This IFRS Supplement provides expanded discussions of accounting guidance under International Financial Reporting Standards (IFRS) for the topics in Intermediate Accounting. The discussions are organized according to the chapters in Intermediate Accounting (13th or 14th Editions) and therefore can be used to supplement the U.S. GAAP requirements as presented in the textbook. Assignment material is provided for each supplement chapter, which can be used to assess and reinforce student understanding of IFRS.

**DISCLOSURE ISSUES**

**Differential Disclosure**

A trend toward differential disclosure is also occurring. The IASB has developed IFRS for small- and medium-sized entities (SMEs). SMEs are entities that publish general-purpose financial statements for external users but do not issue shares or other securities in a public market. Many believe a simplified set of standards makes sense for these companies because they do not have the resources to implement full IFRS.

Simplified IFRS for SMEs is a single standard of fewer than 230 pages. It is designed to meet the needs and capabilities of SMEs, which are estimated to account for over 95 percent of all companies around the world. Compared with full IFRS (and many national accounting standards), simplified IFRS for SMEs is less complex in a number of ways:

- Topics not relevant for SMEs are omitted. Examples are earnings per share, interim financial reporting, and segment reporting.
- Simplified IFRS for SMEs allows fewer accounting policy choices. Examples are no option to revalue property, equipment, or intangibles, and no corridor approach for actuarial gains and losses.
- Many principles for recognizing and measuring assets, liabilities, revenue, and expenses are simplified. For example, goodwill is amortized (as a result, there is no annual impairment test) and all borrowing and R&D costs are expensed.
- Significantly fewer disclosures are required (roughly 300 versus 3,000).
- To further reduce standard overload, revisions to the IFRS for SMEs will be limited to once every three years.

Thus, the option of using simplified IFRS helps SMEs meet the needs of their financial statement users while balancing the costs and benefits from a preparer perspective. [1]

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[1] The IASB is evaluating disclosure issues such as those related to fair value measurements and management commentary. However, as noted by one standard-setter, the usefulness of expanded required disclosure also depends on users’ ability to distinguish between disclosed versus recognized items in financial statements. Research to date is inconclusive on this matter. See Katherine Schipper, “Required Disclosures in Financial Reports,” Presidential Address to the American Accounting Association Annual Meeting (San Francisco, Calif.: August 2005).

[2] In the United States, there has been a preference for one set of GAAP except in unusual situations. With the advent of simplified IFRS for SMEs, this position is under review. Both the FASB and the AICPA are studying the big GAAP/little GAAP issue to ensure that any kind of differential reporting is conceptually sound and meets the needs of users. The FASB has formed a Private Company Financial Reporting Committee, whose primary objectives are to provide recommendations on FASB standard-setting for privately held enterprises (see http://www.pcfr.org/).
Events after the Reporting Period (Subsequent Events)

Notes to the financial statements should explain any significant financial events that took place after the formal statement of financial position date, but before the statements are authorized for issuance (hereafter referred to as the authorization date). These events are referred to as events after the reporting date, or subsequent events. Illustration 24-1 shows a time diagram of the subsequent events period.

A period of several weeks, and sometimes months, may elapse after the end of the fiscal year but before the management or the board of directors authorizes issuance of the financial statements. Various activities involved in closing the books for the period and issuing the statements all take time: taking and pricing the inventory, reconciling subsidiary ledgers with controlling accounts, preparing necessary adjusting entries, ensuring that all transactions for the period have been entered, obtaining an audit of the financial statements by independent certified public accountants, and printing the annual report. During the period between the statement of financial position date and its authorization date, important transactions or other events may occur that materially affect the company’s financial position or operating situation.

Many who read a statement of financial position believe the financial condition is constant, and they project it into the future. However, readers must be told if the company has experienced a significant change—e.g., sold one of its plants, acquired a subsidiary, suffered unusual losses, settled significant litigation, or experienced any other important event in the post-statement of financial position period. Without an explanation in a note, the reader might be misled and draw inappropriate conclusions.

Two types of events or transactions occurring after the statement of financial position date may have a material effect on the financial statements or may need disclosure so that readers interpret these statements accurately:

1. Events that provide additional evidence about conditions that existed at the statement of financial position date, including the estimates inherent in the process of preparing financial statements. These events are referred to as adjusted subsequent events and require adjustments to the financial statements. All information available prior to the authorization date of the financial statements helps investors and

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3In many jurisdictions, management is required to issue its financial statements to a supervisory board (made up solely of non-executives) for approval. In such cases, the financial statements are authorized for issue—the end of the subsequent events period—when the management authorizes them for issue to the supervisory board. In other jurisdictions, companies are required to submit the financial statements to its shareholders for approval after the financial statements have been made public. In such cases, the subsequent events period ends on the date of issue, not the date when shareholders approve the financial statements. [2]
creditors evaluate estimates previously made. To ignore these subsequent events is to pass up an opportunity to improve the accuracy of the financial statements. This first type of event encompasses information that an accountant would have recorded in the accounts had the information been known at the statement of financial position date.

For example, if a loss on an account receivable results from a customer’s bankruptcy subsequent to the statement of financial position date, the company adjusts the financial statements before their issuance. The bankruptcy stems from the customer’s poor financial health existing at the statement of financial position date.

The same criterion applies to settlements of litigation. The company must adjust the financial statements if the events that gave rise to the litigation, such as personal injury or patent infringement, took place prior to the statement of financial position date.

2. Events that provide evidence about conditions that did not exist at the statement of financial position date but arise subsequent to that date. These events are referred to as non-adjusted subsequent events and do not require adjustment of the financial statements. To illustrate, a loss resulting from a customer’s fire or flood after the statement of financial position date does not reflect conditions existing at that date. Thus, adjustment of the financial statements is not necessary. A company should not recognize subsequent events that provide evidence about conditions that did not exist at the date of the statement of financial position but that arose after the statement of financial position date.

The following are examples of non-adjusted subsequent events:

- A major business combination after the reporting period or disposing of a major subsidiary.
- Announcing a plan to discontinue an operation or commencing the implementation of a major restructuring.
- Major purchases of assets, other disposals of assets, or expropriation of major assets by government.
- The destruction of a major production plant or inventories by a fire or natural disaster after the reporting period.
- Major ordinary share transactions and potential ordinary share transactions after the reporting period.
- Abnormally large changes after the reporting period in asset prices, foreign exchange rates, or taxes.
- Entering into significant commitments or contingent liabilities, for example, by issuing significant guarantees after the statement date. [3]

Some non-adjusted subsequent events may have to be disclosed to keep the financial statements from being misleading. For such events, a company discloses the nature of the event and an estimate of its financial effect.

Illustration 24-2 presents an example of subsequent events disclosure, excerpted from the annual report of Cadbury plc (GBR).

