IFRS 9, IFRS 15 and IAS 34: Disclosing the Effects of Adopting New Standards

Extract, IFRS® Discussion Group Report on the Meeting – October 5, 2017

Entities adopting IFRS 9 *Financial Instruments* and IFRS 15 *Revenue from Contracts with Customers* on or after January 1, 2018 have raised questions around what they should be disclosing in their condensed interim financial statements after adopting these two new standards. The Group is asked to discuss five fact patterns relating to these questions.

The following guidance is relevant for Fact Patterns 1 and 2.

Paragraph 40A of IAS 1 *Presentation of Financial Statements* states:

> "An entity shall present a third statement of financial position as at the beginning of the preceding period in addition to the minimum comparative financial statements required in paragraph 38A if:
>
> (a) it applies an accounting policy retrospectively, makes a retrospective restatement of items in its financial statements or reclassifies items in its financial statements; and
>
> (b) the retrospective application, retrospective restatement or the reclassification has a material effect on the information in the statement of financial position at the beginning of the preceding period."

There is no explicit requirement for an opening statement of financial position in IAS 34 *Interim Financial Reporting*.

From a securities regulation perspective, Section 4.3(2)(d) in National Instrument 51-102 *Continuous Disclosure Obligations* (NI 51-102) indicates that an interim financial report must include:

> "in the following circumstances, a statement of financial position as at the beginning of the immediately preceding financial year:
>
> (i) the reporting issuer discloses in its interim financial report an unreserved statement of compliance with International Accounting Standard 34 *Interim Financial Reporting*, and
>
> (ii) the reporting issuer
>
> (A) applies an accounting policy retrospectively in its interim financial report,
>
> (B) makes a retrospective restatement of items in its interim financial report, or
>
> (C) reclassifies items in its interim financial report;"

Fact Pattern 1

A reporting issuer with a calendar year-end prepares its Q1-2018 interim financial statements for the three months ending March 31, 2018. IAS 34 requires, among other things, a comparative statement of comprehensive income for the three months ending March 31, 2017 and a

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comparative statement of financial position as at the end of the preceding financial year (i.e., December 31, 2017).

The reporting issuer adopted IFRS 9 and IFRS 15 on January 1, 2018 on a retrospective basis with prior period comparatives restated. The effect on the opening statement of financial position as at January 1, 2017 is immaterial.

Issue 1: Is an opening statement of financial position as at January 1, 2017 required in the Q1-2018 interim financial statements?

The Group's Discussion

For the fact pattern described above, Group members noted that an opening statement of financial position is not required.

Representatives from the Canadian Securities Administrators (CSA) noted there is no materiality threshold in NI 51-102. Therefore, if the reporting issuer concluded that the effect of adopting the new standards on the opening statement of financial position as at January 1, 2017 is immaterial, it would be prudent to disclose this fact in the notes to the financial statements.

Fact Pattern 2

The facts and circumstances presented in Fact Pattern 1 are the same, except that the reporting issuer adopted IFRS 9 and IFRS 15 on January 1, 2018 on a retrospective basis without prior period comparatives restated (sometimes called the modified retrospective basis). The cumulative effect of initially adopting the new standards is recognized at January 1, 2018, and is material to the statement of financial position.

Issue 2: Is an opening statement of financial position as at January 1, 2018 required in the Q1-2018 interim financial statements?

A point of consideration is that when the effect of adopting the new standards is recognized as an adjustment to opening equity as at January 1, 2018, the inclusion of an opening statement of financial position would not be meaningful to users. The disclosure of the nature of the adjustments recognized in opening equity as of January 1, 2018 is addressed in the transition disclosure requirements in the respective standards.

The Group's Discussion

For the fact pattern described above, Group members noted that an opening statement of financial position is not required because that would negate the effect of adopting a modified retrospective approach for transition.

CSA representatives also noted that NI 51-102 does not require an opening statement of financial position in this situation.

Fact Pattern 3

A reporting issuer prepares its Q1-2018 interim financial statements for the three months ending March 31, 2018. The reporting issuer adopts IFRS 9 on January 1, 2018, and is considering the extent of disclosures required when preparing its Q1-2018 interim financial statements.

Issue 3: What financial instrument disclosure requirements apply to Q1-2018 interim financial statements prepared in accordance with IAS 34?

Paragraph 16A(j) of IAS 34 sets out information to be disclosed for financial instruments. However, this paragraph was not amended as a result of the issuance of IFRS 9. Instead, IFRS 7 *Financial Instruments: Disclosures* was amended to include paragraphs 42I to 42S about disclosures to be provided upon the initial application of IFRS 9.

View 3A – Only the disclosure requirements in paragraph 16A(j) of IAS 34 apply.

