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ABU DHABI ACCOUNTABILITY AUTHORITY

ADAA IFRS digest

IFRS news, updates from ADAA, IASB and the Accounting Profession | **April 2017**

WHAT'S NEW THIS MONTH

ADAA's hot topics

G'day sport! Ten years on from the demise of Aussie GAAP we learn from Australia's IFRS journey.
IFRIC Update. It's technical, its detailed and mostly not on the agenda.
Right here, Right now IAS 7 Amendment.
EY IFRS Update. All the standards and interpretations in issue at 31 March 2017.
PWC IFRS news. IFRS 9, 15, 16 and IAS 32.
IASB Update. Goodwill and impairment in the IASB spotlight.
Its one thing to know something is wrong. It's another thing to act upon it.
UAE & VAT. Have you done your homework?
Deloitte IFRS in Focus. The IASB Disclosure initiative.
KPMG The Bank Statement. Even if you are not a bank you should read this.
And on the back page ***Escaping or embracing IFRS 16?*** An insight from ADAA's Syed Shabbir.

WHAT'S NEW FROM THE IASB?

The IASB is located in Cannon Street, London

G'day sport! Ten years on from the demise of Aussie GAAP we learn from Australia's IFRS journey. For listed entities IFRS has been positive:

- Greater scrutiny and analyst forecast accuracy.
- Much less earnings management than before.
- Annual reporting is longer but easier to read.
- Improved comparability with global peers for Australian entities financial reporting practices.
- However, prior AGAAP treatments for identifiable intangible assets deemed more appropriate. More here.

IFRIC Update. It's technical, its detailed and mostly not on the agenda. Fruit growing on oil palms are a biological asset. More here.

Right here, Right now IAS 7 Amendment. Investors seek two things:
1) By how much has net debt changed in the year.
2) By how much has cash and non-cash equivalents changed.
From January 2017 this is a required disclosure. More here.

IASB Update. Goodwill and impairment in the IASB spotlight. The IASB agenda papers can be a fascinating source of What Could Go Wrong. WCGWs to paraphrase one audit firm. Two models (FVLCTS & VIU), too complex, too many intangibles, too little information. First, the IASB is considering turning back the clock to 2004 and removing the reliably measurable test for the separation test of intangibles on acquisition. Hurrah we say. Intangible assets acquired in a business combination rarely deliver cash separate from the tangible assets of the business – just ask the people. So why was there any need to assess brand, customer relationship and any other intangible you could not shake a stick at? Second, the IASB realizes what UK GAAP realized in 1998 – Pre-existing internally generated goodwill of the acquirer can shield subsequent impairment testing of goodwill arising on acquisition of the acquiree. Which it should not be allowed to do. Third, goodwill changes over time. What is assessed subsequently isn't what was acquired. It is reported the Indian Premier League brand value is USD 4 billion. So why not sell it? It's just not cricket, you wouldn't buy the brand and leave the business behind.
Fair value or rather not fair value is one of IFIAR's top performers for audit and accounting errors. The IASB is correct, impairments are not recognised early enough, something has to change. More here.

WHAT'S NEW FROM THE ACCOUNTING PROFESSION?

And finally please turn the page for ADAA's monthly accounting insight…

EY IFRS Update. All the standards and interpretations in issue at 31 March 2017. All the large audit firms have many tools freely available to help you navigate the amendments and updates to IFRS. Choose your supplier or choose your favourite. In truth, there is not much change for 2017. You must say the impacts of IFRS 15 and 16 this year. You cannot still say you do not know. More here.

PWC IFRS news. IFRS 9, 15, 16 and IAS 32. When is a lease not a lease – when it is in the revenue standard. PWC are running a series of articles that cover aspects in the new standards you might not have thought of. Plus they set the context of a NIFRIC in IFRS.
A NIFRIC is 'Not an IFRIC' its an issue that was not taken on to the agenda. They are codified in the green book and technically have no standing.
PWC take us through them, this month the 14 NIFRICs in IAS 32. More here.

Its one thing to know something is wrong. It's another thing to act upon it. AICPA proposal raises the ethical bar. Link.

UAE & VAT. The GCC and the UAE is introducing VAT (most likely at 5%) on all goods and services of businesses that have a minimum turnover level from 1 January 2018. More here.

Deloitte IFRS in Focus. The IASB Disclosure initiative. It is widely commented IFRS financial statements are on the large side. However, instead of taking action to change the input the output remains the same. The most significant actions to take are to stop the cut and paste and tailor instead, less is more so remove the immaterial. Link.

KPMG The Bank Statement. Even if you are not a bank you should read this. A focus on stage transfer criteria. In other words measure the loss allowance as 12 month or life time expected credit losses. Link.

