NEED TO KNOW

IFRSs and Amendments effective in periods after 31 December 2017 year ends

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1. INTRODUCTION

2017 was the final year before entities are required to implement two significant new accounting standards – IFRS 9 *Financial Instruments* (IFRS 9) and IFRS 15 *Revenue from Contracts with Customers* (IFRS 15) – with IFRS 16 *Leases* (IFRS 16) being mandatory a year later (although early adoption is permitted).

In May 2017, the International Accounting Standards Board (IASB) issued IFRS 17 *Insurance Contracts* (IFRS 17) which applies to annual reporting periods beginning on or after 1 January 2021. Two new interpretations were also issued during 2017 – IFRIC 22 – *Foreign Currency Transactions and Advance Consideration* (IFRIC 22) with an effective date of 1 January 2018 and IFRIC 23 – *Uncertainty over Income Tax Treatments* (IFRIC 23) with an effective date of 1 January 2019. The IASB also issued several amendments to various standards that are detailed in the pursuant sections.

The new accounting standards for financial instruments, revenue and leases are complex, may require significant judgements and estimates, and are likely to have significant commercial effects. The impact of changes arising from other new requirements should not be underestimated. The two new interpretations may bring significant change for some entities, and, for those in the insurance sector, IFRS 17 introduces fundamental accounting changes from current practice.

Implementation projects should be nearing completion for IFRS 9 and IFRS 15 with implementation of IFRS 16 in process. Securities regulators worldwide have indicated that they expect to see meaningful disclosures about the likely effects of adoption of IFRSs 9 and 15 in 31 December 2017 annual reports, with many calling for quantitative information about the anticipated effects of those standards. Our experience indicates that many companies continue to significantly underestimate the likely effects of these new requirements, in particular those for revenue recognition. As we are now in the effective period, the risk of surprises, both internally and externally in the market place, becomes greater. These include profit warnings, delays in filing financial statements, qualified audit reports, a loss of investor confidence and associated reductions in share prices.

This publication summarises significant changes to IFRSs that will need to be adopted in future reporting periods, together with a discussion about major projects that are currently in progress at the IASB.

2. IFRSs AND AMENDMENTS EFFECTIVE IN PERIODS AFTER 31 DECEMBER 2017 YEAR ENDS

The following tables summarise new standards and amendments to standards which are mandatorily effective for year ends subsequent to 31 December 2017. The first table looks at the timing of mandatory adoption for an entity with a 31 December financial year end. The second table has more detail, including links to BDO's *International Financial Reporting Bulletins* and, for those entities that report in accordance with European Union (EU) – endorsed IFRS, a note of the current endorsement status.

Wide ranging and significant changes in financial statements are likely in the years ending 31 December 2018 and 2019 with the adoption of major new standards for revenue, financial instruments and leases. These will require careful planning and communication to investors and other users of financial statements, together with the need to address commercial considerations such as compliance with bank covenants, performance based remuneration schemes and business combinations (in particular, transactions where contingent consideration is to be calculated on the basis of future revenues or profits).

In common with normal practice, early adoption is permitted and for some entities this will be an attractive option. In particular, because the criteria for the recognition of a sale in a sale and leaseback transaction in IFRS 16 have been aligned with IFRS 15, some entities might wish to adopt IFRS 16 a year early.

2.1. Timing of mandatory adoption

For an entity with a 31 December year end, new standards, amendments to standards and interpretations will need to be adopted in the following financial years at the latest:

2018	2019	2021
Standards		
IFRS 9 (2014) *Financial Instruments*	IFRS 16 *Leases*	IFRS 17 *Insurance Contracts*
IFRS 15 *Revenue from Contracts with Customers*		
Amendments		
IFRS 2 *Share-Based Payments* (Amendment – Classification and Measurement of Share-Based Payment Transactions)	IFRS 9 (2014) *Financial Instruments* (Amendment – Prepayment Features with Negative Compensation)	
IFRS 4 *Insurance Contracts* (Amendment – Applying IFRS 9 *Financial Instruments* with IFRS 4 *Insurance Contracts*)	IAS 28 – *Investments in Associates and Joint Ventures* (Amendment – Long-term Interests in Associates and Joint Ventures)	
IAS 40 *Investment Property* (Amendment – Transfers of Investment Property)	Annual Improvements to IFRSs 2015-2017 Cycle (IFRS 3 *Business Combinations* and IFRS 11 *Joint Arrangements*, IAS 12 *Income Taxes*, and IAS 23 *Borrowing Costs*)	
IFRS 15 *Revenue from Contracts with Customers* (Amendment – Clarifications to IFRS 15 *Revenue from Contracts with Customers*)		
Annual Improvements to IFRSs 2014-2016 Cycle (IFRS 1 *First-time Adoption of IFRS* , IFRS 12 *Disclosures of Interests in Other Entities* and IAS 28 *Investments in Associates and Joint Ventures*)		
Interpretations		
IFRIC Interpretation 22 *Foreign Currency Transactions and Advance Consideration*	IFRIC Interpretation 23 *Uncertainty over Income Tax Treatments*	

In addition, at the same time as the amendment to IFRS 9 for prepayment features with negative compensation was issued, the IASB amended the Basis for Conclusions to IFRS 9 to clarify the accounting requirements in IFRS 9 for the modification or exchange of a financial liability that does not result in the derecognition of the existing financial liability and the recognition of a new one. There has been no change to the requirements of the relevant parts of IFRS 9, and these introduce an approach that is different from the approach that many companies have followed in accordance with the existing guidance in IAS 39 *Financial Instruments: Recognition and Measurement* (IAS 39). To date, few entities have taken account of this change and, since it will need to be implemented on a fully retrospective basis which may be complex, it is important for this issue to be addressed sooner rather than later.

