IAS 1 Presentation of Financial Statements - A Closer Look

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IAS 1

Presentation of

Financial Statements -

A Closer Look

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In 1994, the International Accounting Standards Committee (IASC) reformatted its three International Accounting Standards (IASs) – IAS 1 *Disclosure of Accounting Policies* (issued in January 1975), IAS 5 *Information to be Disclosed in Financial Statements* (issued in October 1976) and IAS 13 *Presentation of Current Assets and Current Liabilities* (issued in November 1979). The IASC issued E53 *Presentation of Financial Statements* in July 1996. In August 1997, the IASC issued IAS 1 *Presentation of Financial Statements*. This standard superseded the earlier standards IAS 1 (1975), IAS 5 and IAS 13. The effective date was fixed as 1 July 1998. On 18 December 2003, the International Accounting Standards Board (IASB) issued the revised version of IAS 1 and is applicable for annual periods beginning on or after 1 January 2005.

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Objective

The objective of IAS 1 is to prescribe the basis for presentation of general purpose financial statements (GPFS), to ensure comparability both with the entity's financial statements of previous periods and with the financial statements of other entities. To achieve this objective, IAS 1 sets out the overall framework and responsibilities for the presentation of financial statements, guidelines for their structure and minimum requirements for the content of the financial statements. Standards for recognising, measuring, and disclosing specific transactions are addressed in other Standards and Interpretations.

Scope

IAS 1 applies to all GPFS based on International Financial Reporting Standards (IFRSs). GPFS are those intended to serve users who do not have the authority to demand financial reports tailored for their own needs. IAS 1 does not apply to interim financial statements prepared in accordance with IAS 34 *Interim Financial Reporting*. Reports that are presented outside of the financial statements -- including financial reviews by management, environmental reports, and value added statements -- are outside the scope of IFRSs.

Specifications

IAS 1 specifies the following about the preparation and presentation of financial statements:

- Financial statements are prepared on a going concern basis unless management either intends to liquidate the entity or to cease trading, or has no realistic alternative but to do so.

- Financial statements, except for cash flow information, are prepared using the accrual basis of accounting.

- The presentation and classification of items in the financial statements are usually retained from one period to the next.

- Each material class of similar items is presented separately. Dissimilar items are presented separately unless they are immaterial. Omissions or misstatements of items are material if they could, individually or collectively, influence the economic decisions of users taken on the basis of the financial statements.

- Assets and liabilities, and income and expenses, are not offset unless required or permitted by an IFRS.

- Assets and liabilities should be classified as current, as non-current, or else presented broadly in their order of liquidity.

- Comparative information is disclosed for all amounts reported in the financial statements, unless an IFRS requires or permits otherwise.

- Financial statements are presented at least annually.

Objective of Financial Statements

The objective of GPFS is to provide information about the financial position, financial performance, and cash flows of an entity that is useful to a wide range of users in making economic decisions. To meet that objective, financial statements provide information about an entity's:

- Assets.
- Liabilities.
- Equity.
- Income and expenses, including gains and losses.
- Other changes in equity.
- Cash flows.

That information, along with other information in the notes, assists users of financial statements in predicting the entity's future cash flows and, in particular, their timing and certainty.

Components of Financial Statements

A complete set of financial statements comprises:

(a) a balance sheet;
(b) an income statement;
(c) a statement of changes in equity showing either:
  (i) all changes in equity, or
  (ii) changes in equity other than those arising from transactions with equity holders acting in their capacity as equity holders;
(d) a cash flow statement; and
(e) notes, comprising a summary of significant accounting policies and other explanatory notes.

Fair Presentation and Compliance with IFRSs

The financial statements must "present fairly" the financial position, financial performance and cash flows of an entity. Fair presentation requires the faithful representation of the effects of transactions, other events, and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the *Framework for the Preparation and Presentation of Financial Statements*. The application of IFRSs (i.e. Standards and Interpretations), with additional disclosure when necessary, is presumed to result in financial statements that achieve a fair presentation.

