset and settle the liability simultaneously. Deferred tax assets and liabilities will generally meet these criteria if they arise within a single taxable entity and in a single jurisdiction.

Disclosures

- G306 An entity shall disclose information that enables users of its financial statements to evaluate the nature and financial effect of the current and deferred tax consequences of recognised transactions and other events.
- G307 An entity shall disclose separately the major components of tax expense (income). Such components of tax expense (income) may include:
- (a) current tax expense (income);
 - (b) any adjustments recognised in the period for current tax of prior periods;
 - (c) the amount of deferred tax expense (income) relating to the origination and reversal of temporary differences;
 - (d) the amount of deferred tax expense (income) relating to changes in tax rates or the imposition of new taxes;
 - (e) adjustments to deferred tax expense arising from a change in the tax status of the entity or its shareholders;
 - (f) any change in the valuation allowance (see paragraphs G300–G301); and
 - (g) the amount of tax expense relating to changes in accounting policies and errors (see Guide Section 10 *Accounting Policies, Estimates and Errors*).
- G308 An entity shall disclose the following separately:
- (a) an explanation of the significant differences in amounts presented in the statement of income and amounts reported to tax authorities;
 - (b) an explanation of changes in the applicable tax rate(s) compared with the previous reporting period;
 - (c) for each type of temporary difference and for each type of unused tax losses and tax credits:
 - (i) the amount of deferred tax liabilities, deferred tax assets and valuation allowances at the end of the reporting period;
 - (ii) an analysis of the change in deferred tax liabilities, deferred tax assets and valuation allowances during the period; and

- (d) the expiry date, if any, of temporary differences, unused tax losses and unused tax credits.

Guide Section 30 *Foreign Currency Translation*

Situations not addressed by this Guide	
An entity shall refer to the <i>IFRS for SMEs</i> :	
(a)	if the entity is required or chooses to prepare financial statements or to keep accounting records in a currency that is not its functional currency, ie not the currency in which it generates and expends cash (see <i>IFRS for SMEs</i> Section 30).
(b)	if the entity has any transactions in foreign currencies, other than the occasional purchase or sale of items or services in a foreign currency, or has any activities, operations or investments that are based or conducted in a different country (see <i>IFRS for SMEs</i> Section 30 and paragraphs 7.11–7.13, 25.1(c) and 29.16(a)).

Functional Currency

- G309 An entity recognises and measures transactions in the currency of the primary economic environment in which the entity operates (known as the functional currency). This is usually the one in which it primarily generates and expends cash.

Reporting foreign currency transactions in the functional currency

- G310 An entity may buy or sell an item, or a service, where the price is denominated in a foreign currency. An entity shall record the foreign currency transaction on initial recognition in its functional currency, by applying to the foreign currency amount the spot exchange rate between the functional currency and the foreign currency at the date of the transaction.
- G311 At the end of each reporting period, an entity shall translate any foreign currency payables or receivables using the closing rate. An entity shall recognise, in profit or loss in the period in which they arise, exchange differences arising on the settlement of monetary items or on translating monetary items at rates different from those at which they were translated on initial recognition during the period or in previous periods.

Use of a presentation currency

- G312 An entity may present its financial statements in a currency different from the one in which it recognises and measures transactions. In that case, the entity shall translate its items of income and expense and financial position into the presentation currency [See box at the start of Guide Section 30].

Guide Section 31 *Hyperinflation*

Situations not addressed by this Guide

An entity shall refer to the *IFRS for SMEs* if the entity has transactions or operations in a currency of a hyperinflationary economy (see *IFRS for SMEs* Section 31).

Guide Section 32 *Events after the End of the Reporting Period*

Events after the end of the reporting period defined

G313 Events after the end of the reporting period are those events, favourable and unfavourable, that occur between the end of the reporting period and the date when the financial statements are authorised for issue.

Recognition and measurement

Adjusting events after the end of the reporting period

G314 An entity shall adjust the amounts recognised in its financial statements, or recognise items that were not previously recognised, including related disclosures, to reflect adjusting events after the end of the reporting period. Adjusting events after the end of the reporting period are those events that provide evidence of conditions that existed at the end of the period.