The following tables set out a list of forthcoming standards and amendments, including their EU-endorsement status and links to BDO's International Financial Reporting Bulletins and IFRS In Practice publications:

IFRS	IASB Effective Date *(Early Adoption permitted)*	EU Endorsement status	BDO IFR Publications
Standards			
IFRS 9 *Financial Instruments* (2014) *Issued: July 2014*	1 January 2018	Endorsed	BDO *IFR Bulletin 2014/12* (click **here**) IFRS In Practice: IFRS 9 *Financial Instruments* (click **here**)
IFRS 15 *Revenue from Contracts with Customers* *Issued: May 2014* *Amendment to change effective date to 1 January 2018* *Issued: September 2015* *Clarifications to* IFRS 15 *Issued: April 2017*	1 January 2018	Endorsed	BDO *IFR Bulletin 2014/08* (click **here**), *2014/21* (click **here**), *and 2016/06* (click **here**) IFRS In Practice: IFRS 15 *Revenue from Contracts with Customers* (click **here**) Need to Know – IFRS 15 vs US GAAP Differences (click **here**)
IFRS 16 *Leases* *Issued: January 2017*	1 January 2019	Endorsed	BDO *IFR Bulletin 2016/01* (click **here**) IFRS In Practice: IFRS 16 *Leases* (click **here**)
IFRS 17 *Insurance Contracts* *Issued: May 2017*	1 January 2021	To be determined	
Amendments			
IFRS	**IASB Effective Date *(Early Adoption permitted)***	**EU Endorsement status *(Early Adoption permitted if endorsed)***	**BDO IFR Bulletin**
IFRS 2 *Share-Based Payments* (Amendment – Classification and Measurement of Share-Based Payment Transactions) *Issued: June 2016*	1 January 2018	Expected Q1-2018	BDO *IFR Bulletin 2017/05* (click **here**)
IFRS 4 *Insurance Contracts* (Amendment – Applying IFRS 9 *Financial Instruments*) *Issued: September 2016*	1 January 2018	Endorsed	BDO *IFR Bulletin 2016/11* (click **here**)

IFRS	IASB Effective Date *(Early Adoption permitted)*	EU Endorsement status	BDO IFR Publications
Amendments (*continued*)			
IFRS	**IASB Effective Date *(Early Adoption permitted)***	**EU Endorsement status *(Early Adoption permitted if endorsed)***	**BDO IFR Bulletin**
Annual Improvements to IFRSs 2014-2016 Cycle *Issued: December 2016*	1 January 2018	Expected Q1-2018	BDO *IFR Bulletin 2016/17* (click **here**)
IAS 40 *Investment Property* (Amendment – Transfers of Investment Property) *Issued: December 2016*	1 January 2018	Expected Q1-2018	BDO *IFR Bulletin 2016/17* (click **here**)
IFRS 9 (2014) *Financial Instruments* (Amendment – Prepayment Features with Negative Compensation *Issued: October 2017*	1 January 2019	Expected in 2018	
IAS 28 – *Investments in Associates and Joint Ventures* (Amendment – Long-term Interests in Associates and Joint Ventures) *Issued: October 2017*	1 January 2019	Expected in 2018	
Annual Improvements to IFRSs 2015-2017 Cycle *Issued: December 2017*	1 January 2019	Expected in 2018	
Interpretations			
IFRIC Interpretation 22 *Foreign Currency Transactions and Advance Consideration* *Issued: December 2016*	1 January 2018	Expected Q1-2018	BDO *IFR Bulletin 2016/16* (click **here**)
IFRIC Interpretation 23 *Uncertainty over Income Tax Treatments* *Issued: June 2017*	1 January 2019	Expected in 2018	BDO *IFR Bulletin 2017/08* (click **here**).

3. MAJOR DEVELOPMENTS – NEW STANDARDS

There are four major standards that will be effective in the coming years. These are IFRS 9 *Financial Instruments*, IFRS 15 *Revenue from Contracts with Customers* (both effective for periods beginning on or after 1 January 2018), IFRS 16 *Leases* (effective for periods beginning on or after 1 January 2019) and IFRS 17 *Insurance Contracts* (effective for periods beginning on or after 1 January 2021). These standards will affect almost all entities and will often result in very significant changes to financial statements.

Key changes from existing guidance are discussed below.

