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2017 Financial Reporting
Matters to consider

We discuss the principal issues arising in respect of 31 December 2017 annual reports, being primarily:

- Observations raised by the Irish Auditing and Accounting Supervisory Authority (IAASA) in their Observations on selected Financial Reporting Issues document for years ending on or after 31 December 2017
- The European Securities and Markets Authority's (ESMA's) common enforcement priorities.
- IAASA's 2017 published surveys including the use of Alternative Performance Measures (APMs) by Irish listed companies
- Issues arising from the current economic environment and developments in reporting standards.

As in previous years, the IAASA observations document provides an assessment of Irish reporting based on examinations of annual and half-yearly financial reports of certain equity, debt and closed-ended fund issuers with securities admitted to trading on an EU regulated market. There is some cross over with the Financial Reporting Council (FRC) in the UK in their Annual Review of Corporate Reporting 2016/2017 ('the FRC Annual Review').

Contents

The Irish regulatory environment

The Irish Auditing and Accounting Supervisory Authority (IAASA) published in September 2017 their observations on selected financial reporting issues. IAASA, as Ireland's accounting enforcer, has responsibility for the examination and enforcement of certain listed entities' periodic financial reporting ('issuers'). As such, IAASA examines the annual and half-yearly financial reports of certain equity, debt and closed-ended fund issuers with securities admitted to trading on an EU regulated market for compliance with the relevant reporting framework (Irish/UK GAAP and IFRS). The observations from these examinations are published yearly and are available on the IAASA website.

The matters raised in IAASA's 2017 document derive from a combination of:

- financial reporting matters identified during IAASA's examinations and surveys undertaken during 2017;
- matters identified in the course of IAASA's work, but not raised with specific issuers;
- IAASA's expectations of issuers regarding the upcoming financial reporting season; and
- Financial reporting matters discussed at the European Securities and Markets Authority ('ESMA') sponsored European Enforcer Co-ordination Sessions ('EECS') meetings at which IAASA is an active participant.

The purpose of IAASA's annual observations document is to assist management and those charged with governance in the preparation of high quality financial reports.

IAASA has also published during 2017 the results of a number of surveys completed as follows:

- Desktop survey – Impairment testing in Irish listed companies' 2016/17 annual financial statements (November 2017)
- Desktop survey of issuers' operating segment disclosures (October 2017)
- Survey on the use of Alternative Performance Measures (APMs) by Irish listed companies (September 2017)
- Desktop survey – disclosures of the new accounting standards in issuers' 2016 annual financial statements (July 2017)
- Mid-year update on IAASA's financial reporting examination activities (June 2017)
- Snapshot of IAASA's financial reporting enforcement activities in 2016 (January 2017)

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'Brexit' and 2017 annual reports

As might be expected given its economic significance and range of possible effects on business, a number of 2016 annual and 2017 interim reports of companies included reference to 'Brexit' either as part of their discussion of risk or in commenting on their performance, but also that there was a consistent theme of it still being too early to measure the longer term effects on their businesses.

It is important, however, that as the landscape develops companies continue to refine their analysis of the potential impacts and, as they do so, continue to provide more detailed and more company-specific discussion of these impacts in their corporate reporting. Such a discussion could be included in a company's narrative reporting as part of, inter alia, the discussion of a company's business model, principal risks and uncertainties or the longer-term viability statement. Equally important is to include the effects of 'Brexit' that a company might already be experiencing in discussions of performance in 2017.

Within the financial statements themselves, such uncertainties could be relevant to disclosure of sources of estimation uncertainty and to the parameters of 'reasonably possible' changes used in sensitivity analyses of fair value measurements, market risks on recognised financial assets and liabilities and impairment reviews.

ESMA's common enforcement priorities also make reference to discussion of 'Brexit', making the specific comment that recognition and measurement of UK deferred tax assets could be an area in which major sources of risks and uncertainties will need to be disclosed. Whilst there could be uncertainty over the generation of future taxable profits to utilise tax losses, this assessment should be made on the basis of currently enacted tax law and as noted in a Deloitte Need to know the triggering of 'Article 50' did not constitute substantive enactment of any changes to existing UK tax law.

As with other economic events, changes in UK tax law should be accounted for when they occur rather than being anticipated based on an expectation of possible future change.

Reporting financial performance and the use of Alternative Performance Measures

The use of 'non-GAAP' or 'Alternative Performance' measures is an area of increasing regulatory focus. ESMA's Guidelines on Alternative Performance Measures were clarified by a series of Questions and Answers published 2017.

IAASA published its Thematic Survey on Alternative Performance Measures in September 2017. This sets out the results of a desk-top survey of the range of APMs that issuers included in their 2016/2017 financial reports and assessed the compliance by issuers with the ESMA Guidelines noted above. IAASA also, as part of its examination cycle for 2016 financial year ends, engaged with seven issuers regarding their use of APMs and examined the level of those issuers compliance with the ESMA Guidelines.

IAASA noted instances of good practice by issuers relative to their use of APMs. Conversely, other instances were detected where the level of compliance with the ESMA APMs Guidelines was below what IAASA expected.

IAASA has committed to continue to focus and engage with issuers on:

- directors' rationale for not including definitions, reconciliations and comparatives for each APM presented in periodic financial reports;
- the reasons why certain items have been excluded from adjusted earnings measures;
- directors' rationale for not considering certain measures to be APMs within the scope of the ESMA APMs Guidelines;
- directors' rationale for not including a discussion of or reference to, IFRS measures when discussing APMs; and
- reasons and explanations for APMs which are redefined or not used by the issuer in subsequent financial reports.

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The ESMA Questions and Answers make clear that 'adjusted' profit figures used in the financial statements themselves (for example, as part of segment information) as well as in narrative reporting remain within the scope of its guidelines on APMs.

In using such measures, it should be noted that:

- a measure labelled as 'operating profit' should not exclude items such as inventory write-downs that would be generally understood as forming part of the entity's operations;
- gains and losses should not be offset unless permitted by IFRS;
- the approach to identifying 'exceptional' or 'adjusting' items should be even handed (with gains excluded as readily as losses), consistent from year to year and clearly disclosed (including an explanation of why it is believed necessary to adjust for certain items); and
- a clear accounting policy for the identification of such items should be provided.

The tax and cash flow effects of any 'exceptional' items should also be clearly presented.

The Deloitte publication 'Alternative performance measures: A practical guide' provides additional guidance on the use of APMs, setting out what is considered best practice and providing real-life examples of how entities present such measures.

Business review and business model reporting

In terms of the business review for equity listed Main Security Market reporters, limited discussion about major revenue sources or product lines or of variations in levels of profitability by some reporters has been noted. Such omissions can also give rise to challenges over the balance of the annual report if it appears that discussion of successful parts of the business is prioritised over less well performing segments.

The comprehensiveness of a review of financial position can also be challenged when it excluded, for example, movements in working capital and cash flows.

Central to a discussion of business performance are a company's Key Performance Indicators (KPIs). Clarity is required on the basis for calculation of KPIs and the reasons for changing them.

In terms of the description of a company's business model, there is a need for linkage and consistency with other information in the annual report, something that can be achieved more naturally if the key drivers of the business are clearly articulated. On a similar theme, an explanation of how a company's KPIs interact with the remuneration paid to its directors would be useful information for readers.

Risk and viability reporting

Main Securities Market equity listed companies are required to include:

- a description of the principal risks and uncertainties facing the company or group;
- the main trends and factors likely to affect the future development, performance and position of the company or group's business; and
- a description of the company or group's strategy and its business model.

In addition the UK Corporate Governance Code now requires a longer term viability statement covering:

- how the directors have assessed the prospects of the company;
- over what period they have done so; and

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- why they consider that period to be appropriate.

The viability statement should also state whether the directors have a reasonable expectation that the company will be able to meet its obligations as they fall due over the period of their assessment, drawing attention to any qualifications or assumptions as necessary.

In respect of Principal Risks and Uncertainties (PRUs), there have been cases where:

- The description was unclear or insufficiently detailed.
- It was unclear how the identification of PRUs had been performed, citing the example of an energy company with no PRU related to climate change.
- A number of risks were discussed but with no clarity over which were deemed to be 'principal'.