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Escaping or embracing IFRS 16? An insight from ADAA's Syed Shabbir

A final article from Syed. As we bade him farewell we thank him for his valued and insightful articles and wish him every success in his new role.

Operating leases are popular for an obvious reason: they keep liabilities off balance sheet. A sample of 1,022 listed companies using IFRS or US GAAP disclosed USD 3 trillion of off balance sheet lease commitments in 2014. An IASB survey concluded long-term liabilities of the heaviest users is understated by 27% in the African and Middle East region, 26% Europe, 22% America, 32% Asia/Pacific and a whopping 45% in Latin America!

Creativity is good, ask Banksy, but not in accounting. With the advent of IFRS 16 operating leases are gone and the search for elusive off balance sheet financing is at an all-time high. Financial reporting should merely be a true and fair result of appropriate accounting. Accounting should not influence business decisions but, unfortunately, this is not always the case. This article evaluates escape routes suggested by some, and the resulting consequences.

Voluntarily exceptions. Mainly two kinds of voluntary exceptions exist.

1- Short term lease exception. Entities may opt for this exemption, which is applied to leases with a lease term of 12 months or less. Expense are typically recognized on a straight line basis over the term of the lease (similar to IAS 17 operating leases). Consequentially, no balance sheet assets and liabilities are recorded other than prepaid and accrued lease payments.

Lease term is defined in IFRS 16, and is not necessarily the contractual maximum term. Especially for leases with expansion options or break clauses. Entities need to make a reasonably certain assessment of the lease term. The exemption cannot be applied to leases containing a purchase option. The exemption must be applied to all assets within the same class with a lease term of 12 months or less.

During the standard setting process the IASB discussed concerns about the possibility of *structuring contracts to qualify for the exemption*. Theoretically this could be done but not without economic consequences. There would be an economic disincentive for lessors to grant shorter leases, because shortening the lease term would increase the risk associated with a lessor's residual interest in the underlying asset. Consequently, the IASB is of the view that a lessor would often either demand increased lease payments from the lessee to compensate for this change in risk or refuse to shorten the non-cancellable period of the lease.

Accordingly, *be wary of economic consequences*, if lease modification is on the charts for you to avail this exemption.

2- Leases of low-value assets exemption. A lessee may elect not to apply the requirements of IFRS 16 for leases for which the underlying asset is of low value. The resulting effect on recognition of expense, asset and liability would be similar to the situation for the short-term lease exemption.
Low value assessment applies to the value of the underlying asset when new (regardless of the age of the asset being leased), on an absolute basis and irrespective of materiality.

The exemption cannot be used if the underlying asset is highly dependent on, or highly interrelated with, other assets or if the lessee cannot benefit from using the underlying asset on its own or with other readily available resources.
And the exemption cannot be applied to the head lease in a sublease arrangement.
The election for leases for which the underlying asset is of low value can be made on a lease-by-lease basis.

The IASB's underlying reasons for these two voluntary exemptions was pragmatic based on costs and benefits. IFRS reporters should use the exemptions in a similar spirit enjoying the substantive relief and focusing their time and efforts on improving their accounting and disclosure of IFRS 16 for users of financial statements.

Scope exceptions, specifically outsourcing. Certain types of arrangements will need detailed evaluation to determine if they are or continue to be leases, including outsourcing contracts, third party manufacturing contracts, power purchase contracts, equipment leases and transportation arrangements.

Generally outsourcing or contracting out is a business practice used by entities to reduce costs or improve efficiency by shifting tasks, operations, jobs or processes to a third party for a specified period of time. Prima facie, such arrangements are outside the scope of IFRS 16.

However, even if a contract is described as an outsourcing contract, or even said to not be a lease, it is still accounted for as a lease as long as it conveys the right to control the use of an identified asset in exchange for consideration. The new lease definition is the new on/off-balance sheet test.

Lease modification. Whether to achieve a desired accounting objective or done in the normal course of business, a lease modification will have accounting consequences. A lease modification is a change in the scope of a lease, or the consideration for a lease, that was not part of the original terms and conditions of the lease. Based on the underlying changes, a lessee may end up recognizing a lease modification as a separate lease if it increases the scope of the lease by adding the right to use one or more underlying assets and consideration increases by an amount commensurate with the stand-alone price for the increase in scope.
For a lease modification that is not a separate lease, at the effective date of the modification, the lessee accounts for the lease modification by remeasuring the lease liability using a discount rate determined at that date.

Concluding thought. Auditors often hear CEO's say 'the accounting should not drive the business.' We agree and say the business should not drive the accounting. Accounting is a happenstance result, concluded by professional accountants presenting information truthfully, based on relevant facts and circumstances, in accordance with appropriate accounting standards.
Transaction structuring and creative accounting should not be part of the equation.

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