GAAP v IFRS – illustrative presentation

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Prepared by: **David Potts FCA**
DMP Training Limited

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1. IFRS for SMEs

Scope of the IFRS

The IFRS contains a definition of SMEs that are considered to be within the scope of the Standard. The IASB recognise that the definition that they apply may not be same as used under local law and other similar regulations.

Two aspects of the legal framework as applied in the UK are not present within the IFRS definition:

(i) A scope application based on a quantitative criteria, such as a turnover or total assets; and
(ii) An application regardless of the purpose for which the accounts are to be used.

The IASB recognise that these two issues may mean that the IFRS for SMEs is not currently legally acceptable in certain countries (such as the UK). Revisions to the Companies Act will be a matter for politicians and not the IASB.

The IFRS is intended to be used by SMEs defined in the IFRS as follows:

(a) Do not have **public accountability**; and
(b) Publish **general purpose financial statements** for external users. Examples of external users include owners who are not involved in managing the business, existing and potential creditors, and credit rating agencies.

Public accountability exists if:

- Debt or equity instruments are traded in a public market or are in the process of being traded in a public market.
- Public markets include local and foreign stock exchanges or an over-the-counter market (including local and regional markets.
- It holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses. This would cover banks, credit unions, insurance companies, securities brokers/dealers, mutual funds and investment banks. Entities that hold assets incidental to the primary business, such as travel and real estate agents, schools, charitable organisations, co-operative organisations and holders of trade deposits are not precluded from using the IFRS.

Publicly accountable entities are not allowed to use the IFRS for SMEs and describe the accounts as conforming to the IFRS for SMEs. Subsidiaries whose parent uses full IFRS, or that is part of a consolidated group that uses IFRS are not prohibited from using this

IFRS (as long as they are not publicly accountable as an entity them selves.

Users of the IFRS for SMEs must still conform to the same concepts and pervasive principles as used in the application of full IFRS. Including guidance on such as:

- Objectives of the financial statements
- Qualitative characteristics of items contained; such as understandable, relevant, material, reliable, substance over form, prudence, complete, comparable, timely and considering benefit over cost.
- Financial position reporting assets, liabilities and equity as defined and performance reporting income and expenses as defined.
- Measurement applying either historic cost or fair value.
- The accrual basis of accounting must be used.

The accounts are prepared applying the IFRS for SMEs. There is no requirement to consider the requirements of full IFRS when deciding on a suitable accounting policy of the application of a principle.

1.2 Presentation of financial statements

As with full IFRS and unlike statutory GAAP, the IFRS for SMEs contains requirements for the presentation of accounts but does not include pro-forma statements to be applied word for word.

Published separate to the IFRS for SMEs is a separate booklet containing illustrative financial statements and a presentation and disclosure checklist.

The following pervasive principles apply to the presented statements:

- Compliance with the IFRS for SMEs is deemed to produce accounts that present a fair presentation in accordance with the main IFRS concept.
- The use of the IFRS for SMEs by an entity with public accountability does not achieve a fair presentation.
- The financial statements must make an explicit and unreserved statement of compliance with the IFRS for SMEs, compliance must be 100% if this statement is made.
- Any departure from the IFRS would only be acceptable in extremely rare circumstances and if certain, appropriate disclosures were made.
- The going concern concept must be applied unless it is not appropriate. If any uncertainty exists the management must review the foreseeable future which is a period of at least 12 months from the balance sheet date. Any material uncertainties casting significant doubt on the application of this basis must be disclosed.

A complete set of financial statements shall include all of the following:

(a) A statement of financial position as at the reporting date.
(b) Either:
    a. A single statement of comprehensive income displaying all items of income and expense recognised during the period determining the profit and loss (sub-total) and items of other comprehensive income, or
    b. A separate income statement and a separate statement of comprehensive income which starts by stating the recognised profit or loss for the period.
(c) A statement of changes in equity for the reporting period.
(d) A statement of cash flows for the reporting period.
(e) Notes comprising:
    a. Summary of significant accounting policy; and
    b. Other explanatory material.

The IFRS for SMES does not cover disclosures of segmental information, interim information or EPS should the SME choose to disclose such details.

