20.4-03.6.2021

Nina Sormunen Ph.D.(Econ.)

Email nina.sormunen@aalto.fi

Course schedule

Date		Time	Topics	Standards	
20.4.2021	Tuesday	17.15-20.00	Welcome!	Conceptual Framework	
			Introduction to IFRS	IAS 1 - Presentation of financial statements	
			Conceptual Framework	IFRS 13 - Fair value measurement	
			Fair value measurement	IFRS 8 - Operating segments	
			Operating segments		
22.4.2021	Thursday	17.15-20.00	Revenue and Leases	IFRS 15 - Revenue from Contracts with Customers	
				IFRS 16 - Leases	
27.4.2021	Tuesday	17.15-20.00	Assets	IAS 38 - Intangible assets	
				IAS 36 - Impairtment of assets	
				IFRS 5 - Discontinued operations	
4.5.2021	Tuesday	17.15-20.00	Liabilities	IAS 37 - Provisions, contingent liabilities and contingent assets	
				IAS 19 - Employee benefits	
				IFRS 2 - Share based payments	
11.5.2021	Tuesday	17.15-20.00	Business combinations	IFRS 3 - Business Combinations	
			Financial instruments and income taxes	IFRS 10 - Consolidated financial statements	
				IAS 12 - Income taxes	
				IFRS 9 - Financial instruments	
18.5.2021	Tuesday	17.15-20.00	Associates and Joint Arrangements	IAS 7 - Statement of Cash Flows	*Attendance is mandatory*
			Cash flow statement	IAS 28 - Investments in associates and joint ventures	*Guest speaker from PWC*
			Exam preparation	IFRS 11 - Joint arrgangements	*Guest speaker from EY*
20.5.2021	Thursday	17.15-20.00	Term Paper presentations & discussion		*Attendance is mandatory*
25.5.2021	Tuesday	17.15-20.00	Term Paper presentations & discussion		*Attendance is mandatory*
3.6.2021	Thursday	09.00-10.30	Exam 1		

IFRS 3 Business Combinations

Textbook: Chapters 6, 18

Learning objectives

- Scope and definitions of IFRS 3
- Explain Business Combinations step-by-step model

Overview of IFRS 3

- What it does:
- IFRS 3 clarifies ***how to identify business combination.***
- It prescribes ***the acquisition method*** in accounting for business combination.
- Applying the acquisition method comprises ***4 steps:***

1. Identifying the acquirer.
2. Determining the acquisition date.
3. Recognizing and measuring the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquiree.
4. Recognizing and measuring goodwill or a gain from a bargain purchase.

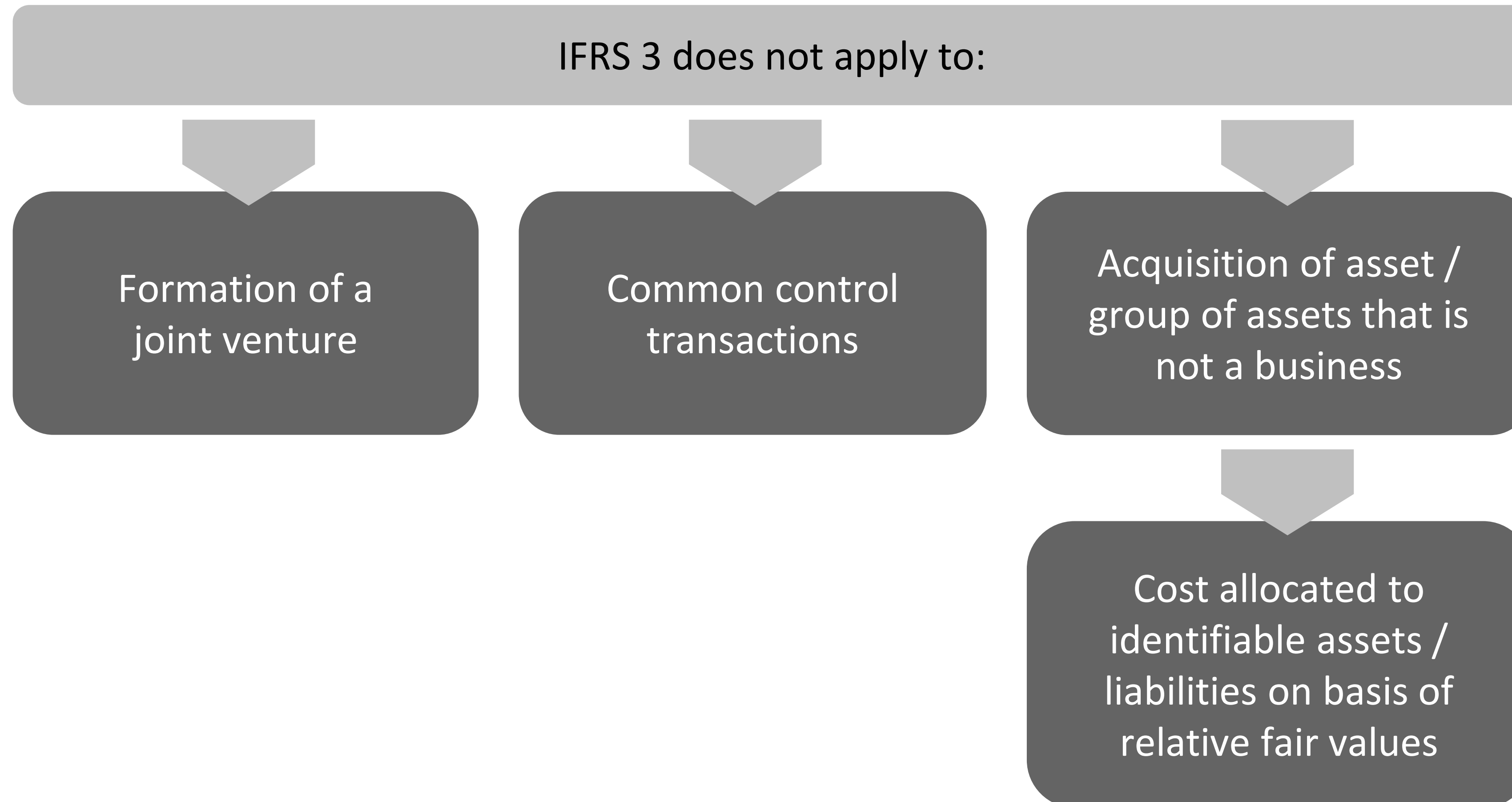
- IFRS 3 sets out the details for all of these steps.
- IFRS 3 gives also ***additional guidance*** for applying the acquisition method to particular types of business combinations, such as achieved in stages or achieved without the transfer of consideration.
- It prescribes the rules for ***subsequent measurement*** and accounting and defines all the necessary ***disclosures.***

When does IFRS 3 apply?

IFRS 3 applies to all business combinations

IFRS 3: ”A business combination should be accounted for by applying the acquisition method. The acquirer recognises the acquiree’s identifiable assets, liabilities and contingent liabilities at their fair values at the acquisition date and also recognises goodwill”.

When does not IFRS 3 apply?



What is a business?