The viability statement is a newer element of corporate reporting and to date most companies have identified a period of three years over which to consider viability, reflecting a company's medium-term business plan.

A two stage approach to developing viability statements is recommended:

- consider and report on the prospects of the company, taking into account its current position and principal risks; then
- state whether they have a reasonable expectation that the company will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, drawing attention to any qualifications or assumptions as necessary.

Accounting policies, judgements and estimates

A primary source of information enabling investors to understand the items in the financial statements is a clear description of the accounting policies applied in producing those numbers. IAS 1 Presentation of Financial Statements requires this to be supplemented by a discussion of:

- the most significant judgements made in applying those policies (apart from those involving estimation); and
- the major sources of estimation uncertainty (including assumptions made about the future) that have a significant risk of resulting in a material adjustment to the carrying amount of assets and liabilities in the next financial year.

An effective description of accounting policies should include clear, entity-specific discussion of the policies applied to material transactions and balances, covering ongoing elements of the business (for example, revenue and cost recognition policies for each revenue stream) as well as one-off transactions such as significant business combinations and, perhaps as importantly, should exclude irrelevant repetition of the requirements of accounting standards in respect of items that are not material to the entity.

Specifically in respect of accounting for revenue transactions, this remains important as a means of explaining how a company's income is generated but takes on an additional significance in the run up to application of IFRS 15 as a basis for explanation of how these policies may change on adoption of the new Standard (for example, in respect of the principal-agent analysis or the basis for 'unbundling' elements of a contract).

The impact of new accounting standards

As the significant new standards IFRS 15 *Revenue from Contracts with Customers* and *IFRS 9 Financial Instruments* are both mandatorily effective for periods beginning on or after 1 January 2018, December 2017 annual reports will be published after the date of initial application of those standards. The effective date of IFRS 16 *Leases* (periods beginning on or after 1 January 2019) also draws closer. As such, both IAASA and ESMA have reiterated the need for entity-specific, quantitative disclosure on the likely changes in accounting in line with the requirements of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.

ESMA's public statements detailing its expectations of disclosure of the likely effect of IFRS 15 and IFRS 9 remain relevant and illustrate an expectation of increasing

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levels and detail of disclosure as the effective date of these standards approaches. For 2017 annual financial statements, the statements encourage:

- further elaboration and development of information provided in previous financial statements;
- an explanation of the changes to amounts reported under existing Standards, disaggregated as appropriate; and
- a quantitative assessment of the impact of the new Standards as of 1 January 2018.

In its common enforcement priorities, ESMA goes on to state that as December 2017 annual reports will be issued after the effective date of IFRS 15 and IFRS 9 implementation, analyses should have been substantially completed. As a result, ESMA expects the impacts of these Standards to be known or reasonably estimable, allowing disclosure of:

- accounting policies to be applied, including in respect of transition and the use of practical expedients; and
- the amount and nature of expected possible impacts compared to previously recognised amounts.

Similarly, IAASA's document notes an expectation that, as the application date of the new standards nears, issuers should provide progressively more entity-specific qualitative and quantitative information about the impact of the application of the new standards in their financial statements.

Recent developments on IFRS 9

The IASB and IFRS Interpretations Committee have discussed issues arising in the standard's implementation.

One of these issues resulted in the publication in October 2017 of an amendment to the standard *Prepayment Features with Negative Compensation*. This adjusts the 'solely payments of principal and interest' (SPPI) criterion to allow, in certain circumstances, for a feature in which a borrower choosing to repay a loan early could receive (rather than, as is more usual, pay) compensation reflecting changes in interest rates. This will allow such loan assets, subject to the other criteria in IFRS 9, to be measured at amortised cost rather than at fair value.

EFRAG (the European Financial Reporting Advisory Group) has accelerated its endorsement advice process with a view to achieving EU endorsement during 2018. This would make the amendment available for use by companies applying IFRS 9 at its mandatory effective date.

The Basis for Conclusions on these amendments also provided clarification on an unrelated issue – that of accounting for a modification or exchange of a financial liability that is not significant enough to result in derecognition of the liability (and recognition of a new liability at its fair value). The Basis for Conclusions states that such a modification should be treated as a revision of estimated cash flows (resulting in an immediate gain or loss) rather than, as is the predominant treatment under IAS 39 *Financial Instruments: Recognition and Measurement*, the changes to cash flows being factored into the interest expense recognised over the remaining life of the liability.

The ESMA common enforcement priorities also include detailed recommendations on disclosure of the impacts of IFRS 15 and IFRS 9 depending on an entity's specific facts and circumstances and (in respect of IFRS 9) whether the company is a corporate entity, credit institution or insurer.

A Deloitte 'A Closer Look' publication provides more detail on the effect of IFRS 9 on the accounting for modifications of financial liabilities.

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Companies intending to adopt IFRS 16 early are expected also to provide quantitative disclosures of the likely impact, including an explanation of the difference between operating lease commitments disclosed under IAS 17 Leases and lease liabilities recognised at the date of transition to IFRS 16.

Companies not intending to early adopt should also be aware of the possibility of additional scrutiny of their operating lease commitments disclosure as it is used as a guide to the likely impact of IFRS 16 and will (depending on the transition method selected) need to be reconciled to the lease liability recognised upon application of IFRS 16.

The need for governance and control over preparation of these disclosures should also not be overlooked. Although not yet reflected in the primary statements, this information is part of the financial statements and should be robust enough to be used for that purpose. In addition, it should be noted that disclosures under IAS 8 are not optional, 'reasonably estimable' effects of applying new Standards are required to be disclosed.

The IASB issued on 12 December 2017 *Annual Improvements to IFRS Standards 2015–2017* Cycle which makes narrow-scope amendments to four IFRS Standards as follows:

- IFRS 3 Business Combinations - A company remeasures its previously held interest in a joint operation when it obtains control of the business.
- IFRS 11 Joint Arrangements - A company does not remeasure its previously held interest in a joint operation when it obtains joint control of the business.
- IAS 12 Income Taxes - The amendments clarify that all income tax consequences of dividends (i.e. distribution of profits) should be recognised in profit or loss, regardless of how the tax arises.
- IAS 23 Borrowing Costs - The amendments clarify that if any specific borrowing remains outstanding after the related asset is ready for its intended use or sale, that borrowing becomes part of the funds that an entity borrows generally when calculating the capitalisation rate on general borrowings.

The amendments are effective from 1 January 2019, with early application permitted. For EU reporters early adoption may not be possible until EU endorsement.

On 7 February 2018, the IASB issued Amendments to IAS 19: Plan Amendment, Curtailment or Settlement. The amendments are effective on or after 1 January 2019 and requires that when a change to a plan—an amendment, curtailment or settlement—takes place the updated assumptions from the re-measurement of the net defined benefit liability or asset required by IAS 19 are also used to determine current service cost and net interest for the remainder of the reporting period after the change to the plan. In addition, amendments have been included to clarify the effect of a plan amendment, curtailment or settlement on the requirements regarding the asset ceiling.

IFRS 13 Fair Value Measurement

IFRS 13 came into effect in 2013. The IASB is conducting its post-implementation review of the effect of IFRS 13 on financial reporting.

ESMA published a report in July 2017 which provided an overview of implementation of IFRS 13 by European issuers. This report assessed the level of compliance with IFRS 13 by IFRS financial statement preparers along with the level of comparability. The results of this assessment noted that the requirements of IFRS 13 had been well incorporated in the sample chosen. It was also noted that there were some areas which showed room for improvement including the following:

- disclosures;
- providing more clarity about judgements of the unit of account;
- the assessment as to when a transaction or quoted price

does not represent fair value; and

- the use of credit value adjustments ('CVA') and debit value adjustments ('DVA') adjustments in the valuation of derivatives.

IAASA completed a survey on the application of IFRS 13 by Irish Companies and published the results in November 2016. The results here were consistent with the ESMA assessment and noted room for improvement in a number of areas.