IAS 1 requires that an entity whose financial statements comply with IFRSs make an explicit and unreserved statement of such compliance in the notes. Financial statements shall not be described as complying with IFRSs unless they comply with all the requirements of IFRSs.

Inappropriate accounting policies are not rectified either by disclosure of the accounting policies used or by notes or explanatory material.

IAS 1 acknowledges that, in extremely rare circumstances, management may conclude that compliance with an IFRS requirement would be so misleading that it would conflict with the objective of financial statements set out in the Framework. In such a case, the entity is required to depart from the IFRS requirement, with detailed disclosure of the nature, reasons, and impact of the departure.

Going Concern

When preparing financial statements, management shall make an assessment of an entity's ability to continue as a going concern. An entity preparing IFRS financial statements is presumed to be a going concern. If management has significant concerns about the entity's ability to continue as a going concern, the uncertainties must be disclosed. If management concludes that the entity is not a going concern, the financial statements should not be prepared on a going concern basis, in which case IAS 1 requires a series of disclosures.

Accrual Basis of Accounting

IAS 1 requires that an entity prepare its financial statements, except for cash flow information, using the accrual basis of accounting.

Consistency of Presentation

The presentation and classification of items in the financial statements shall be retained from one period to the next unless a change is justified either by a change in circumstances or a requirement of a new IFRS.

Materiality and Aggregation

Each material class of similar items must be presented separately in the financial statements. Dissimilar items may be aggregated only if the are individually immaterial.

Offsetting

Assets and liabilities, and income and expenses, may not be offset unless required or permitted by a Standard or an Interpretation.

Comparative Information

IAS 1 requires that comparative information shall be disclosed in respect of the previous period for all amounts reported in the financial statements, both face of financial statements and notes, unless another Standard requires otherwise.

If comparative amounts are changed or reclassified, various disclosures are required.

Structure and content of financial statements in general

The financial statements shall be identified clearly and distinguished from other information in the same published document.
Clearly identify:

- the financial statements
- the reporting enterprise
- whether the statements are for the enterprise or for a group
- the date or period covered
- the presentation currency
- the level of precision (thousands, millions, etc.)

Reporting Period

There is a presumption that financial statements will be prepared at least annually. If the annual reporting period changes and financial statements are prepared for a different period, the enterprise must disclose the reason for the change and a warning about problems of comparability.

Disclosures Requirements

IAS 1 specifies the minimum line item disclosures on the face of, or in the notes to, the balance sheet, the income statement, and the statement of changes in equity. Current and non-current assets, and current and non-current liabilities are presented as separate classifications on the face of the balance sheet.

IAS 1 specifies disclosures about information to be presented in the financial statements, including judgements, key sources of estimation uncertainty, and accounting policies. Financial statements shall present fairly the financial position, financial performance and cash flows of an entity. In virtually all circumstances, a fair presentation is achieved by compliance with applicable IFRSs.

Balance Sheet

An entity must normally present a classified balance sheet, separating current and non-current assets and liabilities. Only if a presentation based on liquidity provides information that is reliable and more relevant may the current/non-current split be omitted. In either case, if an asset (liability) category commingles amounts that will be received (settled) after 12 months with assets (liabilities) that will be received (settled) within 12 months, note disclosure is required that separates the longer-term amounts from the 12-month amounts.

Current assets are cash; cash equivalent; assets held for collection, sale, or consumption within the enterprise's normal operating cycle; or assets held for trading within the next 12 months. All other assets are non-current.

Current liabilities are those to be settled within the enterprise's normal operating cycle or due within 12 months, or those held for trading, or those for which the entity does not have an unconditional right to defer payment beyond 12 months. Other liabilities are non-current.

Long-term debt expected to be refinanced under an existing loan facility is non-current, even if due within 12 months.

If a liability has become payable on demand because an entity has breached an undertaking under a long-term loan agreement on or before the balance sheet date, the liability is current, even if the lender has agreed, after the balance sheet date and before the authorisation of the financial statements for issue, not to demand payment as a consequence of the breach. However, the liability is classified as non-current if the lender agreed by the balance sheet date to provide a period of grace ending at least 12 months after the balance sheet date, within which the entity can rectify the breach and during which the lender cannot demand immediate repayment.