Many subsequent events or developments do not require adjustment of or disclosure in the financial statements. Typically, these are non-accounting events or conditions that management normally communicates by other means. These events include legislation, product changes, management changes, strikes, unionization, marketing agreements, and loss of important customers.

The effects from natural disasters, like the eruption of the Icelandic volcano, which occurred after the year-end for companies with March fiscal years, require disclosure in order to keep the statements from being misleading. Some companies may have to consider whether these disasters affect their ability to continue as going concerns.
Interim Reports

Another source of information for the investor is interim reports. As noted earlier, interim reports cover periods of less than one year. The securities exchanges, market regulators, and the accounting profession have an active interest in the presentation of interim information.

Because of the short-term nature of the information in these reports, there is considerable controversy as to the general approach companies should employ. One group, which favors the discrete approach, believes that companies should treat each interim period as a separate accounting period. Using that treatment, companies would follow the principles for deferrals and accruals used for annual reports. In this view, companies should report accounting transactions as they occur, and expense recognition should not change with the period of time covered.

Another group, which favors the integral approach, believes that the interim report is an integral part of the annual report and that deferrals and accruals should take into consideration what will happen for the entire year. In this approach, companies should assign estimated expenses to parts of a year on the basis of sales volume or some other activity base. In general, IFRS requires companies to follow the discrete approach. [4]

Interim Reporting Requirements

Generally, companies should use the same accounting policies for interim reports and for annual reports. They should recognize revenues in interim periods on the same basis as they are for annual periods. For example, if Cedars Corp. uses the percentage-of-completion method as the basis for recognizing revenue on an annual basis, then it should use the percentage-of-completion method for interim reports as well. Also, Cedars should treat costs directly associated with revenues (product costs, such as materials, labor and related fringe benefits, and manufacturing overhead) in the same manner for interim reports as for annual reports.

Companies should use the same inventory pricing methods (FIFO, average cost, etc.) for interim reports and for annual reports. However, companies may use the gross profit method for interim inventory pricing. But, they must disclose the method and adjustments to reconcile with annual inventory.
Discrete Approach. Following the discrete approach, companies record in interim reports revenues and expenses according to the revenue and expense recognition principles. This includes costs and expenses other than product costs (often referred to as period costs). No accruals or deferrals in anticipation of future events during the year should be reported. For example, the cost of a planned major periodic maintenance or overhaul for a company like *Airbus* (FRA) or other seasonal expenditure that is expected to occur late in the year is not anticipated for interim reporting purposes. The mere intention or necessity to incur expenditure related to the future is not sufficient to give rise to an obligation.

Or, a company like *Carrefour* (FRA) may budget certain costs expected to be incurred irregularly during the financial year, such as advertising and employee training costs. Those costs generally are discretionary even though they are planned and tend to recur from year to year. However, recognizing an obligation at the end of an interim financial reporting period for such costs that have not yet been incurred generally is not consistent with the definition of a liability.

While year-to-date measurements may involve changes in estimates of amounts reported in prior interim periods of the current financial year, the principles for recognizing assets, liabilities, income, and expenses for interim periods are the same as in annual financial statements. For example, *Wm Morrison Supermarkets plc* (GBR) records losses from inventory write-downs, restructurings, or impairments in an interim period similar to how it would treat these items in the annual financial statements (when incurred). However, if an estimate from a prior interim period changes in a subsequent interim period of that year, the original estimate is adjusted in the subsequent interim period.

Interim Disclosures. IFRS does not require a complete set of financial statements at the interim reporting date. Rather, companies may comply with the requirements by providing condensed financial statements and selected explanatory notes. Because users of interim financial reports also have access to the most recent annual financial report, companies only need provide explanation of significant events and transactions since the end of the last annual reporting period. Companies should report the following interim data at a minimum.

1. Statement that the same accounting policies and methods of computation are followed in the interim financial statements as compared with the most recent annual financial statements or, if those policies or methods have been changed, a description of the nature and effect of the change.
2. Explanatory comments about the seasonality or cyclicality of interim operations.
3. The nature and amount of items affecting assets, liabilities, equity, net income, or cash flows that are unusual because of their nature, size, or incidence.
4. The nature and amount of changes in accounting policies and estimates of amounts previously reported.
5. Issuances, repurchases, and repayments of debt and equity securities.
6. Dividends paid (aggregate or per share) separately for ordinary shares and other shares.
7. Segment information, as required by *IFRS 8*, “Operating Segments.”
8. Changes in contingent liabilities or contingent assets since the end of the last annual reporting period.
9. Effect of changes in the composition of the company during the interim period, such as business combinations, obtaining or losing control of subsidiaries and long-term investments, restructurings, and discontinued operations.
10. Other material events subsequent to the end of the interim period that have not been reflected in the financial statements for the interim period.

If a complete set of financial statements is provided in the interim report, companies comply with the provisions of *IAS 1*, “Presentation of Financial Statements.”
Unique Problems of Interim Reporting

IFRS reflects a preference for the discrete approach. However, within this broad guideline, a number of unique reporting problems develop related to the following items.

Income Taxes. Not every dollar of corporate taxable income may be taxed at the same rate if the tax rate is progressive. This aspect of business income taxes poses a problem in preparing interim financial statements. Should the company use the **annualized approach**, which is to annualize income to date and accrue the proportionate income tax for the period to date? Or should it follow the **marginal principle approach**, which is to apply the lower rate of tax to the first amount of income earned? At one time, companies generally followed the latter approach and accrued the tax applicable to each additional dollar of income.

**IFRS requires use of the annualized approach.** Income tax expense is recognized in each interim period based on the best estimate of the weighted-average annual income tax rate expected for the full financial year. This approach is consistent with applying the same principles in interim reports as applied to annual report; that is, income taxes are assessed on an annual basis. However, amounts accrued for income tax expense in one interim period may have to be adjusted in a subsequent interim period of that financial year if the estimate of the annual income tax rate changes. [5]

Seasonality. **Seasonality** occurs when most of a company’s sales occur in one short period of the year, while certain costs are fairly evenly spread throughout the year. For example, the natural gas industry has its heavy sales in the winter months. In contrast, the beverage industry has its heavy sales in the summer months.

The problem of seasonality is related to the expense recognition principle in accounting. Generally, expenses are associated with the revenues they create. In a seasonal business, wide fluctuations in profits occur because off-season sales do not absorb the company’s fixed costs (for example, manufacturing, selling, and administrative costs that tend to remain fairly constant regardless of sales or production).

To illustrate why seasonality is a problem, assume the following information.