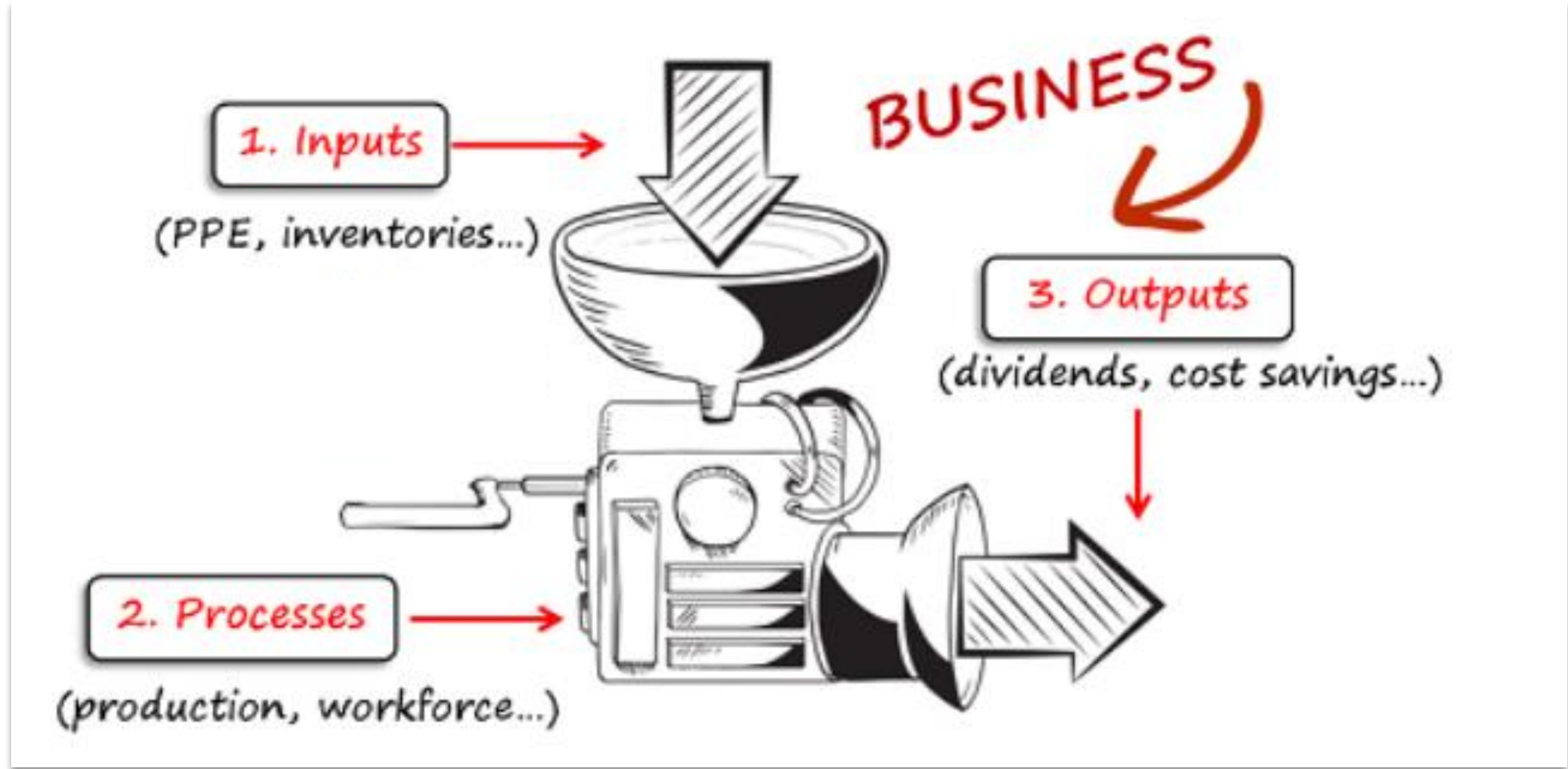
A *business* is an integrated set of activities and assets capable of being managed to provide a return to investors via dividends,
lower costs or other economic benefits

Inputs

Processes

Ability to create outputs

Rebuttable presumption that a group of assets
in which goodwill is present is a business


BUSINESS
1. Inputs
(PPE, inventories...)
2. Processes
(production, workforce...)
3. Outputs
(dividends, cost savings...)

Case

- Which of the following transactions are in the scope of IFRS 3 and why?
  A. Company A purchases a building from Company B
  B. Company A purchases 100 % of shares in Company C
  C. Company A purchases a development project, e.g. test results, rights
  D. Company A purchases a development company with only one development project
  E. Company A purchases Company B. The owners are the same.

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Step – by – step

What is a business combination	A *business combination* is a transaction or other event in which an acquirer obtains *control* of one or more *businesses*
Step 1:	Identify the acquirer
Step 2:	Identify the date for obtaining control
Step 3:	Recognition and measurement of assets acquired and liabilities assumed
Step 4:	Determine the consideration transferred
Step 5:	Measure non-controlling interest (NCI)

IFRS 3

Step – by – step

Step 6:	Determine goodwill or negative goodwill, including allocation
Step 7:	Recognise any adjustment in the allowed adjustment period

STEP 1
Identify the acquirer

The *acquirer* is the entity that obtains control of the business

Use IFRS 10 to determine who has control

Consider additional factors identified in IFRS 3

- Relative voting rights in combined entity
- Existence of large minority voting interest in combined entity
- Composition of governing body and senior management of combined entity
- Terms of exchange of equity instruments
- Relative size of entities

Normally Group Accounting will determine the acquirer

STEP 2
Determine the acquisition date

The *acquisition date* is the date on which acquirer obtains control of acquiree

Date on which fair values of identifiable assets acquired and liabilities assumed determined and goodwill is measured

Date from which comprehensive income of acquiree is included in consolidated financial statements of acquirer

Normally Group Accounting will determine the acquisition date

Determine the acquisition date
Case

- Based on the information below, please assess the acquisition date to be used for accounting purposes.

A. Letter of intent is signed on 1 January 2019
B. Sale and purchase agreement (SPA) is signed on 15 September 2019
C. According to the contract, the sale will be effective as of 1 January 2020, the expected date of closing
D. Payment of 90% of the purchase price is due 15 days after the SPA has been signed and the remaining 10% 15 days after closing

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Same scenario as before but according to the SPA, the sale is effective as of 1 January 2019, the same date as letter of intent was signed. Does this change the conclusion?

Answer: No it does not. The answer is C.

- It cannot be artificially backdated or otherwise altered, for example, by the inclusion of terms in the agreement indicating that the acquisition is to be effective as of an earlier date, with the acquirer being entitled to profits arising after that date, even if the purchase price is based on the net asset position of the acquiree at that date.

Determine the acquisition date
Case

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  C. According to the contract, the sale will be effective as of 1 January 2020, the expected date of closing
  D. Payment of 90% of the purchase price is due 15 days after the SPA has been signed and the remaining 10% 15 days after closing

Same scenario as above but the contract is contingent upon approval from the competition authorities. Does this change the conclusion?

Answer: Yes it does. Until there is an approval, it is unlikely that control could have been obtained prior to the approval. (keeping in mind the nature of an approval)

- Where the offer is conditional upon receiving some form of regulatory approval, then it will depend on the nature of that approval.
- Where it is a substantive hurdle (block), such as obtaining the approval of a competition authority, it is unlikely that control could have been obtained prior to that approval.
- However, where the approval is merely a formality, or 'rubber-stamping' exercise, then this would not preclude control having been obtained at an earlier date.