3.1. IFRS 9 *Financial Instruments*

In July 2014 the IASB published IFRS 9 which incorporated the final requirements on all three phases of the financial instruments projects – classification and measurement, impairment and hedge accounting.

IFRS 9 contains four categories for the classification and measurement of financial assets. These are:

- Amortised cost;
- Fair Value Through Other Comprehensive Income – FVTOCI;
- Fair Value Through Profit or Loss – FVTPL (residual category);
- Fair Value Through Other Comprehensive Income – FVTOCI (optional for some investments in equity instruments).

IFRS 9 introduces new criteria for the classification and measurement of financial assets to be measured at amortised cost. In order to qualify for amortised cost measurement, a two-stage test is applied. Firstly, the entity's business model must be to collect the contractual cash flows from the asset, rather than generating cash flows by selling the asset to realise its fair value. Secondly, the asset must have contractual cash flows which are comprised solely of payments of principal and interest on the principal amount outstanding (often referred to as 'solely payments of principal and interest' or 'the SPPI test'). Interest is principally the time value of money plus a margin for credit risk, with revisions made in 2014 to IFRS 9 adding guidance which notes that interest can contain other elements such as liquidity risk, a profit margin, and servicing/administrative costs. Guidance has also been included to cover circumstances in which the contractual cash flows do not precisely meet the definitions, such as a loan for which the interest rate is reset every three months to the six month rate.

Financial assets that pass both the business model and SPPI tests are required to be measured at amortised cost (unless the fair value option is available and elected), with all other financial assets being measured at fair value. The business model and SPPI tests are applied to the assets as a whole, with the previous guidance in IAS 39 for embedded derivatives no longer applying to financial assets.

The second measurement category is Fair Value Through Other Comprehensive Income (FVTOCI). This measurement category applies to debt instruments that meet the SPPI contractual cash flow characteristics test and where the entity is holding the debt instrument in a business model which is both to collect contractual cash flows and to sell financial assets. For example, an entity with this business model might purchase a government bond with a 10 year maturity, but expect to sell the asset after collecting interest income for only three years. Financial assets in the FVTOCI category are required to be recorded on balance sheet at fair value (to reflect the cash flows that would be generated from sale) with amortised cost measurement being applied in the income statement (to reflect the collection of contractual cash flows). The difference is recorded in other comprehensive income, with the cumulative difference being recycled to profit or loss on the disposal of the financial asset.

Financial assets that fail the SPPI test, or where the entity's business model for holding the asset is not to collect contractual cash flows (in whole or in part), must be classified at fair value through profit and loss (FVTPL). In certain circumstances an entity may also be able to designate a debt instrument as at FVTPL.

The default classification of investments in equity instruments is FVTPL, because an equity instrument does not have contractual cash flows and will therefore always fail the SPPI test. However, IFRS 9 permits an entity to make an irrevocable election on the initial recognition of an equity investment, on an investment by investment basis, to include changes in fair value in other comprehensive income. This election is not available for investments that are held for trading (that is, held for short term investment and profit taking). Note that the IFRS 9 FVTOCI category for equity investments is not the same as the Available-for-Sale category in IAS 39 as fair value gains and losses recorded in other comprehensive income are never recycled to profit or loss (including on the disposal of the investment, although the cumulative gain or loss in equity can be transferred to retained earnings by way of a reserves transfer). It is important to note that the election to include changes in fair value in other comprehensive income is only available for instruments that meet the definition of equity in IAS 32 *Financial Instruments: Presentation* (IAS 32). The election is not available for puttable instruments that are classified as equity instruments in accordance with the exception in IAS 32.16A-D. This is because they meet the definition of financial liabilities, with the exception to the normal requirements in IAS 32 meaning that they are classified as equity instruments.

The classification and measurement requirements for financial liabilities have been carried forward from IAS 39 largely unchanged, including a continuation of the requirement to separate embedded derivatives. However a significant change is that, if a financial liability is designated (under the option available in IFRS 9) as at fair value through profit or loss, changes in the fair value of that financial liability that are attributable to changes in the entity's own credit risk will normally be recorded in other comprehensive income instead of profit or loss. This change has been made in order to prevent a deterioration in an entity's financial position (and hence credit status) resulting in gains being reported in profit or loss.

The existing guidance for the derecognition of financial assets and liabilities has been carried forward from IAS 39 unchanged, with some improvements to disclosure requirements being added to IFRS 7 *Financial Instruments: Disclosures*.

For the impairment of financial assets, an 'expected credit loss' model in IFRS 9 replaces the 'incurred loss' model in IAS 39. The new impairment requirements will affect all entities with financial assets measured at amortised cost and FVTOCI, and will bring significant changes. Provisions for trade receivables will need to be determined using a forward looking approach, which is significantly different from, and more complex in comparison with, the incurred loss model, meaning that new systems and processes may well be needed. For financial institutions, the changes are likely to be very significant and require major changes to internal systems and processes in order to capture the required information. Because of the likely complexity, the IASB formed a Transition Resource Group for Impairment of Financial Instruments (the ITG). Entities, in particular those in the financial services sector, need to be aware of the issues discussed by the ITG and their implications for adoption of the expected loss model.