**ILLUSTRATION 24-3**

<table>
<thead>
<tr>
<th>Data for Seasonality Example</th>
</tr>
</thead>
<tbody>
<tr>
<td>Selling price per unit</td>
</tr>
<tr>
<td>Annual sales for the period (projected and actual)</td>
</tr>
<tr>
<td>100,000 units @ $1</td>
</tr>
<tr>
<td>Manufacturing costs</td>
</tr>
<tr>
<td>Variable</td>
</tr>
<tr>
<td>Fixed</td>
</tr>
<tr>
<td>Non-manufacturing costs</td>
</tr>
<tr>
<td>Variable</td>
</tr>
<tr>
<td>Fixed</td>
</tr>
</tbody>
</table>

Sales for four quarters and the year (projected and actual) were:

**ILLUSTRATION 24-4**

<table>
<thead>
<tr>
<th>Sales Data for Seasonality Example</th>
</tr>
</thead>
<tbody>
<tr>
<td>Percent of Sales</td>
</tr>
<tr>
<td>1st Quarter</td>
</tr>
<tr>
<td>2nd Quarter</td>
</tr>
<tr>
<td>3rd Quarter</td>
</tr>
<tr>
<td>4th Quarter</td>
</tr>
<tr>
<td>Total for the year</td>
</tr>
</tbody>
</table>

Under the present accounting framework, the income statements for the quarters might be as shown in Illustration 24-5.

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5The estimated annual effective tax rate should reflect anticipated tax credits, foreign tax rates, percentage depletion, capital gains rates, and other available tax-planning alternatives.
This approach solves some of the problems of interim reporting: Sales in the first quarter are 20 percent of total sales for the year, and net income in the first quarter is 20 percent of total income. In this case, as in the previous example, the investor cannot rely on multiplying any given quarter by four but can use comparative data or rely on some estimate of sales in relation to income for a given period.

The greater the degree of seasonality experienced by a company, the greater the possibility of distortion. Because there are no definitive guidelines for handling such items as the fixed non-manufacturing costs, variability in income can be substantial. To alleviate this problem, IFRS requires companies subject to material seasonal variations to disclose the seasonal nature of their business and consider supplementing their interim reports with information for 12-month periods ended at the interim date for the current and preceding years.

The two illustrations highlight the difference between the discrete and integral approaches. Illustration 24-5 represents the discrete approach, in which the fixed non-manufacturing expenses are expensed as incurred. Illustration 24-6 shows the integral approach, in which expenses are charged to expense on the basis of some measure of activity.

Continuing Controversy. While IFRS has developed some rules for interim reporting, additional issues remain. For example, there is continuing debate on the independent
auditor’s involvement in interim reports. Many auditors are reluctant to express an opinion on interim financial information, arguing that the data are too tentative and subjective. On the other hand, more people are advocating some examination of interim reports. Generally, auditors perform a review of interim financial information. Such a review, which is much more limited in its procedures than the annual audit, provides some assurance that the interim information appears to be in accord with IFRS.6

Analysts and investors want financial information as soon as possible, before it’s old news. We may not be far from a continuous database system in which corporate financial records can be accessed via the Internet. Investors might be able to access a company’s financial records whenever they wish and put the information in the format they need. Thus, they could learn about sales slippage, cost increases, or earnings changes as they happen, rather than waiting until after the quarter has ended.

A steady stream of information from the company to the investor could be very positive because it might alleviate management’s continual concern with short-run interim numbers. Today, many contend that management is too oriented to the short-term. The truth of this statement is echoed by the words of the president of a large company who decided to retire early: “I wanted to look forward to a year made up of four seasons rather than four quarters.”

**AUDITOR’S AND MANAGEMENT’S REPORTS**

**Auditor’s Report**

Another important source of information, which is often overlooked, is the auditor’s report. An auditor is an accounting professional who conducts an independent examination of a company’s accounting data.

If satisfied that the financial statements present the financial position, results of operations, and cash flows fairly in accordance with IFRS, the auditor expresses an unmodified opinion. An example is shown in Illustration 24-7.7

In preparing the report, the auditor follows these reporting standards.

1. The report states whether the financial statements are in accordance with the financial reporting framework (IFRS) and the responsibilities of the directors and auditors with respect to the financial statements.
2. The report identifies those circumstances in which the company has not consistently observed such policies in the current period in relation to the preceding period.
3. Users are to regard the informative disclosures in the financial statements as reasonably adequate unless the report states otherwise.

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6These are referred to as review engagements, which are less extensive than an audit. See International Standards on Review Engagements (ISRE) 2410, “Review of Interim Financial Information Performed by the Independent Auditor of the Entity,” Handbook of International Quality Control, Auditing, Review, Other Assurance, and Other Related Services Pronouncements (April 2010).

7This auditor’s report and the following discussion are consistent with international auditing standards. See International Standard on Auditing 700, “Forming an Opinion and Reporting on Financial Statements” and International Standard on Auditing 705, “Modifications to the Opinion in the Independent Auditor’s Report,” Handbook of International Quality Control, Auditing, Review, Other Assurance, and Other Related Services Pronouncements (New York: International Federation of Accountants (IFAC), April 2010). They are also similar to the specifications for U.S. auditors contained in “Reports on Audited Financial Statements,” Statement on Auditing Standards No. 58 (New York: AICPA, 1988). U.S. standards differ due to the required audit opinion on the company’s internal controls, as required by the SEC.
flows of the entity in conformity with accepted accounting principles.

That is, the auditor expresses the opinion that the financial statements set out on page 43, the Directors are responsible for the preparation of the Parent Company financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board’s (APB) Ethical Standards for Auditors.

Respective responsibilities of directors and auditors
As explained more fully in the Directors’ Responsibilities Statement set out on page 43, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board’s (APB) Ethical Standards for Auditors.

Scope of the audit of the financial statements
A description of the scope of an audit of financial statements is provided on the APB’s website at www.frc.org.uk/apb/scope/UKP

Opinion on financial statements
In our opinion:
- The financial statements give a true and fair view of the state of the Group’s and of the Parent Company’s affairs as at 31 January 2010 and of the Group’s profit for the year then ended;
- The Group financial statements have been properly prepared in accordance with IFRS as adopted by the EU;
- The Parent Company financial statements have been properly prepared in accordance with UK Generally Accepted Accounting Practice; and
- The financial statements have been prepared in accordance with the requirements of the Companies Act 2006; and, as regards the Group financial statements, Article 4 of the IAS Regulation.

Opinion on other matters prescribed by the companies Act 2006
In our opinion:
- The part of the Directors’ remuneration report to be audited has been properly prepared in accordance with the Companies Act 2006; and
- The information given in the Directors’ report for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which we are required to report by exception
We have nothing to report in respect of the following:
Under the Companies Act 2006 we are required to report to you if, in our opinion:
- Adequate accounting records have not been kept by the Parent Company, or returns adequate for our audit have not been received from branches not visited by us; or
- The Parent Company financial statements and the part of the Directors’ remuneration report to be audited are not in agreement with the accounting records and returns; or
- Certain disclosures of Directors’ remuneration specified by law are not made; or
- We have not received all the information and explanations we require for our audit.

