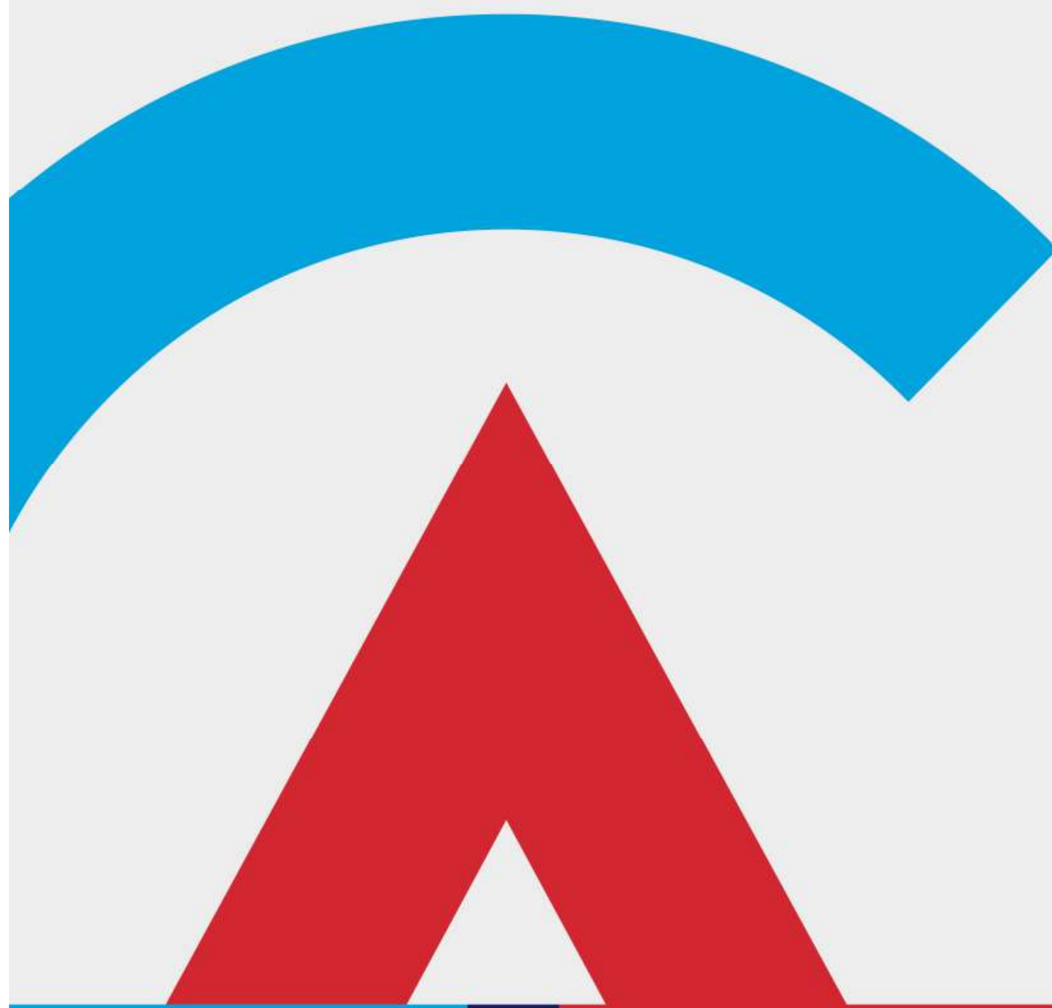
A Special Purpose Financial Reporting Framework for use by For-Profit Entities (SPFR for FPEs)

Designed for use in New Zealand by Small and Medium Sized Entities

2018



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Introduction

Design principles

A Special Purpose Financial Reporting Framework for use by For-Profit Entities (*SPFR for FPEs*) is an optional set of self-contained guidelines designed to assist in the preparation of single entity, historical, special purpose financial reports (SPFR) for small and medium sized for-profit entities (SMEs).

SPFR for FPEs is less complex than New Zealand equivalents to International Financial Reporting Standards (NZ IFRS). *SPFR for FPEs* does not constitute generally accepted accounting practice (GAAP) as defined in section 8 of the *Financial Reporting Act 2013* and paragraph 4 of Standard XRB A1 *Application of the Accounting Standards Framework*. The accounting principles forming the basis for *SPFR for FPEs* are intended to be the most appropriate for the preparation of SME financial statements based on the needs of financial statement users and cost-benefit considerations.

SPFR for FPEs is issued by Chartered Accountants Australia and New Zealand (CA ANZ). It has been endorsed by and is the result of extensive consultations with a Working Group comprising representatives from the major banking institutions, Inland Revenue and CA ANZ members.

Application

This is a SPFR framework for use by for-profit SMEs. It is by no means the only SPFR framework that can be used in the preparation of single entity historical financial statements SPFR.

The use of *SPFR for FPEs* is optional. Those responsible for an entity's financial reporting may opt to use *SPFR for FPEs* to prepare its financial statements. In determining the most appropriate basis of preparation to ensure an accurate record of financial position and financial performance, consideration should be given to information that will be required by the intended users of the financial statements.

Key features of *SPFR for FPEs*

The key features of *SPFR for FPEs* that make it appropriate for use by SMEs are:

(a) Historical cost is the primary measurement basis;

(b) Disclosures are less complex than NZ IFRS, while still providing users with relevant information;

(c) Recognition and measurement methods are simple and straightforward;

(d) Adjustments needed to reconcile tax return income are reduced;

(e) Reporting guidelines are principle-based and can be applied across various industry sectors;

(f) For more complex transactions entities can step up to NZ IFRS for the accounting treatment of those complex transactions whilst still asserting compliance with *SPFR for FPEs*;

(g) Financial statements prepared in accordance with *SPFR for FPEs* meet the Inland Revenue minimum financial reporting requirements;

(h) Financial statements prepared in accordance with *SPFR for FPEs* can be audited; and

(i) Implementation guidance, in the form of illustrative financial statements for various sectors of the New Zealand economy, is provided as a companion to *SPFR for FPEs*.

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Preface

The current and future role of CA ANZ in issuing accounting guidance

P1 On 31 March 2015, New Zealand accounting standards commonly referred to as "Old GAAP[1]" and NZ IFRS Differential Reporting (NZ IFRS Diff Rep) were revoked. From this date, they no longer have authoritative support as a source of generally accepted accounting practice (GAAP) in New Zealand.

P2 The *Financial Reporting (Amendments to Other Enactments) Act 2013* removed the requirement for many SMEs to prepare general purpose financial reports (GPFR) in accordance with GAAP. For some of these entities this represents a welcome cost reduction, however, many SMEs still opt or are required by end users[2] to prepare financial statements in order to record their financial position and financial performance.

P3 In light of this, CA ANZ recognised that a SPFR framework would be useful for SMEs, not only to meet the continued financial reporting demands of this sector, but to ensure that the consistency, reliability and integrity of SME financial reporting is maintained. This led to the development of *SPFR for FPEs* for for-profit SMEs with no statutory requirement to prepare GPFR under the new financial reporting framework.

[1] Statements of Standard Accounting Practice (SSAPs) and Financial Reporting Standards (FRSs)

[2] Companies, other than exempt companies (as defined), are required to prepare financial statements that comply with the Inland Revenue minimum financial reporting requirements

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Section 1 Scope and purpose

Intended scope of *SPFR for FPEs*

1.1 *SPFR for FPEs* is intended for use in the preparation of historical single entity financial statements by for-profit SMEs that have no statutory requirement to prepare general purpose financial reports (GPFR) in accordance with generally accepted accounting practice (GAAP) in New Zealand. It is recognised that SMEs often produce financial statements only for the purposes of meeting the user needs of owners, tax authorities or banks.

1.2 The determination of whether an entity has a statutory requirement to prepare GPFR requires the careful consideration of applicable New Zealand legislation and regulations.

1.3 When an entity has no statutory requirement to prepare GPFR, consideration should be given to whether *SPFR for FPEs* is the most appropriate basis for financial statement preparation.

1.4 Circumstances in which the preparation of financial statements in accordance *SPFR for FPEs* could be deemed inappropriate may include, but are not limited to, when the reporting entity:

(a) has a wide range of users;

(b) receives financial support from the Government or wider public in the form of donations and grants;

(c) anticipates preparing GPFR in the future due to growth or capital raising strategies, in which case the adoption of NZ IFRS may be more suitable;

(d) is an aggregation or consolidation of multiple entities;

(e) is a not-for-profit (NFP) public benefit entity (PBE), in which case PBE SFR-A (NFP) or PBE SFR-C (NFP) issued by the External Reporting Board (XRB) may be more suitable.

1.5 *SPFR for FPEs* covers the transactions most likely to be encountered by SMEs, but it cannot satisfy all needs of all users. Entities applying *SPFR for FPEs* are permitted to “step up” to NZ IFRS for more complex transactions while continuing to assert compliance with *SPFR for FPEs*.

Purpose of SPFR for FPEs

1.6 GPFR are designed to meet the common information needs of a wide range of users, for example, shareholders, creditors, employees and the public at large. In contrast to this, the purpose of *SPFR for FPEs* is more narrow and has been designed for users who have the ability to demand financial information which meets their specific needs.

1.7 *SPFR for FPEs* has been designed primarily for the following key users:

(a) banks and other credit providers who use financial statements to assess profitability, security and liquidity;

(b) owners who use financial statements to assess financial performance, and make capital investment decisions; and

(c) tax authorities to assess income tax liabilities.

1.8 *SPFR for FPEs* provides less detailed guidance than GAAP. Instead, general principles are provided that encourage the use of professional judgement in the particular circumstances of a transaction or event.

Updating of SPFR for FPEs

1.9 CA ANZ will endeavour to regularly update *SPFR for FPEs* in order to incorporate member feedback where relevant, and to reflect changes in the financial reporting environment where necessary.

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1.10 *SPFR for FPEs* was initially issued in May 2014. After three years of operation, a post-implementation review was conducted. As a result of the review, *SPFR for FPEs* was amended and a revised version of *SPFR for FPEs* was issued in November 2017.

NZICA Professional and Ethical Standards

1.11 *SPFR for FPEs* should be used in conjunction with the Professional and Ethical Standards issued by the New Zealand Institute of Chartered Accountants (NZICA).

Fair presentation framework

1.12 *SPFR for FPEs* is a fair presentation framework as defined in paragraph 13(a)(i) of ISA (NZ) 200 *Overall Objective of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing (New Zealand).*

1.13 In order to achieve fair presentation of the financial statements, it may be necessary for the management of an entity to provide disclosures beyond those specifically required by *SPFR for FPEs*; or to depart from a requirement of *SPFR for FPEs*. Such departures are expected to be necessary only in extremely rare circumstances.

Audit implications

1.14 Auditors should give consideration to ISA (NZ) 800 *Special Considerations – Audits of Financial statements Prepared in Accordance with Special Purpose Frameworks* when undertaking an audit of financial statements prepared in accordance with *SPFR for FPEs*.

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Section 2 Underlying concepts and principles

Purpose and scope of section

2.1 This section describes the underlying concepts and principles that should be taken into consideration when preparing financial statements in accordance with *SPFR for FPEs*. It also sets out the qualities and assumptions that will make the information disclosed in the financial statements useful for decision making.

2.2 Nothing is this section overrides any specific guidance provided in other sections of *SPFR for FPEs*.

Objective of *SPFR for FPEs*

2.3 The objective of *SPFR for FPEs* is to ensure the preparation of single entity financial statements that provide useful information to users regarding the financial performance and financial position of the reporting entity.

2.4 *SPFR for FPEs* has been developed to satisfy anticipated user needs. The cost-benefit equation has been a key component in the development of *SPFR for FPEs* with a simplified approach taken towards the preparation of financial statements.

Reporting entity

2.5 The reporting entity is the entity/entities represented by the financial statements. *SPFR for FPEs* has been primarily developed to provide guidance on the preparation of single entity financial statements. Aggregated or consolidated financial statements are not within the scope of *SPFR for FPEs*. The need for aggregated or consolidated financial statements arises from the existence of control for reporting purposes or because certain entities form a tax group, a funding group or a security group. *SPFR for FPEs* covers the accounting treatment for other types of interests in other entities. The following table outlines how to account for interests in other entities.

Relationship	Definition	Treatment	Reference
Control	Exposure, or rights, to variable returns from involvement with an entity and the ability to affect those returns through power over the entity	Consolidation	Step up to NZ IFRS 10 *Consolidated Financial Statements;* and NZ IFRS 12 *Disclosure of Interests in Other Entities*
Joint control	The agreed sharing of control over an activity by a binding arrangement	Depends on form of activity and nature of agreement	Unincorporated joint ventures: Section 14 *Unincorporated joint venture arrangements*; or Incorporated joint ventures: Section 15 *Financial instruments*
Significant influence	The power to participate in the financial and operating policy decisions of an entity but not the control or joint control over those policies	Account for as an equity instrument	Section 15 *Financial instruments*

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Qualitative characteristics of information in financial statements

2.6 The quality of information provided in SME financial statements determines the usefulness of those financial statements to the user. In the development of *SPFR for FPEs* the requirements for the quality of the preparation and presentation of financial information in the resulting financial statements has been moderated against potential costs to the end user.

2.7 The most important and fundamental qualitative characteristics are relevance and reliability (faithful representation). The other qualitative characteristics are less critical but still very important. Sometimes it may be necessary to put the principles of one of the other qualitative characteristics above another in order to improve the relevance and reliability of the financial statements overall.

Relevance

2.8 Information provided in the financial statements should be relevant to the decision-making needs of its users. Relevant information can influence the economic decisions of users by aiding them in assessing events in the past, present or future; or by confirming, or amending, their past assessment.

2.9 Timeliness is a cornerstone of relevance, because if financial information is not available when needed its relevance and therefore its usefulness is reduced.