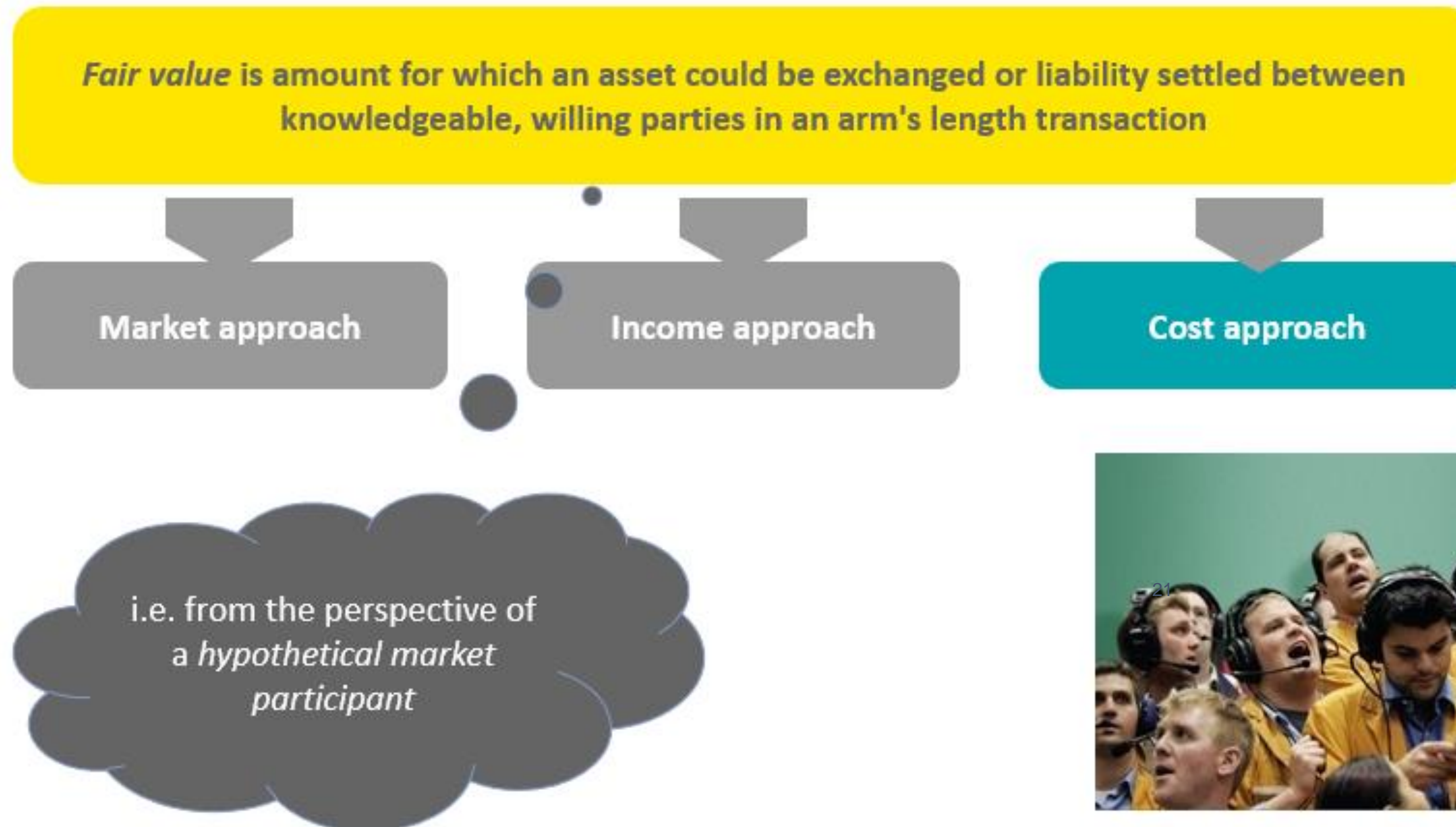
STEP 3

Recognition and measurement of assets acquire and liabilities assumed

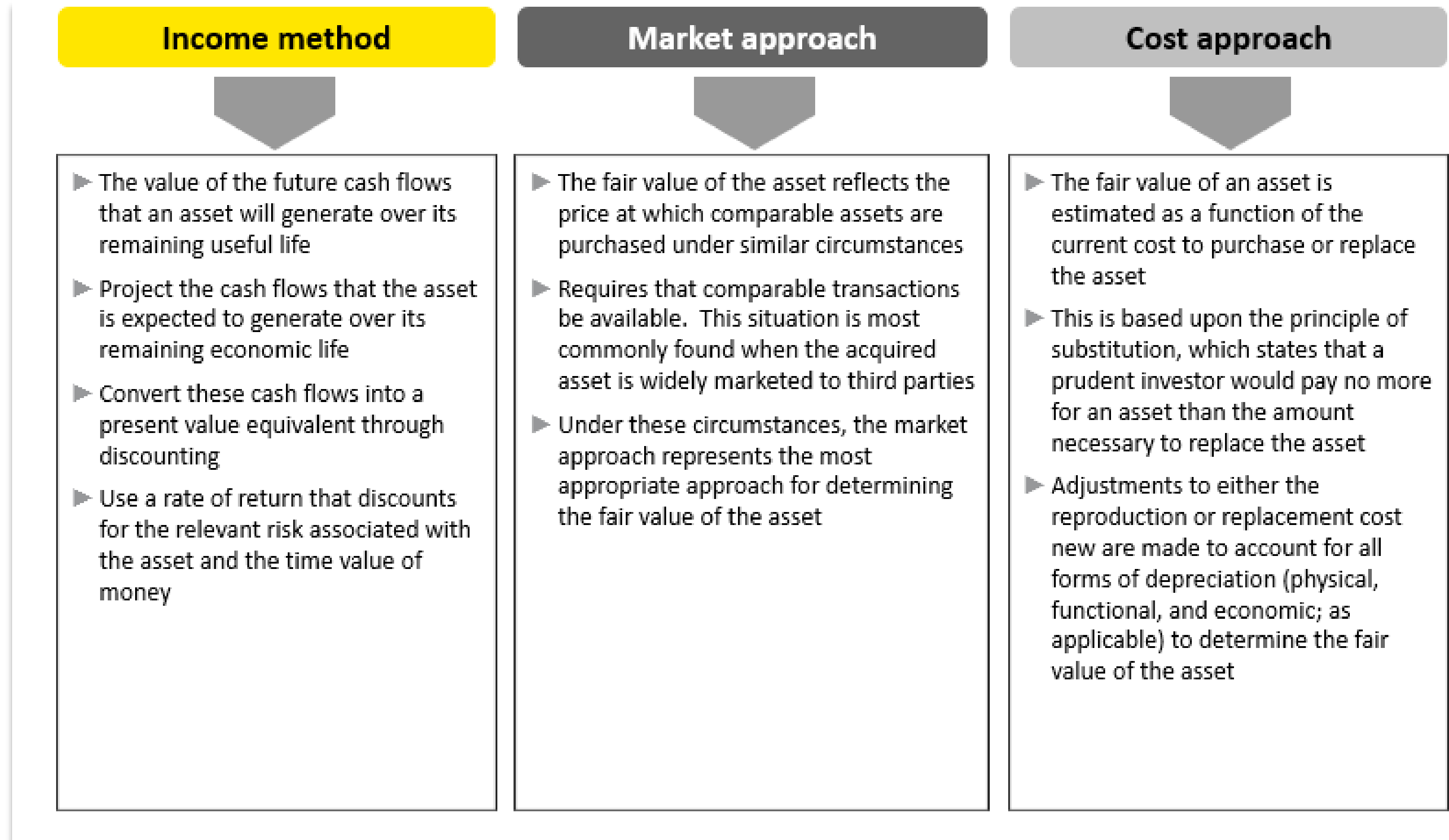
Acquired assets and liabilities

- An acquirer or investor shall recognize all identifiable assets acquired, liabilities assumed and non-controlling interests in the acquiree separately from goodwill.
- Made at acquisition date
- All assets and liabilities are measured at acquisition-date fair value.
- However, some exceptions apply.

Fair value measurement in a business combination (IFRS 13)



Overview of valuation methods used in practice



STEP 4
Identify and measure consideration transferred

Consideration transferred is measured at fair value at the acquisition date and includes:

- **Assets transferred**
- **Liabilities incurred to previous owners**
- **Equity instruments issued**

Acquisition-related costs excluded from consideration transferred, and expensed as incurred

Costs related to issue of equity or debt recognised in accordance with financial instruments standards

Cost of acquisition

Case

What would be the cost of acquisition when Entity N acquires Entity M?

Entity N acquires Entity M. The outflows of economic benefits from Entity N in respect of this transaction are as follows:

a) Entity N issues 1000 new shares to shareholders of Entity M with terms equivalent to those traded on the market. The market price of Entity N's shares is CU4.
b) Entity N pays CU1000 in cash to the previous shareholders of Entity M.
c) Entity N has an acquisition department, which incurred CU200 in running costs over the period of completing the business combination. Staff in the department estimate they have spent 25% of their time on the acquisition of Entity M over this period.
d) Entity N incurs liability of CU500 to a customer of Entity M in respect of termination of a supply agreement that was necessitated by the business combination.
e) Entity N will incur expenditure of CU200 on updating Entity M's accounting systems to be consistent with those used by Entity N.
f) Entity N pays accounting fees in relation to the transaction of CU200 and legal fees of CU200.