IAASA has indicated it will continue to focus on compliance with IFRS 13 for 2017 financial year-ends. They note in their observations document the areas which management, Directors and Audit Committees should ensure the disclosures address as follows:

- The disclosures are entity-specific and inform users of the financial statements of the measurement bases and valuation techniques used in determining fair values;
- The disclosures clearly set out the key fair value judgements and assumptions made and that have the most significant effect on the carrying amounts of assets recognised in the financial statements;
- The disclosures are sufficient to detail how material liabilities are fair valued;
- The disclosures provide fair value disclosures by class of assets and liabilities where appropriate; and
- The disclosures provide sufficient details as to whether or not reasonably possible alternative assumptions would change fair value significantly.

Sources of Estimation Uncertainty (Uncertain Tax Positions) and Judgement (IAS 36 Impairment of Assets)

A Deloitte 'Need to know' publication provides more detail on the disclosure of significant judgements and sources of estimation uncertainty.

The requirements for disclosure of critical **judgements** and of estimation uncertainty are separate and address distinct issues. In broad terms, a critical judgement is applied in characterising a transaction or item (for example, whether a debt restructuring is a modification or an extinguishment or which party was the acquirer in a business combination) whilst **estimation** uncertainty is concerned with the value of, for example, a provision for an uncertain tax position or the net realisable value of inventory. Both in preparing and presenting useful disclosures, it is helpful to distinguish clearly between the two.

It is also important to bear in mind that IAS 1 refers to the judgements that have had "the most significant effect" and to "major sources" of estimation uncertainty. A comprehensive discussion of a small number of issues that genuinely demanded management scrutiny in the current year is of more value than a superficial reference to many items which may have been relatively unproblematic. In respect of estimation uncertainties, it should also be noted that this disclosure requirement refers specifically to a risk of material adjustment **within the next financial year**. Information about longer term uncertainties might be useful as additional disclosure, but does not form part of this IAS 1 requirement and should be kept separate from the IAS 1 disclosures.

Uncertain Tax Positions

IFRIC Interpretation 23 Uncertainty over Income Tax Treatments was published in 2017 and whilst it is not mandatorily effective until 2019 the conclusions it reaches are consistent with already effective accounting standards and provide an appropriate approach to dealing with uncertain tax positions.

In brief, its conclusions are as follows:

- Uncertainties in income tax liabilities or assets should be reflected in recognising a tax liability or asset only when payment or recovery becomes probable.
- Judgement is required in identifying the unit of account to be applied in making this judgement (i.e. whether there is a single tax uncertainty or group of related uncertainties).

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- Full 'detection risk' (i.e. all relevant information being available to the tax authorities) is assumed in making these judgements.

IAASA notes in its observations document that a number of issuers disclosed 'Taxation' as a source of estimation uncertainty and within this narrative, issuers referred to uncertain tax positions ('UTPs') liabilities.

IAASA challenged issuers' rationale for not disclosing their UTP liabilities separately in accordance with IAS 1.125. IAASA considered the following matters:

- UTP liabilities have a separate carrying value and create a separate tax liability;
- UTP liabilities practically comprise the full amount of the current income tax liability of each issuer;
- each issuer included taxation as a source of estimation uncertainty and tax uncertainties were referred to therein; and

Base Erosion and Profit Shifting
The OECD and the G20 project on 'Base Erosion and Profit Shifting' ('BEPS') was initiated in 2015 to address perceived inequalities and inconsistencies in the global tax landscape. This had resulted in a 15-point action plan to modernise the principles underlying today's international tax landscape and to develop a consistent framework for countries to base their tax legislation upon.

Core principles of the project are:

- the elimination of tax mismatches such that all income is taxed;
- the alignment of profits with value creation;
- the increase of transparency with tax authorities; and
- the implementation of change in a coordinated fashion.

While some of the proposals will be seen as increasing tax risk and bringing greater complexity, ultimately having a consistent tax platform is important to global businesses.

Similarly, the European Commission is launching initiatives to address tax evasion and tax fraud with the focus on improving tax transparency and create a more fair tax environment within the European Union.

During 2016 and 2017, individual territories have started to frame their responses to the BEPS initiative.

These initiatives highlight the importance that companies should give to consideration of risks relating to tax as these can have significant effects on the recognition and measurement of tax balances.

The United States Tax Cuts and Jobs Act
The United States Tax Cuts and Jobs Act ('the US Tax Act') was signed into law on 22 December 2017 and introduces significant changes in US tax laws taking effect on 1 January 2018. The US Tax Act reduces tax rates and modifies policies, credits, and deductions for individuals and businesses. As the Act was signed into law quite close to the calendar year end some EU issuers and auditors have expressed concerns over their ability to account fully for the effects of the act in their 2017 financial statements under IAS 12. In January 2018 ESMA issued a statement to reduce inconsistency in the application of IFRS in the EU. The statement reminds issuers of their obligations under IAS 12 and the fact that there is no relief from these requirements where complex legislation is substantively enacted close to the year-end. While they acknowledge that a full understanding of the implications of the Act will take some time to assess, they do expect issuers to a reasonable estimate of the impact of the material aspects of the Act on their current and deferred taxes in their 2017 annual financial statements. They further acknowledge that these reported amounts may be subject to a higher degree of estimation uncertainty than usually the case and that measurement adjustments may need to be made in subsequent reporting periods. It should be noted that disclosure of this fact should be reflected in the 2017 financial statements if the effect is deemed to be material.

- the disclosure of the UTP liability is considered by IAASA to be relevant information for an understanding of the line item 'current income tax liability' in accordance with IAS 1.112(c).

IAASA concluded that the UTPs are separate liabilities comprising specific individual balances (i.e. the unit of account is the individual UTP rather than the aggregated current tax liability). IAASA also observes that the nature and the carrying amounts recognised in respect of individual material UTPs falling within the scope of IAS 1.125 must be disclosed. In instances where the tax balances does not contain individually material UTP amounts but the UTP liabilities are material on an aggregated basis, then issuers must disclose the nature and the carrying amounts of the UTP liabilities at an aggregated level.

Impairment Testing – IAS 36 Impairment of Assets
The performance and disclosure of impairment reviews remains an area of regulatory challenge. In conducting an impairment review under IAS 36 Impairment of Assets, it is important to consider carefully all inputs into a calculation of value-in-use (both cash flow forecasts and the discount rate(s) applied to them). It is also important to exercise care in the identification of cash-generating units and in aggregating those cash generating units for the purposes of testing goodwill for impairment. An appropriate discount rate should also be applied to each cash-generating unit (or group of cash-generating units) rather than the same rate being applied across an entity.

In terms of disclosure, the following should be considered:

- Pre-tax discount rates, reflecting current market assessments of the time value of money and the risks of each cash-generating unit or group of cash-generating units, should be disclosed.

IASB Practice Statement – Making Materiality Judgements
The consideration of materiality in financial statements, including what information should be excluded to avoid 'disclosure overload' remains a significant issue in financial reporting. Recognising this, in September 2017 the IASB issued a Practice Statement providing guidance on how to make materiality judgements in preparing financial statements. The guidance is non-mandatory and, as such, not subject to EU-endorsement so is available for immediate use.

The Practice Statement lays out a four-step process that could be helpful in framing a consideration of whether items are material, although it acknowledges that other methods may also be appropriate.

- Step 1 – Identification of potentially material information, taking into account both the requirements of accounting standards and the information needs of primary users.
- Step 2 – Assessment of whether this information is material through consideration of various quantitative and qualitative factors.
- Step 3 – Organisation of information identified as material to communicate it effectively and efficiently.
- Step 4 – An overall review of the draft financial statements to determine whether all material information has been identified as an item judged immaterial in isolation could be deemed material in the context of other information in a complete set of financial statements.

A Deloitte 'Need to know' publication provides more detail on the Practice Statement.

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- Key assumptions behind value-in-use calculations (not restricted to discount and terminal growth rates) and the approach to determining those assumptions should be disclosed.
- A quantified sensitivity analysis is required when a reasonably possible change in assumptions would result in impairment of goodwill.
- The reasons for significant changes in, for example, discount rates compared to previous years should also be explained.