G315 Examples include:

- (a) the receipt of information after the end of the reporting period indicating that an asset was impaired at the end of the reporting period, or that the amount of a previously recognised impairment loss for that asset needs to be adjusted. For example:
 - (i) the bankruptcy of a customer that occurs after the end of the reporting period usually confirms that a loss existed at the end of the reporting period on a trade receivable and that the entity needs to adjust the carrying amount of the trade receivable; and
 - (ii) the sale of inventories after the end of the reporting period may give evidence about their selling price at the end of the reporting period for the purpose of assessing impairment at that date.
- (b) the determination after the end of the reporting period of the cost of assets purchased, or the proceeds from assets sold, before the end of the reporting period.

Non-adjusting events after the end of the reporting period

G316 An entity shall not adjust the amounts recognised in its financial statements to reflect non-adjusting events after the end of the reporting period. Non-adjusting events after the end of the reporting period are those events that are indicative of conditions that arose after the end of the reporting period.

- G317 An example of a non-adjusting event after the end of the reporting period is a loss caused by flood, fire, or other event that occurred after the end of the reporting period.

Dividends

- G318 If an entity declares dividends to holders of its equity instruments after the end of the reporting period, the entity shall not recognise those dividends as a liability at the end of the reporting period. The amount of the dividend may be presented as a segregated component of retained earnings at the end of the reporting period.

Disclosure

Date of authorisation for issue

- G319 An entity shall disclose the date when the financial statements were authorised for issue and who gave that authorisation. If the entity's owners or others have the power to amend the financial statements after issue, the entity shall disclose that fact.

Non-adjusting events after the end of the reporting period

- G320 An entity shall disclose the following for each category of non-adjusting event after the end of the reporting period:

- (a) the nature of the event; and
- (b) an estimate of its financial effect or a statement that such an estimate cannot be made.

- G321 The following are examples of non-adjusting events after the end of the reporting period that would generally result in disclosure; the disclosures will reflect information that becomes known after the end of the reporting period but before the financial statements are authorised for issue:

- (a) major purchases or disposals of assets;
- (b) the destruction of a major production plant by a fire;
- (c) commencement of a major restructuring;
- (d) issues or repurchases of an entity's equity instruments or the taking out or paying off of significant loans;
- (e) changes in tax rates or tax laws enacted or announced that have a significant effect on current and deferred tax assets and liabilities;
- (f) entering into significant commitments or contingent liabilities; and
- (g) commencement of major litigation arising solely out of events that occurred after the end of the reporting period.

Guide Section 33

Related Party Disclosures

Situations not addressed by this Guide
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An entity shall refer to the <i>IFRS for SMEs</i> if the entity is under significant influence, control or joint control by a national, regional or local government (see <i>IFRS for SMEs</i> paragraph 33.11).
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Purpose of related party disclosures

- G322 Disclosures about an entity's related parties are necessary in the entity's financial statements to draw attention to the possibility that its financial position and profit or loss may have been affected by the existence of related parties and by transactions and outstanding balances with those parties. The definition of a related party is set out below. There are no specific measurement requirements for related party transactions.
- G323 A related party transaction is a transfer of resources, services or obligations between a reporting entity and a related party, regardless of whether a price is charged. Examples of related party transactions that a micro-entity may encounter include, but are not limited to:
- (a) transactions between the entity and its principal owner(s);
 - (b) transactions between the entity and another entity when both entities are under the common control of a single entity or person; and
 - (c) transactions in which an entity or person that controls the reporting entity incurs expenses directly that otherwise would have been borne by the reporting entity.

Related party defined

- G324 A related party is a person or entity that is related to the entity that is preparing its financial statements (the reporting entity).
- (a) A person or a close member of that person's family is related to a reporting entity if that person:
 - (i) is a member of the key management personnel of the reporting entity or of a parent of the reporting entity;
 - (ii) has control over the reporting entity; or
 - (iii) has joint control or significant influence over the reporting entity or has significant voting power in it.
 - (b) An entity is related to a reporting entity if any of the following conditions applies:
 - (i) the entity and the reporting entity are members of the same group (which means that each parent, subsidiary and fellow subsidiary is related to the others);