Reliability

2.10 The information provided in financial statements should be reliable. Information is reliable when it:

(a) faithfully represents the actual underlying transactions and events;

(b) is free from bias and material error; and

(c) can be independently verified if requested by the user.

Completeness

2.11 To be reliable, the information in financial statements must be complete within the bounds of materiality and cost. An omission can cause information to be false or misleading and thus unreliable and deficient in terms of its relevance.

Cost benefit balance

2.12 The benefits derived from financial information (based on an assessment of the specific user needs) should exceed the cost of providing it. As an example, the benefits of satisfying tax reporting obligations are presumed to always exceed the cost of compiling the required information.

Materiality

2.13 Information is material, and therefore has relevance, if its omission or misstatement could individually or collectively influence or change decisions of users made on the basis of the financial statements. Materiality depends on the nature and size of the omission or misstatement judged in the surrounding circumstances.

2.14 The users of financial statements prepared by SMEs are expected to have a reasonable knowledge of the reporting entity's activities. Therefore the assessment of materiality should consider the likely users of the financial statements, and the information needs of those users.

2.15 Where financial statements are prepared for tax purposes, financial information is material if the disclosure could impact the entity's tax obligations.

2.16 The assessment of materiality should be considered for determining whether:

(a) it is probable that an omission or misstatement impacting the reported financial performance or financial position should be adjusted; and

(b) it is probable that an omission or misstatement impacting a specific disclosure in the financial statement or accompanying notes should be disclosed.

2.17 Specific disclosure of transactions or events as prescribed within *SPFR for FPEs* is not required if the information is not material to the specified users. If there are no such transactions or events, an affirmative statement is not required.

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Prudence

2.18 Where estimates are necessary for measurement purposes, judgement needs to be applied using all readily available information. A degree of caution and a conservative approach is recommended when making measurement decisions.

Assumptions underlying the preparation of financial statements

2.19 Unless there are special circumstances, the preparation of financial statements should apply the following assumptions:

(a) the entity is a going concern; and

(b) the entity's financial statement elements are reported on an accrual basis.

Going concern

2.20 Financial statements are normally prepared on the assumption that the entity will continue in existence for the foreseeable future. The going concern basis of accounting presumes that an entity will be able to realise its assets and discharge its liabilities in the ordinary course of business. In particular, this means that there is no intention or necessity to liquidate or significantly reduce operations.

2.21 When assessing whether an entity will continue in existence for the foreseeable future, consideration should be given to changes in circumstances which are likely to occur during a period for at least one year from the date on which the financial statements are authorised for issue by the governing body.

2.22 In the event that an entity is not viewed as a going concern, the carrying value of assets and liabilities should be measured at their expected realisable value.

2.23 Measuring assets and liabilities at their expected realisable value results in:

(a) assets being carried at the amount of cash or cash equivalents that could currently be obtained by selling the asset in an orderly disposal;

(b) liabilities being carried at amount of cash or cash equivalents required to settle the debt in the short term; and

(c) recognising liabilities for future expenses that will be incurred.

Accrual accounting

2.24 Under the accrual basis of accounting, the effects of transactions and other events are recognised when they occur and are recorded in the appropriate period to which they relate.

Definition of financial statement elements

2.25 Financial statement elements are the categories in which transactions and other events are grouped and reported, in accordance with their economic characteristics. There are two broad groups of financial statement elements:

(a) those that describe the financial position of the entity as of a specific date – assets, liabilities and equity; and

(b) those that describe the financial performance during a reporting period – revenue and expenses.

2.26 Notes to the financial statements, which are useful for the purpose of clarification and for further explanation of items in the financial statements, although an integral part of financial statements, are not considered to be an element.

Financial position

2.27 Some items that meet the definition of an asset or liability below may not be recognised in the Balance sheet because they do not satisfy the recognition criteria in paragraphs 2.41 – 2.44.

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Assets

2.28 An asset is a resource controlled by an entity resulting from a past event and from which future economic benefits are expected to flow to the entity.

2.29 In determining the existence of an asset, legal ownership is not essential.

Liabilities

2.30 A liability is a present obligation of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits.

2.31 An essential characteristic of a liability is that the entity has a present obligation to act or perform in a particular way, resulting in the entity having no realistic alternative to settling the obligation.

2.32 The obligation leading to the recognition of a liability may be either a legal obligation or a constructive obligation. A constructive obligation is created by an entity's actions when:

(a) by an established pattern of past practice, the entity has indicated to other parties that it will act or perform in a particular way; and

(b) as a result, the entity has created a valid expectation on the part of other parties that it will discharge those responsibilities.

Equity

2.33 Equity is the residual interest in the assets of an entity after all liabilities have been deducted.

Financial performance

2.34 The recognition of revenue and expenses results directly from the recognition of assets and liabilities as discussed in paragraphs 2.28 – 2.32.

Revenue

2.35 Revenue is an increase in economic benefits during the reporting period in the form of inflows of or enhancements to assets or decreases in liabilities that result in increases in equity, other than those relating to contributions from owners.

2.36 The definition of revenue encompasses:

(a) revenue resulting from the ordinary activities of the entity, normally arising from the sale of goods, the rendering of services, or use by others of an entity's resources yielding rent, interest, royalties or dividends; and

(b) gains resulting from other incidental movements that meet the definition of revenue but do not arise from the operating activities of the entity.

2.37 When gains are recognised in profit or loss, they are usually displayed separately on the face of the Statement of profit or loss or in the notes to the financial statements as knowledge of them is useful for making economic decisions.

Expenses

2.38 Expenses are decreases in economic benefits during the period in the form of outflows or depletions of assets or incurrence of liabilities which result in decreases in equity, other than those relating to distributions to owners.

2.39 The definition of expenses encompasses:

(a) expenses resulting from the ordinary activities of the entity, for example, cost of sales, wages and depreciation; and

(b) losses resulting from other incidental items that meet the definition of expenses but do not arise from the operating activities of the entity.

2.40 When losses are recognised in profit or loss, they are usually displayed separately on the face of the Statement of profit or loss or in the notes to the financial statements because knowledge of them is useful for making economic decisions.

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Recognition of assets, liabilities, revenue and expenses

2.41 Accounting elements are recognised when:

(a) it is probable that future economic benefits associated with the item will flow to or from the entity; and

(b) an item has a cost or value that can be measured reliably.

2.42 The first criterion for recognition of an item is an assessment of the degree of probability attached to flows of future economic benefits. Such an assessment is made on the basis of the evidence available relating to conditions at the end of the reporting period when the financial statements are prepared.

2.43 The second criterion for recognition of an item is that it possesses a cost or value that can be measured with reliability. In many cases, the cost or value of an item is not known, and requires estimation. The use of reasonable estimates is an essential part of the preparation of financial statements and does not undermine their reliability.

2.44 An item that fails to meet the recognition criteria may qualify for recognition at a later date as a result of subsequent circumstances or events.

2.45 An entity shall recognise only the assets held by the entity on its own account as principal. An entity shall not recognise any assets held as an agent on behalf of third parties.

Measurement of assets, liabilities, revenue and expenses

2.46 Measurement is the process of determining the amount at which financial statement elements are recognised in the financial statements at each balance date.

2.47 There are two common measurement bases:

(a) Historical cost, where:

(i) assets are recognised at the amount of cash or cash equivalents paid (or payable) or the fair value of the consideration given (or to be given), at the time of acquisition; and

(ii) liabilities are recognised as the amount of cash or cash equivalents, or the fair value of non-cash assets received in exchange for the liability when it is incurred, or the amounts of cash or cash equivalents expected to be paid to settle the liability in the normal course of business; or

(b) Fair value, which is:

(i) the amount for which an asset would be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

Measurement at initial recognition

2.48 At initial recognition, an entity shall measure assets and liabilities at historical cost, unless the section relating to a specific asset or liability class requires initial measurement on another basis such as fair value.

Subsequent measurement

2.49 With the exception of equity investments, financial assets and financial liabilities (as defined by Section 15 *Financial instruments*) are subsequently carried at amortised cost less impairment. Listed equity investments may be measured either at cost less impairment, or at fair value with changes in fair value recognised in profit or loss. Unlisted equity investments are carried at cost less impairment.

2.50 Non-financial assets are initially measured at historical cost and are subsequently measured on a basis appropriate to the asset class, as determined by giving consideration to the specific section of *SPFR for FPEs* for that class of asset. For example an entity measures:

(a) classes of property, plant and equipment at depreciated historical cost or revalued amounts;

(b) investment property at depreciated historical cost or revalued amounts;

(c) inventories at the lower of cost and selling price less costs to complete and sell;

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(d) non-financial assets classified as available for sale at the lower of their carrying value and fair value less costs to sell; and

(e) agricultural assets (biological assets and agricultural produce at the point of harvest) at depreciated historical cost or fair value less estimated selling costs.

2.51 Unless otherwise stated elsewhere within *SPFR for FPEs*, all changes in subsequent measurement of non-financial assets are recognised in profit or loss.

2.52 Non-financial liabilities are subsequently measured at the best estimate of the amount that would be required to settle the obligation at the balance date.

2.53 Reducing the carrying amount of an asset through the recognition of impairment losses is intended to ensure an asset is not measured at an amount greater than the entity expects to recover from the sale or use of that asset.

2.54 With the exception of assets that have been measured at fair value, all assets should be assessed for indicators of impairment at least annually.

2.55 The underlying principle of the framework is to balance cost and benefit for users. Such a principle does not readily support the use of actuaries or registered valuers where simpler proxies might be obtained.

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Section 3 Financial statement presentation

Purpose and scope of section

3.1 This section sets out the general principles for presentation of financial statements in accordance with *SPFR for FPEs*.

3.2 "Financial statements" are the statements prepared by an entity to communicate information about its financial performance and financial position. Notes and schedules that are needed to clarify or further explain items disclosed form an integral part of the financial statements.

3.3 The presentation requirements of this section and accompanying illustrative financial statements distinguish between:

(a) core components, which are required to assert compliance with *SPFR for FPEs*; and

(b) non-core components, which are not required to assert compliance with *SPFR for FPEs*.

Whole set of financial statements

3.4 A whole set of financial statements of an entity shall include the following:

Core components (required)

(a) Balance sheet as at the balance date – Section 4 *Balance sheet;*

(b) Statement of profit or loss for the reporting period – Section 5 *Statement of profit or loss*; and

(c) Notes to the financial statements – Section 7 *Notes to the financial statements*

(d) Statement of changes in equity for the reporting period. This may be included either as a primary financial statement or in the notes to the financial statements – Section 6 *Statement of changes in equity*.

Non-core components (optional)

(a) Statement of cash flows for the reporting period. No guidance on the preparation of a Statement of cash flows has been provided in *SPFR for FPEs*. Entities wishing to prepare a Statement of cash flows should step up to NZ IAS 7 *Statement of Cash Flows*.

3.5 An entity may use titles for the financial statements other than those used in *SPFR for FPEs* (eg statement of financial position, statement of financial performance) as long as they are used consistently throughout the financial statements and are not misleading.

Disclosure of compliance

3.6 An entity that prepares its financial statements in accordance with *SPFR for FPEs* should disclose the basis for preparation and its compliance with *SPFR for FPEs* in the notes to the financial statements.

3.7 Where due to its nature, complexity or materiality a transaction, other event or condition is outside the scope of *SPFR for FPEs,* and the entity has stepped up to NZ IFRS, the entity shall provide the following note disclosure:

(a) that the entity has complied with *SPFR for FPEs*, except that it has stepped up to NZ IFRS for a particular transaction, other event or condition;

(b) the reason for stepping up; and

(c) identification of the applicable NZ IFRS that has been applied instead and whether application of that NZ IFRS is in full or partial.

3.8 Where an entity has departed from *SPFR for FPEs* other than to step up to NZ IFRS, preparers must refrain from using misleading terms such as 'complies with CA ANZ SPFR framework, except for …', or 'complies with *SPFR for FPEs*, except for …'.

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Naming of the financial statements

3.9 An entity shall clearly name each of the primary financial statements and the notes to the financial statement and distinguish them from other information. In addition the financial statements shall display the following information prominently:

(a) the name of the reporting entity and any change in name since the last reporting period;

(b) whether the financial statements cover a single entity or are an aggregation or consolidation of multiple entities;

(c) the date at the end of the reporting period (Balance sheet date) and the period covered by the financial statements;

(d) the presentation currency; and

(e) the level of rounding, if any, in presenting amounts in the financial statements.

3.10 Where applicable, the notes to the financial statements shall disclose the legal basis of the reporting entity and a short description of the nature of the entity's operations.

Overarching presentation requirements

Fair presentation

3.11 Financial statements shall fairly present the financial position and financial performance of an entity in accordance with the underlying concepts and principles set out in Section 2 *Underlying Concepts and Principles*.

3.12 Fair presentation in accordance with *SPFR for FPEs* requires the faithful representation of the results of transactions, other events and conditions in accordance with the underlying concepts and principles set out in Section 2 *Underlying Concepts and Principles*.

3.13 Fair presentation is achieved by:

(a) applying *SPFR for FPEs*; and

(b) providing additional disclosures when compliance with the specific requirements of *SPFR for FPEs* is insufficient to enable users to understand the effect on material transactions, other events or conditions on the entity's financial performance and financial position.

Frequency of reporting

3.14 An entity shall present a whole set of financial statements at least annually and in accordance with the relevant legislation.

3.15 When the end of the reporting entity's reporting period changes and the annual financial statements are presented for a period longer or shorter than one year, the entity shall disclose this fact.

Consistency of presentation

3.16 An entity shall retain the presentation and classification of items in the financial statements from one period to the next, unless a change is deemed appropriate due to a change in operations, events or conditions.

3.17 When the presentation or classification of items in the financial statements changes materially from one period to the next, the nature and impact of the change should be disclosed in the financial statements.