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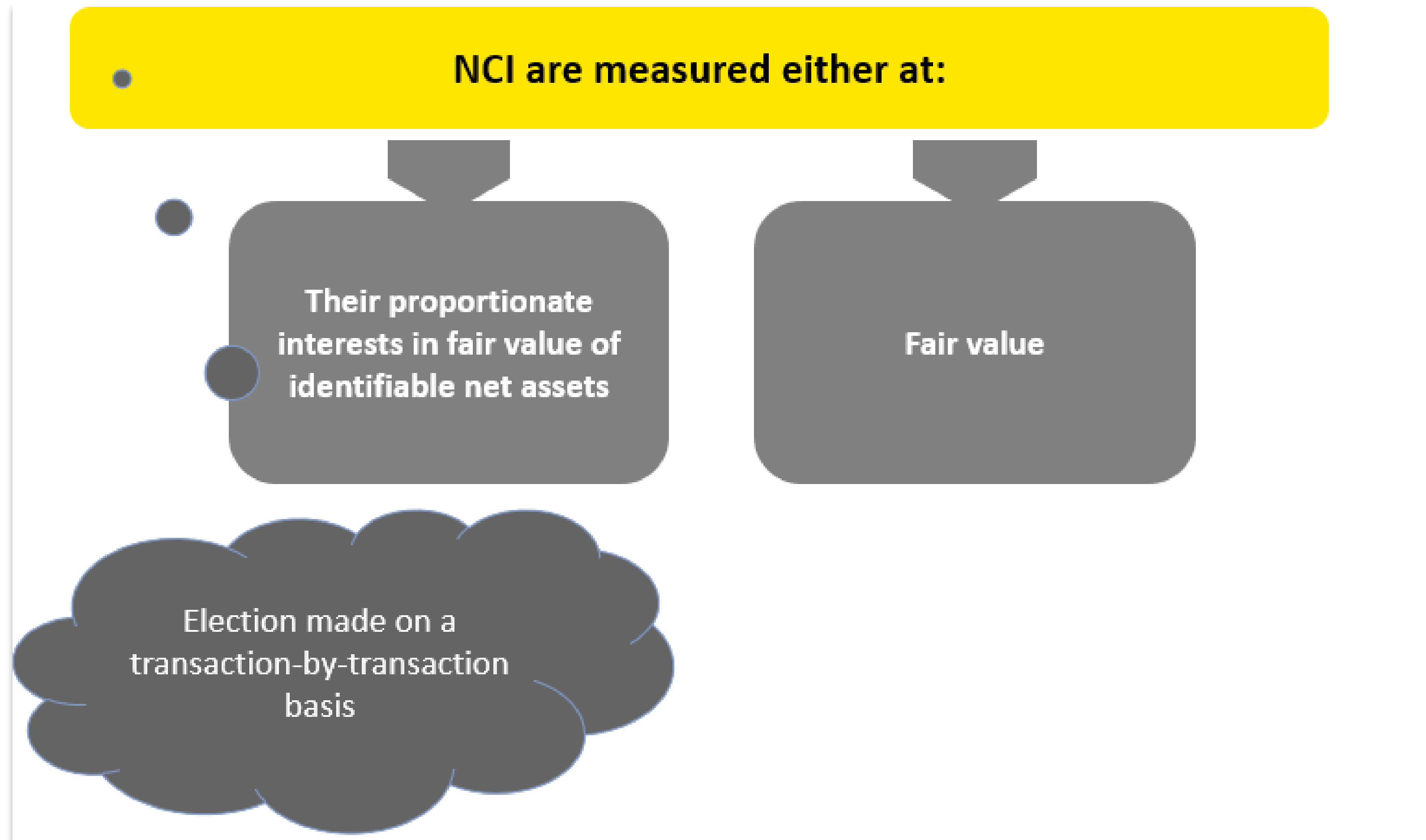
  e) Entity N will incur expenditure of CU200 on updating Entity M's accounting systems to be consistent with those used by Entity N.
  f) Entity N pays accounting fees in relation to the transaction of CU200 and legal fees of CU200.

Cost of acquisition
Case

The following items would be included in the cost of acquisition:

Equity instruments issued	4,000
Cash	1,000
Liability	500
Total cost of acquisition	**5,500**

STEP 5
Measure non-controlling interest (NCI)



NCI
Case

Company P pays 800 to acquire an 80% interest in the ordinary shares of S. The aggregated fair value of 100% of S's identifiable assets and liabilities (determined in accordance with the requirements of IFRS 3) is 600, and the fair value of the non-controlling interest (the remaining 20% holding of ordinary shares) is 185.

- The measurement of the non-controlling interest, and its resultant impacts on the determination of goodwill, under each option is illustrated below:

	NCI based on fair value	NCI based on net assets
Consideration transferred	800	800
Non-controlling interest	185*	120**
	985	920
Net assets	(600)	(600)
Goodwill	385	320
*The fair value of the 20% non-controlling interest in S will not necessarily be proportionate to the price paid by P for its 80% interest, primarily due to any control premium or discount [IFRS 3.B45]		
**Calculated as 20% of the fair value of the net assets of 600.		

STEP 6
Determine goodwill or gain on bargain purchase

Option 1: NCI measured at fair value, the aggregate of

Option 2: NCI measured at their proportionate interest in identifiable net assets, the net of the acquisition-date fair values

Goodwill

- Goodwill acquired in a business combination represents a **payment made by the acquirer in anticipation of future economic benefits from assets that are not capable of being individually identified and separately recognised.**

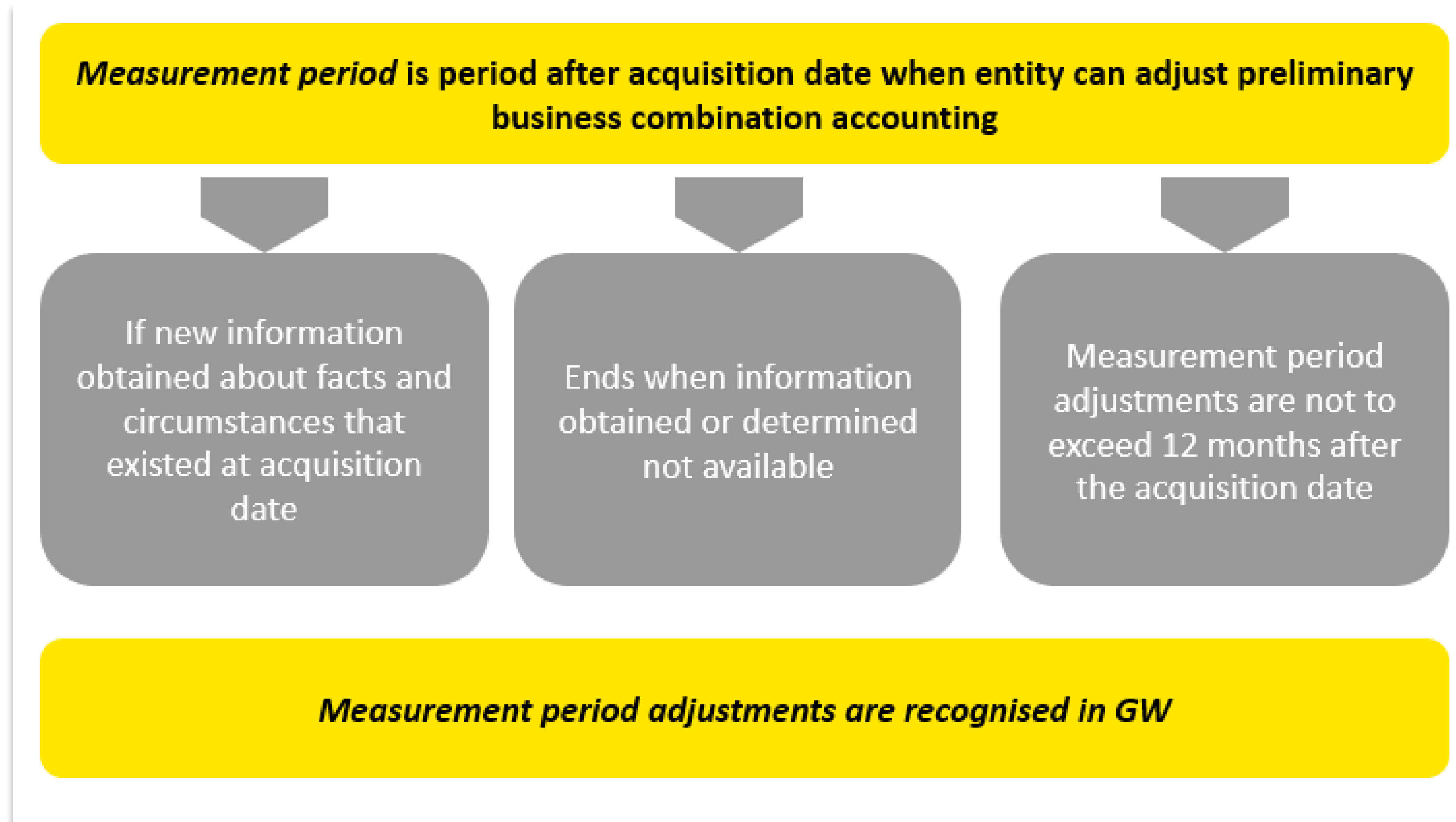
- Goodwill is measured as the **residual cost of the business combination** after recognising the acquiree's identifiable assets, liabilities and contingent liabilities.
  - Negative goodwill can consequently arise.

- Goodwill is subject to **impairment testing** in accordance with IAS 36.

Negative goodwill – Gain on bargain purcha

- Negative goodwill arises if the acquirer's interests in the net fair value of acquired identifiable assets and liabilities exceed the cost
- When negative goodwill arises:
    1. The acquirer is **required to undertake a review** to ensure the identification of assets and liabilities is complete, and that measurements appropriately reflect consideration of all available information.
    2. Negative goodwill/gain on bargain purchase is to be immediately **recognised as a gain in profit or loss.**

STEP 7
Recognise any measurement period adjustments



So what is control?

IFRS 10 Consolidated Financial Statements

Control in accordance with IFRS 10

- An investor controls an investee when the investor:

Is exposed to, or has right to variable returns from its involvement with the investee;

Has the ability to affect those returns

Through its power over the investee.