Examination of compliance with IAS 36 has been a recurring theme with IAASA in recent years. Accurate forecasting of cash flows (both timing and amount) has become increasingly difficult in recent years and requires significant management judgement. IAASA has noted room for improvement in disclosures of the key impairment judgements and is currently conducting a desk-top thematic survey of issuers' impairment testing methodologies which includes looking at the following topics:

- whether or not Cash Generating Units (CGUs) have been tested for impairment at an appropriate level;
- the period covered by issuers value-in-use cash flow forecasts – whether the forecast period appears long enough to achieve 'normalised' growth and profit margins;
- consistency or otherwise of the CGU used for impairment testing with the segment reporting;
- the approach to determining the key assumptions and whether greater weight has been given to external evidence;
- whether all key assumptions are realistic and consistent with other information in the financial statements e.g. segment disclosures;
- long terms growth rates and the discount rate (including determining the terminal values);
- aggregation or disaggregation of the relevant assumptions by class of CGU; and
- enhanced disclosures required when a reasonably possible change in a key assumption would cause the CGU(s) carrying amount to exceed its recoverable amount [IAS 36.134(f)].

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Business combinations

Business combinations are often very large, very complex transactions that can give rise to a variety of issues not encountered in other circumstances. Some of these issues are discussed below.

Identification of a business combinations and of the acquirer

In characterising a transaction in which, by whatever means, one entity obtains control of another, it is first necessary to ask two questions:

- Is this a business combination?
- If so, which entity is the acquirer?

These questions are significant as they determine, firstly, whether the fair value exchange model of IFRS 3 *Business Combinations* (resulting in the recognition of assets and liabilities at fair value and of goodwill) applies, or whether a cost allocation approach (with no goodwill recognised) is appropriate and, if there is a business combination, which of the entities' assets and liabilities should be fair valued (the acquiree) and which should not (the acquirer). As such, insufficient consideration of these points can give rise to fundamentally incorrect accounting.

IFRS 3 provides guidance on both of these issues, but by means of a number of indicators that must be considered carefully. This can be a judgemental exercise requiring input from experts, but is not one that should be undertaken in isolation of other elements of financial reporting. In particular, assumptions used to value an intangible asset (for example, its useful life) should be consistent with assumptions used in subsequent impairment reviews and in determining the period over which an asset is amortised.

Identification and valuation of intangible assets

Business combinations resulting in the recognition of a large amount of goodwill, but few or no intangible assets are likely to attract regulatory attention.

IFRS 3 requires the recognition at fair value of intangible assets that are either separable (capable of being separated from the acquiree and monetised in some way) or that arise from contractual or legal rights. This results in the recognition of many assets (e.g. brands and customer relationships) that might not be recognised outside a business combination. Careful consideration of which assets should be identified is needed.

Once intangible (and, indeed, other) assets are identified, their fair value must then be determined in accordance with IFRS 13 *Fair Value Measurement*.

IAASA published in 2016 a paper entitled "Recognition of Intangible Assets and Scale of Acquisition Activity – a survey" setting out the results of a desk-top survey.

Following on from this and developments relating to IFRS 3 IAASA anticipates that it will continue to engage with issuers on:

- directors' judgements as to why certain intangible assets have not been recognised in a business combination;
- directors' key assumptions used in determining the fair value measurement of intangible assets;
- significant factors used to determine the useful lives of material intangible assets;
- methods used to amortise intangible assets;
- required disclosures for intangible assets with indefinite useful lives; and
- acquisition related liabilities including debt like items and contingent consideration.

Consideration vs Remuneration

It is often the case, particularly in the acquisition of an owner-managed business, for one or more shareholders of an acquiree to continue as employees of the enlarged group after the business combination has completed. In such cases, it becomes important to determine whether payments due to those people are:

- consideration for the business combination (in which case a liability is recognised at the date of acquisition, with only subsequent movements in its value recognised in profit or loss); or

- remuneration for post-combination employment (in which case no liability is recognised at the date of acquisition, with the payments recognised in profit or loss in full as an employee cost over the related service period).

Paragraphs B54-B55 of IFRS 3 provide guidance on making this judgement, but should be read in light of the January 2013 agenda decision by the IFRS Interpretations Committee that contingent payments which are automatically forfeited if employment terminates are remuneration for post-combination services.

Bargain purchases
In most business combinations, the value of consideration paid by the acquirer exceeds the fair value of the acquiree's identifiable net assets, resulting in (subject to adjustments in respect of non-controlling interests and previously held equity interests in the acquiree) the recognition of goodwill.

However, in the rare circumstances of a 'bargain purchase' this relationship is reversed, resulting in the recognition of an immediate gain in profit or loss but only after a reassessment of whether all relevant assets and liabilities have been identified and whether the fair values of all relevant items have been appropriately determined. It is important that such a reassessment is performed robustly and if it is finally determined that a bargain purchase has occurred, that appropriate disclosure is provided on how assets and liabilities were reassessed and why a bargain purchase arose (sometimes due to the requirements of IFRS 3 to measure certain assets and liabilities at other than fair value).

Transactions not addressed by IFRS 3
Given the range and complexity of business combination transactions, it is perhaps unsurprising that IFRS 3 does not address every possible variant that arises in practice. Notably, the standard:

- Excludes from its scope the accounting for business combinations under common control (BCUCC), with no other IFRS specifically addressing such transactions.
- Does not address the treatment of a Mandatory Tender Offer (MTO) under which law or regulation requires an acquirer to offer to purchase shares held by remaining non-controlling interests.

An accounting policy for BCUCC is often, using the hierarchy in IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*, developed by reference to other accounting frameworks, sometimes resulting in the use of 'merger' or 'pooling of interest' accounting.

The IFRS Interpretations Committee discussed the issue of MTOs in March 2013. No final conclusions were reached but the Committee highlighted the need to determine whether either a contractual financial liability (as defined in IAS 32 Financial Instruments: Presentation) or an onerous contract (in the scope of IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*) arise in the circumstances of a particular MTO.

In both cases, it is important that an accounting policy is applied consistently between transactions and is properly disclosed.

The importance of disclosure
Given the complexity of many business combination transactions and the level of judgement required in measuring resulting assets and liabilities, proper disclosure becomes particularly important.

Amongst other things, clear disclosure should be provided on:

- Business combinations for which the accounting is incomplete at the end of the reporting period in which the combination occurred. In those circumstances, IFRS 3 requires disclosure of the fact that provisional values have been used, why that is the case, the provisional amounts used and any adjustments recognised during the 12 month 'measurement period' permitted by the Standard.
- Assumptions and sensitivities in fair value measurements. For example, contingent consideration

based on a company's future performance is required to be measured at fair value on an ongoing basis and is likely to fall into 'Level 3' of the fair value hierarchy, requiring detailed disclosures under IFRS 13 *Fair Value Measurement.*

Non-recurring fair value measurements at the date of a business combination are outside the scope of IFRS 13's disclosure requirements (although IFRS 3 does require disclosure of acquisition date fair values, it does not specify disclosure of the methodology used to determine those values). In its common enforcement priorities, ESMA encourages disclosure of the assumptions and measurement techniques used in business combination valuations be provided in light of the general requirements of IAS 1 in respect of estimation uncertainties.

In instances where more than one business combination has been undertaken in the year, care should be taken before concluding that aggregation of the disclosures is appropriate as IFRS 3 requires each material business combination to be disclosed separately.

Statement of cash flows

The proper presentation of cash flows and related disclosures remain an area of regulatory focus, with issues raised on amongst other things:

- Purchases of shares from non-controlling interests which should, consistently with their treatment as an equity transaction, be classified as financing cash flows.
- Payments such as acquisition expenses which might be thought of as relating to an investment but do not result in a recognised asset and, as such, should be classified as operating cash flows.
- Factoring transactions, with care needed in the classification of cash in and outflows as operating or financing depending on the circumstances of the transaction. Proper disclosure of an entity's use of, and reliance upon, factoring facilities is also encouraged.