The hedge accounting requirements of IFRS 9 are also significantly different from those set out in IAS 39, and are designed to align hedge accounting more closely with entities' risk management processes. In practice, it will be significantly more straightforward to apply hedge accounting under the new model and we expect that entities that have previously decided not to hedge account may do so in future. For those entities that have previously applied hedge accounting, there is an option to continue with the approach required by IAS 39. Although this might not initially appear to be an attractive option, in practice some entities have internal systems that are designed for an IAS 39 approach.

The effective date of the fully completed version of IFRS 9 is for periods beginning on or after 1 January 2018 with retrospective application. Early application is permitted.

In addition, there is an option to early adopt the 'own credit' provisions for financial liabilities which have been designated at fair value through profit or loss (FVTPL) under the fair value option without adopting any of the other requirements of IFRS 9. This option was available until 1 January 2018.

Since the issuance of IFRS 9 in July 2014, two amendments to the standard have been made. In September 2016, the IASB issued Applying IFRS 9 '*Financial Instruments*' with IFRS 4 '*Insurance Contracts*' (Amendments to IFRS 4) to address concerns about the different effective dates of IFRS 9 and IFRS 17. These concerns relate mainly to the potential for insurers to produce financial statements that contain two very significant changes in accounting in a short period of time, and volatility that might arise in financial statements during the period between the effective date of IFRS 9 and the new insurance standard IFRS 17, due to changes in measurement requirements. The amendments permit either the deferral of the adoption of IFRS 9 for entities whose predominant activity is issuing insurance contracts or an overlay approach which moves the additional volatility created by having non-aligned effective dates from profit or loss to other comprehensive income. An entity choosing to apply the overlay approach retrospectively to qualifying financial assets does so when it first applies IFRS 9. An entity choosing to apply the deferral approach does so for annual periods beginning on or after 1 January 2018.

The second amendment was issued October 2017. The IASB issued Prepayment Features with Negative Compensation (Amendments to IFRS 9) to address the concerns about how IFRS 9 classifies particular pre-payable financial assets. Prepayment Features with Negative Compensation amends the existing requirements in IFRS 9 regarding termination rights in order to allow measurement at amortised cost (or, depending on the business model, at fair value through other comprehensive income) even in the case of negative compensation payments. Under the amendments, whether compensation on prepayment is payable or receivable by the borrower is not relevant. The calculation of this compensation payment must be the same for both the case of an early repayment penalty and the case of an early repayment gain. . The amendments are to be applied retrospectively for fiscal years beginning on or after 1 January 2019 with early application permitted.

The final amendments also contain additional paragraphs in the Basis for Conclusions regarding the accounting for a modification or exchange of a financial liability measured at amortised cost that does not result in the derecognition of the financial liability. The additional paragraphs confirm that an entity recognises any adjustment to the amortised cost of the financial liability arising from a modification or exchange in profit or loss at the date of the modification or exchange. No change was made to any of the associated requirements in IFRS 9, meaning that the accounting approach is required to be adopted at the same point as IFRS 9, being periods beginning on or after 1 January 2018.

For more information on IFRS 9 see:

– BDO *IFR Bulletin* 2014/12 (click ***here***);
– BDO *IFR Bulletin* 2015/17 (click ***here***);
– BDO IFRS In Practice – IFRS 9 *Financial Instruments* (click ***here***).

3.2. IFRS 15 *Revenue from Contracts with Customers*

In May 2014, the IASB published IFRS 15 *Revenue from Contracts with Customers*. The new Standard, which was fully converged with equivalent new US GAAP guidance issued at the same time, contains comprehensive guidance for accounting for revenue and will replace existing requirements which are currently set out in two existing standards (IAS 18 *Revenue* and IAS 11 *Construction Contracts*) and related interpretations (IFRIC 13 *Customer Loyalty Programmes*, IFRIC 15 *Agreements for the Construction of Real Estate*, IFRIC 18 *Transfers of Assets from Customers* and SIC 31 *Revenue – Barter Transactions Involving Advertising Services*). Some minor differences between IFRS and US GAAP were subsequently introduced, due to the IASB and the FASB making slightly different changes to their respective standards.

IFRS 15 contains significantly more prescriptive and precise requirements in comparison with existing standards. In future, revenue will be recognised from the application of the following five steps:

1. Identify the contract;
2. Identify the performance obligation(s);
3. Determine the transaction price;
4. Allocate the transaction price to each performance obligation;
5. Recognise revenue when each performance obligation is satisfied.

The introduction of the new requirements means that for many entities the timing and profile of revenue recognition will change. In some areas the changes will be very significant and will require careful planning, including for commercial effects (such as compliance with bank covenants, performance based remuneration and business combinations). Significant changes to systems and processes may be required in order to comply with the new accounting and significantly enhanced disclosure requirements.

Due to the extent of changes in accounting that will arise from the adoption of IFRS 15, the IASB and the FASB formed a Joint Transition Resource Group for Revenue Recognition (the TRG). This comprised preparers and users of financial statements and auditors, with knowledge and experience of revenue recognition under both IFRS and US GAAP.