Under the Listing Rules we are required to review:
- The Directors’ statement, set out on page 42, in relation to going concern; and
- The part of the Corporate governance statement relating to the Company’s compliance with the nine provisions of the June 2008 Combined Code specified for our review.

Chris Hearld
(Senior Statutory Auditor)
for and on behalf of KPMG Audit Plc, Statutory Auditor
Chartered Accountants
1 The Embankment
Neville Street
Leeds
LS1 4DW
10 March 2010

4. The report contains either an expression of opinion regarding the financial statements taken as a whole or an assertion to the effect that an opinion cannot be expressed. When the auditor cannot express an overall opinion, the report should state the reasons. In all cases where an auditor’s name is associated with financial statements, the report should contain a clear-cut indication of the character of the auditor’s examination, if any, and the degree of responsibility being taken.

In most cases, the auditor issues a standard unmodified or clean opinion, as shown in Illustration 24-7. That is, the auditor expresses the opinion that the financial statements present fairly, in all material respects, the financial position, results of operations, and cash flows of the entity in conformity with accepted accounting principles.
Certain circumstances, although they do not affect the auditor’s unmodified opinion, may require the auditor to add an explanatory paragraph to the audit report. Some of the more important circumstances are as follows.

1. **Going concern.** The auditor must evaluate whether there is substantial doubt about the entity’s ability to continue as a going concern for a reasonable period of time, taking into consideration all available information about the future. (Generally, the future is at least, but not limited to, 12 months from the end of the reporting period.) If substantial doubt exists about the company continuing as a going concern, the auditor adds to the report an explanatory note describing the potential problem.

2. **Lack of consistency.** If a company has changed accounting policies or the method of their application in a way that has a material effect on the comparability of its financial statements, the auditor should refer to the change in an explanatory paragraph of the report. Such an explanatory paragraph should identify the nature of the change and refer readers to the note in the financial statements that discusses the change in detail. The auditor’s concurrence with a change is implicit unless the auditor takes exception to the change in expressing an opinion as to fair presentation in conformity with accepted accounting principles (IFRS).

3. **Emphasis of a matter.** The auditor may wish to emphasize a matter regarding the financial statements but nevertheless intends to express an unqualified opinion. For example, the auditor may wish to emphasize that the entity is a component of a larger business enterprise or that it has had significant transactions with related parties. The auditor presents such explanatory information in a separate paragraph of the report.

In some situations, however, the auditor expresses a modified opinion. A modified opinion can be either (1) a qualified opinion or (2) an adverse opinion, or (3) a disclaimer opinion.

A **qualified opinion** contains an exception to the standard opinion. Ordinarily, the exception is not of sufficient magnitude to invalidate the statements as a whole; if it were, an adverse opinion would be rendered. The usual circumstances in which the auditor may deviate from the standard unqualified report on financial statements are as follows.

1. The scope of the examination is limited or affected by conditions or restrictions.
2. The statements do not fairly present financial position or results of operations because of:
   (a) Lack of conformity with accepted accounting principles and standards.
   (b) Inadequate disclosure.

If confronted with one of the situations noted above, the auditor must offer a qualified opinion. A qualified opinion states that, except for the effects of the matter to which the qualification relates, the financial statements present fairly, in all material respects, the financial position, results of operations, and cash flows in conformity with accepted accounting principles.

Illustration 24-8 shows an example of an auditor’s report with a modified opinion—in this case, a qualified opinion of Helio Company (USA). The auditor modified the opinion because the company used an accounting policy at variance with accepted accounting principles.

An **adverse opinion** is required in any report in which the exceptions to fair presentation are so material that in the independent auditor’s judgment, a qualified opinion is not justified. In such a case, the financial statements taken as a whole are not presented in accordance with IFRS. Adverse opinions are rare, because most companies change their accounting to conform with IFRS. Market regulators will not permit a company listed on an exchange to have an adverse opinion.

A **disclaimer of an opinion** is appropriate when the auditor has gathered so little information on the financial statements that no opinion can be expressed.
The audit report should provide useful information to the investor. One investment banker noted, “Probably the first item to check is the auditor’s opinion to see whether or not it is a clean one—‘in conformity with accepted accounting principles’—or is qualified in regard to differences between the auditor and company management in the accounting treatment of some major item, or in the outcome of some major litigation.”

**Management’s Reports**

**Management Commentary**

Management commentary helps in the interpretation of the financial position, financial performance, and cash flows of a company. For example, a company like Delhaize Group (BEL) may present, outside the financial statements, a financial review by management that describes and explains the main features of the company’s financial performance and financial position, and the principal uncertainties it faces. Such a report may include a review of:

- The main factors and influences determining financial performance, including changes in the environment in which the entity operates, the entity’s response to those changes and their effect, and the company’s policy for investment to maintain and enhance financial performance, including its dividend policy;
- The company’s sources of funding and its targeted ratio of liabilities to equity; and
- The company’s resources not recognized in the statement of financial position in accordance with IFRS.

Such commentary also provides an opportunity to understand management’s objectives and its strategies for achieving those objectives. Users of financial reports, in their capacity as capital providers, routinely use the type of information provided in management commentary as a tool for evaluating an entity’s prospects and its general risks, as well as the success of management’s strategies for achieving its stated objectives.

For many companies, management commentary is already an important element of their communication with the capital markets, supplementing as well as complementing the financial statements. Management commentary encompasses reporting that is described in various jurisdictions as management’s discussion and analysis (MD&A), operating and financial review (OFR), or management’s report.

Illustration 24-9 presents an excerpt from the MD&A section of Lectra’s (FRA) annual report.
Management Discussion and Analysis (in part)

4. RISK FACTORS—MANAGEMENT OF RISKS
This chapter describes the main risks facing the company having regard to the specific characteristics of its business, its structure and organization. It further describes how the company manages and prevents these risks, depending on their nature.

Identification of Risks
For internal controls to be effective, the company needs to identify and assess the risks to which it is subject. These risks are identified by means of a continuous process of analyzing the Group’s external environment together with the organizational changes rendered necessary by the evolving nature of its markets. This process is overseen by the Finance division and the Legal Affairs division, with input from all Group operating and corporate divisions. The key risks that could prevent the Group from achieving its objectives are described below.

Economic Risks Specific to the Company's Business
Lectra designs, produces and markets full-line technological solutions, comprising software, CAD/CAM equipment and related services dedicated to a broad array of major global markets: fashion (apparel, accessories, and footwear), automotive (car seats and interiors, airbags), and furniture as well as a wide variety of other industries, such as the aeronautical and marine industries, wind power, personal protective equipment, etc. This activity demands continuous creativity and a relentless search for innovation, and the company consequently invests heavily in research and development. The corresponding expenditures are fully expensed in the year.