- (ii) either entity is an associate or joint venture of the other entity (or of a member of a group of which the other entity is a member);
 - (iii) both entities are joint ventures of a third entity;
 - (iv) either entity is a joint venture of a third entity and the other entity is an associate of the third entity;
 - (v) the entity is a post-employment benefit plan for the benefit of employees of either the reporting entity or an entity related to the reporting entity. If the reporting entity is itself such a plan, the sponsoring employers are also related to the plan;
 - (vi) the entity is controlled or jointly controlled by a person identified in (a);
 - (vii) a person identified in (a)(i) has significant voting power in the entity;
 - (viii) a person identified in (a)(ii) has significant influence over the entity or significant voting power in it;
 - (ix) a person or a close member of that person's family has both significant influence over the entity or significant voting power in it and joint control over the reporting entity; or
 - (x) a member of the key management personnel of the entity or of a parent of the entity, or a close member of that member's family, has control or joint control over the reporting entity or has significant voting power in it.
- G325 In considering each possible related party relationship, an entity shall assess the substance of the relationship and not merely the legal form.
- G326 The following are not necessarily related parties:
- (a) two entities simply because they have a director or other member of key management personnel in common;
 - (b) providers of finance by virtue of their normal dealings with an entity (even though they may affect the freedom of action of an entity or participate in its decision-making process); and
 - (c) a customer, or supplier with whom an entity transacts a significant volume of business, merely by virtue of the resulting economic dependence.
- G327 Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly, including any director (whether executive or otherwise) of that entity. Compensation includes all forms of consideration paid, payable or provided by the entity, or on behalf of the entity (for example, by its parent or owner), in exchange for services rendered to the entity. It also includes such consideration paid on behalf of a parent of the entity in respect of goods or services provided to the entity.

Disclosures

Disclosure of parent-subsidiary relationships

- G328 Relationships between a parent and its subsidiaries shall be disclosed irrespective of whether there have been related party transactions. An entity shall disclose the name of its parent and, if different, the ultimate controlling party. If neither the entity's parent nor the ultimate controlling party produces financial statements available for public use, the name of the next most senior parent that does so (if any) shall also be disclosed.

Disclosure of key management personnel compensation

- G329 An entity shall disclose key management personnel compensation in total.

Disclosure of related party transactions

- G330 If an entity has related party transactions, it shall disclose the nature of the related party relationship as well as information about the transactions, outstanding balances and commitments necessary for an understanding of the potential effect of the relationship on the financial statements. Those disclosure requirements are in addition to the requirements in paragraph G329 to disclose key management personnel compensation. At a minimum, disclosures shall include:

- (a) the amount of the transactions;
- (b) the amount of outstanding balances;
 - (i) their terms and conditions, including whether they are secured, and the nature of the consideration to be provided in settlement; and
 - (ii) details of any guarantees given or received;
- (c) provisions for uncollectible receivables related to the amount of outstanding balances; and
- (d) the expense recognised during the period in respect of bad or doubtful debts due from related parties.

Such transactions could include purchases, sales, or transfers of goods or services; leases; guarantees; and settlements by the entity on behalf of the related party or vice versa.

- G331 An entity shall make the disclosures required by paragraph G330 separately for each of the following categories:
- (a) entities with control, joint control or significant influence over the entity;
 - (b) key management personnel of the entity or its parent (in the aggregate); and
 - (c) other related parties.
- G332 The following are examples of transactions that shall be disclosed if they are with a related party:

- (a) purchases or sales of goods (finished or unfinished);
- (b) purchases or sales of property and other assets;
- (c) rendering or receiving of services;
- (d) leases;
- (e) transfers of research and development;
- (f) transfers under licence agreements;
- (g) transfers under finance arrangements (including loans and equity contributions in cash or in kind);
- (h) provision of guarantees or collateral;
- (i) settlement of liabilities on behalf of the entity or by the entity on behalf of another party; and
- (j) participation by a parent in a defined benefit plan that shares risks between group entities.

G333 An entity shall not state that related party transactions were made on terms equivalent to those that prevail in arm's length transactions unless such terms can be substantiated.

G334 An entity may disclose items of a similar nature in the aggregate except when separate disclosure is necessary for an understanding of the effects of related party transactions on the financial statements of the entity.