As a result of some of the TRG discussions, in April 2016 the IASB issued the following clarifications to the standard:

– Identification of performance obligations;
– Principal vs. agent considerations;
– Licensing agreements;
– Transitional relief.

Although the effective date remains aligned with the equivalent US GAAP guidance, as noted above some of the clarifications issued by the IASB and FASB are not consistent, and the FASB has made some changes where the IASB did not. As a result the standards are no longer fully converged.

For more information see BDO International's *Revenue Recognition Resource Centre* (click ***here***).

3.3. IFRS 16 *Leases*

In January 2016 the IASB issued IFRS 16 *Leases*. IFRS 16 supersedes IAS 17 *Leases*, IFRIC 4 *Determining whether an Arrangement contains a Lease*, SIC-15 *Operating Leases – Incentives* and SIC-27 *Evaluating the Substance of Transactions Involving the Legal Form of a Lease*.

The accounting requirements for lessors have largely been carried forward unchanged from IAS 17. This means that a lessor continues to classify leases as operating or finance. The major changes are for lessees, with IFRS 16 setting out a single model for lessees which eliminates the distinction between operating and finance leases, and results in the statement of financial position reflecting a 'right of use' asset and a corresponding liability for most lease contracts. The asset is subsequently accounted for as property, plant and equipment or investment property and the liability is unwound using the interest rate implicit in the lease. However, entities have an option not to bring onto the statement of financial position short term leases (i.e. those with a term of twelve months or less) and leases of low value items.

As a result, a key question changes from whether a lease is an operating or a finance lease under current guidance, to whether an arrangement gives rise to something that meets the definition of a lease. The scope of IFRS 16 is wide, and some arrangements involving the use of assets that might be viewed as service contracts (which are executory and not recorded in the statement of financial position) may in fact result in a lease within the scope of IFRS 16. Significant changes to systems and processes may be required in order to comply with the new requirements.

For many entities the effect of bringing all leases onto the statement of financial position will be very significant and will require careful planning, including for commercial effects (such as compliance with bank covenants, performance based remuneration and business combinations).

IFRS 16 is converged in certain significant respects with new guidance covering accounting for leases under US GAAP. Convergence has been reached for:

– Definition of a lease;
– Measurement of lease liabilities.

Substantial convergence was reached for a requirement to include almost all leases on balance sheet. However, IFRS 16 contains an exemption for leases of low value assets which is not included in the equivalent US GAAP. Although IFRS 16 does not specify a threshold for what is regarded as 'low value', the discussion in the Basis for Conclusions notes that in 2015 when it reached its decisions about the exemption towards the end of 2015, the IASB had in mind leases of assets which, when new, had a value of USD 5,000 or less.

Other differences relate to a requirement in IFRS 16 for a lessee to reassess variable lease payments which depend on an index or rate when the reference index or rate changes and affects future lease payments (there is no equivalent requirement in US GAAP), the requirements for the recognition of gains and losses arising from sale and leaseback transactions, and in determining the classification of subleases.

There will also be differences between IFRS and US GAAP for the presentation of:

– Lease expenses in the income statement; and
– The cash flow statement.

In the income statement, the application of IFRS 16 will result in a depreciation charge (within operating expenses) and an interest expense. Assuming depreciation is charged on a straight-line basis, the total expense will be higher in the first part of a lease in comparison with later periods, because the lease liability and related interest expense will be higher. Under US GAAP, for leases which meet the existing definition of an operating lease, a single charge will be included within operating results. The depreciation charge will be adjusted in each period so that the periodic expense is the same throughout the lease period.

Consistent with the differences in the income statement presentation, in the cash flow statement under IFRS the cash flows will be split into principal repayments and interest, while under US GAAP the cash flows will appear in a single line item.

IFRS 16 has an effective date of 1 January 2019, with early application permitted only if IFRS 15 has also been adopted.

For more information on IFRS 16 see:

– BDO *IFR Bulletin* 2016/01 (click ***here***);
– BDO IFRS In Practice – IFRS 16 *Leases* (click ***here***).

3.4. IFRS 17 *Insurance Contracts*

In May 2017, the IASB issued IFRS 17 *Insurance Contracts*. The standard establishes the principles for the recognition, measurement, presentation and disclosure of insurance contracts.

The scope of IFRS 17 includes insurance contracts, including reinsurance contracts issued and held by an entity, and investment contracts with discretionary participation features an entity issues provided the entity also issues insurance contracts. In addition, some contracts an entity issues meet the definition of an insurance contract but their primary purpose is the provision of services for a fixed fee. An entity may choose to apply IFRS 15 *Revenue from Contracts with Customers* instead of IFRS 17 to these contracts if certain conditions are met.

Components of the insurance contract that would be within the scope of another standard if they were separate contracts should be identified and accounted for separately from the insurance contract. IFRS 9 *Financial Instruments* is applied to determine whether there are any embedded derivatives to be separated, and if so, how to account for them. IFRS 9 is also applied to investment components that are distinct. Any promises to transfer distinct goods or non-insurance services to a policyholder are separated and accounted for in accordance with IFRS 15.