As a corollary of this policy, the company must ensure both that its innovations are not copied and that its products do not infringe third parties’ intellectual property. It therefore has a dedicated team of intellectual property specialists that takes both offensive and defensive measures with regard to patents. A substantial portion of the manufacturing of the equipment the company markets is subcontracted, with Lectra providing only the R&D, final assembly and testing. . . .

Inventory valuation risk is minimized by means of just-in-time supply and manufacturing methods. Where software is concerned, the main risk lies in the revenue recognition criteria of this intangible revenue source. This risk is covered by the internal control procedures relative to the quality of accounting and financial information.

Macroeconomic Environment Risk
The solutions marketed by Group sometimes represent a major investment for clients. Part of the decision to make these investments depends on the general macroeconomic environment and on the state of the sector of activity in which the client operates. Group clients generally tend to scale back or defer their investment decisions when global economic growth slows or when a particular sector suffers a downturn or is in crisis. The current global economic and financial crisis is an additional risk factor. Its unprecedented scale is expected to lead to further deterioration in the situation of both countries and individual firms, in all sectors and in all parts of the world. The resulting sharp slowdown in activity among Group clients, their deteriorating financial performance, their uncertain outlook, and reduced access to credit are making it hard for them to finance their investments. Most companies have therefore taken drastic steps to reduce their costs, cut back or temporarily halt production, and to close plants. These situations impact Group revenues and financial results.

Some companies use the management commentary section of the annual report to disclose company efforts in the area of sustainability. An excerpt from the annual report of Marks and Spencer plc (GBR) is presented in Illustration 24-10.

Additional reporting on sustainability is important because it indicates the company’s social responsibility and can provide insights about potential obligations that are reported in the financial statements.

While there are no formal IFRS requirements for management commentary, the IASB has initiated a project that offers a non-binding framework and limited guidance on its application, which could be adapted to the legal and economic circumstances of individual jurisdictions. While the proposal is focused on publicly traded entities, to
the extent that the framework is deemed applicable, it may be a useful tool for non-exchange traded entities, for example, privately held and state-owned enterprises.\textsuperscript{8}

\textbf{ILLUSTRATION 24-10}

\textbf{Sustainability Reporting}

\textit{Marks and Spencer plc}

\textbf{3 more green success stories to build on...}

1. We recycled 75\% of all construction waste in 2007/08, and aim to achieve 85\% in 2008/09.
2. How we design, procure and build our stores is now clearly laid out in our Sustainable Construction Manual produced in conjunction with the Building Research Establishment (BRE).
3. Like-for-like store energy usage is down by 4\%.

\textbf{A greener way to shop...}

In September 2007, we opened the first of our new ‘eco stores’. Located in Bournemouth, we deliberately decided to modernise one of our older stores, to find out how eco-friendly we could make it. Rising to the challenge, we incorporated a wide range of eco-features—from a green roof to capture airborne pollutants and escalators running at reduced voltage, to more efficient heating, lighting and refrigeration systems. In this way, we hope to achieve energy savings of up to 55\%.

Following Bournemouth, we opened a further two green stores: at Silverburn in Pollok and a new Simply Food in Galashiels. As we continue to introduce more ‘eco stores’, we’ll be testing a number of cutting edge techniques, such as using hempcrete—which uses hemp plant fibers as the aggregate—instead of concrete. We’ll continue to trial many further innovations to ensure that as our property portfolio grows larger it also grows greener.

\textbf{Wm Morrison Supermarkets plc}

\textbf{Statement of Directors’ responsibilities in respect of the Annual report and financial statements}

The Directors are responsible for preparing the Annual report and the Group and Parent Company financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare Group and Parent Company financial statements for each financial year. Under that law they are required to prepare the Group financial statements in accordance with IFRS as adopted by the EU and applicable law and have elected to prepare the Parent Company financial statements in accordance with UK Accounting Standards and applicable law (UK Generally Accepted Accounting Practice).

Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and Parent Company and of their profit or loss for that period. In preparing each of the Group and Parent Company financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- for the Group financial statements, state whether they have been prepared in accordance with IFRS as adopted by the EU;
- for the Parent Company financial statements, state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the Parent Company financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and the Parent Company will continue in business.

\textbf{ILLUSTRATION 24-11}

Report on Management’s Responsibilities

\textsuperscript{8}See http://www.ifrs.org/Current+Projects/IASB+Projects/Management+Commentary/Management+Commentary.htm. The proposal will not result in an IFRS. Accordingly, it would not be a requirement for an entity to comply with the framework for the preparation and presentation of management commentary as a condition for asserting compliance with IFRS.
FIRST-TIME ADOPTION OF IFRS

As discussed in Chapter 1, IFRS is growing in acceptance around the world. For example, recent statistics indicate 40 percent of the Global Fortune 500 companies use IFRS. And the chair of the IASB predicts that IFRS adoption will grow from its current level of 115 countries to nearly 150 countries in the near future.

When countries accept IFRS for use as accepted accounting policies, companies need guidance to ensure that their first IFRS financial statements contain high-quality information. Specifically, IFRS 1 requires that information in a company’s first IFRS statements (1) be transparent, (2) provide a suitable starting point, and (3) have a cost that does not exceed the benefits. [6]

The overriding principle in converting from national GAAP to IFRS (the conversion process) is full retrospective application of all IFRS. Retrospective application—recasting prior financial statements on the basis of IFRS—provides financial statement users with comparable information. However, the IASB recognizes that full retrospective application may be difficult in some situations, particularly when information related to past periods is not readily available. In response, the IASB has established guidelines to ensure that financial statement users have high-quality comparable information while balancing the costs and benefits of providing comparable data.

General Guidelines

The objective of the conversion process is to present a set of IFRS financial statements as if the company always reported on IFRS. To achieve this objective, a company must:

1. Identify the timing for its first IFRS statements.
2. Prepare an opening statement of financial position at the date of transition to IFRS.
3. Select accounting policies that comply with IFRS, and apply these policies retrospectively.
4. Consider whether to apply any optional exemptions and apply mandatory exceptions.
5. Make extensive disclosure to explain the transition to IFRS.

Relevant Dates

Once a company decides to convert to IFRS, it must decide on the following dates—the transition date and the reporting date. The transition date is the beginning of the earliest period for which full comparative IFRS information is presented. The reporting date is the closing statement of financial position date for the first IFRS financial statements.

To illustrate, assume that FirstChoice Company plans to provide its first IFRS statements for the year ended December 31, 2014. FirstChoice decides to present comparative information for one year only. Therefore, its date of transition to IFRS is January 1, 2013, and its reporting date is December 31, 2014. The timeline for first-time adoption is presented in Illustration 24-12.