Outside the statement of cash flows itself, it should be noted that amendments to IAS 7, requiring disclosure of changes in liabilities from financing activities (sometimes termed a 'gross debt reconciliation'), are effective for December 2017 year-ends. Presentation of a 'net debt reconciliation' is already common practice and one which remains acceptable, but previously adopted presentations should be reviewed to ensure they comply with the requirements of the amended standard – particularly that they enable users to link items in the reconciliation to the statement of financial position and statement of cash flows.

More generally, disclosures supporting the statement of cash flows should not be overlooked. For example, policies on the identification of cash and cash equivalents and in respect of uncommitted bank facilities and cash pooling facilities and any 'restricted cash' balances should be clearly explained. Restricted cash disclosures might be particularly relevant for groups operating in jurisdictions with controls over currency exchange or repatriation.

Reporting the effects of income tax

A Deloitte 'Need to know' publication provides more detail on issues surrounding the reporting of income tax.

The reporting of income tax remains an area of high focus, both from the point of view of quality reporting on, for example, the effects of uncertain tax positions (discussed above) and possible future changes to a company's effective tax rate, but more generally as a result of regulatory and media scrutiny of companies' tax affairs.

Many generic elements of quality financial reporting are relevant to income tax. For example:

- **Accounting policies** related to tax should be clear, specific to the group's circumstances and should address all key issues including the recognition and measurement of uncertain tax positions, if relevant.
- Income tax is a common source of **estimation uncertainty**, particularly in respect of uncertain

tax positions (discussed above), to be disclosed in accordance with IAS 1. Significant risks of material adjustment in the next financial year should be disclosed, including quantitative information such as sensitivities or ranges of possible outcomes. The possibility of material adjustments in later periods is also valuable information which could be included in, for example, the tax note.

- The business review should include an appropriate discussion of tax, particularly on variances in and expectations of the effective tax rate. Income tax should also be considered as a potential principal risk.
- The effects of income tax should be appropriately reflected in **reporting financial performance**. For example, a policy on presentation of 'exceptional' or 'non-recurring' items should cover the reporting of items such as one-off tax credits.

The effective tax rate reconciliation required by IAS 12 should also be prepared carefully so that it provides clear information about the key factors affecting the effective tax rate and its sustainability in the future. This can be achieved by describing the nature of reconciling items and why they have arisen and by distinguishing clearly between significant one-off or unusual items and those that are expected to recur.

Interest and penalties relating to income taxes
The September 2017 IFRIC Update reported an agenda decision by the IFRS Interpretations Committee on the treatment of interest and penalties charged by a tax authority for late payment of an income tax liability. The Committee concluded that the determination of whether such a cost is within the scope of IAS 12 Income Taxes (and, as a result, presented within the tax line in profit or loss) or IAS 37 Provisions, Contingent Liabilities and Contingent Assets (and, as a result, presented as an operating or finance cost) is not an accounting policy choice but should be considered based on the circumstances in which the interest or penalty arose.

It is appropriate to base this judgement on whether interest and/or penalties can be seen as forming part of a larger uncertain tax position (for example, if interest or penalties are accepted as a cost of delaying payment to avoid prejudicing the overall tax position).

Regardless of the judgement reached, information about material interest and penalties should be disclosed.

Recognition of deferred tax assets
IAS 12 requires entities to recognise a deferred tax asset derived from deductible tax differences and unused tax losses (even if the entity is currently loss making) over and above the level of deferred tax liabilities relating to the same taxation authority and taxable entity provided that it is probable that the entity will generate future taxable profits to utilise the benefit from them. In many cases, the assessment as to whether the entity will generate future taxable income involves the use of significant judgement, for example the time period considered (which should be based on the facts and circumstances of the entity rather than an arbitrary limit), tax planning strategies, impact of future contracts etc.

Entities are required to disclose the judgements made and evidence that supports the recognition of those deferred tax assets. For example, where a company is loss making, disclosure of the evidence over the availability of future profits to support a deferred tax asset is required.

Defined benefit pension schemes
Defined benefit pension schemes are a complex area of accounting, giving rise to a surplus or deficit figure that is in fact the net of:

- The obligation to pay benefits to members, measured using the projected unit credit method.

- Plan assets, measured at their fair value.
- The effect of IAS 19's 'asset ceiling', a function of the refunds or reductions in future contributions available to the employer.

As a result, even when the statement of financial position shows a small (or even nil) net position, that can result from two or three very large balances subject to future changes subject to different risks and uncertainties. This, in conjunction with the complexity of some pension arrangements (either the plan itself, or the employer's strategy to fund it), means that effective disclosure of the arrangement and of the judgements applied in accounting for it is important to investors.

IAS 19 includes many disclosure requirements in respect of defined benefit schemes (for example, a reconciliation of opening and closing amounts for each of the three balances above and a description of the rules and regulatory framework under which the plan operates). However, high quality financial reporting requires consideration of what detail is needed to fulfil the purpose of each disclosure, particularly in respect of the amount, timing and uncertainty of future cash flows.

- **At a minimum**, IAS 19 requires disclosure of the expected contributions to be paid in the next accounting period. A fuller understanding of the funding arrangements affecting future contributions can be provided by disclosure of:
  - Expected contributions for subsequent years, distinguishing between deficit remedy payments and payments relating to current service.
  - The system for revision of contribution levels, often as part of a funding valuation exercise.
  - Any interdependencies between pension contributions and other transactions. For example, in the UK it can be the case that, to ensure plan members are not disadvantaged, increased levels of dividend payments require an increase in contributions to a company's pension scheme.
- A sensitivity analysis is required for each significant actuarial assumption (e.g. discount rate, inflation forecast and mortality rates). In uncertain times, the level of variation in these amounts that is deemed '**reasonably possible**' should be reassessed at each reporting date. It should also be noted that the level of possible variation may differ between actuarial assumptions.
- **Asset-liability matching strategies** (for example, longevity swaps) are becoming more common and more complex in the UK. Effective disclosure includes not just the existence of such arrangements but also of the underlying nature of such instruments, the risks inherent in the strategy adopted and the means by which they are valued.

In respect of plan assets more generally, an appropriate level of disaggregation (beyond simply quoted and unquoted assets) can provide valuable insight into a plan's investment strategy and the risks to which it is exposed.

Due to the requirements of IAS 19 and of IFRIC 14 IAS 19 – *The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction* in respect of the effect of the asset ceiling and the complexity of many funding requirements, a significant level of judgement can be required in determining whether a net surplus (or, indeed, liability for a minimum funding requirement) should be recognised. In circumstances where this is relevant, a clear description (as per paragraph 122 of IAS 1) of the judgements made in respect of this accounting requirement should be provided. This will often need to cover the assessment of **trustees' rights** to either enhance members' benefits or wind up the plan before making any payment back to the employer.

Discussion of a company's pension arrangements should not be limited to the financial statements. A high quality Directors' Report should provide an explanation of significant changes in a surplus or deficit (addressing, for example, changes in discount and/or inflation rates), actions being taken to remedy a deficit and risks and uncertainties arising from the scheme.

Topical issues

Reporting on the year to 31 December 2017

Other topics

IAASA have also highlighted the following items in their observations document:

- **IAS 37 Provisions, Contingent Liabilities and Contingent Assets – class of provision** IAASA challenged issuers' directors on their rationale as to why different classes of provisions were aggregated into one single class of provision. As a result, the disclosures required by IAS 37.84 and IAS 37.85 were only provided for the aggregated class of provisions. It is IAASA's expectation that issuers will provide the disclosures required by IAS 37.84 and IAS 37.85 by class of provision.

- **IFRS information located outside the financial statements** IAASA has identified instances where issuers have relied upon information presented outside the audited financial statements to comply with IFRSs including but not limited to IFRS 7. On a number of occasions, IAASA has determined that issuers either failed to cross-reference to information outside the financial statements or the cross-reference provided did not clearly link the financial statements to the relevant information located outside the financial statements. In IAASA's view, such a practice reduces the understandability of the information provided as not all the information located outside the financial statements is intended to comply with IFRS and much of this information will not have been audited.

  IAASA reminds issuers which present information required by IFRS outside the financial statements to:

  A. ensure that the relevant IFRS being applied permits the disclosure of information outside the financial statements;
  B. cross-reference, clearly, from the relevant note in the financial statements directly to information located outside the financial statements that is intended to provide the information required; and
  C. identify precisely the information that is intended to provide the information required by IFRS 7.31 – 41.