Statement of financial position

As a minimum must contain:

(a) cash and cash equivalents
(b) trade and other receivables
(c) financial assets
(d) inventories
(e) property, plant and equipment
(f) investment property carried at fair value through profit and loss
(g) intangible assets
(h) biological assets carried at cost
(i) biological assets carried at fair value
(j) investments in associates
(k) investments in jointly controlled entities
(l) trade and other payables
(m) financial liabilities
(n) liabilities and assets for current tax
(o) deferred tax liabilities and deferred tax assets (always classified as non-current)
(p) provisions
(q) non-controlling interest presented within equity but separate from the equity attributable to the owners of the parent
(r) equity attributable to the owners of the parent

Information should be split between current and non-current and additional headings may be added if necessary. The IFRS does not prescribe a sequence to be used for presentation.

Information to be presented either on the face of the statement of position or in the notes:

(a) Classifications of property, plant and equipment as appropriate to the entity

(b) Trade and other receivables showing separately related parties, other parties and accrued income not yet billed.
(c) Inventories – showing held for sale, in the process of production and materials and supplies to be consumed.
(d) Trade and other payables
(e) Provisions for employee benefits and other provisions
(f) Classes of equity held

Considerable additional details are required relating to equity instruments issued and assets held for sale (disposal assets).

Total comprehensive income

This statement must show as a minimum:

(a) Revenue
(b) Finance costs
(c) Share of profit or loss of investments in associates and jointly controlled entities accounted for using the equity method
(d) Tax expense
(e) Post tax profit and loss of discontinued operations plus the gain and loss on the disposal of the net assets of the operation
(f) Profit or loss
(g) Each item of other comprehensive income
(h) Share of other comprehensive income of associates and jointly controlled entities
(i) Total comprehensive income

Expenses shall be presented and analysed either by function or by type of expense.

Statement of changes in equity

This statement must show:

(a) Total comprehensive income for the period – as attributable to the owners and to non-controlling interests.
(b) For each component of equity the effect of any restatement recognised in respect of prior period adjustments
(c) For each component of equity a reconciliation of the opening and closing amount detailing the effect of:
    a. Profit and loss
    b. Other comprehensive income
    c. Transactions with shareholders
        i. Dividends
        ii. Issues of shares
        iii. Treasury share transactions
        iv. Other distributions to owners
        v. Changes in subsidiary ownership not resulting in a loss of control

Statement of income and retained earnings

As an alternative to the statement of comprehensive income and changes in equity an entity may present a statement of income and retained earnings.

This can only be applied when the only changes in equity are as follows:

- Profit or loss
- Payment of dividends
- Correction of prior period errors
- Changes in accounting policy

Statement of cash flows

This statement must always be shown. It will reconcile movements in cash and cash equivalents. Cash equivalents include short-term, highly liquid investments held to meet short-term cash commitments rather than for investment. They will usually have less than three months to maturity on acquisition.

Bank overdrafts may be included in financing activities except if they are repayable on demand and are an integral part of the entity's cash management then they are a component of cash and cash equivalents.

The entity may prepare the cash flow using either the direct or the indirect method.

Other notes

The financial statements must include the disclosures required elsewhere in the IFRS for SMEs. They should also include disclosures about:

- Accounting policies
  - o Measurement basis or bases
  - o Other policies necessary or relevant to understanding
- Information about judgements
- Key sources of estimation uncertainty

2. Presentation example

2.1 Presentation of net income required under IAS 1 revised

XYZ Limited
Statement of comprehensive income for the year ended 31 December 2007

	Notes	2007	2006
		£	£
Revenue*			
Cost of goods sold			
Gross profit			
Other income			
Distribution costs			
Administrative expenses			
Other expenses			
Share of profit from associates and joint ventures*			
Finance costs*			
Profit before tax*			
Income tax expense*			
Profit for the year from continuing operations*			
Loss for the year from discontinued operation			
Profit for the year*			
Profit attributable to:			
Owners of the parent			
Minority interest			

* = headings that must be shown on the face of the income statement.

2.2 Presentation of the balance sheet

XYZ Group
Statement of financial position as at 31 December 2007

	Notes	2007 £	2006 £
Assets			
Non-current assets			
Property, plant and equipment			
Goodwill			
Other intangible assets			
Investment in associates			
Available for sale financial assets			
Current assets			
Inventories			
Trade receivables			
Other current assets			
Cash and cash equivalents			
Total assets			
Equity and liabilities			
Equity attributable to owners of the parent			
Share capital			
Retained earnings			
Other components of equity			
Minority interests			
Total equity			
Non-current liabilities			
Long-term borrowings			
Deferred tax			
Long term provisions			
Total non-current liabilities			
Current liabilities			
Trade and other payables			
Short-term borrowings			
Current portion of long term borrowings			
Current tax payable			
Short term provisions			
Total current liabilities			
Total liabilities			
Total liabilities and equity			

Points to note:

- Current does not equal one year, it can be the length of the usual business cycle (if longer than one year).
- Layout – assets are listed in order of increasing liquidity followed by the liabilities, sub-headings for ‘net current assets’ and ‘total assets less current liabilities’ are not given.
- Provisions are not given a separate heading; they are included under current and non-current liabilities. The same applies to deferred tax provisions.