ILLUSTRATION 24-12
First-Time Adoption Timeline

---

<table>
<thead>
<tr>
<th>Date of Transition (Opening IFRS Statement of Financial Position)</th>
<th>Beginning of First IFRS Reporting Period</th>
<th>Reporting Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>January 1, 2013</td>
<td>January 1, 2014</td>
<td>December 31, 2014</td>
</tr>
</tbody>
</table>

---
Illustration 24-14 shows the following.

1. The opening IFRS statement of financial position for FirstChoice on January 1, 2013, serves as the starting point (date of transition) for the company’s accounting under IFRS.

2. The first full IFRS statements are shown for FirstChoice for December 31, 2014. In other words, a minimum of two years of IFRS statements must be presented before a conversion to IFRS occurs. As a result, FirstChoice must prepare at least one year of comparative financial statements (for 2013) using IFRS.

3. FirstChoice presents financial statements in accordance with its national GAAP annually to December 31, 2013.

Following this conversion process, FirstChoice provides users of the financial statements with comparable IFRS statements for 2013 and 2014.

**Implementation Steps**

**Opening IFRS Statement of Financial Position**

As indicated, to start the conversion process, companies first prepare an opening IFRS statement of financial position. This process involves the following steps.

1. Include all assets and liabilities that IFRS requires.
2. Exclude any assets and liabilities that IFRS does not permit.
3. Classify all assets, liabilities, and equity in accordance with IFRS.
4. Measure all assets and liabilities according to IFRS.

Completing this process requires knowledge of both the prior GAAP used and IFRS (which you have obtained by your study of this text). To illustrate, the following facts for NewWorld Company are presented in Illustration 24-13.

**OPENING STATEMENT OF FINANCIAL POSITION**

Facts: NewWorld Company is preparing to adopt IFRS. It is preparing its opening statement of financial position on January 1, 2012. NewWorld identified the following accounting policy differences between IFRS and the national GAAP it currently uses. Under national GAAP, NewWorld:

1. Expenses development costs of €500,000 on a project that had met economic viability.
2. Does not make a provision for a warranty of €100,000 because the concept of a “constructive obligation” was not recognized.
3. Does not capitalize design fees of €150,000 into the cost of machinery that was put into service at the beginning of 2010, even though those costs were necessary to bring the asset to its working condition. The machinery has a 5-year life, no residual value, and NewWorld uses straight-line depreciation.

**Question:** How should NewWorld account for these items in its opening IFRS statement of financial position?

**Solution:**

1. IFRS allows the deferral of development costs in this case (see Chapter 12), and NewWorld should capitalize these costs.
2. IFRS requires recognition of a warranty provision (see Chapter 13), so a liability should be recorded.
3. Under IFRS, all costs incurred in bringing an asset to its place and condition for its intended use are capitalized into the cost of the asset.
Adjustments as a result of applying IFRS for the first time are generally recorded in retained earnings. NewWorld makes the following entries on January 1, 2012, to adjust the accounts to IFRS treatment.

- **Development Costs (or related intangible asset)** \(500,000\)
- **Retained Earnings** \(500,000\)
  
  (To capitalize development costs)

- **Retained Earnings** \(100,000\)
- **Warranty Liability** \(100,000\)
  
  (To recognize warranty liability)

- **Equipment** \(150,000\)
- **Accumulated Depreciation—Equipment** \(30,000\)
- **Retained Earnings** \(120,000\)
  
  (To recognized cost of machinery)

In each of these situations, NewWorld adjusts retained earnings for the differences between IFRS and national GAAP to ensure that the opening statement of financial position is reported in accordance with IFRS.

After recording these adjustments, NewWorld prepares its opening IFRS statement of financial position. The January 1, 2012, statement of financial position is the starting point (the date of transition). Subsequently, in 2012 and 2013 NewWorld prepares IFRS financial statements internally. At December 31, 2013, it will formally adopt IFRS.\(^9\)

**Exemptions from Retrospective Treatment**

In some cases, adjustments relating to prior periods cannot be reasonably determined. In other cases, it is “impracticable” to provide comparable information because the cost of generating the information exceeds the benefits. The IASB therefore targeted exemptions from the general retrospective treatment where it appeared appropriate. Two types of exemptions are provided—required and elective.

**Required Exemptions.** The Board identified three areas in which companies are prohibited from retrospective application in first-time adoption of IFRS:

1. Estimates.
2. Hedge accounting.

These required exemptions are imposed because implementation of retrospective application in these areas generally requires companies to obtain information that may not be readily available. In these cases, companies may have to re-create information about past transactions with the benefit of hindsight.\(^9\) For example, retrospective application with respect to non-controlling interests requires information about conditions and estimates made at the time of a business combination—an often difficult task. In addition, this exception provides relief for companies that otherwise might have to determine the allocation of transactions between owners and non-controlling interests in periods prior to the transition period.

**Elective Exemptions.** In addition to the required exemptions for retrospective treatment, the IASB identified specific additional areas in which companies may elect exemption from retrospective treatment. These exemptions provide companies some

\(^9\)To maintain comparisons in the transition year, companies may present comparative information in accordance with previous GAAP as well as the comparative information required by IFRS. Companies must (a) label the previous GAAP information prominently as not being prepared in accordance with IFRS, and (b) disclose the nature of the main adjustments that would make it comply with IFRS. Companies need not quantify those adjustments. \(^8\)
Optional exemption from retrospective treatment is understandable for certain situations. The accounting for the areas identified above generally requires a number of estimates and assumptions at initial recognition and in subsequent accounting. Depending on the accounting under previous GAAP, the information necessary for retrospective application may not be available, or may be obtained only at a high cost. We discuss two examples.\(^{11}\)

**Exemption Example: Compound Securities.** As discussed in Chapter 16, IFRS requires splitting the debt and equity components of convertible debt, using the “with and without” approach. The subsequent accounting for the debt element reflects effective-interest amortization on the estimated debt component. However, if the liability component is no longer outstanding at the date of first-time adoption, retrospective application involves separating two portions of equity. The first portion is in retained earnings and represents the cumulative interest accredited on the liability component. The other portion represents the original equity component. Since the company would not have records on the debt once it is no longer outstanding, it would be costly to re-create that information for retrospective application. As a result, a first-time adopter need not separate these two portions if the liability component is no longer outstanding at the date of transition to IFRS.