Minimum items on the face of the balance sheet

- (a) property, plant and equipment;
- (b) investment property;
- (c) intangible assets;
- (d) financial assets (excluding amounts shown under (e), (h) and (i));
- (e) investments accounted for using the equity method;
- (f) biological assets;
- (g) inventories;
- (h) trade and other receivables;
- (i) cash and cash equivalents;

- (j) trade and other payables;
- (k) provisions;
- (l) financial liabilities (excluding amounts shown under (j) and (k));
- (m) liabilities and assets for current tax, as defined in IAS 12 *Income Taxes*;
- (n) deferred tax liabilities and deferred tax assets, as defined in IAS 12;
- (o) minority interest, presented within equity; and
- (p) issued capital and reserves attributable to equity holders of the parent.

Additional line items may be needed to fairly present the entity's financial position.

IAS 1 does not prescribe the format of the balance sheet. Assets can be presented current then non-current, or vice versa, and liabilities and equity can be presented current then non-current then equity, or vice versa. A net asset presentation (assets minus liabilities) is allowed. The long-term financing approach used in UK and elsewhere – fixed assets + current assets - short term payables = long-term debt plus equity – is also acceptable.

Regarding issued share capital and reserves, the following disclosures are required:

- numbers of shares authorised, issued and fully paid, and issued but not fully paid
- par value
- reconciliation of shares outstanding at the beginning and the end of the period
- description of rights, preferences, and restrictions
- treasury shares, including shares held by subsidiaries and associates
- shares reserved for issuance under options and contracts
- a description of the nature and purpose of each reserve within owners' equity

Income Statement

In the 2003 revision to IAS 1, the IASB is now using "profit or loss" rather than "net profit or loss" as the descriptive term for the bottom line of the income statement.

All items of income and expense recognised in a period must be included in profit or loss unless a Standard or an Interpretation requires otherwise.

Minimum items on the face of the income statement should include:

(a) revenue;

(b) finance costs;

(c) share of the profit or loss of associates and joint ventures accounted for using the equity method;

(d) pre-tax gain or loss recognised on the disposal of assets or settlement of liabilities attributable to discontinuing operations;

(e) tax expense; and

(f) profit or loss.

The following items must also be disclosed on the face of the income statement as allocations of profit or loss for the period:

(a) profit or loss attributable to minority interest; and

(b) profit or loss attributable to equity holders of the parent.

Additional line items may be needed to fairly present the enterprise's results of operations.

No items may be presented on the face of the income statement or in the notes as "extraordinary items".

Certain items must be disclosed either on the face of the income statement or in the notes, if material, including:

(a) write-downs of inventories to net realisable value or of property, plant and equipment to recoverable amount, as well as reversals of such write-downs;

(b) restructurings of the activities of an entity and reversals of any provisions for the costs of restructuring;

(c) disposals of items of property, plant and equipment;

(d) disposals of investments;

(e) discontinuing operations;

(f) litigation settlements; and

(g) other reversals of provisions.

Expenses should be analysed either by nature (raw materials, staffing costs, depreciation, etc.) or by function (cost of sales, selling, administrative, etc.) either on the face of the income statement or in the notes. If an enterprise categorises by function, additional information on the nature of expenses -- at a minimum depreciation, amortisation, and staff costs -- must be disclosed.

Cash Flow Statement

Rather than setting out separate standards for presenting the cash flow statement, IAS 1 refers to IAS 7, *Cash Flow Statements.*

Statement of Changes in Equity

IAS 1 requires an entity to present a statement of changes in equity as a separate component of the financial statements. The statement must show:

(a) profit or loss for the period;

(b) each item of income and expense for the period that is recognised directly in equity, and the total of those items;

(c) total income and expense for the period (calculated as the sum of (a) and (b)), showing separately the total amounts attributable to equity holders of the parent and to minority interest; and

(d) for each component of equity, the effects of changes in accounting policies and corrections of errors recognised in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.