2.3 Statement of comprehensive income

XYZ Group
Statement of comprehensive income for the year ending 31 December 2007

	2007 £	2006 £
Profit for the year		
Other comprehensive income:		
Exchange differences on translating foreign operations		
Available for sale financial assets		
Cash flow hedges		
Gains on property revaluation		
Actuarial gains (losses) on defined benefit pension plans		
Share of other comprehensive income of associates		
Income tax relating to components of other comprehensive income		
Other comprehensive income for the year net of tax		
Total comprehensive income for the year		
Total comprehensive income attributable to:		
Owners of the parent		
Minority interest		

2.4 Reporting cash flows

Numbers not provided as not part of the IAS 1 example

XYZ Group
Consolidated Cash Flow Statement for the year ended 31st December 2007

I		**2007**		2006
	£	**£**	£	£
Operating activities				
Net profit of consolidated companies	**X**		X	
Depreciation of tangible fixed assets	**X**		X	
Impairment of tangible fixed assets	**X**		X	
Amortisation of goodwill	**X**		X	
Depreciation of intangible assets	**X**		X	
Impairment of goodwill	**X**		X	
Increase/(decrease) in provisions and deferred taxes	**X**		x	
Decrease/(increase) in working capital	**X**		X	
Other movements	**X**		X	
Operating cash flow		**X**		X
Investing activities				
Expenditure on tangible fixed assets	**X**		X	
Expenditure on intangible assets	**X**		X	
Sale of tangible fixed assets	**X**		X	
Acquisitions	**X**		X	
Disposals	**X**		X	
Income from associated companies	**X**		X	
Other movements	**X**		X	
Cash flow from investing activities		**X**		X
Financing activities				
Dividend for the previous year	**X**		X	
Purchase of treasury shares (net)	**X**		X	
Premium on warrants issued	**X**		X	
Movements with minority interests	**X**		X	
Bonds issued	**X**		X	
Bonds repaid	**X**		X	
Increase/(decrease) in other medium/long term financial liabilities	**X**		x	
Increase/(decrease) in short term financial liabilities	**X**		X	
Decrease/(increase) in marketable securities and other liquid assets	**X**		x	
Decrease/(increase) in short term investments	**X**		x	
Cash flow from financing activities		**X**		X

Translation differences on flows		**X**		X
Increase/(decrease) in cash and cash equivalents		**X**		X
Cash and cash equivalents at the beginning of the year	**X**		x	
Effects of exchange rate changes on opening balance	**X**		x	
Cash and cash equivalents retranslated at beginning of year		**X**		X
Cash and cash equivalents at end of year		**X**		X

3. IFRS presentation example

3.1 Example

Given the following list of balances and using the blank pro-formas, you should prepare the following primary statements:

1. A statement of financial position; and
2. Statement of comprehensive income

Account name	**$,£, €**	**$,£ €**
Property plant and equipment - cost	550,700	
Property plant and equipment – accumulated depreciation		200,000
Goodwill acquired	80,800	
Customer lists acquired	227,470	
Investment in associate	100,150	
Quoted investments – available for sale	142,500	
Inventories	135,230	
Trade receivables	101,600	
Provision for bad debts		10,000
Loan to directors	25,650	
HSBC – current account	312,400	
Trade payables		115,100
HSBC credit facility – renewal 2011		150,000
Corporate tax payable (9 months from y/e)		35,000
HSBC term loan – (10,000 in < 1 year)		130,000
Deferred tax liabilities		28,800
Potential warranty claims (5,000 , 1 year)		33,850
Share capital		650,000
Profit and loss		161,700
Other equity reserves		21,200
Minority interest		48,600
Gross sales revenues		390,000
Cost of goods sold	245,000	
Rental income		20,667
Carriage costs and shipping	9,000	
Admin expenses	20,000	
Professional fees	2,100	
Interest payable on loans	8,000	
Share of profits of associate		35,100
Income and deferred tax expense	40,417	
Exchange gain for foreign subsidiaries		6,000
Losses on investments – available for sale	9,000	
Loss on property revaluation	11,000	
Dividends payable and paid	15,000	
Total	2,036,017	2,036,017