**Exemption Example: Fair Value or Revaluation as Deemed Cost.** Companies can elect to measure property, plant, and equipment at fair value at the transition date and use that fair value as their *deemed cost* in accounting for those assets subsequent to the adoption of IFRS. This exemption may also be applied to intangible assets in certain situations. By using the exemption, companies avoid re-creating depreciation records for property, plant, and equipment, which is a costly exercise for many companies. In fact, in providing this exemption, the IASB noted that reconstructed cost data might be less relevant to users, and less reliable, than current fair value data. The Board therefore concluded that it would allow companies to use fair value as deemed cost. A company that applies the fair value as deemed cost exemption is not required to revalue the assets subsequent to first-time adoption. [12]\(^{12}\)

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\(^{10}\)Other areas subject to the option are (1) business combinations; (2) insurance contracts; (3) investments in subsidiaries, jointly controlled entities, and associates; (4) designation of previously recognized financial instruments; (5) financial assets or intangible assets accounted for as Service Concession Arrangements; and (6) transfers of assets from customers. [10]

\(^{11}\)Specific implementation guidance for other areas is provided in IFRS 1. [11]

\(^{12}\)In addition, IFRS does not restrict the use of fair value as deemed cost to an entire class of assets, as is done for revaluation accounting (see discussion in Chapter 11). For example, a company can use fair value for deemed cost for some buildings and not for others. However, if a company uses fair value as deemed cost for assets whose fair value is above cost, it cannot ignore indications that the recoverable amount of other assets may have fallen below their carrying amount. Thus, an impairment may need to be recorded.
Presentation and Disclosure

Upon first-time adoption of IFRS, a company must present at least one year of comparative information under IFRS. \[13\] To comply with IAS 1, an entity’s first IFRS financial statements shall include at least three statements of financial position, two statements of comprehensive income, two separate income statements (if presented), two statements of cash flows, and two statements of changes in equity and related notes, including comparative information. Companies must explain how the transition from previous GAAP to IFRS affected its reported financial position, financial performance, and cash flows.

A company’s first IFRS financial statements shall include reconciliations of:

- Its equity reported in accordance with previous GAAP to its equity in accordance with IFRS at the transition date.
- Its total comprehensive income in accordance with IFRS to total comprehensive income in accordance with previous GAAP for the same period. The reconciliation should be prepared for latest period in the company’s most recent annual financial statements under the previous GAAP. \[14\]

For example, Jones plc first adopted IFRS in 2012, with a date of transition to IFRS January 1, 2011. Its last financial statements in accordance with previous GAAP were for the year ended December 31, 2011. An example of Jones plc’s reconciliations for first-time adoption is provided in Illustration 24-15 for the non-current asset section of the statement of financial position.

ILLUSTRATION 24-15
Reconciliation of Equity for 2011

<table>
<thead>
<tr>
<th>Note</th>
<th>Previous GAAP</th>
<th>Effect of Transition to IFRS</th>
<th>IFRS</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Property, plant, and equipment £8,299</td>
<td>£100</td>
<td>£8,399</td>
</tr>
<tr>
<td>2</td>
<td>Goodwill 1,220</td>
<td>150</td>
<td>1,370</td>
</tr>
<tr>
<td>2</td>
<td>Intangible assets 208</td>
<td>(150)</td>
<td>58</td>
</tr>
<tr>
<td>3</td>
<td>Financial assets 3,471</td>
<td>420</td>
<td>3,891</td>
</tr>
<tr>
<td>Total non-current assets</td>
<td>£13,198</td>
<td>£520</td>
<td>£13,718</td>
</tr>
</tbody>
</table>

Notes to the reconciliation at January 1, 2011:
1. Depreciation was influenced by tax requirements in accordance with previous GAAP, but in accordance with IFRS reflects the useful life of the assets. The cumulative adjustment increased the carrying amount of property, plant, and equipment by £100.
2. Intangible assets in accordance with previous GAAP included £150 for items that are transferred to goodwill because they do not qualify for recognition as intangible assets in accordance with IFRS.
3. Financial assets are all classified as non-trading equity investments in accordance with IFRS and are carried at their fair value of £3,891. They were carried at cost of £3,471 in accordance with previous GAAP. The resulting gains of £294 (£420, less related deferred tax of £126) are included in the accumulated other comprehensive income.

Through this reconciliation, statement users are provided information to evaluate the impact of the adoption of IFRS on the statement of financial position. In practice, it may be helpful to include cross-references to accounting policies and supporting analyses that give further explanation of the adjustments shown in the reconciliations.

The reconciliation for total comprehensive income for Jones with respect to the gross profit section of the income statement is presented in Illustration 24-16.
Summary

When companies adopt IFRS, they must ensure that financial statement users receive high-quality information in order to compare financial statements prepared under IFRS and previous GAAP. IFRS guidelines are designed to ensure that upon first-time adoption, financial statements are comparable and that the costs and benefits of first-time adoption are effectively managed.

Notes to the reconciliation of total comprehensive income for 20X4:
1. A pension liability is recognized in accordance with IFRS but was not recognized in accordance with previous GAAP. The pension liability increased by £130 during 2011, which caused increases in cost of sales (£50), distribution costs (£30), and administrative expenses (£50).
2. Cost of sales is higher by £47 in accordance with IFRS because inventories include fixed and variable production overhead in accordance with IFRS but not in accordance with previous GAAP.
3. Depreciation was influenced by tax requirements in accordance with previous GAAP but reflects the useful life of the assets in accordance with IFRS. The effect on the profit for 2011 was not material.

Explanation of material adjustments to the statement of cash flows for 2011:
Income taxes of £133 paid during 2011 are classified as operating cash flows in accordance with IFRS but were included in a separate category of tax cash flows in accordance with previous GAAP. There are no other material differences between the statement of cash flows presented in accordance with IFRS and the statement of cash flows presented in accordance with previous GAAP.

AUTHORITATIVE LITERATURE

Authoritative Literature References

QUESTIONS

1. What are the major types of subsequent events? Indicate how each of the following “subsequent events” would be reported.
   (a) Collection of a note written off in a prior period.
   (b) Issuance of a large preference share offering.
   (c) Acquisition of a company in a different industry.
   (d) Destruction of a major plant in a flood.
   (e) Death of the company’s chief executive officer (CEO).
   (f) Additional wage costs associated with settlement of a four-week strike.
   (g) Settlement of an income tax case at considerably more tax than anticipated at year-end.
   (h) Change in the product mix from consumer goods to industrial goods.

2. What are interim reports? Why is a complete set of financial statements often not provided with interim data?

3. What are the accounting problems related to the presentation of interim data?

4. Dierdorf Inc., a closely held corporation, has decided to go public. The controller, Ed Floyd, is concerned with presenting interim data when an inventory write-down is recorded. What problems are encountered with inventories when quarterly data are presented?

5. What approaches have been suggested to overcome the seasonality problem related to interim reporting?

6. An article in the financial press entitled “Important Information in Annual Reports This Year” noted that annual reports include a management commentary section. What would this section contain?

7. “The financial statements of a company are management’s, not the accountant’s.” Discuss the implications of this statement.