Guide Section 34 *Specialised Activities*

Situations not addressed by this Guide	
An entity shall refer to the <i>IFRS for SMEs</i> :	
(a)	if the entity is involved in agricultural activity, ie the management of the biological transformation of living animals or plants for sale, into agricultural produce (ie the harvested product) or into additional animals or plants (see <i>IFRS for SMEs</i> paragraphs 13.2–13.3, 13.15, 17.3(a), 20.1(d), 23.2, 27.1(e) and 34.2–34.10).
(b)	if the entity is engaged in extractive activities, ie the exploration for, evaluation or extraction of mineral resources (see <i>IFRS for SMEs</i> paragraphs 13.3(a), 17.3(b), 18.3(b), 20.1(a) and 34.11).
(c)	if the entity enters into service concession arrangements, ie arrangements whereby a government or other public sector body (the 'grantor') contracts with a private operator to develop (or upgrade), operate and maintain the grantor's infrastructure assets such as roads, bridges, tunnels, airports, energy distribution networks, prisons or hospitals (see <i>IFRS for SMEs</i> paragraphs 34.12–34.16).

Guide Section 35

Transition to the IFRS for SMEs

Situations not addressed by this Guide	
	An entity shall refer to the <i>IFRS for SMEs</i> :
(a)	if the entity applied hedge accounting under its previous accounting framework (see <i>IFRS for SMEs</i> paragraph 35.9(b)).
(b)	if the entity accounted for a discontinued operation under its previous accounting framework (see <i>IFRS for SMEs</i> paragraph 35.9(d)).
(c)	if the entity has had one or more business combinations in the past (see <i>IFRS for SMEs</i> paragraph 35.9(e) and 35.10(a)).
(d)	if the entity encounters transactions not covered by this Guide (ie those listed in the boxes at the start of each of the Guide Sections), there may be additional optional exemptions available, for example, there are optional exemptions for business combinations, share-based payments and extractive industries (see <i>IFRS for SMEs</i> paragraph 35.10 for the full list).

Scope of Guide Section 35

- G335 Guide Section 35 applies to a first-time adopter of the *IFRS for SMEs* regardless of whether its previous accounting framework was full IFRSs or another set of generally accepted accounting principles (GAAP) such as its national accounting standards, or another framework such as the local income tax basis.
- G336 An entity can be a first-time adopter of the *IFRS for SMEs* only once. If an entity using the *IFRS for SMEs* stops using it for one or more reporting periods and then is required, or chooses, to adopt it again later, the special exemptions, simplifications and other requirements in Guide Section 35 do not apply to the re-adoption.

First-time adoption

- G337 A first-time adopter of the *IFRS for SMEs* using this Guide shall apply Guide Section 35 in its first financial statements that conform to the *IFRS for SMEs*.
- G338 An entity's first financial statements that conform to the *IFRS for SMEs* are the first annual financial statements in which the entity makes an explicit and unreserved statement in those financial statements of compliance with the *IFRS for SMEs*. Financial statements prepared in accordance with this Guide are an entity's first such financial statements if, for example, the entity:
- (a) did not present financial statements for previous periods;
 - (b) presented its most recent previous financial statements under national requirements that are not consistent with the *IFRS for SMEs* in all respects; or

- (c) presented its most recent previous financial statements in conformity with full IFRSs.
- G339 Paragraph G26 defines a complete set of financial statements.
- G340 An entity's date of transition to the *IFRS for SMEs* when using this Guide for that transition is the beginning of the earliest period for which the entity presents full comparative information in accordance with the *IFRS for SMEs* in its first financial statements that conform to the *IFRS for SMEs*.