Comparative information

3.18 An entity shall include comparative information in respect of the previous comparable period for all amounts presented in the current period's financial statements. An entity shall include comparative information for narrative and descriptive information when it is relevant to an understanding of the current period's financial statements.

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Right of set-off

3.19 An entity shall not offset assets and liabilities, or revenue and expenses, unless required or permitted by legal right of set-off.

3.20 Disclosing the carrying value of assets net of valuation allowances such as depreciation, allowances for uncollectable receivables or inventory obsolescence, is not offsetting.

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Section 4 Balance sheet

Purpose and scope of section

4.1 This section specifies both the information that is to be presented in the Balance sheet and how it is required to be presented. The Balance sheet displays an entity's assets, liabilities and equity at a specific date, normally the end of the reporting period.

Information to be presented

4.2 Where applicable and as a minimum the Balance sheet should include line items that present the following amounts at balance date:

Assets

(a) Cash and short-term deposits;
(b) Trade and other receivables;
(c) Income tax receivable;
(d) Inventories;
(e) Property, plant and equipment
(f) Investment property;
(g) Investment in shares/ownership interests;
(h) Term deposits;
(i) Intangible assets;
(j) Biological assets;
(k) Other current assets; and
(l) Other non-current assets.

Liabilities

(a) Trade and other payables;
(b) Current loans;
(c) Non-current loans;
(d) Income tax payable; and
(e) Provisions.

Equity[3]

(a) Share capital/Available subscribed capital;
(b) Retained earnings/Accumulated losses;
(c) Minority interests; and
(d) Other equity reserves.

4.3 The Balance sheet should disclose the following classification totals and subtotals:

(a) Current assets;
(b) Non-current assets;
(c) Total assets;
(d) Current liabilities;
(e) Non-current liabilities;
(f) Total liabilities;
(g) Net assets; and
(h) Total equity.

[3] Components of equity may be disclosed on either the face of the Balance sheet, in the Statement of changes in equity (if presented) or in the reconciliation of equity movements in the notes to the financial statements.

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4.4 An entity shall present additional line items, headings and subtotals in the Balance sheet when such presentation is relevant to an understanding of the entity's financial position.

Current/non-current distinction

4.5 An entity shall present current and non-current assets and current and non-current liabilities as separate classifications in the Balance sheet.

Current assets

4.6 An entity shall classify assets as current when:

(a) it expects to realise, sell or consume the asset within twelve months of the balance date;

(b) it holds the asset primarily for trading purposes; or

(c) the asset is cash and not a short-term deposit restricted from use in the entity's normal operating activities.

4.7 An entity shall classify all other assets as non-current.

Current liabilities

4.8 An entity shall classify a liability as current when:

(a) it expects to settle the liability within twelve months of the balance date;

(b) it holds the liability primarily for the purpose of trading;

(c) it does not have an unconditional right to defer settlement of the liability for at least twelve months after the balance date; or

(d) there is breach of a financial covenant and that breach is not rectified before balance date.

4.9 An entity shall classify all other liabilities as non-current.

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Section 5 Statement of profit or loss

Purpose and scope of section

5.1 This section sets out the information that is to be presented in the Statement of profit or loss and how to present it. The Statement of profit or loss presents an entity's revenue and expenses for a reporting period.

Single statement approach

5.2 *SPFR for FPEs* provides for movements in the year to be taken directly to equity and not reported within profit or loss in limited circumstances when:

(a) the movements relate to transactions with owners in their capacity as owners, such as shares issued and dividend distributions;

(b) the effects of corrections or errors and changes in accounting policies that relate to retrospective adjustments of amounts reported in previous years (see Section 8 *Accounting policies, Estimates and Errors*); or

(c) a specific section of *SPFR for FPEs* allows the fair value revaluation or restatement of an asset or liability to be reflected through a separate equity reserve.

Information to be presented

5.3 Where applicable and as a minimum the Statement of profit or loss or the notes to the financial statements should include line items that present the following amounts for the period:

Revenue

(a) Revenue from sale of goods;

(b) Revenue from provision of services;

(c) Rental revenue;

(d) Interest and investment revenue;

(e) Other revenue;

(f) Exceptional items (refer to paragraph 5.10); and

(g) Gain on sale of assets.

Expenses

Expenses classified based on either the nature or function of the expense, including the following specific disclosures:

(a) Depreciation of property, plant and equipment;

(b) Amortisation of intangible assets;

(c) Impairment losses;

(d) Foreign currency gains or losses;

(e) Loss on sale of assets;

(f) Finance costs;

(g) Exceptional items (refer to paragraph 5.10);

(h) Income tax expense; and

(i) Write-off of goodwill.

5.4 The Statement of profit or loss should disclose the following classification totals and sub-totals:

(a) Net operating profit or loss before tax;

(b) Gross profit or loss; and

(c) Net profit or loss.

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5.5 An entity shall present additional line items, headings and subtotals in the Statement of profit or loss when such presentation is relevant to the understanding of the entity's financial performance.

Classification of expenses

5.6 An entity shall present an analysis of expenses using a classification based on either the nature of expenses or the function of expenses within the entity, whichever provides information that is reliable and more relevant.

5.7 Under the nature of expense classification, expenses are aggregated in the Statement of profit or loss according to their nature; eg purchase of materials, transport costs, employee benefits and advertising costs.

5.8 Under the function of expense classification, expenses are aggregated according to their function; eg cost of sales, distribution costs and administrative activities. At a minimum an entity shall disclose its expenses using this method.

Gross margin ratio

5.9 An entity may elect to disclose its gross margin ratio, and this can be either on the face of the Statement of profit or loss or in the notes to the financial statements.

Exceptional items

5.10 Exceptional items are large items of revenue or expenses that do not arise as a result of normal business operations and are not expected to recur. In particular, the following revenue and/or expense categories are exceptional items:

(a) Results from the sale or disposal of the entity or a significant part of it;

(b) Results from natural disasters, ie Acts of God;

(c) Major restructuring costs paid or provided for;

(d) Major impairments or write-offs;

(e) Reversal of major impairments, write-offs or restructuring provisions; and

(f) Large one-off non-operational receipts.

An entity should disclose exceptional items only where they total more than 5% of revenue.

5.11 Exceptional items should be disclosed net on the face of the Statement of profit or loss (above the line before net operating profit or loss before tax), and by transaction type for both revenue and expenses in the notes to the financial statements.[4]

[4] The IR10 requires exceptional items to be presented as a net figure.

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Section 6 Statement of changes in equity

Purpose and scope of section

6.1 The Statement of changes in equity provides a reconciliation of movements in equity for the period.

6.2 The inclusion of the Statement of changes in equity as a primary financial statement is optional. Alternatively a reconciliation of equity movements may be provided in the notes to the financial statements.

Information to be presented

6.3 For each component of equity (ie share capital, retained earnings, and reserves related to unrealised fair value movements taken directly to equity), the following is to be presented:

(a) a reconciliation between the carrying amount at the beginning and end of the period, separately disclosing changes resulting from the following:

(i) net profit or loss;

(ii) distributions to owners;

(iii) contributions from owners;

(iv) fair value movements taken directly to equity, as permitted by specific sections of *SPFR for FPEs*;

(v) accumulated fair value movements previously recognised directly in equity, recycled to profit or loss on disposal or derecognition of the asset carried at fair value, as permitted by specific sections of *SPFR for FPEs*;

(b) Opening positions for correction of prior period errors; and

(c) Opening positions for changes in accounting policies.

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Section 7 Notes to the financial statements

Purpose and scope of section

7.1 This section sets out the general principles underlying information that is to be presented in the notes to the financial statements, and how that information should be presented. Notes to the financial statements provide additional information to that presented on the primary financial statements.

7.2 The disclosure requirements relating to specific financial statement elements are contained within the applicable section of *SPFR for FPEs*.

Structure of the notes

7.3 The notes shall:

(a) present information about the basis of preparation of the financial statements and the specific accounting policies used;

(b) disclose information required by *SPFR for FPEs* that is not presented elsewhere in the financial statements; and

(c) disclose information, where necessary, that further explains the components presented in the primary financial statements in order to provide an adequate understanding of them.

7.4 An entity shall present the notes in a systematic manner and cross reference each item in the primary financial statements to any related information in the notes.

7.5 An entity shall present the notes :

(a) the nature of the entity and what legislation, if any, it is governed by;

(b) a statement that the financial statements comply with *SPFR for FPEs* (see paragraphs 3.6 – 3.8);

(c) a summary of significant accounting policies applied (statement of accounting policies);

(d) supporting information for items presented in the primary financial statements; and

(e) any other disclosures.

Disclosures

7.6 An entity shall disclose the following in the summary of significant accounting policies:

(a) the measurement basis (or bases) used in preparing the financial statements; and

(b) where relevant, other accounting policies used that are useful to an understanding of the financial statements when significant judgement and estimates have been made.

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Section 8 Accounting policies, estimates and errors

Purpose and scope of section

8.1 This section provides guidance for:

(a) selecting and applying accounting policies; and

(b) accounting for and disclosing the impact of changes in accounting policies, estimates and errors.

Accounting policy selection and use

8.2 Accounting policies are the specific principles, bases, conventions, rules and practices applied by an entity in preparing and presenting financial statements.

8.3 If *SPFR for FPEs* specifically addresses a transaction, other event or condition, an entity shall apply an accounting policy in accordance with *SPFR for FPEs*.

8.4 If *SPFR for FPEs* does not specifically address a transaction, other event or condition, the following sources should be considered:

(a) sections of *SPFR for FPEs* dealing with similar and related issues;

(b) the definitions, recognition criteria and measurement concepts for assets, liabilities, revenue and expenses and the general principles in Section 2 *Underlying Concepts and Principles*; and

(c) NZ IFRS.

8.5 The use of judgement is required to develop accounting policies based on appropriate guidance and ensure the application of accounting policies results in information being reported that is relevant and reliable as defined in Section 2 *Underlying Concepts and Principles*.

Consistency of application of accounting policies

8.6 An entity shall select and apply its accounting policies consistently for similar transactions, other events and conditions.

Changes in accounting policies

8.7 An entity shall change accounting policies only if the change:

(a) is required by changes to *SPFR for FPEs*; or

(b) results in the financial statements providing more reliable and more relevant information about the effects of transactions, other events or conditions on the entity's financial position and performance.

8.8 The following are not changes in accounting policies:

(a) the application of an accounting policy for transactions, other events or conditions that differ in substance from those previously occurring; and

(b) the application of a new accounting policy for transactions, other events or conditions that did not occur previously or were not material.

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Accounting for changes in accounting policies

8.9 Changes in accounting policy shall be applied prospectively.

8.10 Prospective recognition of the effect of a change in accounting policy means that the change is applied to transactions, other events and conditions from the date of change in accounting policy.

8.11 To the extent that a change in accounting policy gives rise to changes in assets and liabilities, or relates to an item of equity, the entity shall recognise it by adjusting the carrying amount of the related asset, liability or equity item in the period of change.

8.12 *SPFR for FPEs* prohibits the amendments of previously reported balances (ie comparatives) as a result of a change in accounting policy. The impact of a change in accounting policy (if any) on previously reported balances is accounted for as a current year movement in the reconciliation of movements in equity, as per paragraph 6.3(c).

Changes in accounting estimates

8.13 As a result of the uncertainties inherent in business activities, many items in the financial statements cannot be measured with precision but can only be estimated. Estimation involves judgements based on the latest available, reliable information. For example, estimates may be required of:

(a) bad debts;

(b) inventory obsolescence; and

(c) the useful lives of, or expected pattern of consumption of future economic benefits embodied in depreciable assets.

8.14 An estimate may need revision due to changes in the circumstances on which the estimate was based or as a result of new information or more experience. By its nature, the revision of an estimate does not relate to prior periods and is not the correction of an error.

Accounting for changes in accounting estimates

8.15 An entity shall recognise the effect of a change in accounting estimates prospectively by recognising the impact in profit or loss in:

(a) the period of the change, if the change affects that period only; or

(b) the period of the change and future periods, if the change affects both.

8.16 Prospective recognition in this context means that the effect of the change in the accounting estimate is recognised in the current and future periods affected by the change.

Correction of prior period errors

8.17 Prior period errors are omissions from, and misstatement in, the entity's financial statements for one or more periods arising from a failure to use, or misuse of, reliable information that:

(a) was available when financial statements for those periods were authorised for issue; and

(b) could reasonably be expected to have been obtained and taken into account in the preparation and presentation of those financial statements.

8.18 Such errors include the effects of mathematical mistakes, mistakes in applying accounting policies, oversights and misinterpretations of facts, and fraud.

Accounting for prior period errors

8.19 An entity shall correct a material prior period error prospectively in the first set of financial statements prepared in accordance with *SPFR for FPEs* after the error has been discovered.

8.20 The prospective correction of a prior period error requires:

(a) restatement of the opening assets, liability or equity balances at the commencement of the current period; and

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(b) recognition of the corresponding movements as an adjustment to opening equity in the reconciliation of movements in equity.

8.21 *SPFR for FPEs* prohibits the amendments of previously reported balances (ie comparatives) as a result of accounting for prior period errors. The impact of accounting for prior period errors on previously reported balances is accounted for as a current year movement in the reconciliation of movements in equity, as per paragraph 6.3(b).

Disclosures

Disclosure of change in accounting policy

8.22 When an entity applies a change in accounting policy, it shall disclose the following:

(a) the nature of the change in accounting policy;

(b) the reasons why applying the new accounting policy provides the most relevant and reliable information; and

(c) the impact of the change on assets, liabilities, revenue and expenses for the current period.

Disclosure of change in accounting estimates

8.23 An entity shall disclose the following about a change in accounting estimates:

(a) the nature of a material change in an accounting estimate; and

(b) the impact of the change on assets, liabilities, revenue and expenses for the current period.