Since IAS 34 was not amended for the changes made to IFRS 7 due to the issuance of IFRS 9, only the requirements in paragraph 16A(j) of IAS 34 apply to the first interim financial statements.

View 3B – The disclosure requirements in paragraph 16A(j) of IAS 34 and the transition disclosures in paragraphs 42I to 42S of IFRS 7 apply.

Paragraphs 42I to 42S of IFRS 7 do not make specific references to interim or annual reporting periods. Therefore, these disclosures apply to the first interim financial statements given their unique transitional status.

Further, although IAS 34 was not amended upon the issuance of IFRS 9, paragraph 15C of IAS 34 requires the following:

> "Individual IFRSs provide guidance regarding disclosure requirements for many of the items listed in paragraph 15B. When an event or transaction is significant to an understanding of the changes in an entity's financial position or performance since the last annual reporting period, its interim financial report should provide an explanation of and an update to the relevant information included in the financial statements of the last annual reporting period."

The disclosure requirements in paragraphs 42I to 42S of IFRS 7 would meet the above requirement such that users of interim financial statements can understand the impact of the initial adoption of IFRS 9 in the first interim period.

View 3C – The disclosure requirements in paragraph 16A(j) of IAS 34 and all disclosure requirements in IFRS 7 apply.

This view is incremental to View 3B. Given the significance of the changes in IFRS 9 compared to IAS 39, all disclosures under IFRS 7 are required in the first interim financial statements, in addition to specific transition disclosures required in paragraphs 42I to 42S of IFRS 7.

View 3D – The level of disclosures provided in the first interim financial statements after adopting IFRS 9 varies depending on an entity's specific circumstances. Applying IAS 34, including paragraphs 15C and 16A(j), requires judgment in terms of determining what to disclose and when to disclose it.

This view is consistent with the discussion at the January 11, 2013 meeting when the Group considered whether all the disclosures required by IFRS 12 *Disclosure of Interests in Other Entities* must be provided in the first interim financial statements after adopting IFRS 12.

At that meeting, Group members supported providing only the disclosures required by IAS 34, which include some of the IFRS 12 disclosures.

The Group's Discussion

The Group noted that it is important to provide users with the right level of information to help them understand the effects of adopting IFRS 9, particularly when an entity has selected the approach not to restate comparatives.

Several Group members supported the view that the disclosure requirements in paragraph 16A(j) of IAS 34 and the transition disclosures in paragraphs 42I to 42S of IFRS 7 apply (View 3B). Other Group members thought that an entity's starting point should be to look at the annual disclosure requirements pertaining to the significant event or transaction and use that as a model for preparing condensed interim disclosures. An entity should stand back and use judgment to assess what condensed disclosures are meaningful to users in order to comply with paragraph 15C of IAS 34. This approach means that an entity may start in View 3B but overlay the thought process described in View 3D.

A CSA representative emphasized the importance of the principle set out in paragraph 15C of IAS 34. Users need to be provided with information to help them understand the changes in an entity's financial position or performance since the last annual reporting period. IFRS 9 and IFRS 15 are major accounting standards, and therefore, the CSA representative expects to see robust disclosures in Q1-2018 to communicate the effects of adoption. The CSA representative echoed the Group's comments that entities should take materiality into consideration and exercise appropriate judgment in providing such relevant disclosures for users.

Fact Pattern 4

The facts and circumstances presented in Fact Pattern 3 are the same, except that the reporting issuer adopts IFRS 15 on January 1, 2018. The reporting issuer is considering the extent of disclosures required in relation to IFRS 15 when preparing the Q1-2018 interim financial statements.

Issue 4: What revenue-related disclosure requirements apply to Q1-2018 interim financial statements prepared in accordance with IAS 34?

Paragraph 16A(l) of IAS 34 was added as a result of the issuance of IFRS 15.

View 4A – Only the disclosure requirements in paragraph 16A(l) of IAS 34 apply.

IAS 34 is the relevant guidance for disclosures in the interim financial statements, and hence only the disclosure requirements in paragraph 16(A)(l) of IAS 34 apply.

View 4B – The disclosure requirements in paragraph 16A(l) of IAS 34, and in paragraphs 110 to 129 and Appendix C of IFRS 15, apply.

Proponents of this view look to the requirement in paragraph 15C of IAS 34 when assessing the extent of disclosures needed. Given the significance of the adoption of IFRS 15, all disclosures under IFRS 15 are required in the first interim financial statements.

Appendix C of IFRS 15 sets out specific disclosures relating to the transition to IFRS 15 (i.e., transition methods, practical expedients applied). Given their unique transitional status, these disclosures are also applicable to the first interim financial statements after adopting IFRS 15.