Procedures for preparing financial statements at the date of transition

- G341 Except as provided in paragraphs G343–G345, an entity shall, in its opening statement of financial position as of its date of transition to the *IFRS for SMEs*:
- (a) recognise all assets and liabilities whose recognition is required by the *IFRS for SMEs*;
 - (b) not recognise items as assets or liabilities if the *IFRS for SMEs* does not permit such recognition;
 - (c) reclassify items that it recognised under its previous financial reporting framework as one type of asset, liability or component of equity, but are a different type of asset, liability or component of equity under the *IFRS for SMEs*; and
 - (d) apply the *IFRS for SMEs* in measuring all recognised assets and liabilities.
- G342 The accounting policies that an entity uses in its opening statement of financial position under the *IFRS for SMEs* may differ from those that it used for the same date using its previous financial reporting framework. The resulting adjustments arise from transactions, other events or conditions before the date of transition to the *IFRS for SMEs*. Therefore, an entity shall recognise those adjustments directly in retained earnings (or, if appropriate, another category of equity) at the date of transition to the *IFRS for SMEs*.
- G343 On first-time adoption of the *IFRS for SMEs*, an entity shall not retrospectively change the accounting that it followed under its previous financial reporting framework for either of the following transactions:
- (a) derecognition of financial assets and financial liabilities. Financial assets and liabilities derecognised under an entity's previous accounting framework before the date of transition should not be recognised upon adoption of the *IFRS for SMEs*. Conversely, for financial assets and liabilities that would have been derecognised under the *IFRS for SMEs* in a transaction that took place before the date of transition, but that were not derecognised under an entity's previous accounting framework, an entity may choose (i) to derecognise them on adoption of the *IFRS for SMEs* or (ii) to continue to recognise them until disposed of or settled.
 - (b) accounting estimates.
- G344 An entity may use one or more of the following exemptions in preparing its first financial statements that conform to the *IFRS for SMEs*:

- (a) **Fair value as deemed cost.** A first-time adopter may elect to measure an item of property, plant and equipment on the date of transition to the *IFRS for SMEs* at its fair value and use that fair value as its deemed cost at that date.
- (b) **Revaluation as deemed cost.** A first-time adopter may elect to use a previous GAAP revaluation of an item of property, plant and equipment at, or before, the date of transition to the *IFRS for SMEs* as its deemed cost at the revaluation date.
- (c) **Deferred income tax.** A first-time adopter is not required to recognise, at the date of transition to the *IFRS for SMEs*, deferred tax assets or deferred tax liabilities relating to differences between the tax basis and the carrying amount of any assets or liabilities for which recognition of those deferred tax assets or liabilities would involve undue cost or effort.
- (d) **Arrangements containing a lease.** A first-time adopter may elect to determine whether an arrangement existing at the date of transition to the *IFRS for SMEs* contains a lease (see paragraph G172) on the basis of facts and circumstances existing at that date, rather than when the arrangement was entered into.

G345 If it is impracticable for an entity to restate the opening statement of financial position at the date of transition for one or more of the adjustments required by paragraph G341 (ie the entity cannot restate after making every reasonable effort to do so), the entity shall apply paragraphs G341–G344 for such adjustments in the earliest period for which it is practicable to do so.

Disclosures

G346 If it is impracticable for an entity to restate the opening statement of financial position at the date of transition for one or more of the adjustments required by paragraph G341 (see paragraph G345), the entity shall disclose which amounts in the financial statements are affected. If it is impracticable for an entity to provide any disclosures required by this Guide, including for comparative periods, the omission shall be disclosed.

Explanation of transition to the *IFRS for SMEs*

G347 An entity shall explain how the transition from its previous financial reporting framework to the *IFRS for SMEs* affected its reported financial position, financial performance and cash flows.

Reconciliations

G348 To comply with paragraph G347, an entity's first financial statements prepared using the *IFRS for SMEs* shall include:

- (a) a description of the nature of each change in accounting policy;
- (b) reconciliations of its equity determined in accordance with its previous financial reporting framework to its equity determined in accordance with the *IFRS for SMEs* for both of the following dates:
 - (i) the date of transition to the *IFRS for SMEs*;

- (ii) the end of the latest period presented in the entity's most recent annual financial statements determined in accordance with its previous financial reporting framework; and
 - (c) a reconciliation of the profit or loss determined in accordance with its previous financial reporting framework for the latest period in the entity's most recent annual financial statements to its profit or loss determined in accordance with the *IFRS for SMEs* for the same period.
- G349 If an entity becomes aware of errors made under its previous financial reporting framework, the reconciliations required by paragraph G348(b) and (c) shall, to the extent practicable, distinguish the correction of those errors from changes in accounting policies.
- G350 If an entity did not present financial statements for previous periods, it shall disclose that fact in its first financial statements that conform to the *IFRS for SMEs*.