Disclosure of prior period errors

8.24 An entity shall disclose the following about prior period errors:

(a) the nature of the prior period error; and

(b) the amount of the correction in relation to each asset, liability or equity balance amended at the commencement of the accounting period as a result of the error.

Disclosures in subsequent periods

8.25 The disclosure of changes in accounting policies, estimates or prior period errors is not required to be repeated in subsequent financial statements.

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Section 9 Revenues

Purpose and scope of section

9.1 This section establishes the principles for the timing, recognition and disclosure of revenue in the financial statements of the entity.

9.2 This section applies to the accounting for revenue arising from the following events:

(a) the sale of goods;

(b) the rendering of services;

(c) the formation of a construction contract in which the entity is the contractor;

(d) the use by others of entity assets yielding interest, royalties or dividends; and

(e) the receipt of government grants.

Measurement

9.3 An entity shall measure revenue at the fair value of the consideration received or receivable.

9.4 The amount of revenue arising on a transaction is usually determined by an agreement between the entity and the buyer or user of the asset. It is measured at the fair value of the consideration received or receivable, net of any trade discounts, prompt settlement discounts and volume rebates allowed by the entity.

9.5 An entity shall include in revenue only the gross inflows of economic benefits received and receivable by the entity on its own account. An entity shall exclude from revenue all amounts collected on behalf of third parties such as sales taxes, goods and services taxes and value-added taxes. In an agency relationship, an entity shall include in revenue only the amount of its commission. The amounts collected on behalf of the principal are not revenue of the entity.

Identification of the revenue transaction

9.6 An entity would usually apply the revenue recognition criteria in this section separately to each transaction. However, an entity may apply the recognition criteria to the separately identifiable components of a single transaction when necessary to reflect the substance of the transaction.

9.7 A single transaction may involve the delivery or performance of multiple products, services or rights to use assets, and performance may occur at different points in time or over different periods of time. For example, when the selling price of a product includes an identifiable amount for subsequent servicing, that amount is deferred and recognised as revenue over the period during which the service is performed. Conversely, the recognition criteria are applied to two or more transactions together when they are linked in such a way that the commercial effect cannot be understood without reference to the series of transactions as a whole.

Recognition of revenue from sale of goods

9.8 The sale of goods includes goods produced by the entity for the purpose of sale and goods purchased for resale, such as merchandise purchased by a retailer or land and other property held for resale.

9.9 An entity shall recognise revenue from the sale of goods upon the satisfaction of all the following conditions:

(a) the entity has transferred to the buyer the significant risks and rewards of ownership of the goods;

(b) the entity retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold;

(c) the amount of revenue can be measured reliably;

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(d) it is probable that the economic benefits associated with the transaction will flow to the entity; and

(e) the costs incurred or to be incurred in respect of the transaction can be measured reliably.

9.10 In most cases, the transfer of the risks and rewards of ownership coincides with the transfer of the legal title or the passing of possession to the buyer, however this may not always be the case. The sale contract terms and conditions require careful consideration.

9.11 An entity does not recognise revenue if it retains significant risks of ownership. Examples of situations in which the entity may retain the significant risks and rewards of ownership are:

(a) when the entity retains an obligation for unsatisfactory performance not covered by normal warranties;

(b) when the receipt of the revenue from a particular sale is contingent on the buyer selling the goods;

(c) when the goods are shipped subject to installation and the installation is a significant part of the contract that has not yet been completed; and

(d) when the buyer has the right to rescind the purchase for a reason specified in the sales contract, or at the buyer's sole discretion without any reason, and the entity is uncertain about the probability of return.

Recognition of revenue from rendering of services

9.12 The rendering of services typically involves the performance by the entity of a contractually agreed task over an agreed period of time. The services may be rendered within a single period or over more than one period.

9.13 An entity shall recognise revenue associated with the delivery of services by reference to the stage of completion (also referred to as the percentage of completion method) at the end of the reporting period, when all the following conditions are satisfied:

(a) the amount of revenue can be measured reliably;

(b) it is probable that the economic benefits associated with the transaction will flow to the entity;

(c) the stage of completion of the transaction at the end of the reporting period can be measured reliably; and

(d) the costs incurred for the transaction and the costs to complete the transaction can be measured reliably.

9.14 Paragraphs 9.23 – 9.25 provide guidance for applying the percentage of completion method.

9.15 When services are performed by an indeterminate number of acts over a specified period of time, an entity recognises revenue on a straight-line basis over the specified period unless there is evidence that some other method better represents the stage of completion.

9.16 When a specific act is much more significant than any other act, the entity postpones recognition of revenue until the significant act is executed.

9.17 When the outcome of the transaction involving the rendering of services cannot be estimated reliably, an entity shall recognise revenue only to the extent of the expenses recognised that are recoverable.

9.18 If the collectability of an amount already recognised as contract revenue is no longer probable, the entity shall recognise the uncollectible amount as an expense rather than as an adjustment of the amount of revenue.

Recognition of revenue from construction contracts

9.19 Revenue from construction contracts is recognised by reference to the stage of completion and principles consistent with the recognition of revenue from rendering of services.

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9.20 When a contract covers a number of assets, the construction of each asset shall be treated as a separate construction contract when, for each asset:

(a) a separate proposal has been submitted;

(b) a separate negotiation has been entered into, and the contractor and customer are able to accept or reject that part of the contract relating to each asset; and

(c) the costs and revenues can be identified.

9.21 A group of contracts, whether with a single customer or with several customers, shall be treated as a single construction contract when:

(a) the group of contracts is negotiated as a single package;

(b) the contracts are so closely interrelated that they are, in effect, part of a single project with an overall profit margin; and

(c) the contracts are performed concurrently or in a continuous sequence.

9.22 When the outcome of a construction contract cannot be estimated reliably:

(a) an entity shall recognise revenue only to the extent of contract costs incurred that it is probable will be recoverable; and

(b) the entity shall recognise contract costs as an expense in the period in which they are incurred.

Percentage of completion method

9.23 This is the method used to recognise revenue from rendering of services and from construction contracts. An entity shall review and, when necessary, revise the estimates of revenue and costs as the service transaction or construction contract progresses.

9.24 An entity shall determine the stage of completion of a transaction or contract using the method that measures most reliably the work performed. Possible methods include:

(a) the proportion of costs incurred for work performed to date as a percentage of estimated total costs for agreed services;

(b) surveys of work performed; and

(c) completion of a physical proportion of the service transaction or contract work.

9.25 Progress payments and advances received from customers often do not reflect the work performed.

Recognition of revenue from interest, royalties and dividends

9.26 An entity shall recognise revenue arising from the use by others of entity assets yielding interest, royalties and dividends when:

(a) it is probable that the economic benefits associated with the transaction will flow to the entity; and

(b) the amount of the revenue can be measured reliably.

9.27 An entity shall recognise revenue on the following bases:

(a) gross interest shall be recognised on an accrual basis;

(b) royalties shall be recognised on an accrual basis in accordance with the substance of the relevant agreement; and

(c) dividends shall be recognised on receipt.

9.28 Recognition of dividends net of imputation credits is encouraged. However, if dividends are recognised gross of imputation credits, then the imputation credits must be offset against the income tax expense recognised in the Statement of Profit or Loss. Unutilised imputation credits convert to tax losses which may be able to be carried forward by the entity. When accounting for income tax using the taxes payable method, such losses are not recognisable as an asset in the Balance sheet of the entity.

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Recognition of revenue from government grants

9.29 A government grant is assistance by government in the form of a transfer of resources to an entity in return for past or future compliance with specified conditions relating to the operating activities of the entity.

9.30 Government grants exclude those forms of government assistance that cannot reasonably have a value placed upon them and transactions with government that cannot be distinguished from the normal trading transactions of the entity.

9.31 An entity shall recognise government grants as follows:

(a) a grant that does not impose specified future performance obligations on the recipient is recognised as revenue when the grant proceeds are receivable;

(b) a grant that imposes specified future performance obligations on the recipient is recognised as revenue only when the performance obligations are met; and

(c) a grant received before the revenue recognition criteria are satisfied is recognised as a liability.

Disclosures

General disclosures

9.32 An entity shall disclose in the notes to the financial statements:

(a) the accounting policies adopted for the recognition of revenue, including the methods adopted to determine the stage of completion of transactions involving the rendering of services or construction contracts;

(b) the amount of each category of revenue recognised during the period, showing separately, at a minimum, revenue arising from:

(i) the sale of goods;

(ii) the rendering of services;

(iii) interest (gross of resident withholding taxes);

(iv) royalties;

(v) dividends (stating whether gross or net of imputation credits);

(vi) government grants;

(vii) rental, lease and licence revenue; and

(viii) any other significant types of revenue.

Government grant disclosures

9.33 An entity shall disclose the following about government grants:

(a) the nature of the amount of government grants in the financial statements; and

(b) unfulfilled performance obligations and other contingencies in relation to government grants that have not been recognised in revenue.

Gross dividends

9.34 Recognition of dividends net of imputation credits upon receipt is encouraged in paragraph 9.28. However, the IR minimum financial reporting requirements, require the disclosure of dividends gross of imputation credits. This disclosure can be achieved via the income tax note to the financial statements by subtracting dividends received net of imputation credits from net profit before tax, and adding back dividends received gross of imputation credits.

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Appendix to Section 9

Examples of revenue recognition and principles

The revenue recognition examples provided below should be read in conjunction with Section 9 *Revenues*.

Source	Revenue recognition	Other comments
Revenue from activities providing services and products		
Sale of goods	When the goods are sold and delivered to the customer.	If the purchaser pays before the goods are completed or delivered (ie a deposit or prepayment), a liability is recognised.
Provision of services	By reference to the stage of completion of the transaction at the balance date, based on the actual services provided as a percentage of the total services provided.	Determination of the most appropriate method for calculating the stage of completion of a revenue contract is required based on the assessment of services to be provided and the pattern of costs to be incurred in the delivery of those services.
Operating lease or rental revenue	On a straight basis over the term of the agreement, unless another systematic basis is representative of the time pattern of the user's benefit.	If the lessee pays in advance, the entity (as lessor) records a liability being the amount of the prepayment. However, if the lessee pays after the leased asset is used, the entity (as lessor) records as asset, being the amount owed to the entity.
Revenue from investments		
Interest	Amount earned during the period on investments and bank accounts.	Gross accrued interest earned but not received at the balance date shall be accrued as a receivable balance.
Dividends and similar revenue	On receipt.	Dividends and similar revenue recognised upon receipt.
Registration/membership fees		
Subscriptions to publications and similar items	Revenue is recognised over the period in which subscription benefits are received.	When the items involved are of similar value in each time period, the seller recognises revenue on a straight-line basis over the period in which the items are dispatched. When the items vary in value from period to period, the seller recognises revenue on the basis of the sale value of the item dispatched in relation to the total estimated sales value of all items covered by the subscriptions.
Entrance fees and on-off fees	When the event takes place.	Any deposits received prior to the event are recognised as a liability.
Fees in relation to a series of events	When each event in the series takes place.	If one fee is charged for all events, revenue recognition is deferred until delivery of each event in the series.

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Section 10 Inventories

Purpose and scope of section

10.1 This section establishes the principles for the recognition of inventories and its subsequent recognition as an expense, including any write-down to realisable value. It also provides guidance on the cost formulas that are used to assign costs to inventories.

10.2 Inventories are assets which are:

(a) held for sale in the ordinary course of business;

(b) in the process of production for such sale; or

(c) in the form of materials or supplies to be consumed in the production process or in the rendering of services.

10.3 This section does not apply to biological assets related to agricultural activity and agricultural produce at the point of harvest (see Section 12 *Agriculture*).

10.4 This section does not apply to the measurement of inventories held by: producers of agricultural and forest products, agricultural products after harvest, and minerals and mineral products, to the extent that they are measured at fair value less costs to sell through profit or loss.

Measurement of inventories

10.5 An entity shall measure inventories at the lower of cost and net realisable value.

Cost of inventories

10.6 An entity shall include in the cost of inventories all costs associated with:

(a) cost of purchase;

(b) cost of conversion; and

(c) other costs incurred in bringing the inventories to their present location and condition.

10.7 Cost of purchase includes:

(a) import duties and other purchase taxes (other than those subsequently recoverable by an entity from the taxing authorities);

(b) transport and handling costs;

(c) any other directly attributable costs of acquisition; and

(d) deductions for trade discounts, rebates and other similar items.

10.8 The cost of conversion of inventories includes:

(a) costs directly related to the unit of production, such as direct labour; and

(b) a systematic allocation of fixed and variable production overheads that are incurred in converting materials into finished goods.

Production overhead allocation

10.9 An entity shall allocate fixed production overheads to the costs of conversion on the basis of the normal capacity of the production facilities.

10.10 Unallocated production overheads are recognised as an expense in the period in which they are incurred.

10.11 Where abnormal amounts of waste, whether of material or labour or other expenses, do not relate to bringing inventories to their present condition and location, the cost of the abnormal waste is to be excluded from the cost of conversion and recognised as an expense in profit or loss in the period in which it is incurred.

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Other costs to be included in inventories

10.12 An entity shall include other costs in the cost of inventories only to the extent that they are incurred in bringing the inventories to their present location and condition.

10.13 Examples of costs excluded from the cost of inventories and recognised as expenses in the period in which they are incurred are:

(a) storage costs, unless those costs are necessary during the production process before a further production stage;

(b) administrative overheads that do not contribute to bringing inventories to their present location and condition; and

(c) selling costs.

Acceptable methods for cost measurement

10.14 Methods for the measurement of the cost of inventories, such as the standard cost method or the retail method, may be used for convenience if the results approximate cost. Standard costs take into account normal levels of materials and supplies, labour, efficiency, and capacity utilisation. They are regularly reviewed and, if necessary, revised in the light of current conditions.

10.15 The retail method is often used in the retail industry for measuring inventories of large numbers of rapidly changing items with similar margins for which it is impracticable to use other costing methods. The cost of the inventory is determined by reducing the sales value of the inventory by the appropriate percentage gross margin.