Control

The three elements of control which are the basis for consolidation under IFRS 10 are depicted below:

In order to apply the control model, several initial steps are necessary before the assessment of whether each of the three elements of control are present. These steps are:

- Identify the investee
- Understand the purpose and design of the investee
- Identify the relevant activities of the investee and how decisions about these relevant activities are made

How to assess control

- Remember 3 basic elements inherent in control: **power, ability to use this power** and **variable returns**.
- Power is the existing rights that give the current ability to direct the relevant activities. Let's break it down a bit:
  - The rights must be substantive, not only some minor rights;
  - The ability must be current, exercisable in the present time;
  - The relevant activities must be significant and related to major activities of investee.
- When assessing whether an investor controls an investee, more than one factor need to be considered. IFRS 10 contains guidance in this area.

Financial Instruments IFRS 9

Textbook: Chapter 11

Learning objectives

- Explain circumstances in which a financial asset or liability should be recognised
- Calculate the amounts at which financial assets and financial liabilities should be measured on initial recognition and subsequently

Why IFRS 9?

IFRS 9 establishes principles for the financial reporting of financial assets and financial liabilities.

- Please note that:
- IFRS 9 does NOT define financial instruments. You can find the definitions of financial instruments in IAS 32 Financial Instruments: Presentation.
- IFRS 9 does NOT deal with your own (issued) equity instruments like your own shares, issued warrants, written options for equity, etc.
- IFRS 9 DOES deal with the equity instruments of someone else, because they are financial assets from your point of view.
- IFRS 9 does NOT deal with your investments in subsidiaries, associates and joint ventures (look to IFRS 10, IAS 28 and related).

Definitions (IAS 32)

A financial instrument *is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity. (IAS 32.11)*

Why IFRS 9?

Classification and measurement of financial assets

Impairment methodology

Hedge accounting (outside the scope of course)

Recognition and measurement

When to recognize a financial instrument?

- You should recognize a financial asset or a financial liability in the statement of financial position when the entity becomes ***a party to the contractual provisions*** of the instrument (please refer to IFRS 9 par. 3.1.1).
- Unlike in other IFRS standards that put emphasis on the future economic benefits, **IFRS 9 is more about the contract.**

When to derecognize a financial instrument?

- You need derecognize the asset when (IFRS 9 par. 3.2.3) the contractual rights to the cash flows from the financial asset expire
- You need to derecognize a financial liability when it is extinguished. It happens when the obligation specified in the contract is discharged, cancelled or expires.

Initial measurement of financial assets and liabilities

Initial measurement: financial assets and liabilities are initially measured **at fair value.**

This is usually the same as the **fair value of the consideration given** (in the case of an asset) **or received** (in the case of a liability).

Subsequent measurement of financial assets

- IFRS 9 classifies financial assets into three categories and then prescribes the way in which assets falling into each category should be measured after initial recognition.
- So what are the categories and measurement rules?

The financial assets can be classified in the following categories

At amortized costs

At fair value through OCI

At fair value through profit and loss

Financial assets at amortised costs

- A financial asset falls into this category if BOTH of the following conditions are met:

Business model test is met, i.e. you hold the financial assets only to collect contractual cash flows (not to sell them), and

Contractual cash flows' characteristics test is met, i.e. the cash flows from the asset are only the payments of principal and interest.

Examples include e.g. receivables, loans

Subsequent measurement

Measured at their amortized costs

Using the effective interest method

E.g. Loan stocks that entity intends to hold until a maturity

Case

- 1 January 2017 company buys 100,000EUR OF 6% loan stock for 93,931EUR
- Interest will be received on 31 December each year
- After initial recognition the loan stock is to be measured at amortised cost using an effective interest rate of 7.5% per annum

A. State the amount at which this loan stock should be measured on 1 January 2017

B. Calculate amount at which this loan stock should be measured on 31 December 2017, 2018, 2019, 2020 & 2021

Financial assets at fair value through OCI

- A financial asset falls into this category if BOTH of the following conditions are met:

If a financial asset meets contractual cash flows characteristics test and

the business model is to collect contractual cash flows AND SELL financial assets

This business model will involve more frequent sales of assets than at amortized cost model

Subsequent measurement

Interest is calculated using effective interest method and recognised as income in PL

Changes in the asset’s fair value are shown in OCI

Changes in asset’s fair value are reclassified to PL when the asset is derecognised

UPM Annual Report 2020

4.3 Energy shareholdings

UPM is both a significant purchaser and producer of energy. The majority of electrical and thermal energy is consumed at the group's pulp and paper production. The production is mainly carried out by energy companies in which UPM has energy shareholdings. Energy shareholdings are unlisted equity investments. UPM does not have control or joint control of or significant influence in the said energy companies.

The value of energy shareholdings amounted to EUR 1,936 million (2,145 million) at the end of 2020. These energy companies supply energy or both energy and heat to their shareholders on a cost-price principle (Mankala-principle) which is widely applied in the Finnish energy industry. Under the Mankala-principle energy and/or heat is supplied to the shareholders in proportion to their ownership and each shareholder is, pursuant to the specific stipulations of the respective articles of association, severally responsible for its respective share of the production costs of the energy company concerned.

In 2020, UPM issued a shareholder loan of EUR 47 million without a maturity date to PVO. Embedded into the loan terms is a right to issue new shares in the PVO B2 series against the remaining, unpaid nominal of the loan starting from 2021. The loan is valued at fair value and is taken into account as a part of the total fair valuation of the PVO B2 series valuation. In addition, UPM issued a similar loan commitment of EUR 123 million to PVO, where also a right to issue new PVO B2 shares is embedded starting from 2023.

UPM Annual Report 2020

	Number of shares	Group holding %	Carrying value, EURm	
			2020	2019
Pohjolan Voima Oyj, A series	8,176,191	61.24	362	360
Pohjolan Voima Oyj, B series	4,140,132	58.11	990	1,191
Pohjolan Voima Oyj, B2 series	2,869,819	51.22	191	188
Kemijoki Oy	179,189	7.33	273	290
Länsi-Suomen Voima Oy	10,220	51.10	114	111
Other	–	–	6	7
Carrying value, at 31 December			1,936	2,145

PVO's share capital is divided into different series of shares. The B and B2 series relate to PVO's shareholdings in Teollisuuden Voima Oyj (TVO). UPM has no direct shareholdings in TVO. TVO operates two nuclear power plants (Olkiluoto 1 and Olkiluoto 2) and is constructing one new nuclear power plant in Olkiluoto (Olkiluoto 3), Finland. The operation of a nuclear power plant is governed by international, European Union and local nuclear regulatory regimes. Pursuant to the Finnish Nuclear Liability Act, the operator of a nuclear facility has a strict third-party liability in relation to nuclear accidents. Shareholders of power companies that own and operate nuclear power plants are not subject to the liability under the Nuclear Liability Act. In Finland, the future costs of conditioning, storage and final disposal of spent fuel, management of low and intermediate level radioactive waste as well as nuclear power plant decommissioning are provided for by a state established fund (the Finnish State Nuclear Waste Management Fund). The contributions to the Fund are intended to be sufficient to cover estimated future costs. These contributions have been taken into consideration in the fair value of the related energy shareholdings.

Energy shareholdings

EURm	2020	2019
Carrying value, at 1 January	2,145	2,159
Disposals	-2	-1
Changes in fair value recognised in other comprehensive income	-207	-13
Carrying value, at 31 December	1,936	2,145

Accounting policies

The group has made an irrevocable election to designate its energy shareholdings as equity instruments where changes in fair value are recognised through OCI. The shareholdings are not held for trading as the group has an intention to hold the investments for the long term. Purchases of energy shareholdings are initially and subsequently measured at fair value through other comprehensive income, net of tax if applicable, with only dividend income recognised through profit and loss. Initial fair value is acquisition cost including transaction costs. Upon disposal of the investment, the accumulated fair value changes in equity are not recycled to the income statement but instead, are reclassified from the fair value reserve to retained earnings.

The fair value of energy shareholdings is a level 3 measure in the fair value measurement hierarchy.

Key estimates and judgements

Fair valuation and sensitivity

Valuation of energy shareholdings requires management's assumptions and estimates of a number of factors that may differ from the actual outcome which could lead to significant adjustment to the carrying amount of the asset. Fair value is determined on a discounted cash flow basis and the main factors impacting the future cash flows include future electricity prices, price trends and discount rates.