- **IFRS 8 Operating Segments – aggregation criteria** Paragraph 22(aa) of IFRS 8 requires issuers to disclose "the judgements made by management in applying the aggregation criteria ... This includes a brief description of the operating segments that have been aggregated in this way and the economic indicators that have been assessed in determining that the aggregated operating segments share similar economic characteristics".

  IAASA reminds those issuers electing to aggregate operating segments into reportable segments for the purposes of IFRS 8 of the disclosure requirements in this regard.

- **Separately disclosed items, exceptional items and non-recurring items – Accounting policy** IAASA has challenged issuers on their accounting policy for separately disclosed items, exceptional items and non-recurring items. It is IAASA's expectation that issuers will disclose a comprehensive accounting policy for these items which properly reflect the specific principles, bases, conventions, rules and practices applied by the directors in preparing and presenting financial statements.

- **Financial reporting of Debt issuers and Closed-Ended Funds ('CEFs')** As at 31 December 2016, a total of 91 issuers (CEFs and debt issuers) had recognised total assets amounting to almost €500bn. As has been reported by IAASA in previous years' Observations documents, the quality of financial reporting by these issuers varies considerably ranging from good to very poor. While acknowledging those issuers which have produced high quality financial reports there remains a cohort of issuers which consistently present poor quality financial statements.

  IAASA recommends that Management, Directors and Audit Committees of CEFs and debt issuers should make themselves aware of IAASA publications and enforcement decisions of relevant CEFs and debt issuers and reassess the quality of the financial statements.

  For entities that issue multiple and segregated series of financial instruments (i.e. listed debt) IAASA recommends that these specific types of entities present the notes to the financial statements by class of financial assets and financial liabilities rather than at an aggregated level.

- **Restatement of comparative amounts** IAASA has detected an increasing number of instances where issuers have restated comparative amounts or have retrospectively corrected material prior period errors and have failed to provide the required IAS 8 disclosures. Where issuers fail to adequately provide the required disclosures it limits the ability of users to understand the nature of and reasons for reclassifications. A common explanation for the reclassification of comparative amounts provided by issuers is 'to more appropriately reflect and enhance comparability'. Depending on the circumstances, such an explanation may not comply in full with the disclosure requirements of IAS 1 and IAS 8.

Irish GAAP developments

The following are the principal amendments to FRS 102 published in December 2017 which are effective for accounting periods beginning on or after 1 January 2019, with early application available:

- Amendments to incorporate the small entities and micro-entities regimes in Irish Company Law (effective for accounting periods beginning on or after 1 January 2017);
- The simplification of the measurement of directors' loans to small entities, following the interim relief granted earlier this year;
- Requirement for fewer intangible assets to be separated from goodwill in a business combination;
- Permission for investment property rented to another group entity to be measured by reference to cost, rather than fair value;
- Expansion of the circumstances in which a financial instrument may be measured at amortised cost, rather than fair value; and
- Simplification of the definition of a financial institution.

Companies (Accounting) Act 2017

The Companies (Accounting) Act 2017 (the '2017 Act') commenced on the 9th June 2017 and marks the most significant update to Irish Company Law since the Companies Act 2014 (the '2014 Act'). The 2017 Act is applicable to financial accounting periods beginning on or after 1 January 2017 with early adoption available for financial accounting periods beginning on or after 1 January 2015. However, the early adoption must be of all the specified provisions of the Act as set out in S.14 of the 2017 Act. The 2017 Act adds to or amends 2014 Act but does not amend the legal citation for financial statements which should still just refer to the "Companies Act 2014".

The following company information disclosure requirements will affect all companies reporting under the 2017 Act:

- The name and legal form of the company
- The place of registration of the company and the number under which it is registered
- The address of its registered office
- Where the company is being wound up, the information required by section 595 - generally a statement that the company is being wound up.

In addition to the above a number of other changes will impact certain companies depending on their individual circumstances. The key changes to be aware of are as follows:

- **Directors' Remuneration Disclosures** - S.305A of 2014 Act as amended now requires that "payments made to third parties for making available the services of directors" are disclosed.

  S.307 now requires disclosure of amounts of loans, quasi-loans and credit to Directors (or connected persons) that have been waived during the year.

- **Directors' Report** - When the group (i.e. holding company and subsidiary) acquires, holds or disposes of own shares, the following additional disclosures are required to be made in the Directors' Report (S.328):

- The reasons for any acquisitions made during the financial year; and the proportion of called-up share capital held at the beginning and end of the financial year.

In the case of Public Interest Entities (PIEs) the directors' report shall also contain details of the date of appointment of the PIE's statutory auditor or audit firm. Where a PIE has sought an extension from the Supervisory Authority under Regulation 105, pursuant to Article 17(6) of Regulation (EU) No 537/2014, the directors' report shall also contain details of the extension granted.

- **Entity Profit & Loss Exemption in Group Accounts** – the company's entity balance sheet must show the company's profit or loss for the financial year (s.304(1)(b)). In cases where Parent companies are applying the exemption from providing the company's P&L Account, the parent company's profit & loss account is still required to be approved by the directors, in accordance with section 324.
- **Thresholds** – The criteria for companies to qualify as small and medium sized companies are now as follows:

	Micro	Small	Medium
Net Turnover	€700,000	€12,000,000	€40,000,000
Balance Sheet Total	€350,000	€6,000,000	€20,000,000
Average Employees	10	50	250

- **Changes Relating to Formats** – The profit and loss account format options have been reduced from four to two (old formats three and four have been deleted). There is also more flexibility permitted in the presentation of the profit and loss account and the balance sheet, providing the information presented is "at least equivalent to that which would have been required by the use of such format had it not been thus adapted" and is "in accordance with generally accepted accounting principles or practice". This change may facilitate wider adoption of FRS 101 by IFRS group companies.
- **Intermediate Parent Consolidation Exemption** - The conditions to be met to avail of the intermediate parent consolidation exemption have now been extended. Where the higher parent holds more than 90% of shares in the intermediate company the remaining shareholders must all approve the availing of the exemption. If the higher parent holds 50% - 90% then the exemption is only available if shareholders holding more than half of the remaining shares or holding 5% or more of the total shares have not served notice requesting the parent to prepare consolidated accounts.
- **Comparative Movement in Fixed Assets and Provisions** – There has been a reinstatement of the relief from providing comparatives relating to note disclosures of movements in fixed assets and provisions. However, comparatives are still required for movements in reserves.

Topical issues

Reporting on the year to 31 December 2017

Climate-related Financial Disclosures

In June 2017, the Task Force on Climate-related Financial Disclosures (TCFD), a body set up by the Financial Stability Board, published its final recommendations for effective disclosure of climate-related financial risks. The TCFD recommends inclusion in mainstream corporate reporting of information on:

- An entity's governance structure in respect of climate-related risks and opportunities.
- The actual and potential impacts of changes in climate on business, strategy and financial planning. This is expected to take into account a scenario of a 2°C increase in global temperatures.
- How the organisation identifies, assesses and manages climate-related risks.
- The metrics and targets used in assessing and managing climate-related risks and opportunities.

Over 100 CEO's of large, multi-national organisations have publicly stated their support for the TCFD's initiative and urged other companies to support better disclosures of climate-related risks and opportunities.

A Deloitte 'Need to know' publication provides more detail on TCFD's recommendations.

Reporting on dividend policy and practice

In October 2017, the FRC's Financial Reporting Lab published an implementation study: Disclosure of dividends – policy and practice, examining how companies have responded to its previous report published in 2015 on a topic which remains an area of high investor interest.

The 2015 report recommended a number of enhancements to the reporting of:

- **Dividend policy**, to provide:
  - An understanding of the board's considerations in setting dividend policy.
  - The rationale for the approach selected.
  - Sufficient detail on how the policy will operate.
- **Dividend practice**, including:
  - The key judgements and constraints considered by the board in applying its dividend policy.
  - The availability of resources (including cash and distributable profits) needed to pay dividends, particularly when this is a constraining factor.
  - Clear linkage between the policy and how it has been applied in the period.