Cost formulas

10.16 The cost of inventories of items that are not ordinarily interchangeable, and goods or services produced and segregated for specific projects, should be assigned by using specific identification of their individual costs.

10.17 Specific identification is a formula that attributes specific costs to identified items of inventory. This is an appropriate treatment for items of inventory that have been made or acquired for a specific project and are separately identifiable.

10.18 The cost of inventories, other than those dealt with in paragraphs 10.14 – 10.15, should be assigned by using the first-in, first-out (FIFO) or weighted average cost formula. An entity shall use the same cost formula for all inventories having a similar nature and use to the entity. For inventories with a different nature or use, different cost formulas may be justified.

10.19 The FIFO formula assumes that items of inventory that were taken into inventories first are sold or used first and therefore assumes that the items of inventory remaining at balance date are those most recently acquired or produced.

10.20 The weighted average cost formula determines the cost of each item of inventory from the weighted average cost of similar items at the beginning of a period and the cost of similar items acquired or produced during the period. The average may be calculated on a periodic basis, or as each individual batch or shipment is received depending on the circumstances of the entity.

10.21 Use of the last-in, first-out method (LIFO) is not permitted.

Net realisable value

10.22 Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

10.23 The cost of inventories may not be recoverable if those inventories are damaged, or have become wholly or partially obsolete, or if the selling prices have declined. The cost of inventories may also not be recoverable if the estimated cost of completion or the estimated costs to be incurred to make the sale have increased. The practice of writing inventories down

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below cost to net realisable value is consistent with the view that assets are not carried in excess of amounts expected to be realised from their sale or use.

10.24 Inventories are usually written down to net realisable value item by item. However, in some circumstances, it may be appropriate to group similar or related items, such as provisions for obsolete stock based on the stock allocated into age brackets.

10.25 Estimates of net realisable value are based on the most reliable evidence available, at the time the estimates are made, of the amounts that inventories are expected to realise. These estimates take into consideration fluctuations of price or cost directly relating to events occurring after the end of the period, to the extent that such events confirm conditions existing at the end of the period.

10.26 When inventories are written down to their net realisable value, an entity shall immediately recognise the loss attributable to the write down of the item or group of inventories in profit or loss.

Recognition as an expense

10.27 When inventories are sold, the entity shall recognise the carrying amount of inventories as an expense in the period in which the related revenue is recognised.

Disclosures

10.28 An entity shall, where applicable, disclose the following in the notes to the financial statements:

(a) the accounting policies adopted in measuring inventories, including a short description of the cost formula used;

(b) the carrying amount of inventories in classifications appropriate to the entity; and

(c) the carrying amount of inventories pledged as security for liabilities.

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Section 11 Property, plant and equipment and investment property

Purpose and scope of section

11.1 This section applies to initial recognition, subsequent measurement and disclosure of property, plant and equipment and of investments in land and buildings that meet the definition of investment property.

11.2 Property, plant and equipment are tangible assets that:

(a) are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes; and

(b) are expected to be used during more than one period.

11.3 Property, plant and equipment does not include:

(a) biological assets related to agricultural activity; or

(b) mineral rights and mineral reserves, such as oil, natural gas and similar non-regenerative resources.

11.4 Investment property is land or a building (or part thereof), or both, held by the owner or by the lessee under a finance lease, primarily to earn rentals or for capital appreciation or both, rather than for:

(a) use in the production or supply of goods or services or for administration purpose; or

(b) sale in the ordinary course of business.

11.5 Development property intended to be held primarily for capital appreciation or rental purposes is classified as investment property.

11.6 Mixed-use property shall be separated between investment property and property, plant and equipment. However, if the investment property component cannot be measured reliably without undue cost or effort, the entire property shall be classified as property, plant and equipment.

11.7 An entity may elect to classify and account for investments in land or a building (or part thereof) which meet both the definition of investment property and property, plant and equipment as described in paragraphs 11.2 – 11.5 as either investment property or property, plant and equipment.

Recognition

11.8 The entity shall recognise the cost of an item of property, plant and equipment or investment property as an asset if, and only if:

(a) it is probable that future economic benefits associated with the item will flow to the entity; and

(b) the cost of the item can be measured reliably.

11.9 Immaterial amounts of spare parts and servicing equipment should be expensed to profit or loss when acquired. However, material spare parts and stand-by equipment are property, plant and equipment when an entity expects to use them during more than one period.

11.10 Parts of some items of property, plant and equipment and investment property may require replacement at regular intervals (eg the roof of a building). An entity shall add to the carrying amount of an item of property, plant and equipment or investment property the cost of replacing part of such an item when that cost is incurred if the replacement part is expected to provide incremental future benefits to the entity. The carrying amount of those parts that are replaced is derecognised in accordance with paragraphs 11.42 – 11.45.

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Allocation of costs to components of property, plant and equipment or investment property

11.11 When the components of an item of property, plant and equipment or investment property have different useful lives or provide benefits to the entity in different patterns, requiring different depreciation rates and methods, the cost of the items should be allocated to its components and each component should be accounted for separately.

11.12 Land and buildings are separable assets, and an entity shall account for them separately, even when they are acquired together.

Measurement at recognition

11.13 An entity shall measure an item of property, plant and equipment or investment property at initial recognition at its cost.

Elements of cost

11.14 The cost of an item of property, plant and equipment or investment property comprises all of the following:

(a) its purchase price, including legal and brokerage fees after allowing for trade discounts and rebates;

(b) its import duties; and

(c) any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended. These can include the costs of site preparation, initial delivery and handling, installation and assembly, and testing of functionality.

11.15 The cost of internally constructed property, plant and equipment or investment property includes direct construction costs (such as materials and labour) and overhead costs directly attributable to the construction of the asset.

11.16 Any obligations in relation to dismantling and removing an item of property, plant and equipment, or investment property, and restoring the site on which it was located to its original state is not recognised until such costs have been incurred and are payable. When site-restoration works are completed (often referred to as make-good provisions) the associated expenses are recognised in profit or loss.

Measurement of cost

11.17 The cost of an item of property, plant and equipment or investment property is the cash price equivalent at the recognition date.

11.18 When the cash price is not easily identifiable, because a single price was paid for a group of assets, the cost price will require allocation to each separate asset, based on the fair value of the individual assets.

11.19 The cost of a donated or subsidised item of property, plant and equipment or investment property is its fair value at the date of acquisition, together with any costs directly incurred in bringing the item to working condition for its intended use. The corresponding amount of the donation or subsidy received is recognised as revenue in profit or loss.

Measurement after initial recognition

11.20 An entity shall choose either the cost model or the revaluation model as its accounting policy and shall apply that policy to an entire class of property, plant and equipment or investment property.

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The cost model

11.21 After recognition as an asset, an item of property, plant and equipment or an investment property shall be carried at its cost less any accumulated depreciation and any accumulated impairment losses.

Depreciation

11.22 Depreciation is the decrease in the carrying value of the item of property, plant and equipment or investment property, which represents the expensing of the asset cost to the periods in which the asset is used.

11.23 Depreciation of an asset begins when it is available for use, ie when it is in the location and condition necessary for it to be capable of operating in the manner intended.

11.24 The depreciable amount of an item of property, plant and equipment or investment property is charged over the item's useful life to profit or loss. An entity shall consider the following factors in determining the useful life of an asset:

(a) the expected usage of the asset;

(b) the expected physical wear and tear based on intended use;

(c) technical or commercial obsolescence; and

(d) the legal or similar limits on the use of the asset, such as the expiry dates of related leases.

11.25 An entity shall select either a depreciation method and rate that reflect the pattern in which it expects to consume the asset's future economic benefits, or a depreciation rate prescribed by Inland Revenue for tax purposes (including zero depreciation rates for long-lived buildings).

11.26 Possible depreciation methods include the straight-line method and the diminishing balance method.

11.27 The useful life of an item of property, plant and equipment or investment property should be assessed annually to determine whether there is any indication that it is inappropriate. If any such indication exists, the depreciation method and rate will be amended accordingly and the depreciation charge for the current and future periods amended.

11.28 A change in the depreciation method and rates is not considered a change in accounting policy.

Impairment

11.29 At each balance date, an entity applying the cost model after initial recognition to a class of property, plant and equipment or investment property is to apply Section 16 *Impairment of Assets* to that class in order to determine whether an item or group of items of property, plant and equipment or investment property is impaired and, if so, how to recognise and measure the impairment loss.

11.30 An entity shall include in profit or loss, any separate transactions from third parties for items of property, plant and equipment or investment property that were impaired, lost or given up when the compensation is virtually certain of being received, such as insurance payments.

The revaluation model

11.31 After recognition as an asset, an item of property, plant and equipment or an investment property whose fair value can be measured reliably may be carried at a revalued amount, being its fair value at the date of the revaluation less any subsequent accumulated depreciation.

11.32 If an item of property, plant and equipment or investment property is revalued, the entire class of property, plant and equipment or investment property to which that asset belongs shall be revalued.

11.33 Revaluations shall be made with sufficient regularity to ensure that the carrying amount does not differ materially from that which would be determined using fair value at the end of the reporting period. At a minimum, a revaluation shall be made every 5 years or more frequently if necessary to ensure its carrying amount is not materially different from fair value as at balance date.

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11.34 Valuations shall be based on the fair value of items within a class determined by:

(a) an independent valuer; or

(b) an employee of the reporting entity with sufficient experience to conduct a valuation, so long as the basis of valuation has been subject to review by an independent valuer; or

(c) for both land and buildings, the most recent valuation provided by the local council for rateable purposes. When this basis of valuation is used, all subsequent revaluation should also be based on rateable value valuations.

Accounting for revaluation movements

Property, plant and equipment

11.35 When an item of property, plant and equipment is revalued, the related accumulated depreciation charged as at the date of revaluation is credited to the gross carrying amount of the item. The gross carrying amount should then be increased or decreased by the amount of the revaluation increase or decrease.

11.36 When an item of property, plant and equipment is revalued, the resultant revaluation movement for the class of property, plant and equipment to which that item belongs is recognised directly in equity.

11.37 The accumulated revaluation movements shall be recorded in a separate asset revaluation reserve as a separate equity component. A record of the accumulated revaluation reserve balance for each class of assets subject to revaluation should be retained.

11.38 If the revaluation of property, plant and equipment results in a revaluation deficit for the class of property, plant and equipment to which the item belongs, the revaluation deficit is recognised in profit or loss, to the extent that no previously accumulated revaluation surpluses are available within the asset revaluation reserve for the class.

11.39 To the extent that the revaluation of a class of property, plant and equipment reverses a previous revaluation deficit recognised in profit or loss for that class, the revaluation movement is to be recognised in profit or loss.

Investment property

11.40 Any gains or losses resulting from the revaluation of land or buildings which meet the definition of an investment property as outlined in paragraphs 11.4 – 11.5 should be recognised in profit or loss.

11.41 When an investment property is revalued, an entity shall recognise the revaluation gains or losses in profit or loss in the period which the revaluation takes place.

Derecognition

11.42 An entity shall derecognise an item of property, plant and equipment or investment property:

(a) on disposal; or

(b) when no future economic benefits are expected from its use or disposal.

11.43 When an item is derecognised, an entity shall recognise the gain or loss attributable to the derecognition of the item of property, plant and equipment or investment property in profit or loss. This may be an exceptional item in accordance with paragraph 5.10(f).

11.44 Upon derecognition, the asset revaluation reserve shall be transferred to retained earnings. The transfer to retained earnings should not be made through profit or loss (that is, no "recycling" through profit or loss).

11.45 An entity shall determine the gain or loss arising from derecognition of an item of property, plant and equipment or investment property as the difference between the net disposal proceeds, if any, and the carrying amount of the item.

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Classification

11.46 Property, plant and equipment and investment property by their nature are not generally held with the intention of sale within one year and therefore should be classified as non-current assets in the Balance sheet.

Disclosures

General

11.47 An entity shall, where applicable, disclose the following in the notes to the financial statements:

(a) the accounting policy adopted for measurement after recognition of each class of property, plant and equipment, and for investment property;

(b) the carrying amount of property, plant and equipment and investment property to which the entity has restricted title or that is pledged as security for liabilities;

(c) the amount of contractual commitments for the acquisition of property, plant and equipment or investment property; and

(d) the carrying value of material property, plant and equipment or investment property available for sale.

Subsequent measurement using the cost model

11.48 An entity shall disclose the following for each class of property, plant and equipment subsequently measured using the cost model:

(a) the accounting policy adopted for measurement after initial recognition;

(b) the depreciation method used;

(c) the useful lives or the depreciation rates used; and

(d) the gross carrying amount and the accumulated depreciation (aggregated with accumulated impairment losses) at the beginning and end of the reporting period.

Subsequent measurement using the revaluation model

11.49 When a class of property, plant and equipment or investment property is carried at revalued amounts, the following shall be disclosed in respect of that class:

(a) the accumulated revaluation surplus at balance date (if any);

(b) the intervals at which valuations take place;

(c) the date of the most recent valuation and the name and qualification of the valuer; and

(d) if valuations are based on values determined for rateable purposes, this fact shall be disclosed.

11.50 In order to meet the Inland Revenue minimum financial reporting requirements, entities shall also prepare an appropriately detailed taxation-based schedule of the entity's fixed assets and depreciable property. The schedule is not required to be disclosed as part of the financial statements and may be maintained in a separate schedule for disclosure to Inland Revenue upon request.

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Section 12 Agriculture

Purpose and scope of section

12.1 This section applies to initial recognition, subsequent measurement and disclosures of agriculture including annual crops, aquaculture, floriculture, forestry activities, horticulture, livestock, silviculture and viticulture.

12.2 Agriculture involves managing the conversion of a biological asset (living animal or plant) into agricultural produce (harvested product from a biological asset) or into additional biological assets.