The electricity price estimate is based on a simulation of the Finnish area electricity price. A change of 5% in the electricity price used in the model would change the total value of the assets by EUR 340 million. The discount rate of 5.47% used in the valuation model is determined using the weighted average cost of capital method. A change of 0.5% percentage points in the discount rate would change the estimated fair value of the assets by approximately EUR 300 million.

Other uncertainties and risk factors in the value of the assets relate to start-up schedule of the fixed price turn-key Olkiluoto 3 EPR nuclear power plant project. UPM's indirect share of the capacity of Olkiluoto 3 EPR is approximately 31%, through its PVO B2 shares. Changes in regulatory environment or taxation could also have an impact on the value of the energy generating assets.

Financial assets at fair value through profit or loss

All other financial assets fall in this category.

Derivative financial assets are automatically classified at FVTPL.

You may decide to designate the financial asset at fair value through profit or loss at its initial recognition.

Impairment of financial assets carried at amortised costs

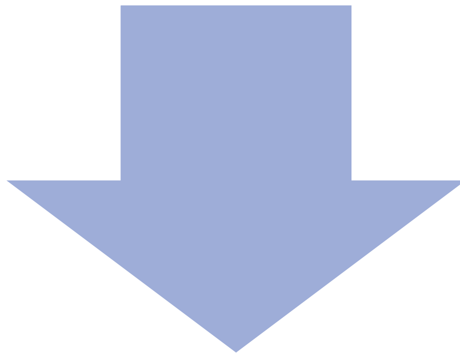
IFRS 9 requires entities to estimate and account for expected credit losses for all relevant financial assets (mostly debt securities, receivables including lease receivables, contract assets under IFRS 15, loans), starting from when they first acquire a financial instrument.

What is a credit loss?

Credit loss

- In general, the amount of an impairment loss is equal to the difference between

The current carrying amount of the asset, and



The PV of the future cash flows that the entity **expects to receive**

When measuring expected credit losses, entities will be required to use all relevant information that is available to them

UPM Annual Report 2020

Trade receivables

Trade receivables arising from selling goods and services in the normal course of business are recognised initially at transaction price and subsequently at amortised cost less loss allowance provision. No element of financing is deemed present as the sales are made with a credit term of 14–60 days, which is consistent with market practice.

The group applies the IFRS 9 simplified approach to measuring expected credit losses which uses a lifetime expected loss allowance for all trade receivables. The group has recognised two types of provisions for trade receivables – a general provision for lifetime expected credit losses and a provision for specified individual trade receivables, both of which are charged to the income statement. The group uses a provision matrix for estimating lifetime expected credit losses where trade receivables are segregated by businesses. The provision matrix is based on historical observed default rates, adjusted by forward looking information. It takes into account trade credit insurances, payment profile of customers and the factor that as debts get older they are more likely not to be paid. Additionally, the group recognises a provision individually for outstanding trade receivables where specific debtor information is available. In these cases there must be objective evidence that the group will not be able to collect all amounts due according to the original terms of the receivables.

Trade receivables are permanently written off when there is no reasonable expectation of recovery. The customer entering into bankruptcy or liquidation proceedings or finalising such proceedings, or entering into debt-restructuring are considered indicators that the trade receivables are no longer expected to be recovered. Subsequent recoveries of amounts previously written off are credited to the income statement. The carrying amount of trade receivables approximates to their fair value due to the short-term nature of the receivables.

	2020			2019		
EURm	TRADE RECEIVABLES	LOSS ALLOWANCE PROVISION	RECEIVABLES, NET OF PROVISION	TRADE RECEIVABLES	LOSS ALLOWANCE PROVISION	RECEIVABLES, NET OF PROVISION
Undue	1,030	-4	1,025	1,128	-3	1,125
Past due up to 30 days	59	-1	58	79	-1	79
Past due 31-90 days	14	-3	11	13	-2	11
Past due over 90 days	26	-22	4	33	-26	8
Total	1,129	-31	1,098	1,253	-31	1,222

Subsequent measurement of financial liabilities

- After initial recognition, financial liabilities should usually be measured at amortised cost, using the effective interest method
- There are some exceptions such as
  - **Financial liabilities at FV through profit of loss:** consists mainly of financial liabilities that are held for trading
  - **Trade payables:** Short term payables may be measured at the original invoice amount if the effect of discounting is not material

Disclosures (IFRS 7)

- The purpose of disclosures is to enable users to evaluate two things:

Significance of financial instruments, and

Nature and extent of risks from financial instruments and how they are managed

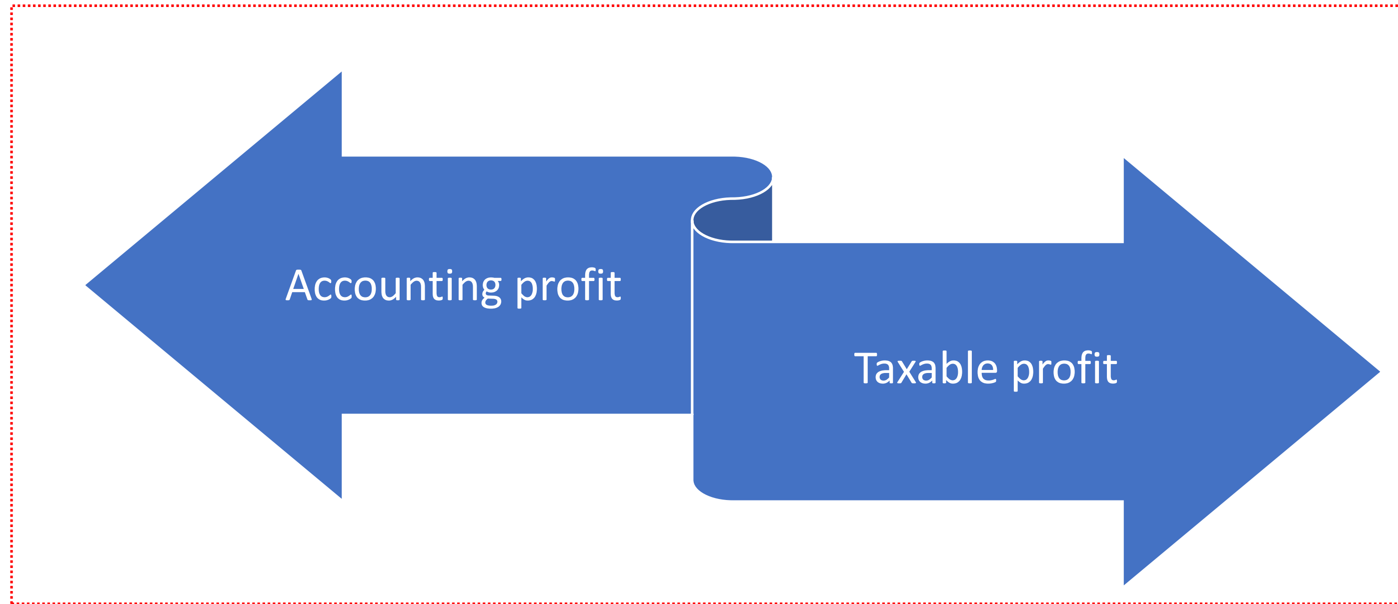
IAS 12 Income Taxes

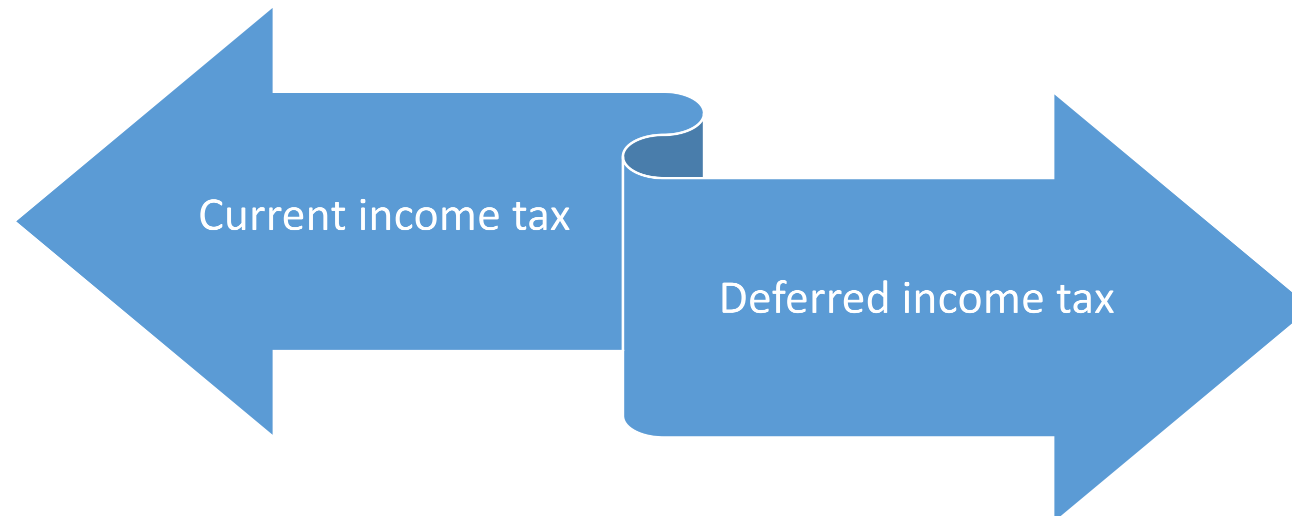
Textbook: Chapter 15

Learning objectives

- Define the term “current tax” and account for current tax
- Define the term “temporary differences”
- Calculate deferred tax assets and liabilities arising from temporary differences
- Account for deferred tax

Understand the differences





Accounting versus taxable profit

Accounting profit

- **is profit or loss for a period before deducting tax expense.** Please note that IAS 12 defines accounting profit as a before-tax figure (not after tax as we normally do) in order to be consistent with the definition of a taxable profit.