An entity next identifies portfolios of insurance contracts where the contracts are subject to similar risks and are managed together. The portfolio is then divided into groups consisting of a minimum of:

(a) Contracts that are onerous at initial recognition, if any;

(b) Contracts that at initial recognition have no significant possibility of becoming onerous subsequently, if any; and

(c) The remaining contracts in the portfolio, if any.

In some circumstances, some contracts would fall into different groups because law or regulation does not permit different prices or levels of benefits to be set for policyholders with different characteristics (for example, if an insurer is not permitted to take male and female risk profiles into account when pricing motor insurance policies). In those cases, the contracts can be included in the same group. However, in all cases, contracts issued more than one year apart cannot be grouped together.

On initial recognition an entity is required to measure a group of insurance contracts at the total of:

(a) The fulfilment cash flows (FCF); and

(b) The contractual service margin (CSM).

The FCF comprise estimates of future cash flows (premium collections, and payouts for claims, benefits and expenses), an adjustment to reflect the time value of money (TVM) and the financial risks associated with the future cash flows, and a risk adjustment for uncertainty about the amount and timing of future cash flows that arise from non-financial risk. The CSM represents expected profit for future insurance coverage (unearned profit).

Subsequently, the carrying amount of a group of insurance contracts at the end of each reporting period is the sum of the liability for remaining coverage and the liability for incurred claims. The liability for remaining coverage is comprised of the FCF related to future services and the unearned CSM of the group at that date. The liability for incurred claims comprises the FCF for claims incurred, but not yet paid, at the reporting date.

The standard provides two methods to measure the liability for remaining coverage of a group of insurance contracts. These are the general approach and a simplified premium allocation approach; however, the method that is used is not a free accounting policy choice. An entity is only permitted to use the premium allocation approach if this method is expected to result in the measurement of the liability for remaining coverage not differing materially from the liability that would be calculated using the general model, and the coverage period of each contract in the group is one year or less.

IFRS 17 also explicitly requires claims liabilities to be discounted. This discount is not permitted to be based on the return on the investment portfolio, but must instead be linked to the characteristics inherent in the claims liabilities cash flows (e.g. duration, risk, etc.).

A further requirement that will result in a change in practice for many entities is that policy acquisition costs are netted against insurance liabilities. However, an entity also has the choice of simply expensing all acquisitions costs as incurred, which may simplify accounting.

The effective date for IFRS 17 is 1 January 2021. Early application is permitted, but only if IFRS 9 and IFRS 15 have also been adopted.

A key difference in the transitional provisions of IFRS 17 compared to other recent IFRSs like IFRS 15 and IFRS 16 is that IFRS 17 requires comparative information for the immediately preceding annual reporting period to be restated. So for an insurance entity with a December year end, their 31 December 2021 financial statements will be the first set of financial statements presented under IFRS 17. In order to determine the opening balance as at 1 January 2020, which will be the starting point for the determination of figures for the 31 December 2020 year end, the entity will need to determine its 31 December 2019 statement of financial position under IFRS 17. This will often require significant time and effort, meaning that entities applying IFRS 17 should begin the process early of determining the impact of the new standard on its financial statements.

4. OTHER DEVELOPMENTS – AMENDMENTS TO IFRSs AND INTERPRETATIONS

The IASB has issued a range of amendments to standards and two IFRIC interpretations. Key requirements of the amendments are discussed below.

4.1. Annual Improvements to IFRSs 2014-2016 Cycle

There were three amendments as part of the 2014-2016 Annual Improvements Cycle. These were made to IFRS 1 *First-time Adoption of International Financial Reporting Standards*, IAS 12 *Disclosure of Interests in Other Entities* and IAS 28 *Investments in Associates and Joint Ventures*.

- **IFRS 1**

  A number of short–term exemptions in IFRS 1 were deleted, since the relief provided by these exemptions was no longer applicable.

- **IFRS 12**

  The scope of IFRS 12 was clarified to make it clear that the disclosure requirements in Paragraphs B10 - B16 are not required for interests classified as held for sale or as discontinued operations in accordance with IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*.

- **IAS 28**

  IAS 28 permits an investment in an associate or joint venture to be measured at FVTPL, instead of the equity method being applied, if the investment is held directly or indirectly through a venture capital organisation, unit trust or similar entities. IAS 28 was amended to specify that a qualifying entity may elect to measure investments in associates and joint ventures at FVTPL on an investment-by-investment basis, upon initial recognition.

For more information see IFRB 2016/17 (click ***here***).

4.2. Amendment to IAS 40 – *Transfers of Investment Property*

This amendment states that a 'an entity transfers a property to, or from, investment property when, and only when, there is change in use.' It also clarifies that the following transfers included in IAS 40.57 are examples of evidence that may support a change in use and not the only possible circumstances in which there is a change in use:

- Commencement of owner-occupation, or of development with a view to owner-occupation, for a transfer from investment property to owner-occupied property;
- Commencement of development with a view to sale, for a transfer from investment property to inventories;
- End of owner-occupation, for a transfer from owner-occupied property to investment property; and
- Inception of an operating lease to another party, for a transfer from inventories to investment property.