12.3 This section is applied to agricultural produce only at the point of harvest. Thereafter, entities should seek guidance from Section 10 *Inventories* or another relevant and applicable section of *SPFR for FPEs*.

12.4 This section does not deal with the processing of agricultural produce after harvest, for example the processing of milk into cheese. Such processing has been specifically excluded from the definition of agricultural activity.

12.5 Grass or other pasture grown on agricultural land is not dealt with in this section, and has been specifically excluded from the definition of a biological asset.

Recognition

12.6 The entity shall recognise the cost of a biological asset and agricultural produce as an asset if, and only if:

(a) it is probable that future economic benefits associated with the item will flow to the entity; and

(b) the fair value or cost of the item can be measured reliably; and

(c) the item has not been expensed in accordance with the provisions of the Income Tax Act 2007.

Initial and subsequent measurement

12.7 With the exception of paragraphs 12.8 – 12.9 below, an entity shall measure biological assets on initial recognition and at each subsequent balance date, either:

(a) at fair value less costs to sell as ascertained by the entity in accordance with paragraphs 12.11 – 12.18 below; or

(b) in accordance with any treatment permitted under the Income Tax Act 2007.

12.8 An entity shall measure annual crops on initial recognition and at each subsequent balance date either:

(a) in accordance with any treatment permitted under the Income Tax Act 2007; or

(b) at cost less accumulated depreciation.

12.9 An entity shall measure agricultural produce on initial recognition and at each subsequent balance date, either:

(a) at fair value less costs to sell at the point of harvest as ascertained by the entity in accordance with paragraphs 12.11 – 12.18 below; or

(b) in accordance with Section 10 *Inventories*; or

(c) the cost prescribed by the Income Tax Act 2007.

Cost of biological assets

12.10 As appropriate, when determining the cost of biological assets under paragraphs 12.8(a) or 12.9(c), an entity should consider the guidance provided in Section 10 *Inventories*, Section 11 *Property, plant and equipment and Investment property*, and Section 16 *Impairment of Assets*.

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Fair value of biological assets and agricultural produce

12.11 The grouping of biological assets or agricultural produce according to significant attributes, for example age or quality, may assist entities in the determination of fair value.

12.12 For the purpose of determining fair value less costs to sell for paragraphs 12.7(a) and 12.19(a) fair value reflects the amount obtainable from the sale of the biological asset or agricultural produce in an arm's length transaction between knowledgeable, willing parties, less the costs of disposal.

12.13 For livestock, herd scheme values, as prescribed annually by Inland Revenue are acceptable as a proxy for fair value.

12.14 The best evidence of the fair value of a biological asset or agricultural produce is the quoted price in an active market. In the event that an entity has access to more than one active market for a biological asset or agricultural produce in its current location and condition, an entity should select the quoted price in the market the entity expects to use.

12.15 If there is no active market for the biological asset or agricultural produce, fair value less costs to sell is based on the best information available to reflect the amount that an entity could obtain, at the balance date, from the disposal of the biological asset or agricultural produce in an arm's length transaction between knowledgeable, willing parties, after deducting the costs to sell.

12.16 In determining this amount, an entity should consider the outcome of recent transactions in similar economic circumstances for similar biological assets or produce within the same industry.

12.17 In the absence of an active market, an entity may also wish to consider sector benchmarks to assist in the determination of fair value. Such benchmarks could include the value of an orchard expressed per export tray, bushel or hectare.

12.18 In some circumstances market-determined prices or values may not be available for a biological asset or for agricultural produce in its present condition. In these circumstances, an entity may use the present value of expected cash flows from the biological asset or agricultural produce, discounted at a current market-determined rate to determine fair value. Any cash flows for financing, taxation or re-establishing the biological asset after harvest (for example the cost of replanting trees in a forest after harvest) should not be included in the calculation of fair value using the method described in this section.

Gains and losses on biological assets

Holding gains and losses

12.19 At balance date, a holding gain or loss in the value of a biological asset or group of assets shall be recognised in profit or loss or directly in equity depending on whether it is assessable/deductible for income tax purposes or not respectively. This depends on the method used to determine the change in value.

12.20 The accumulated movements shall be recorded in a separate asset revaluation reserve as a separate equity component for that biological asset or group of assets. A record of the accumulated revaluation reserve balance for each biological asset or group of assets should be maintained.

12.21 To the extent that a holding gain in the value of a biological asset or group of assets reverses a previous holding loss in the value of a biological asset or group of assets that was recognised in profit or loss, such revaluation movements are recognised in profit or loss.

12.22 A holding loss arising from a change in value of a biological asset or group of biological assets at balance date shall be included in profit or loss for the period in which it arises to the extent that no previously accumulated revaluation surpluses are available within the biological asset revaluation reserve for that biological asset or group of assets.

12.23 When a biological asset is disposed of for which a holding gain or loss has previously been incurred, any revaluation surplus may be transferred directly to retained earnings, or it may be

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left in equity under the heading revaluation surplus. The transfer to retained earnings should not be made through profit or loss (that is, no "recycling" through profit or loss).

Biological transformation

12.24 A biological asset may undergo biological transformation resulting in asset changes through:

(a) growth (an increase in quantity or improvement in quality of an animal or plant);

(b) degeneration (a decrease in the quantity or deterioration in quality of an animal or plant); or

(c) procreation (creation of additional living animals or plants).

12.25 A gain or loss arising from procreation or degeneration of a biological asset, resulting in an increase or decrease in the number of biological assets recognised as an asset by that entity at balance date shall be included in profit or loss for the period in which it arises.

Gains and losses on agricultural produce

12.26 A gain or loss arising after the initial recognition of agricultural produce shall be included in profit or loss for the period in which it arises.

Disclosures

General

12.27 An entity shall disclose a brief description of each group of biological assets.

12.28 Those biological assets that are not held with the intention of sale within one year should be separately described and classified as non-current assets in the Balance sheet.

Other disclosures

12.29 The entity shall, where applicable, also disclose the following in the notes to the financial statements:

(a) the accounting policies applied in determining the initial value and subsequent measurement of a biological asset, or group of biological assets, and for agricultural produce at the point of harvest;

(b) where a group of biological assets or agricultural produce at the point of harvest have been measured using fair value, the methods and significant assumptions applied in determining the fair value;

(c) a reconciliation of changes in the carrying amount of biological assets, or group of biological assets, showing separately changes in value, purchases, sales, harvesting, foreign exchange differences and other changes; and

(d) the existence and carrying amounts of biological assets to which the entity has restricted title or that are pledged as security for liabilities.

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Section 13 Intangible assets other than goodwill

Purpose and scope of section

13.1 This section applies to initial recognition, subsequent measurement and disclosure of intangible assets, excluding goodwill (refer to Section 23 *Business combinations*). Included within this section is specific guidance on treatment of research and development costs.

13.2 An intangible asset is an identifiable non-monetary asset without physical substance. An intangible asset is identifiable when:

(a) it is separable, that is, capable of being separated or divided from the entity and sold, transferred, licensed, rented or exchanged, either individually or together with a related contract, asset or liability; or

(b) it arises from contractual or other legal rights, regardless of whether those rights are transferable or separable from the entity or from other rights and obligations.

13.3 Intangible assets do not include:

(a) financial assets; or

(b) mineral rights and mineral reserves, such as oil, natural gas and similar non-regenerative resources.

13.4 Entities seeking guidance on the accounting for financial assets should refer to Section 15 *Financial instruments*. For guidance on the accounting treatment of intangible mineral rights and mineral reserves entities should step up to NZ IFRS 6 *Exploration for and Evaluation of Mineral Resources*.

13.5 In determining whether an asset that incorporates both intangible and tangible elements is classified as property, plant and equipment or intangible assets, judgement should be used to assess which element is more significant. For example, computer software for a computer-controlled machine tool that cannot operate without that specific software is an integral part of the related hardware, and it is treated as property, plant and equipment. When the software is not an integral part of the related hardware, computer software is treated as an intangible asset.

Recognition

13.6 An entity shall recognise an intangible asset as an asset if, and only if:

(a) it is probable that the expected future economic benefits that are attributable to the asset will flow to the entity;

(b) the cost or value of the asset can be measured reliably; and

(c) with the exception of development costs of a project which meet the criteria outlined in paragraph 13.20, the asset does not result from expenditure incurred internally on an intangible item.

13.7 The probability of expected future economic benefits should be assessed using reasonable and justifiable assumptions representing the best estimate of the economic conditions that will exist over the useful life of the asset.

13.8 Judgement is used in the assessment of the degree of certainty attached to the flow of future economic benefits attributable to the use of the asset based on the evidence available at the time of initial recognition. Greater weight should be given to external evidence.

Initial measurement

13.9 An entity shall measure an intangible asset initially at cost.

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13.10 The cost of an acquired intangible asset comprises:

(a) its purchase price, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates; and
(b) any directly attributable cost of preparing the asset for its intended use.

13.11 Examples of directly attributable costs are:

(a) the cost of salaries, wages, and employee benefits arising directly from bringing the asset to its working condition;
(b) professional fees arising directly from bringing the asset to its working condition; and
(c) the cost of testing whether the asset is functioning properly.

13.12 Examples of expenditure that are not part of the cost of an intangible asset are:

(a) the costs of introducing a new product or service (including the cost of advertising and promotional activities);
(b) the cost of conducting business in a new location or with a new class of customer; and
(c) administration and other general overhead costs.

13.13 The capitalisation of costs in relation to an intangible asset ceases when the asset is in the condition necessary for it to be capable of operating in the manner intended. Therefore the following costs are not part of the cost of an intangible asset:

(a) costs incurred while an asset capable of operating in the manner intended has yet to be brought into use; and
(b) initial operating losses, such as those incurred while demand for the asset's output builds up.

13.14 The cost of a donated or subsidised intangible asset includes its fair value at the date of acquisition, together with any costs directly incurred in bringing the item to working condition for its intended use. The corresponding amount of the donation or subsidy received is recognised as revenue in profit or loss.

Internally generated intangible assets

13.15 To assess whether an internally generated asset meets the criteria for recognition, the generation of the asset should be classified into:

(a) a research phase; and
(b) a development phase.

13.16 Expenditure on internally generated brands, mastheads, publishing titles, customer lists, and items similar in substance cannot be distinguished from the cost of developing the business as a whole. Therefore, such items are not recognised as intangible assets and costs are expensed when incurred.

Research phase

13.17 In the research phase of an internal project, an entity cannot demonstrate that an intangible asset exists that will generate probable future economic benefits. Therefore, this expenditure is recognised as an expense when it is incurred.

13.18 Examples of research activities are:

(a) activities aimed at obtaining new knowledge;
(b) the search for, evaluation, and final selection of applications of research findings or other knowledge;
(c) the search for alternatives for materials, devices, products, processes, systems or services; and
(d) the formulation, design, evaluation, and final selection of possible alternatives for new or improved materials, devices, products, processes, systems or services.

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Development phase

13.19 In accounting for expenditures on internally generated intangible assets during the development phase, an accounting policy choice should be made to either:

(a) expense such expenditures as incurred; or

(b) capitalise such expenditures as an intangible asset (provided the criteria in paragraph 13.20 are met).

This accounting policy choice should be applied consistently to expenditure on all internal projects in the development phase.

13.20 The development costs of a project shall be recognised as an asset if, and only if, an entity can demonstrate all of the following:

(a) the technical feasibility of completing the intangible asset so that it will become available for use or sale;

(b) its intention to complete the intangible asset and use or sell it;

(c) its ability to use or sell the intangible asset;

(d) the availability of adequate technical, financial and other resources to complete the development to use or sell the intangible asset;

(e) its ability to measure reliably the expenditure attributable to the intangible asset during the development; and

(f) how the intangible asset will generate probable future economic benefits. Among other things, the entity can demonstrate the existence of a market for the output of the intangible asset or the intangible asset itself or, if it is to be used internally, the usefulness of the intangible asset.

13.21 Examples of development activities are:

(a) the design, construction and testing of preproduction or pre-use prototypes and models;

(b) the design of tools, jigs, moulds and dies involving new technology;

(c) the design, construction and operation of a pilot plant that is not of a scale economically feasible for commercial production; and

(d) the design, construction and testing of a chosen alternative for new or improved materials, devices, products, processes, systems or services.

13.22 The development costs of a project recognised as an asset shall not exceed the amount that is probable of recovery from future economic benefits, after deducting further development costs, related production costs and selling and administrative costs directly incurred in marketing the project.

Measurement after initial recognition

13.23 After recognition as an asset, an intangible asset shall be carried at cost less accumulated amortisation and impairment losses.

Amortisation

13.24 An entity shall allocate the amortisable amount of an intangible asset on a systematic basis over its useful life.

13.25 The entity shall choose an amortisation method that reflects the pattern in which it expects to consume the asset's future economic benefits, or an amortisation rates prescribed by Inland Revenue for tax purposes.

13.26 Amortisation begins when the intangible asset is available for use, ie when it is in the location and condition necessary for it to be usable in the manner intended. Amortisation ceases when the asset is derecognised.

13.27 The useful life of an intangible asset that arises from contractual or other legal rights shall not exceed the period of the contractual or other legal rights, but may be shorter depending on the period over which the entity expects to use the asset. If the contractual or other legal rights are

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conveyed for a limited term that can be renewed, the useful life of the intangible asset shall include the renewal period(s) only if there is evidence to support renewal by the entity without significant cost.

13.28 If an entity is unable to make a reliable estimate of the useful life of an intangible asset, the life shall be presumed to be ten years. An indefinite life is not deemed to be a reliable estimate.

13.29 The useful lives of intangible assets should be assessed annually to determine whether there is any indication that it is inappropriate. If any such indication exists, the amortisation method and rate will be amended accordingly and the amortisation charge for the current and future periods amended.