8. What is the difference between an auditor’s unmodified opinion or “clean” opinion and a modified one?

9. How is the date of transition and the date of reporting determined in first-time adoption of IFRS?

10. What are the characteristics of high-quality information in a company’s first IFRS financial statements?

11. What are the steps to be completed in preparing the opening IFRS statement of financial position?

12. What is the rationale for exemptions to retrospective application at first-time adoption of IFRS?

13. Briefly describe the deemed cost exemption to retrospective application at first-time adoption of IFRS.

14. Briefly describe the presentation and disclosure requirements for first-time adoption of IFRS.

BRIEF EXERCISES

BE24-1 Morlan Corporation is preparing its December 31, 2010, financial statements. Two events that occurred between December 31, 2010, and March 10, 2011, when the statements were issued, are described below.

1. A liability, estimated at €160,000 at December 31, 2010, was settled on February 26, 2011, at €170,000.
2. A flood loss of €80,000 occurred on March 1, 2011.

What effect do these subsequent events have on 2010 net income?
E24-1 (Subsequent Events)  Keystone Corporation issued its financial statements for the year ended December 31, 2010, on March 10, 2011. The following events took place early in 2011.

(a) On January 10, 10,000 ordinary shares of $5 par value were issued at $66 per share.
(b) On March 1, Keystone determined after negotiations with the taxing authorities that income taxes payable for 2010 should be $1,320,000. At December 31, 2010, income taxes payable were recorded at $1,100,000.

Instructions
Discuss how the preceding subsequent events should be reflected in the 2010 financial statements.

E24-2 (Subsequent Events)  For each of the following subsequent events, indicate whether a company should (a) adjust the financial statements, (b) disclose in notes to the financial statements, or (c) neither adjust nor disclose.

1. Settlement of a tax case at a cost considerably in excess of the amount expected at year-end.
2. Introduction of a new product line.
3. Loss of assembly plant due to fire.
4. Sale of a significant portion of the company’s assets.
5. Retirement of the company president.
6. Issuance of a significant number of ordinary shares.
7. Loss of a significant customer.
8. Prolonged employee strike.
9. Material loss on a year-end receivable because of a customer’s bankruptcy.
11. Settlement of prior year’s litigation against the company.
12. Merger with another company of comparable size.

E24-3 (Opening Statement of Financial Position)  Goodman Company is preparing to adopt IFRS. In preparing its opening statement of financial position on January 1, 2012, Goodman identified the following accounting policy differences between IFRS and its previous GAAP.

1. Under its previous GAAP, Goodman classified proposed dividends of €45,000 as a current liability.
2. Goodman had deferred advertising costs of €500,000.
Instructions
(a) Prepare the journal entries (if any) needed before preparation of Goodman’s opening statement of financial position.
(b) Determine the net change in equity from these adjustments.

E24-4  (Opening Statement of Financial Position, Disclosure) Lombardo Group is preparing to adopt IFRS. It is preparing its opening statement of financial position on January 1, 2012. Lombardo identified the following accounting policy differences between IFRS and its previous GAAP.

1. Lombardo had not made a provision for a warranty of €75,000 under previous GAAP because the concept of a “constructive obligation” was not recognized.
2. Under previous GAAP, €60,000 paid for certain architect fees was not capitalized into the cost of a building that was put into service at the beginning of 2011, even though those costs were necessary to bring the asset to its working condition. The building has a 40-year life, no residual value, and Lombardo uses straight-line depreciation.

Instructions
(a) Prepare the journal entries (if any) needed before preparation of Lombardo’s opening statement of financial position.
(b) Determine the net change in equity from these adjustments.
(c) Brief describe the disclosures that Lombardo will make related to the adjustments in its first IFRS financial statements.

CONCEPTS FOR ANALYSIS
CA24-1  (Interim Reporting) Snider Corporation, a publicly traded company, is preparing the interim financial data which it will issue to its shareholders at the end of the first quarter of the 2010–2011 fiscal year. Snider’s financial accounting department has compiled the following summarized revenue and expense data for the first quarter of the year.

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>$60,000,000</td>
</tr>
<tr>
<td>Cost of goods sold</td>
<td>36,000,000</td>
</tr>
<tr>
<td>Variable selling expenses</td>
<td>1,000,000</td>
</tr>
<tr>
<td>Fixed selling expenses</td>
<td>3,000,000</td>
</tr>
</tbody>
</table>

Included in the fixed selling expenses was the single lump-sum payment of $2,000,000 for television advertisements for the entire year.

Instructions
(a) Snider Corporation must issue its quarterly financial statements in accordance with IFRS regarding interim financial reporting.
(1) Explain whether Snider should report its operating results for the quarter as if the quarter were a separate reporting period in and of itself, or as if the quarter were an integral part of the annual reporting period.
(2) State how the sales, cost of goods sold, and fixed selling expenses would be reflected in Snider Corporation’s quarterly report prepared for the first quarter of the 2010–2011 fiscal year. Briefly justify your presentation.
(b) What financial information, as a minimum, must Snider Corporation disclose to its shareholders in its quarterly reports?

CA24-2  (Reporting of Subsequent Events) In June 2010, the board of directors for McElroy Enterprises Inc. authorized the sale of £10,000,000 of corporate bonds. Jennifer Grayson, treasurer for McElroy Enterprises Inc., is concerned about the date when the bonds are issued. The company really needs the cash, but she is worried that if the bonds are issued before the company’s year-end (December 31, 2010) the additional liability will have an adverse effect on a number of important ratios. In July, she explains to company president, William McElroy, that if they delay issuing the bonds until after December 31, the bonds will not affect the ratios until December 31, 2011. They will have to report the issuance as a subsequent event which requires only footnote disclosure. Grayson expects that with expected improved financial performance in 2011 ratios should be better.
Financial Reporting Problem

Marks and Spencer plc (M&S)

As stated in the chapter, notes to the financial statements are the means of explaining the items presented in the main body of the statements. Common note disclosures relate to such items as accounting policies, segmented information, and interim reporting. The financial statements of M&S can be accessed at the book’s companion website, www.wiley.com/college/kiesoifrs.

Instructions

Refer to M&S’s financial statements and the accompanying notes to answer the following questions.

(a) What specific items does M&S discuss in its Note 1—Summary of Significant Accounting Policies? (List the headings only.)
(b) For what segments did M&S report segmented information? Which segment is the largest? Who is M&S’s largest customer?
(c) What interim information was reported by M&S?

Bridge to the Profession

Professional Research

As part of the year-end audit, you are discussing the disclosure checklist with your client. The checklist identifies the items that must be disclosed in a set of IFRS financial statements. The client is surprised by the disclosure item related to accounting policies. Specifically, since the audit report will attest to the statements being prepared in accordance with IFRS, the client questions the accounting policy checklist item. The client has asked you to conduct some research to verify the accounting policy disclosures.

Instructions

Access the IFRS authoritative literature at the IASB website (http://eifrs.iasb.org/). When you have accessed the documents, you can use the search tool in your Internet browser to respond to the following questions. (Provide paragraph citations.)

(a) In general, what should disclosures of accounting policies encompass?
(b) List some examples of the most commonly required disclosures.