View 4C – The level of disclosures provided in the first interim financial statements after adopting IFRS 15 varies depending on an entity's specific circumstances. Applying IAS 34, including paragraphs 15C and 16A(l), requires judgment in terms of determining what to disclose and when to disclose it.

The rationale behind this view is the same as View 3D under Issue 3.

The Group's Discussion

Group members held the same views as expressed for Issue 3.

One CSA representative commented that from attending international meetings on this topic, it seems the disclosure expectations on a global level are consistent with the Group's discussion. An important point to note is that the extent of disclosures on adopting the new standards would vary by entity because information disclosed should be commensurate to the effect on the entity's business. Group members also noted that if an entity concludes the effect of adopting the new standards is immaterial, the entity needs to perform sufficient analysis to support that view.

On a separate note, another CSA representative commented that some entities have provided helpful disclosures indicating the directional effect of adopting the new standards. However, there is room to provide better information such as providing a discussion on the readiness to adopt the new standards and describing the work undertaken on any related system or internal control changes.

A few Group members briefly discussed whether the additional disclosure requirements in paragraph C8 of IFRS 15 apply to interim financial reporting periods. One Group member thought that the disclosure requirements for condensed interim financial statements are set out in IAS 34. However, in satisfying the requirements in paragraphs 15C and 16A(a) of IAS 34, an entity should look at the annual disclosure requirements as a model for preparing interim disclosures in order to provide sufficient information to help users understand the effects of adopting IFRS 15. As such, paragraph C8 of IFRS 15 should be considered when the modified retrospective transition method is applied.

Fact Pattern 5

A reporting issuer prepares Q2-2018 and Q3-2018 interim financial statements for the six months and nine months ending June 30 and September 30, 2018, respectively. The reporting issuer adopts IFRS 9 and IFRS 15 on January 1, 2018, and is considering the extent of disclosures required relating to accounting policies in order to comply with the minimum disclosure requirements under IAS 34.

Issue 5: When the reporting issuer's accounting policies under IFRS 9 and IFRS 15 have not changed relative to Q1-2018, can the reporting issuer cross-reference to the Q1-2018 interim financial statements when applying paragraph 16A(a) of IAS 34 in Q2 and Q3 of 2018?

Paragraph 16A of IAS 34 specifies what additional information is required in the notes to the interim financial statements or elsewhere in the interim financial report. In particular, paragraph 16A(a) of IAS 34 requires:

> "a 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."

For a reporting issuer adopting IFRS 9 or IFRS 15 on January 1, 2018, the first discussion of new accounting policies and methods under the new standards is included in the Q1-2018 interim financial statements and not in the most recent annual financial statements (i.e., year ending December 31, 2017).

View 5A – No.

Paragraph 16A of IAS 34 allows for cross-referencing to "some other statement (such as management commentary or risk report) that is available to users of the financial statements on the same terms as the interim financial statements and at the same time."

Proponents of this view note that the above does not contemplate an IAS 34 interim financial statement for an earlier interim period. Therefore, the reporting issuer's disclosures in Q1-2018 of new accounting policies and methods applied since the 2017 year-end financial statements are repeated in Q2-2018 and Q3-2018.

View 5B – Yes.

Unlike View 5A, proponents of this view think that the phrase "some other statement" is not restricted to items such as management commentary or risk reports as these are just examples rather than an exhaustive list. Provided that the Q1-2018 interim financial report is available to users on the same terms as the Q2-2018 and Q3-2018 interim financial reports and at the same time, cross-referencing is appropriate. These criteria are typically met when the earlier period interim financial report is in the public domain (e.g., available on SEDAR).

The Group's Discussion

Some Group members supported View 5A, noting that the disclosures in Q1-2018 would be repeated and updated in Q2 and Q3 of 2018. Cross-referencing is generally used when referring to disclosures in the last annual report but not to interim financial reports.

Other Group members noted that View 5A is a conservative approach but find it difficult to justify that View 5B is not acceptable. This is particularly the case if the Q2 and Q3 disclosures are identical to the Q1 disclosures. A CSA representative did not object to the use of cross-referencing, but at the same time, entities should not assume cross-referencing is applicable in all circumstances. For example, if the disclosures are identical, it raises the question of how useful it is to duplicate the information from quarter to quarter. However, if there is a significant change in the quarter and including disclosures from Q1-2018 provides additional context, it might be helpful to users to have all the information in one place.

Overall, the Group's discussion on the five fact patterns raises awareness about the disclosures after adopting IFRS 9 and IFRS 15. No further action was recommended to the AcSB.

(For a full understanding of the discussions and views expressed, listen to the audio clip).

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