13.30 A change in the amortisation method and rates is not considered a change in accounting policy.

Impairment

13.31 At each balance date, an entity should apply Section 16 *Impairment of Assets* to determine whether an intangible asset is impaired and, if so, how to recognise and measure the impairment loss.

Review of internally generated intangible assets

13.32 The development costs of an internally generated asset shall be reviewed for impairment at the end of each accounting period.

13.33 When the criteria of paragraph 13.20, which previously justified the recognition of the development costs as an asset, no longer apply, the unamortised balance shall be written off and recognised immediately as an expense in profit or loss.

Derecognition

13.34 An entity shall derecognise an intangible asset:

(a) on disposal; or

(b) when no future economic benefits are expected from its use or disposal.

13.35 An entity shall determine the gain or loss arising from derecognition of an intangible asset as the difference between the net disposal proceeds, if any, and the carrying amount of the asset.

13.36 An entity shall recognise any gain or loss on the derecognition of an intangible asset in profit or loss when the item is derecognised.

Disclosures

13.37 An entity shall disclose the following for each class of intangible assets:

(a) the useful lives or the amortisation rates used;

(b) the amortisation methods used; and

(c) the gross carrying amount and the accumulated amortisation (aggregated with accumulated impairment losses) at the beginning and end of the reporting period.

13.38 The entity shall also disclose the following:

(a) the existence and carrying amount of intangible assets to which the entity has restricted title or that is pledged as security for liabilities; and

(b) the amount of contractual commitments for the acquisition of intangible assets.

13.39 An entity shall disclose the aggregate amount of research and development expenditure recognised as an expense during the period.

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Section 14 Unincorporated joint venture arrangements

Purpose and scope of section

14.1 This section establishes the principles for accounting for interests in unincorporated joint venture arrangements, that is, jointly controlled operations and jointly controlled assets. Jointly controlled entities (incorporated joint ventures), are considered to be equity instruments, and should be accounted for in accordance with the principles set out in Section 15 *Financial instruments*.

14.2 Activities conducted with no formal contractual arrangements that are jointly controlled in substance are joint ventures for the purposes of this section.

14.3 A venturer is a party to a joint venture who has joint control over that joint venture, has the right and ability to obtain future economic benefits from the resources of the joint venture, and is exposed to the related risks.

14.4 A distinctive characteristic common to all joint ventures is that the venturers have joint control over the joint venture, regardless of the difference that may exist in their ownership interest. None of the individual venturers is in a position to exercise unilateral control over the joint venture. Decisions in all areas essential to the accomplishment of the joint venture require the consent of the venturers in such manner as defined in the terms of the contractual arrangement. This characteristic of joint control distinguishes interests in joint ventures from interests in other entities over which an investor may exercise control or significant influence.

Accounting for jointly controlled operations

14.5 The operation of some joint ventures involves the use of the assets and other resources of the venturers rather than the establishment of a corporation, partnership or other entity, or financial structure that is separate from the venturers themselves. Each venturer uses its own property, plant and equipment and carries its own inventories. It also incurs its own expenses and liabilities and raises its own finance, which represent its own obligations. The joint venture activities may be carried out by the venturers' employees alongside the venturers' similar activities. The joint venture agreement usually provides a means by which the revenue from the sale of goods or services by the joint venture and any expenses incurred in common are shared among the venturers.

14.6 In respect of its interests in jointly controlled operations, a venturer shall recognise in its financial statements:

(a) the assets that it controls and the liabilities that it incurs; and

(b) the expenses that it incurs and its share of the revenue that it earns from the sale of goods or services by the joint venture.

Accounting for jointly controlled assets

14.7 Some joint ventures involve the joint control, and often the joint ownership, by the venturers of one or more assets contributed to, or acquired for the purpose of the joint venture and dedicated to the purposes of the joint venture.

14.8 In respect of its interests in jointly controlled assets, a venturer shall recognise in its financial statements:

(a) their share of assets and the liabilities associated with the venture; and

(b) their share of expenses incurred and revenue earned from the sale of goods or services by the joint venture.

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Financial statements

14.9 The following shall be presented separately on the face of the Statement of profit or loss, in relation to jointly controlled assets and jointly controlled operations:

(a) fair value gains or losses;

(b) impairment losses or reversals;

(c) revenue generated from jointly controlled assets and jointly controlled operations;

(d) expenses incurred from jointly controlled assets and jointly controlled operations; and

(e) gains or losses on derecognition of jointly controlled assets and liabilities and assets and liabilities held by jointly controlled operations.

Accounting policies

14.10 An entity shall disclose, in the statement of accounting policies, the measurement basis for investments in jointly controlled assets and jointly controlled operations.

Notes to the financial statements

14.11 An entity shall disclose in the notes to the financial statements a listing and description of material jointly controlled assets and jointly controlled operations.

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Section 15 Financial instruments

Purpose and scope of section

15.1 This section applies to the initial recognition, subsequent measurement and disclosure of financial instruments.

15.2 This section addresses the accounting for financial instrument arrangements that are most often entered into by SMEs. Common examples of financial instruments include:

(a) cash and short term deposits;

(b) fixed-interest bonds and treasury notes;

(c) accounts receivable and accounts payable;

(d) borrowings;

(e) bonds issued and similar debt instruments;

(f) equity investments (including an investment in an associate and an incorporated joint venture); and

(g) forward foreign exchange contracts and interest rate swaps.

15.3 An entity should apply this section to all financial instruments except the following:

(a) financial instruments that meet the definition of an entity's own equity;

(b) lease contracts;

(c) employer's rights and obligations for retirement and other post-employment benefits;

(d) insurance contracts;

(e) share-based payment arrangements;

(f) financial guarantee contracts; and

(g) compound financial instruments which include both debt and equity components.

Initial recognition of financial assets and liabilities

15.4 An entity shall recognise a financial asset or a financial liability only when the entity becomes a party to the contractual provisions of the instrument.

Initial measurement

15.5 When a financial asset or financial liability is recognised initially, an entity shall measure it at its fair value.

15.6 All loans are to be stated at their face value less impairment (if any).

15.7 The best evidence of fair value at initial recognition is usually the transaction price, being the amount of consideration paid or received to acquire the financial instrument, less deductions for integral fees. Transaction and financing fees (with the exception of integral fees) should be expensed as incurred.

15.8 If an entity determines that there is a difference between the transaction price and the fair value of a financial asset or financial liability at initial recognition, the entity should recognise the difference between the fair value and the transaction price by adjusting the cost price of the financial instrument and recognising a corresponding gain or loss in profit or loss at the date of acquisition.

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Subsequent measurement of financial assets and financial liabilities

Financial assets

15.9 At the end of each reporting period, an entity shall measure all financial instruments within the scope of this section at either:

(a) amortised cost;

(b) cost; or

(c) fair value.

15.10 A financial asset shall be subsequently measured at amortised cost if both the following conditions are met:

(a) the asset is held within a business model whose objective is to hold the assets to collect contractual cash flows; and

(b) the contractual terms of the financial asset give rise on specified dates to cash flows that are solely of principal and interest on the principal amount outstanding.

15.11 Examples of financial assets which contractually provide cash flows in the form of principal and interest payments, but would require subsequent measurement at fair value are:

(a) trade debtor books which have been acquired for the purpose of sale to generate short-term gains, rather than holding the receivable balance until contractual cash receipts are collected; and

(b) fixed-interest bonds and treasury notes which are traded for the purpose of generating short-term gains, rather than holding the financial instrument until maturity.

15.12 A financial asset which is an equity investment in another entity (ie shares), may be either classified as being subsequently measured at cost, or at fair value (where the equity investment meets the criteria in paragraph 15.26).

15.13 For listed equity investments in another entity information regarding subsequent measurement at fair value with reference to an active market will be readily obtainable, however this will not be the case for unlisted equity investments in another entity. Accordingly, entities wishing to subsequently measure unlisted equity instruments at fair value for which no active market exists, may opt to seek guidance from the relevant NZ IFRS.

15.14 All financial assets that are neither subsequently classified as measured at amortised cost or cost should be classified as financial assets subsequently measured at fair value.

15.15 The classification of financial assets is done on a class-by-class basis (eg trade receivables, fixed interest investments, equity investments and other financial assets). The classification will require an assessment of the entity's business model for managing financing assets. While the entity may have sold financial assets before maturity in previous reporting periods, the key consideration is the intention and purpose for holding certain classes of financial assets.

Financial liabilities

15.16 An entity shall classify all financial liabilities as subsequently measured at amortised cost.

Amortised cost

15.17 Financial assets and financial liabilities classified as subsequently measured at amortised cost shall be measured using the effective interest method.

15.18 Under the effective interest method financial assets or financial liabilities that are classified as current assets or current liabilities (such as cash and trade receivables and overdrafts and accounts payable) are carried at the undiscounted amount of cash or other consideration expected to be paid or received, net of any impairment provisions where relevant.

15.19 The amortised cost of a financial asset or financial liability at each balance date is the net amount of the following:

(a) the amount at which the financial asset or financial liability is measured at initial recognition;

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(b) minus any repayments of principal received;

(c) plus or minus the cumulative amortisation using the effective interest method and any difference between the amount at initial recognition and the maturity amount; and

(d) minus any reduction for impairment or uncollectibility (in the case of financial assets).

15.20 Financial asset or financial liability cash flows received subsequent to initial recognition include both principal and interest (for the time value of money). The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability (or a group of financial assets or financial liabilities) and of allocating the interest income or interest expense over the relevant period.

15.21 The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period, to the carrying amount of the financial asset or financial liability. The effective interest rate is determined on the basis of the carrying amount of the financial asset or liability at initial recognition. Under the effective interest method:

(a) the amortised cost of a financial asset (financial liability) is the present value of future cash receipts (payments) discounted at the effective interest rate, and

(b) the interest expense (income) in a period equals the carrying amount of the financial liability (financial asset) at the beginning of a period multiplied by the effective interest rate for the period.

15.22 When calculating the effective interest rate, an entity shall estimate cash flows considering all contractual terms of the financial instrument and known credit losses, but it shall not consider possible or future credit losses not yet incurred.

15.23 If an entity revises its estimates of payments or receipts, the entity shall adjust the carrying amounts of the financial asset or financial liability to reflect the revised estimated cash flows.

15.24 All measurement movements after initial recognition for financial assets and financial liabilities measured at amortised cost are recognised in profit or loss.

Example of determining amortised cost for a five-year loan using the effective interest method

On 1 January 2014, an entity takes out a loan for $10,000. In doing so it incurs an establishment fee of $100 which is deducted from the loan amount to arrive at the initial carrying amount. A fixed amount of interest is payable, $700 a year over the next 5 years, with the principle of $10,000 to be repaid on 31 December 2018.

Year	Carrying amount beginning of period	Interest payable @7.245496%	Cash flow	Carrying amount at end of period
2014	$9,900	$717	($700)	$9,917
2015	$9,917	$719	($700)	$9,936
2016	$9,936	$720	($700)	$9,956
2017	$9,956	$721	($700)	$9,977
2018	$9,977	$723	($10,700)	-

The effective interest rate of 7.245496% is used to discount the expected cash flows of the loan to the initial carrying amount.

$700/(1.072245496)^1 + 700/(1.072245496)^2 + 700/(1.072245496)^3 + 700/(1.072245496)^4 + 10{,}700/(1.072245496)^5$

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Equity investments in other entities (ie shares)

15.25 Equity investments in other entities (ie shares) do not meet the criteria outlined in paragraph 15.10(b) to enable them to be subsequently measured at amortised cost, ie they do not provide cash flows that are solely principal and interest in nature. Therefore, an entity may opt to subsequently measure such instruments either at cost less any allowance for impairment in accordance with paragraph 15.29, or, at fair value, when the fair value of the instrument can be reliably measured as outlined in paragraph 15.26.

Fair value

15.26 Equity investments in other entities (and other financial assets measured at fair value) shall be subsequently measured at fair value only when the fair value of the instrument can be reliably measured based on the quoted price for an identical asset in an active market, where the information is readily obtainable and reliable; for example the quoted price from the New Zealand Stock Exchange, Reuters or Bloomberg.

15.27 If the fair value of an equity investment cannot be reliably measured in line with paragraph 15.26, the financial asset shall continue to be measured at the carrying value reported in the previous financial reporting period, less any allowance for impairment.

15.28 If for commercial reasons an entity needs to revalue financial assets for which an active market does not exist at fair value, such is the case for unlisted equity investments in other entities, the entity should seek guidance from the relevant NZ IFRS.

Cost

15.29 An entity may alternatively elect to measure an equity investment in other entity (ie shares) at cost less any allowance for impairment (refer to Section 16 *Impairment of Assets*. In most cases, the cost of a financial asset will equate to fair value at initial recognition.

Impairment

15.30 At each balance date, an entity shall apply Section 16 *Impairment of Assets* to determine whether a financial asset is impaired and, if so, how to recognise and measure the impairment loss.

Derecognition of a financial asset

15.31 An entity shall derecognise a financial asset only when:

(a) the contractual rights to the cash flows from the financial asset expire or are settled; or

(b) the entity transfers to another party substantially all of the risks and rewards of ownership of the financial asset.

Derecognition of a financial liability

15.32 An entity shall derecognise a financial liability (or a part of a financial liability) only when it is extinguished ie when the obligation specified in the contract is discharged, is cancelled or expires.

15.33 If an existing borrower and lender exchange financial instruments with substantially different terms, the entities shall account for the transaction as an extinguishment of the original financial liability and the recognition of a new financial liability. Similarly, an entity shall account for a substantial modification of the terms of an existing financial liability or a part of it (whether or not attributable to the financial difficulty of the debtor) as an extinguishment of the original financial liability and the recognition of a new financial liability.

15.34 The entity shall recognise in profit or loss any difference between the carrying amount of the financial liability (or part of a financial liability) extinguished or transferred to another party and the consideration paid, including any non-cash assets transferred or liabilities assumed.