The 2017 study reveals an increasing level of uptake of these recommendations amongst FTSE 100 companies, with nearly half now providing either quantitative information on distributable reserves or a reference to them being 'sufficient' or 'significant'. Fewer FTSE 250 companies are providing such disclosures.

The Lab's report also identifies that further improvements could be made on:

- Identification of links between dividend strategy and required elements of narrative reporting, specifically the business model, viability statement and principal risks.
- Enhancing disclosure of constraints on dividend payments through details on the sustainability of a dividend or the levels of cash and distributable profits.
- Explaining more clearly what a dividend policy means in practice, for example by clarifying terms such as 'progressive policy' and 'pay-out ratio'.
- Clarity over structure and process, covering where profit is generated in the group and how that profit flow to the parent company together with any relevant constraints on that flow (for example, a 'dividend block' restricting distribution of profits from a subsidiary to its parent company).

Given the high and continuing level of investor interest in this area, the Lab's suggestions should be carefully considered in preparing 2017 annual reports.

A Deloitte 'Need to know' publication provides more guidance on the Financial Reporting Lab's recommendations and wider issues surrounding distributions.

A Deloitte 'Need to know' publication provides more guidance on realised and distributable profits under the Companies Act 2006

Appendices

The EU Non-Financial Reporting Directive

The requirements of the EU Non-Financial Reporting (NFR) Directive have been enacted Irish law and are effective for periods beginning on or after 1 August 2017. The following are the disclosure requirements under the new legislation and the companies to which the requirements apply:

Disclosure Requirement	Disclosure Content	Companies Impacted
Non-Financial Statement (included as a specific section in the Directors' Report)	A. information, to the extent necessary for an understanding of the development, performance, position and impact of its activity relating to, at least, the following matters: i. environmental matters; ii. social and employee matters; iii. respect for human rights; iv. bribery and corruption, B. a brief description of the company's business model C. a description of the policies pursued by the company in relation to the matters referred to in paragraph (a), including due diligence processes implemented and a description of the outcome of those policies D. a description of the principal risks related to the matters referred to in paragraph (a), linked to the company's operations including, where relevant and proportionate i. its business relationships, products or services which are likely to cause adverse impacts in those areas, and ii. how the company manages those risks E. an analysis of the non-financial key performance indicators relevant to the particular business	A Company which in relation to a financial year: i. qualifies as a large company under section 280H* of the Companies Act 2014, ii. has an average number of employees which exceeds 500, and iii. is an ineligible entity**
Diversity Report	A. a description of the diversity policy applied in relation to the company's board of directors with regard to aspects such as age, gender or educational and professional backgrounds B. the objective of that diversity policy C. how that diversity policy has been implemented by the company D. the results of that policy in the financial year	Large Traded Companies

* A large company is any company that does not qualify as a micro, small or medium company

** An ineligible company is one that:
i. have transferable securities admitted to trading on a regulated market of any Member State
ii. are credit institutions
iii. are insurance undertakings
iv. fall within any of the provisions of Schedule 5
v. are otherwise designated

Appendices

ESMA guidelines on 'Alternative Performance Measures' and IOSCO statement on 'Non-GAAP Financial Measures'

Concerns over the proper use of performance figures other than those stipulated by IFRSs has been an area of concern for regulators in many jurisdictions around the world. As can be seen below, the ESMA Guidelines on Alternative Performance Measures (APMs) are very similar to a Final Statement on Non-GAAP Financial Measures issued by the International Organisation of Securities Commissions (IOSCO) in 2016.

Other regulators have their own requirements that limit (in some case more strictly than these guidelines) the use of such information.

ESMA Guidelines on Alternative Performance Measures
Scope – Applies to 'Alternative Performance Measures' being financial measures of historical or future financial performance, financial position or cash flows other than a financial measure defined or specified in the applicable financial reporting framework. APMs disclosed in financial statements are not within the scope of guidelines. The guidelines are also not applicable to: – physical or non-financial measures; – information on major shareholdings, acquisitions or disposals of own shares and total number of voting rights; or – information to explain compliance with the terms of an agreement (such as a lending covenant) or legislative requirement (such as the basis of calculating directors' remuneration).
Presentation and **Explanation on the use of APMs** – A clear and readable definition of APMs should be provided. APMs should also be given meaningful labels reflecting their content and basis of calculation. The use of APMs should be explained to allow users to understand their relevance and reliability.
Presentation – Overly optimistic or positive labels for APMs should not be used.
Prominence and presentation of APMs – APMs should not be displayed with more prominence, emphasis or authority than, or distract from, measures directly stemming from financial statements. The ESMA Questions and Answers stress that the notion of prominence is a qualitative as well as a quantitative one, covering factors such as font size, frequency of use and location within the document.
Reconciliations – Each APM should be reconciled to its most directly reconcilable item in the financial statements. The ESMA Questions and Answers provide specific guidance on the reconciliation of an 'organic growth' figure to IFRS revenue.
Comparatives and Consistency – APMs should be presented consistently from period to period with comparative information provided. Any changes to the definition or calculation of an APM (or cessation of use of an APM) should be explained, with restated comparative figures provided.
Presentation – Items should not be mislabelled as non-recurring, infrequent or unusual. For example, items that affected past periods and will affect future periods (such as restructuring costs or impairment losses) will rarely be considered as non-recurring, infrequent or unusual.
Compliance by reference – Disclosure principles in the guidelines may be replaced by a direct reference to other documents previously published which contain disclosures on APMs and are readily and easily accessible to users.

Appendices

IOSCO Statement on Non-GAAP Financial Measures
Scope – Applies to 'non-GAAP financial measures' being numerical measures of an issuer's current, historical or future financial performance, financial position or cash flow that is not a GAAP measure (defined as a measure determined pursuant to the issuer's financial reporting framework included in, for example, a press release or narrative section of an annual report). Disclosures contained within the financial statements are not within the scope An operating or statistical measure that is not a financial measure is not within scope.
Defining the non-GAAP Financial measure – The measure should be defined, explained (including a statement that it is not a standardised measure), clearly labelled and the reason for its use (including an explanation of why the information is useful to investors) explained.
Unbiased purpose – Non-GAAP measures should not be used to avoid the presentation of adverse information.
Prominence of presentation of GAAP measures – Non-GAAP measures should not be presented with more prominence than the most directly equivalent GAAP measure.
Reconciliation to comparable GAAP measures – A clear and quantitative reconciliation to the most directly equivalent GAAP measure should be provided.
Presentation consistently over time – Comparative values should be presented and non-GAAP measures generally presented consistently from year to year. Any changes to a non-GAAP measure (or cessation of use of a non-GAAP measure) should be explained with comparative figure adjusted accordingly.
Recurring items – In IOSCO's experience, there are rarely circumstances in which restructuring costs or impairment losses can be justified as being 'non-recurring', 'infrequent' or 'unusual'.
Access to associated information – Information supporting the use and calculation of non-GAAP measures should be readily available to users either by directly accompanying the measure or by a cross-reference to where the information is available.

Appendices

Amendments to accounting standards mandatorily effective for years ending 31 December 2017

IFRS	Effective Date-periods commencing on or after:	EU-endorsed effective Date – periods commencing on or after:
Amended Standards:		
Amendments to IAS 12 – Recognition of Deferred Tax Assets for Unrealised Losses	1 January 2017	1 January 2017
Amendments to IAS 7 – Disclosure Initiative	1 January 2017	1 January 2017
Amendments to IFRS 12 issued in the Annual Improvement Cycle 2014-2016	1 January 2017	At the time of writing, this amendment was expected to be endorsed in the first quarter of 2018 with an effective date of 1 January 2017.

Amendments to IAS 12 *Income Taxes* – Recognition of Deferred Tax Assets for Unrealised Losses

The amendments to IAS 12 clarify that unrealised losses on debt instruments measured at fair value for financial reporting purposes but at cost for tax purposes can give rise to a deductible temporary difference and how such a temporary difference should be assessed in determining whether a deferred tax asset should be recognised.