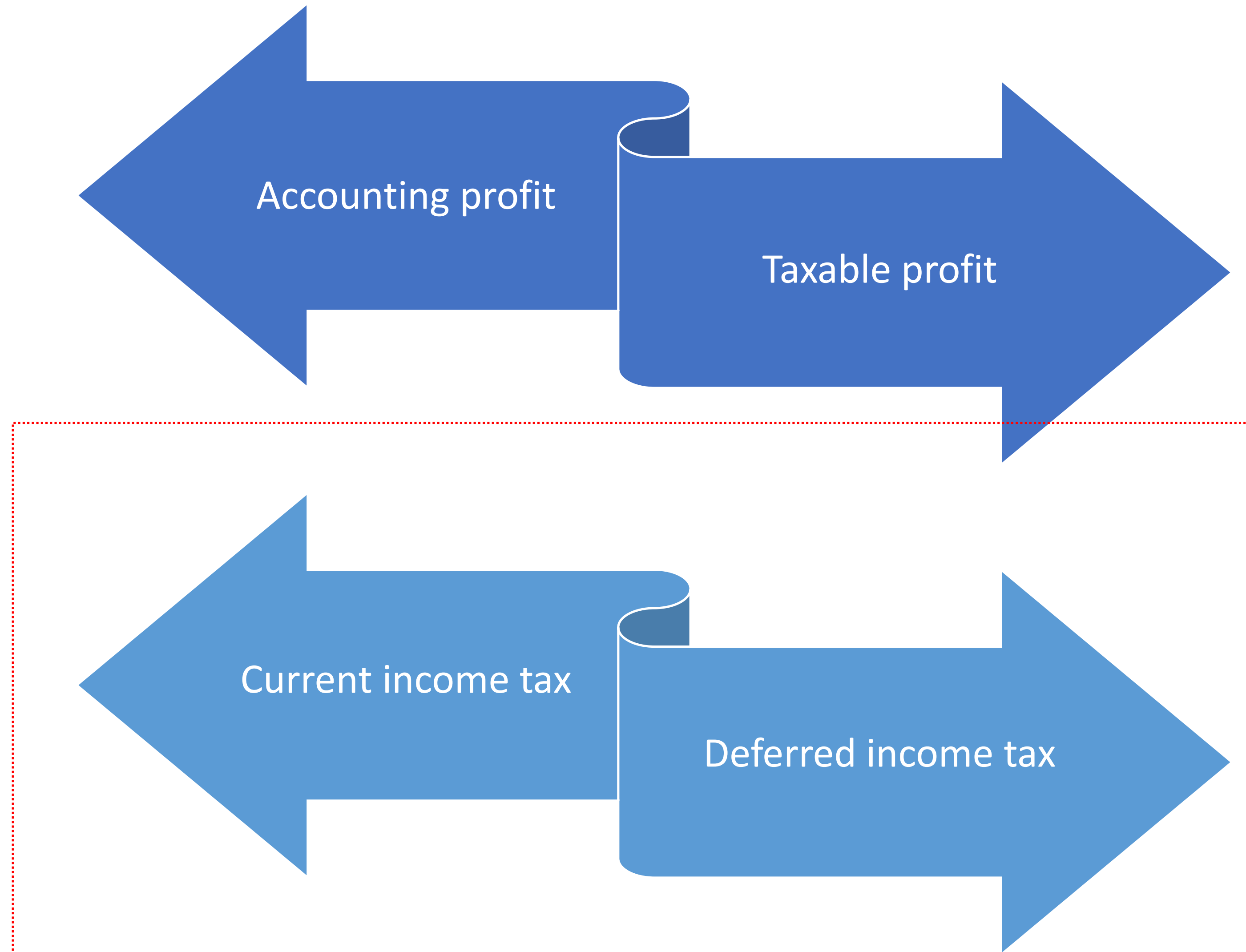
Taxable profit (tax loss)

- **is the profit (loss) for a period determined in accordance with the rules established by the taxation authorities** upon which income taxes are payable (recoverable).

A number of differences can pop out between accounting profit and taxable profit you have to make the following adjustments to your accounting profit:

- Add back the expenses recognized but non-deductible for tax purposes
- Add income not recognized but included under tax regulations
- Deduct expenses not recognized but deductible for tax purposes
- Deduct income recognized but not taxable under tax regulations.

Understand the differences



Current tax versus deferred tax

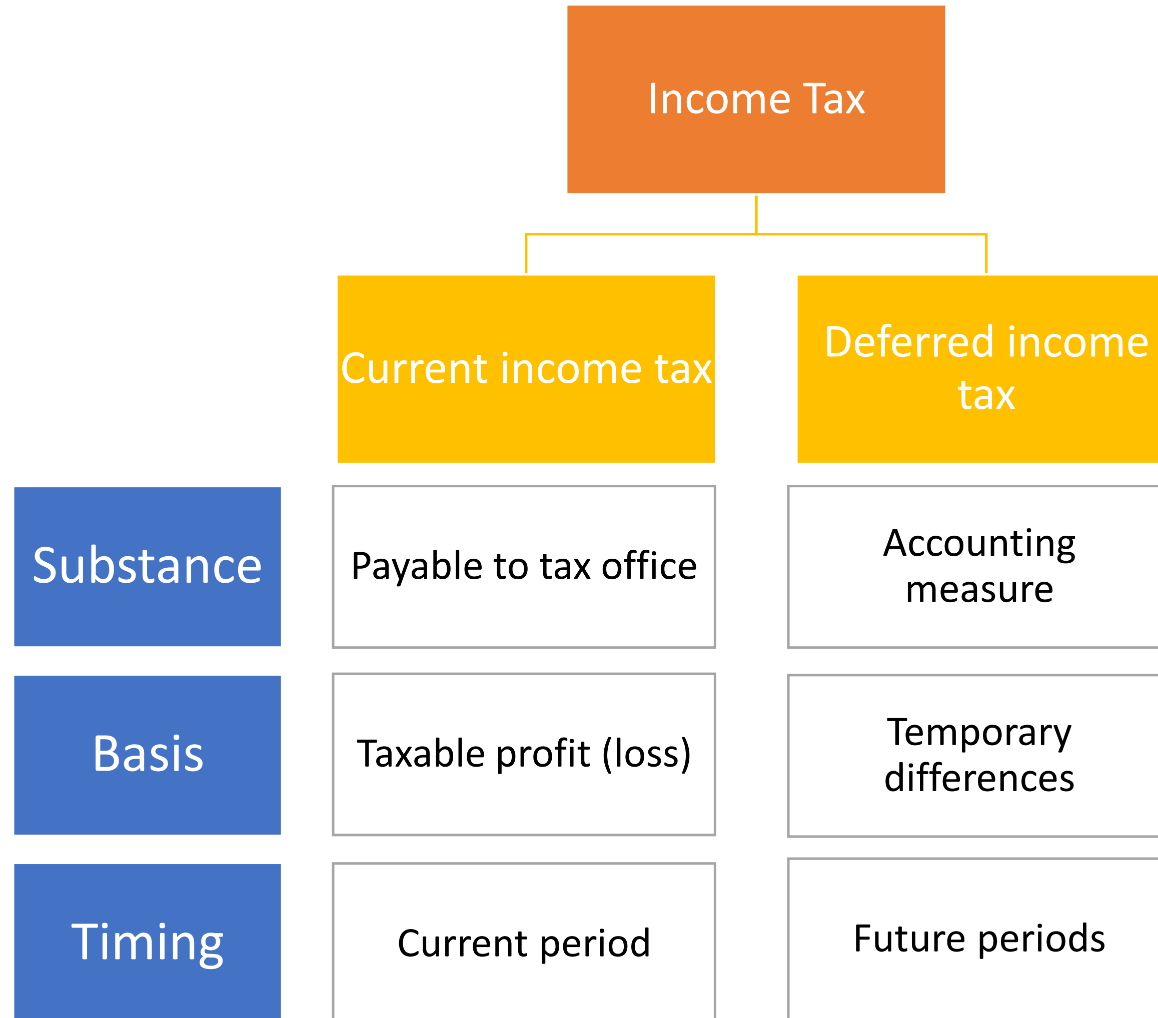
Current income tax

- is the amount of income tax **that you actually need to pay to your tax office.**