The following amounts may also be presented on the face of the statement of changes in equity, or they may be presented in the notes:

(a) capital transactions with owners;

(b) the balance of accumulated profits at the beginning and at the end of the period, and the movements for the period; and

(c) a reconciliation between the carrying amount of each class of equity capital, share premium and each reserve at the beginning and at the end of the period, disclosing each movement.

Notes to the Financial Statements

The notes must:

- present information about the basis of preparation of the financial statements and the specific accounting policies used;

- disclose any information required by IFRSs that is not presented on the face of the balance sheet, income statement, statement of changes in equity, or cash flow statement; and
- provide additional information that is not presented on the face of the balance sheet, income statement, statement of changes in equity, or cash flow statement that is deemed relevant to an understanding of any of them.

Notes should be cross-referenced from the face of the financial statements to the relevant note.

IAS 1 suggests that the notes should normally be presented in the following order:

- a statement of compliance with IFRSs;
- a summary of significant accounting policies applied, including:
  - the measurement basis (or bases) used in preparing the financial statements; and
  - the other accounting policies used that are relevant to an understanding of the financial statements.
- supporting information for items presented on the face of the balance sheet, income statement, statement of changes in equity, and cash flow statement, in the order in which each statement and each line item is presented; and
- other disclosures, including:
  - contingent liabilities (see IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*) and unrecognised contractual commitments; and
  - non-financial disclosures, such as the entity's financial risk management objectives and policies (see IAS 32 *Financial Instruments: Presentation*).

Disclosure of judgements

New in the 2003 revision to IAS 1, an entity must disclose, in the summary of significant accounting policies or other notes, the judgements, apart from those involving estimations, that management has made in the process of applying the entity's accounting policies that have the most significant effect on the amounts recognised in the financial statements.

Examples cited in IAS 1 include management's judgements in determining:

- whether financial assets are held-to-maturity investments;
- when substantially all the significant risks and rewards of ownership of financial assets and lease assets are transferred to other entities;
- whether, in substance, particular sales of goods are financing arrangements and therefore do not give rise to revenue; and
- whether the substance of the relationship between the entity and a special purpose entity indicates that the special purpose entity is controlled by the entity.

Disclosure of key sources of estimation uncertainty

Also new in the 2003 revision to IAS 1, an entity must disclose, in the notes, information about the key assumptions concerning the future, and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year. These disclosures do not involve disclosing budgets or forecasts.

The following other note disclosures are required by IAS 1 if not disclosed elsewhere in information published with the financial statements:

- domicile of the enterprise;
- country of incorporation;
- address of registered office or principal place of business;
- description of the enterprise's operations and principal activities;
- name of its parent and the ultimate parent if it is part of a group.

Disclosures about Dividends

The following must be disclosed either on the face of the income statement or the statement of changes in equity or in the notes:

- the amount of dividends recognised as distributions to equity holders during the period, and
- the related amount per share.

The following must be disclosed in the notes:

- the amount of dividends proposed or declared before the financial statements were authorised for issue but not recognised as a distribution to equity holders during the period, and the related amount per share; and
- the amount of any cumulative preference dividends not recognised.

An entity shall disclose information that enables users of its financial statements to evaluate the entity's objectives, policies and processes for managing capital.

Post issue Developments

Capital Disclosures

On 18th August 2005, as part of its project to develop IFRS 7 *Financial Instruments: Disclosures*, the IASB also amended IAS 1 to add requirements for disclosures of:

* the entity's objectives, policies and processes for managing capital;
* quantitative data about what the entity regards as capital;
* whether the entity has complied with any capital requirements; and
* if it has not complied, the consequences of such non-compliance.

These disclosure requirements apply to all entities, effective for annual periods beginning on or after 1 January 2007, with earlier application encouraged.

Revised IAS

On 16 March 2006, the IASB issued an Exposure Draft of Proposed Amendments to IAS 1 Presentation of Financial Statements–A Revised Presentation. On 6 September 2007, the IASB issued a revised version of IAS 1 *Presentation of Financial Statements*. The revision is aimed at improving users' ability to analyse and compare the information given in financial statements. The changes made are to require information in financial statements to be aggregated on the basis of shared characteristics and to introduce a statement of comprehensive income. This will enable readers to analyse changes in a company's equity resulting from transactions with owners in their capacity as owners (such as dividends and share repurchases) separately from 'non-owner' changes (such as transactions with third parties).