Amendments to IAS 7 *Statement of Cash Flows* – Disclosure Initiative

The amendments to IAS 7 require disclosure of both cash and non-cash changes in liabilities arising from financing activities (being liabilities for which cash flows were, or future cash flows will be, classified as being from financing activities).

Amendments to IFRS 12 *Disclosure of Interests in Other* Entities issued in the Annual Improvements Cycle 2014-2016

The amendments to IFRS 12 introduced in the 2014-2016 annual improvement cycle clarify that all requirements of that Standard (other than those covered by an existing exemption from disclosure of summarised financial information on interests in subsidiaries, joint ventures and associates) apply to interests classified as held for sale or discontinued operations in accordance with IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*.

IFRS Interpretations Committee agenda decisions in 2017

Along with its activity developing formal interpretations of IFRSs and proposing that the IASB make amendments to Standards, the IFRS Interpretations Committee regularly publishes summaries of issues that it has decided not to add to its agenda, often accompanied by a discussion of the accounting issue submitted.

Whilst the commentary included in an agenda decision is not formally part of IFRSs, it is an important source of guidance that should be carefully considered when selecting a suitable accounting policy for a transaction. In many jurisdictions, there is an expectation from regulators that agenda decisions will be considered, with ESMA, for example, publicly stating an expectation to this effect.

In 2017, the following agenda decisions have been published by the Committee.

March IFRIC Update	IFRS 10 – Investment entities and subsidiaries
	IAS 12 – Deferred taxes when acquiring a single-asset entity that is not a business
	IAS 28 – Fund manager's assessment of significant influence
	Commodity loans
June IFRIC Update	IAS 19 – Discount rate in a country that has adopted another country's currency
	IAS 32 – Centrally cleared client derivatives
	IAS 33 – Tax arising from payments on participating equity instruments
	IAS 41 – Biological assets growing on bearer plants
September IFRIC Update	IFRS 1 – Subsidiary as a first-time adopter
	IFRS 9 – Financial assets eligible for the election to present changes in fair value in other comprehensive income
	IAS 12 – Interest and penalties relating to income taxes
	IAS 38 – Goods acquired for promotional activities
November IFRIC Update	IFRS 3 – Acquisition of a group of assets

Appendices

New and revised IFRSs and Interpretations available for early application in years ending 31 December 2017

Paragraph 30 of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* requires entities to consider and disclose the potential impact of new and revised IFRSs that have been issued but are not yet effective. As discussed above, the sufficiency of these disclosures (particularly as they relate to IFRS 9 on financial instruments and IFRS 15 on revenue) is a current area of regulatory focus.

The list below reflects a cut-off date of 19 January 2018. The potential impact of the application of any new and revised IFRSs issued by the IASB after that date but before the financial statements are issued should also be considered and disclosed.

For those reporting under EU-endorsed IFRSs, to the extent that the below conflict with current standards, such items cannot be early adopted until they have been endorsed for use in the EU.

<table>
<tr><th>IFRS</th><th>IASB Effective Date – periods commencing on or after:</th><th>EU-endorsed effective Date – periods commencing on or after:</th></tr>
<tr><td>New Standards</td><td></td><td></td></tr>
<tr><td>IFRS 9 – Financial Instruments</td><td>1 January 2018*</td><td>1 January 2018</td></tr>
<tr><td>IFRS 14 – Regulatory Deferral Accounts</td><td>First time adopters whose first annual IFRS financial statements are for a period beginning on or after 1 January 2016.</td><td>EU has decided not to endorse as very few European companies would fall within its scope. **</td></tr>
<tr><td>IFRS 15 – Revenue from Contracts with Customers</td><td>1 January 2018</td><td>1 January 2018</td></tr>
<tr><td>IFRS 16 – Leases</td><td>1 January 2019</td><td>1 January 2019</td></tr>
<tr><td>IFRS 17 – Insurance Contracts</td><td>1 January 2021</td><td>TBC – Endorsement outstanding</td></tr>
<tr><td>Amended Standards</td><td></td><td></td></tr>
<tr><td>Amendments to IFRS 10 and IAS 28 – Sale or Contribution of Assets between an Investor and its Associate or Joint Venture</td><td colspan="2">The IASB decided in December 2015 to defer indefinitely the effective date of these amendments. EU endorsement has, likewise, been indefinitely postponed.</td></tr>
<tr><td>Clarifications to IFRS 15 Revenue from Contracts with Customers</td><td>1 January 2018</td><td>1 January 2018</td></tr>
<tr><td>Amendments to IFRS 4 – Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts</td><td>1 January 2018</td><td>1 January 2018</td></tr>
<tr><td>Amendments to IFRS 2 – Classification and Measurement of Share-based Payment Transactions</td><td>1 January 2018</td><td rowspan="2">TBC – Endorsement outstanding</td></tr>
<tr><td>Amendments to IFRS 1 and IAS 28 issued in the Annual Improvement Cycle 2014-2016</td><td>1 January 2018</td></tr>
</table>

Appendices

Amendments to IAS 40 – Transfers of Investment Property	1 January 2018	TBC – Endorsement outstanding
Amendments to IFRS 9 – Prepayment Features with Negative Compensation	1 January 2019	
Amendments to IAS 28 – Long-term interests in Associates and Joint Ventures	1 January 2018	
Annual Improvements to IFRS Standards 2015-2017 Cycle (issued on 12 December 2017)	1 January 2018	
Amendments to IAS 19 – Plan Amendment, Curtailment or Settlement	1 January 2019	

IFRIC Interpretations		
IFRIC 22 – Foreign Currency Transactions and Advance Consideration	1 January 2019	TBC – Endorsement outstanding
IFRIC 23 – Uncertainty over Income Tax Treatments	1 January 2019	

* For periods beginning before 1 January 2018, previous versions of IFRS 9 may be adopted provided the relevant date of initial application is before 1 February 2015.
** IFRS 14 is available only to first-time adopters of IFRSs who recognised regulatory deferral account balances under their previous GAAP and permits those entities to continue (with limited changes) their previous GAAP accounting for rate-regulated activities, although with separate presentation of balances and items of income and expense arising from that accounting. As the EU has decided not to endorse this standard for use in the European Union, the option to retain previous GAAP accounting on transition to IFRSs is not available to entities (such as those in the UK) required to apply EU-endorsed IFRSs.

The clarifications to IFRS 15 issued in April 2016 addressed a number of issues highlighted by discussions of the IASB and FASB's joint Transition Resource Group (TRG) for Revenue Recognition. Details of the group's discussions can be found here.

A similar group, the IFRS Transition Resource Group for Impairment of Financial Instruments (ITG) has been instigated by the IASB to discuss issues arising from the expected loss-based impairment model of IFRS 9. Details of this group's discussions can be found here.

A Transition Resource Group for Insurance Contracts has also been set up following publication of IFRS 17 with meetings scheduled to commence in 2018.

Deloitte resources

There are a number of resources prepared by Deloitte that can assist you during the upcoming reporting season. Many have been highlighted throughout this publication, key resources are listed below.

The Closing Out 2017 page on UK Accounting Plus

A dedicated page on UK accounting plus, providing links to a full suite of resources. This page will continue to be updated to reflect developments after the date of this publication.

Annual report insights 2017 – Surveying FTSE reporting

Our dedicated annual report insights site provides access to:

- Annual report insights: Surveying FTSE reporting which details the findings from our review of 100 listed UK company reports, covering a variety of contemporary issues in corporate reporting such as the use of Alternative Performance Measures, company purpose and the value generation story and the long-term viability statement.
- An updated **interactive benchmarking tool** enabling you to understand how your annual report stacks up against those of other listed companies.

Governance in focus – On the board agenda – the 2018 reporting season

This Governance in focus reviews the topics boards and their committees need to focus on in the 2018 reporting season including:

- an update on the UK corporate governance reform agenda and future changes to corporate governance;
- tips on stakeholder management and employee engagement;
- insight into crisis management and resilience – preparing for future crises;
- how to get the most from your internal audit function;
- a summary of developments in cyber risk and General Data Protection Regulations (GDPR); and
- a round-up of other emerging governance themes for 2018.

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