Deferred income tax

- is an accounting **measure used to match the tax effect of transactions with their accounting impact and thereby produce less distorted results.**

Current tax versus deferred tax

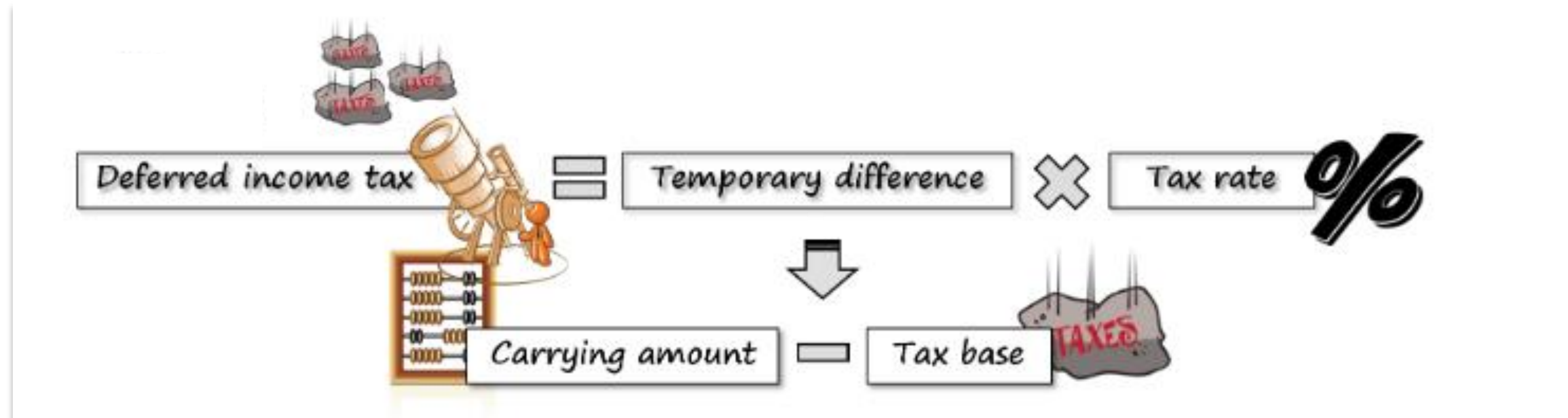


Current income tax

- ***Current tax*** is the amount of income tax payable (recoverable) in respect of the taxable profit (loss) for a period.
- ***Measurement*** of current tax liabilities (assets) is very straightforward.
  - We need to use the tax rates that have been enacted or substantively enacted by the end of the reporting period and apply these rates to the taxable profit (loss).
- ***Current income tax expense*** shall be ***recognized*** directly to profit or loss in most cases.
  - However, If the current tax arises from a transaction or event recognized outside profit or loss, either in other comprehensive income or directly in equity, then current income tax shall be recognized in the same way.

Deferred tax

- ***Deferred tax*** is the tax payable (recoverable) in future periods in respect of the temporary differences, unused tax losses and unused tax credits.
- Taxable profit will often be different from the profit shown in the financial statements (the “accounting profit”)



Case

- Company has the following results for the 3 years. There are no other differences and the rate of tax is 20%.

	2017	2018	2019
Profit before tax	800	800	800
Depreciation charged in the year	200	200	200
Depreciation for tax purposes	400	150	50

What is company’s profit after tax for each accounting period?

Case

- **Tax expense** for each year is calculated as follows

	2017	2018	2019
Profit before tax	800	800	800
Add: Depreciation charged in the year	200	200	200
Profit before depreciation	**1000**	**1000**	**1000**
Less: Depreciation for tax purposes	400	150	50
Taxable profit	**600**	**850**	**950**
Tax expense 20%	120	170	190

Case

- **Profit after tax** calculation for each year is:

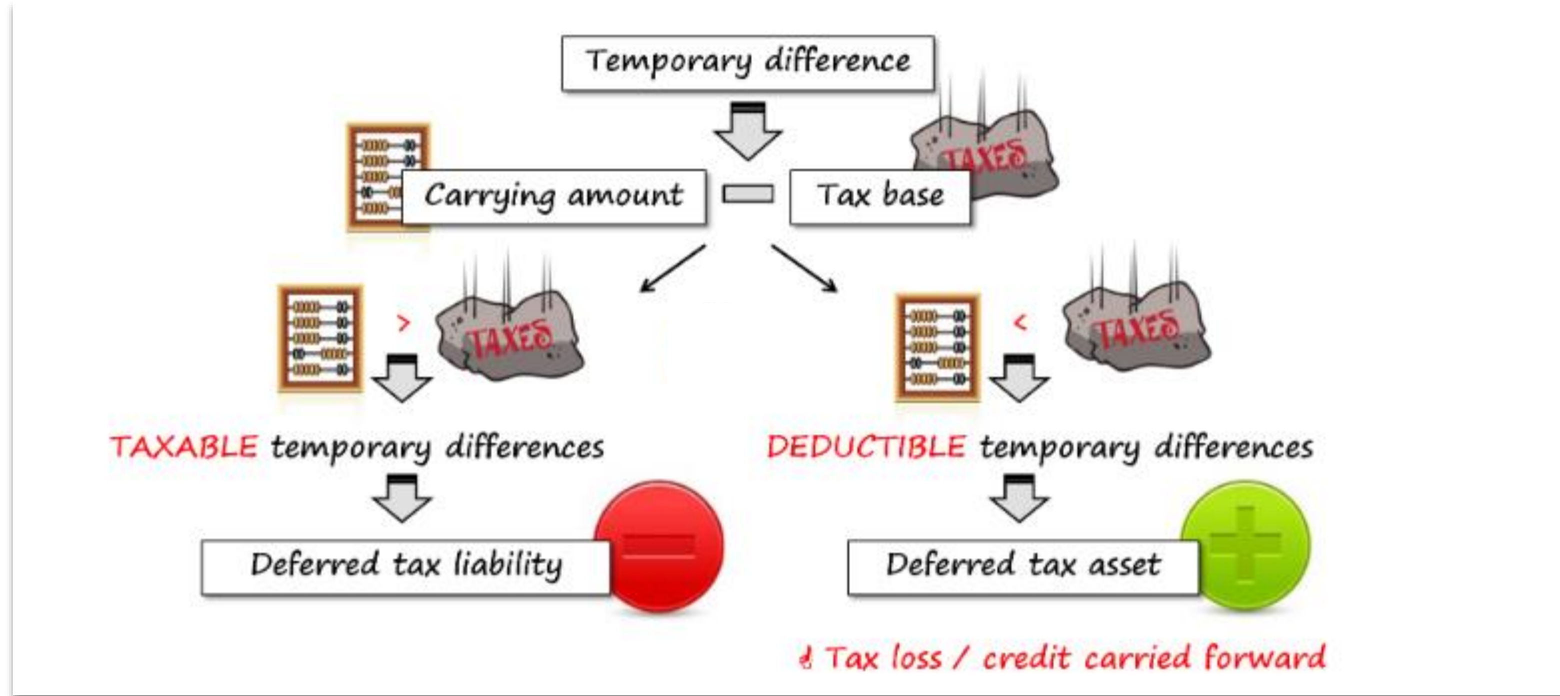
	2017	2018	2019
Profit before tax	800	800	800
Tax expense 20%	120	170	190
Profit after tax	**680**	**630**	**610**

What are the necessary transfers to and from the company’s deferred tax account?

Case

		2017		2018		2019
Profit before tax		800		800		800
Tax expense:						
Current tax	120		170		190	
Deferred tax	40	160	-10	160	-30	160
Profit after tax		**640**		**640**		**640**

Temporary difference



NEXT TIME: Guest lecturers from PWC & EY!