For more information see IFRB 2016/17 (click ***here***).

4.3. Amendment to IAS 28 – *Long-term Interests in Associates and Joint Ventures*

This amendment clarifies that IFRS 9, including its impairment requirements, applies to long-term interests in associates and joint ventures. Furthermore, in applying IFRS 9 to long-term interests, an entity does not take into account adjustments to their carrying amount that are or may also be required by IAS 28 (i.e. adjustments to the carrying amount of long-term interests arising from the allocation of losses of the investee or assessment of impairment in accordance with IAS 28). The amendment is accompanied by an example illustrating how the requirements of IAS 28 and IFRS 9 interact.

4.4. Annual Improvements to IFRSs 2015-2017 Cycle

There were four amendments as part of the 2015-2017 Annual Improvements Cycle. These were made to IFRS 3 *Business Combinations* and IFRS 11 *Joint Arrangements*, IAS 12 *Income Taxes* and IAS 23 *Borrowing Costs*.

– **IFRS 3**

  A company remeasures its previously held interest in a joint operation when it obtains control of the business.

– **IFRS 11**

  A company does not remeasure its previously held interest in a joint operation when it obtains joint control of the business.

– **IAS 12**

  A company accounts for all income tax consequences of dividend payments in the same way.

– **IAS 23**

  A company treats as part of general borrowings any borrowing originally made to develop an asset when the asset is ready for its intended use or sale.

The amendments are effective from 1 January 2019, with early application permitted.

For more information see IFRB 2017/16 (click ***here***).

4.5. IFRIC Interpretation 22 – *Foreign Currency Transactions and Advance Consideration*

IFRIC 22 addresses how to determine the date of transaction for the purpose of determining the spot exchange rate used to translate foreign currency transactions on initial recognition in circumstances when an entity pays or receives some or all of the foreign currency consideration in advance of the recognition of the related asset, expense or income.

The interpretation states that the date of the transaction for the purpose of determining the exchange rate to use on initial recognition of the related asset, expense or income (or part of it) is the date on which an entity initially recognises the non-monetary asset or non-monetary liability arising from the payment or receipt of advance consideration. In other words, the related income, expense or asset should not be remeasured for changes in exchange rates occurring between the date of initial recognition of the advance consideration and the date of recognition of the transaction to which that consideration relates.

For more information see IFRB 2016/16 (click ***here***).

4.6. IFRIC Interpretation 23 – *Uncertainty over Income Tax Treatments*

IFRIC 23 clarifies how to apply the recognition and measurement requirements in IAS 12 when there is uncertainty over income tax treatments, addressing four specific issues:

- Whether an entity considers uncertain tax treatments separately;
- The assumptions an entity should make about the examination of tax treatments by taxation authorities;
- How an entity determines taxable profit or loss, tax bases, unused tax losses, unused tax credits and tax rates; and
- How an entity considers changes in facts and circumstances.

IFRIC 23 also provides disclosure requirements for uncertain tax positions.

For more information see IFRB 2017/08 (click ***here***).

4.7. Amendment to IAS 19 – *Employee Benefits*

In February 2018 *Plan Amendment, Curtailment or Settlement* (Amendments to IAS 19) was issued. The amendment specifies how entities determine pension expenses when changes to a defined benefit pension plan occur during an annual reporting period.

IAS 19 *Employee Benefits* requires an entity to remeasure its net defined benefit liability or asset, but had not specified how to determine the expenses for the period after the date of change to the plan. The amendment provides clarification by requiring the use of the updated assumptions from this remeasurement to determine current service cost and net interest for the remainder of the reporting period after the date of change to the plan.

The amendments are effective on or after 1 January 2019.

5. IASB PROJECTS IN PROGRESS

The IASB has a number of projects in progress, with the most significant for which *Discussion Papers* or *Exposure Drafts* have been issued being the *Conceptual Framework* and the *Disclosure Initiative*.

5.1. Conceptual Framework

In July 2013 the IASB released Discussion Paper DP/2013/1 A *Review of the Conceptual Framework for Financial Reporting*. In May 2015 the IASB published Exposure Draft ED/2015/3 *Conceptual Framework for Financial Reporting* which takes into account the feedback received on the Discussion Paper.

In November 2016 the IASB issued a *Staff Paper* outlining where and how the proposals in the 2015 Exposure Draft would change as a result of the IASB's tentative decisions to date.

In October 2017 the IASB met to discuss comments on the pre-ballot draft of the revised *Conceptual Framework* for Financial Reporting (*Conceptual Framework*) that will provide a more complete, clear and updated set of concepts to use when the Board develops or revises IFRS Standards.

The Board expects to publish the *Conceptual Framework* and to update references to the *Conceptual Framework in IFRS Standards* in March 2018.