In response to comments received through the consultation process the revised standard gives preparers of financial statements the option of presenting items of income and expense and components of other comprehensive income either in a single statement of comprehensive income with subtotals, or in two separate statements (a separate income statement followed by a statement of comprehensive income). Comprehensive income for a period includes profit or loss for that period plus other comprehensive income recognised in that period. The components of other comprehensive income include:

changes in revaluation surplus (IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets*).
actuarial gains and losses on defined benefit plans recognised in accordance with paragraph 93A of IAS 19 *Employee Benefits*.
gains and losses arising from translating the financial statements of a foreign operation (IAS 21 *The Effects of Changes in Foreign Exchange Rates*).
gains and losses on remeasuring available-for-sale financial assets (IAS 39 *Financial Instruments: Recognition and Measurement*).
the effective portion of gains and losses on hedging instruments in a cash flow hedge (IAS 39).
Components of comprehensive income may not be presented in the statement of changes in equity.

The other main changes from the previous version are to require that an entity must:

Present a statement of financial position (balance sheet) as at the beginning of the earliest comparative period in a complete set of financial statements when the entity applies an accounting policy retrospectively or makes a retrospective restatement.

Disclose income tax relating to each component of other comprehensive income.

Disclose reclassification adjustments relating to components of other comprehensive income.

The revisions include changes in the titles of some of the financial statements as they will be used in IFRSs to reflect their function more clearly :

'balance sheet' will become 'statement of financial position'
'income statement' will become 'statement of comprehensive income'
'cash flow statement' will become 'statement of cash flows'.

The new titles will be used in accounting standards, but are not mandatory for use in financial statements. Entities are not required to use the new titles in their financial statements. All existing Standards and Interpretations are being amended to reflect the new terminology. The revised IAS 1 resulted in consequential amendments to 5 IFRSs, 23 IASs, and 10 Interpretations.

The revised standard will come into effect for the annual periods beginning on or after 1 January 2009, but early adoption is permitted.

The publication of IAS 1 marks the completion of the first phase of the IASB's joint initiative with the US Financial Accounting Standards Board (FASB) to review and harmonise the presentation of financial statements. The second phase, which has already begun, is examining more fundamental questions about the presentation of information in financial statements and the IASB expects to publish a discussion paper on the subject shortly
.
Introducing the revised IAS 1, Sir David Tweedie, Chairman of the IASB, said:
"Any changes to the way financial information is presented will quite rightly attract much interest. With the first phase of this project now completed we look forward to addressing the more fundamental questions as part of a broad consultation that will start at the beginning of next year. I would strongly encourage all those who have an interest in financial reporting to participate in this consultation in order to ensure that the best ideas available are given due consideration by the Board."

Disclosures about Puttable Shares and Obligations Arising Only on Liquidation

On 22 June 2006, the IASB issued an Exposure Draft of proposed amendments to IAS 32 relating to Puttable Instruments and Obligations Arising on Liquidation would add new disclosure requirements to IAS 1. On 14 February 2008, the IASB published an amendment to IAS 1 that requires the following additional disclosures if an entity has a puttable instrument that is presented as equity:

summary quantitative data about the amount classified as equity;
the entity's objectives, policies and processes for managing its obligation to repurchase or redeem the instruments when required to do so by the instrument holders, including any changes from the previous period;
the expected cash outflow on redemption or repurchase of that class of financial instruments; and
information about how the expected cash outflow on redemption or repurchase was determined.

If an instrument is reclassified into and out of each category (financial liabilities or equity) the amount, timing and reason for that reclassification must be disclosed. If an entity is a limited-life entity, disclosure is also required regarding the length of its life.

The foregoing disclosures are required for annual periods beginning on or after 1 January 2009, with earlier application permitted.

Conclusion

The second phase of the joint project of financial statement presentation will focus on more detailed issues related to the presentation of information on the face of financial statements, including required totals and subtotals.

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