5.2. Disclosure Initiative

The *Disclosure Initiative* was introduced by the IASB in order to explore the potential for the improvement of disclosures in financial statements. It is comprised of the following separate projects of which the current status and the next steps are summarised below:

Standard-setting projects

- *IAS 1 Amendments* **–** The IASB published the final amendments in December 2014 and they became mandatorily effective for annual periods beginning on or after 1 January 2016.
- *Reconciliation of liabilities from financing activities* – In 2016 the IASB published amendments to IAS 7 which were mandatorily effect for annual periods beginning on or after 1 January 2017.
- The IASB issued the IFRS Practice Statement *Making Materiality Judgements* on 14 September 2017. The objective of this IFRS Practice Statement is to assist management in presenting financial information about the entity that is useful to existing and potential investors, lenders and other creditors in making decisions about providing resources to the entity. A Practice Statement is not a Standard and its application is not required in order to state compliance with IFRS. However, the IASB has noted that a jurisdiction that permits or requires IFRS could choose to formally adopt a Practice Statement into its national financial reporting requirements.
- The IASB issued Exposure Draft ED/2017/6 *Definition of Material (Proposed amendments to* IAS 1 *and* IAS 8*)* on 14 September 2017 to clarify the definition of 'material' and to align the definition used in the *Conceptual Framework* and the standards themselves.
- An Exposure Draft ED/2017/5 *Accounting Policies and Accounting Estimates (Proposed amendments to* IAS 8) was published on 12 September 2017. The Board proposed clarifying the distinction between a change in accounting policy and a change in an accounting estimate – the two are accounted for differently.

The comment period for both of these exposure drafts closed on 15 January 2018, and the IASB is currently scheduled to discuss feedback in March 2018.

Research projects

- *Principles of Disclosure* – A Discussion Paper *Disclosure Initiative* – Principles of Disclosure was published 30 March 2017.
- *Standards-level review of disclosure* – Research for conflicts, duplications and overlaps in existing Standards. The project is being informed by the results of the *Principles of Disclosures* project.

5.3. IASB Workplan

The following is a complete list of research projects at 31 December 2017:

Project	Next Milestone	Expected Date
Business Combinations under Common Control	Discussion Paper	H2 2018
Discount Rates	Research Summary	Q2 2018
Dynamic Risk Management	Discussion Paper	H2 2019
Financial Instruments with Characteristics of Equity	Discussion Paper	Q2 2018
Goodwill and Impairment	Discussion Paper or Exposure Draft	Q2 2018
Post-implementation Review of IFRS 13 *Fair Value Measurement*	Request for Information Feedback	To be determined
Primary Financial Statements	Discussion Paper or Exposure Draft	Q2 2018
Principles of Disclosure	Discussion Paper Feedback	March 2018
Share-Based Payment	Research Summary	Q2 2018

The following is a complete list of standard-setting projects at 31 December 2017:

Project	Next Milestone	Expected Date
Conceptual Framework	Conceptual Framework	March 2018
Definition of Material (Amendments to IAS 1 and IAS 8)	Exposure Draft Feedback	March 2018
Management Commentary	Exposure Draft	To be determined
Rate-regulated Activities	Discussion Paper or Exposure Draft	H1 2019

The following is a complete list of maintenance projects at 31 December 2017:

Project	Next Milestone	Expected Date
Accounting Policies and Accounting Estimates (Amendments to IAS 8)	Exposure Draft Feedback	March 2018
Accounting Policy Changes (Amendments to IAS 8)	Exposure Draft	March 2018
Availability of a Refund (Amendments to IFRIC 14)	IFRS Amendment	Q2 2018
Classification of Liabilities (Amendments to IAS 1)	IFRS Amendment	H2 2018
Definition of a Business (Amendments to IFRS 3)	IFRS Amendment	Q2 2018
Fees in the '10 per cent' test for Derecogntion (Amendments to IFRS 9)	Exposure Draft	To be determined
Improvements to IFRS 8 Operating Segments (Amendments to IFRS 8 and IAS 34)	Decide Project Direction	January 2018
Plan Amendment, Curtailment or Settlement (Amendment to IAS 19)	IFRS Amendment	To be determined
Property, Plant and Equipment: Proceeds before Intended Use (Amendments to IAS 16)	IFRS Amendment	To be determined
Subsidiary as a First-time Adopter (IFRS 1)	Exposure Draft	To be determined

6. CONCLUSION

The coming years will bring very significant changes to accounting requirements, which will affect the financial statements of almost every entity that reports in accordance with IFRS, in particular changes introduced by IFRSs 9, 15,16 and 17. For IFRSs 9 and 15, if implementation projects are not already well under way or close to completion, there is a considerable risk that they will not be adopted satisfactorily and that investors, lenders and other users of financial statements will not be adequately informed in advance of the related effects.

As we progress through the 2017 year end reporting season, this is the time to discuss how the changes will affect your organisation with your BDO contact.

CONTACT

For further information about how BDO can assist you and your organisation, please get in touch with one of our key contacts listed below.

Alternatively, please visit **www.bdointernational.com/Services/Audit/IFRS/IFRS Country Leaders** where you can find full lists of regional and country contacts.

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