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Subsequent measurement of derivatives

15.35 Derivative financial instruments (such as foreign exchange contracts and interest rate swaps) shall be subsequently measured at fair value and recognised in the Balance sheet at each balance date, with changes in fair value recognised in profit or loss.

15.36 The fair value of derivatives shall be based on mark-to-market values or other fair value measurements as may be provided by the financial institution or other party who issued the derivative.

15.37 Where the fair value of a derivative financial instrument cannot be reliably measured, an entity should seek guidance from the relevant NZ IFRS.

Disclosures

Accounting policies

15.38 An entity shall disclose, in the statement of accounting policies, the measurement basis (or bases) used for financial instruments and other accounting policies used for financial instruments that are relevant to an understanding of the financial statements.

Subsequent measurement of financial assets

15.39 An entity shall disclose the total carrying amount of each of the following categories of financial assets at the balance date:

(a) financial assets measured at amortised cost;

(b) financial assets measured at fair value; and

(c) financial assets measured at cost.

Where the entity only holds financial instruments measured at amortised cost (such as cash and short-term deposits, accounts receivable and fixed-interest bond and treasury notes held until maturity), the classification disclosure in (a) to (c) above is not required.

Fair value disclosures

15.40 For financial assets classified as subsequently measured at fair value, the following categories shall be reported in total in the notes to the financial statements:

(a) financial assets measured at fair value based on quoted prices for an identical asset in an active market; and

(b) financial assets classified as subsequently measured at fair value, but where not subject to re-measurement in the current year because quoted market prices were not available.

15.41 For financial assets classified as (b) above, the following additional note disclosure shall be provided:

(a) the balance of financial assets which have not been subject to fair value re-measurement since initial recognition (because no market information is available);

(b) the balance of financial assets subject to fair value re-measurement in the current reporting period; and

(c) the remaining balance of financial assets, allocated to appropriate time bands to provide the reader with an understanding of when the last fair value measurement of the financial asset occurred.

15.42 For all financial assets measured at fair value, the entity shall disclose the basis and source for determining the fair value.

15.43 For all financial assets measured at cost, such as equity investments in other listed entities (ie shares) for which the fair value is readily obtainable and able to be reliably measured, fair value should be disclosed in the notes to the financial statements. The total balance of financial assets which have been measured at cost should also be disclosed in the notes to the financial statements.

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Derivatives

15.44 The source of the fair value measurement of derivative financial instruments recognised in the Balance sheet shall be disclosed in the notes to the financial statements.

Collateral

15.45 When an entity has pledged financial assets as collateral for liabilities or contingent liabilities it shall disclose the following:

(a) the carrying amount of the financial assets pledged as collateral; and

(b) the terms and conditions relating to its pledge.

Defaults and breaches on loans payable

15.46 For loans payable recognised at the balance date for which there is a breach of terms or default of principal or interest that has not been remedied by the balance date, an entity shall disclose the following:

(a) details of that breach or default;

(b) the carrying amount of the related loans payable at the balance date; and

(c) whether the breach or default was remedied, or the terms of the loans payable were renegotiated, before the financial statements were authorised for issue.

Items of revenue, expense, gains or losses

15.47 An entity shall disclose the following items of revenue and expenses in relation to financial instruments:

(a) interest revenue;

(b) financial impairment losses;

(c) financial instrument impairment losses reversed; and

(d) financial asset fair value gains or losses.

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Section 16 Impairment of assets

Purpose and scope of section

16.1 This section establishes the principles for accounting for the impairment of property, plant and equipment, investment property, financial assets and intangible assets. Inventory is excluded from the scope of this section.

16.2 The write down of inventories to net realisable value is addressed in Section 10 *Inventories*.

16.3 All assets recognised in the Balance sheet that are within the scope of this section as outlined in paragraph 16.1 are subject to potential impairment review to ensure the carrying amount of the asset does not exceed the amount of future economic benefits the entity expects to generate from the assets' use or sale.

16.4 An impairment loss occurs when the carrying amount of an asset exceeds its recoverable amount.

Assets subject to impairment consideration

16.5 At each balance date, all assets that fall within the scope of paragraph 16.1 are allocated into one of the following four categories for the purpose of assessing whether any impairment losses require recognition in the financial statements of the entity.

Impairment tier classification	Value from use and sale	Impairment review
1. Assets measured at fair value[5] in accordance with the entity's accounting policies.	The asset's value is expected to be realised from future use or sale.	No impairment review necessary.
2. Assets that are currently available for their intended use that the entity intends to retain for use until either their useful life comes to an end or right to use expires.	The asset's value is expected to be realised from use over the asset's useful life.	No impairment review necessary.
3. Assets that are expected to be sold prior to the end of their useful life.	The asset's value is expected to be realised from future use or sale.	At balance date, review for indicators of impairment and, where indicators are present, test for impairment.
4. Assets which are damaged or idle at the balance date.	The asset's value is not expected to be realised from use or sale.	At balance date, determine the recoverable amount of the asset and record appropriate impairment.

Indicators of impairment

Tier 3 and Tier 4

16.6 At each balance date, an entity should assess all assets allocated to tier 3 for indicators of impairment. Where such indications exist for assets allocated to tier 3, and in all instances for assets allocated to tier 4, the entity should estimate the recoverable amount of the asset in accordance with the guidance provided in paragraphs 16.13 – 16.15.

[5] An entity should be mindful of the requirement under Section 11 *Property, Plant and Equipment and Investment Property* for assets to be revalued with sufficient regularity to ensure that the carrying amount does not differ materially from that which would be determined using fair value at the end of the reporting period. At a minimum, a revaluation is required every five years, or more frequently if necessary to ensure carrying amounts are not materially different from fair value as at balance date.

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16.7 Where there is no indication that an asset is impaired the estimation of the asset's recoverable amount is unnecessary.

Indicators of impairment for non-financial assets

16.8 An entity shall assess non-financial assets for impairment either individually or, where it is not possible or practical to assess impairment for individual items, by group of assets.

16.9 An entity should consider at least the indicators listed below when assessing whether there is any indication that a non-financial asset may be impaired:

External sources of information

(a) during the period, an asset's market value has declined significantly more than would be expected as a result of the passage of time or normal use;

(b) significant changes with an adverse effect on the entity have taken place during the period, or will take place in the near future, in the technological, market, economic or legal environment in which the entity operates or in the market to which an asset is dedicated; or

(c) the carrying amount of the net assets of the entity is more than the estimated fair value of the entity as a whole (such an estimate may have been made, for example, in relation to the potential sale of part or all of the entity).

Internal sources of information

(a) evidence is available of obsolescence or physical damage of an asset;

(b) significant changes with an adverse effect on the entity have taken place during the period, or are expected to take place in the near future, in the extent to which, or manner in which, an asset is used or is expected to be used. These changes include the asset becoming idle, plans to discontinue or restructure the operation to which an asset belongs, plans to dispose of an asset before the previously expected date, and reassessing the useful life of an asset as finite rather than indefinite; or

(c) evidence is available from internal reporting that indicates that the economic performance of an asset is, or will be, worse than expected. In this context economic performance includes operating results and cash flows.

Indicators of impairment for financial assets

16.10 An entity shall assess financial assets for impairment either individually or as a group of assets.

16.11 An entity should consider at least the indicators listed below when assessing whether there is any indication that a financial asset may be impaired:

(a) significant financial difficulty of the issuer of the financial asset or debtor;

(b) a breach of contract, such as a default or delinquency in interest or principal payments;

(c) it has become probable that the debtor will enter bankruptcy or other financial reorganisation;

(d) observable data indicating that there has been a measurable decrease in the estimated future cash flows from a group of financial assets since the initial recognition of those assets, even though the decrease cannot yet be identified with the individual financial assets in the group, such as adverse national or local economic conditions or adverse changes in industry conditions; or

(e) significant changes with an adverse effect that have taken place in the technological, market, economic or legal environment in which the issuer or debtor operates.

16.12 If there is an indication that an asset may be impaired, this may indicate that the entity should also review the remaining useful life, the depreciation (amortisation) method or the residual value for the asset and adjust it accordingly, even if no impairment loss is recognised for the asset.

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Measuring the recoverable amount

16.13 The recoverable amount of an asset is defined as the fair value less costs to sell.

16.14 Fair value less costs to sell is the amount obtainable from the sale of an asset in an arm's length transaction between knowledgeable, willing parties, less the costs of disposal.

Impairment loss

16.15 Only when the recoverable amount of an asset is less than its carrying amount, the entity shall reduce the carrying amount of an asset or group of assets to its recoverable amount. This reduction is an impairment loss and is recorded as an expense in profit or loss.

16.16 Impairment losses recognised for a group of assets should be allocated to the assets of the group pro rata based on the carrying amount of each asset in the group. Where determinable, the carrying amount of any asset in the group should not be reduced below its fair value less costs to sell.

Reversal of an impairment loss

16.17 At each balance date an entity shall assess all assets within the scope of paragraph 16.1 for any indication that an impairment loss recognised in prior periods may no longer exist or may have decreased. If any such indication exists, the entity shall determine whether all or part of the prior impairment loss should be reversed. Impairment losses recognised on goodwill shall not be reversed.

16.18 The procedure for reversing an impairment loss is as follows:

(a) The entity shall estimate the recoverable amount of the asset at the current balance date;

(b) If the estimated recoverable amount of the asset is greater than its carrying amount, the entity shall increase the carrying amount to recoverable amount subject to paragraph 16.18(c). The entity shall recognise the reversal immediately in profit or loss;

(c) The reversal of an impairment loss shall not increase the carrying amount of the asset above the carrying amount that would have been determined (net of amortisation or depreciation) if no impairment loss had been recognised for the asset in prior years;

(d) After a reversal of an impairment loss is recognised, the entity shall adjust the depreciation (amortisation) charge for the asset in future periods to allocate the asset's revised carrying amount, less its residual value (if any), on a systematic basis over its remaining useful life.

Disclosures

16.19 An entity shall, where applicable, disclose the following in the notes to the financial statements for each class of asset presented on the face of the Balance sheet:

(a) the amount of impairment losses recognised in profit or loss for the period; and

(b) the amount of reversals of impairment losses recognised in profit or loss during the period.

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Section 17 Equity vs liabilities

Purpose and scope of section

17.1 This section establishes the principles for classifying financial instruments as either liabilities or equity and addresses accounting for equity instruments issued to individuals or other parties in their capacity as owners of the entity.

Classification of an instrument as liability or equity

Equity

17.2 Equity is residual interest in the assets of the entity after deducting all of its liabilities.

17.3 Equity includes investments by the owners of the entity, plus additions to those investments earned through accumulated profits from operations and retained for future use, minus reductions to owners' investments as a result of accumulated losses from operations and distributions to owners.

17.4 For entities such as Trusts, the initial contribution to the Trust is considered to be equity.

17.5 The owners of an entity are defined as the holders of equity instruments which provide them with rights to the net assets of an entity. For a non-profit orientated entity, the owners are defined as those parties with voting interests to appoint the governing body of the entity.

Liability

17.6 A liability is a present obligation of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits.

Puttable financial instruments

17.7 Some financial instruments that meet the definition of a liability are classified as equity because they represent the residual interest in the net assets of the entity. These include puttable instruments.

17.8 A puttable instrument is a financial instrument that gives the holder the right to sell that instrument back to the issuer for cash or another financial asset or is automatically redeemed or repurchased by the issuer on the occurrence of an uncertain future event or the death or retirement of the instrument holder.

17.9 An entity that holds a financial instrument that has the characteristics of a puttable financial instrument as described in paragraph 17.8 should step up to the relevant NZ IFRS.

Initial recognition of share capital or other equity instruments

17.10 An entity shall recognise the issue of shares or other equity instruments as equity when it issues those instruments and another party is obliged to provide cash or other resources to the entity in exchange for the instruments.

17.11 An entity shall measure the equity instruments at the fair value of the cash or other resources received or receivable, net of direct costs of issuing the equity instruments.

17.12 An entity shall account for the transaction costs of an equity transaction as a deduction from equity, net of any related income tax benefit.

Bonus issues of shares and share splits

17.13 Capitalisation or bonus issues and share splits do not change total equity.

17.14 Under these arrangements the number of shares issued is adjusted; however, no adjustment is required in relation to the carrying value of share capital.

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Convertible debt or similar compound financial instruments

17.15 Convertible debt or similar compound financial instruments shall be treated as debt instruments with no equity component.

Treasury shares

17.16 Treasury shares are the equity instruments of an entity that have been issued and subsequently reacquired by the entity. An entity shall deduct from equity the fair value of the consideration given for the treasury shares. The entity shall not recognise a gain or loss in profit or loss on the purchase, sale, issue or cancellation of treasury shares.

Distributions to owners

17.17 An entity shall reduce equity for the amount of distributions to its owners.

Disclosures

17.18 An entity shall present the following components of equity on either the face of the Balance sheet, in the Statement of changes in equity (if presented) or in the reconciliation of equity movements in the notes to the financial statements:

(a) retained earnings/accumulated losses;

(b) share capital; and

(c) other components of equity.

17.19 Disclosure of the following is required in the notes to the financial statements:

(a) the number of shares issued and fully paid at balance date;

(b) the number of shares issued but not fully paid at balance date, with details of the unpaid portion and when outstanding equity amounts are expected to be received;

(c) share type by class; and

(d) the rights attached to each class of shares.

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Section 18 Provisions and contingencies

Purpose and scope of section

18.1 This section establishes principles for the initial recognition, subsequent measurement and disclosure of:

(a) provisions;

(b) contingent liabilities; and

(c) contingent assets.

18.2 The section excludes provisions specifically addressed by other sections, including provisions relating to:

(a) leases;

(b) construction contracts;

(c) employee benefits; and

(d) income tax.

18.3 The word “provision” is sometimes used in the context of such items as depreciation, impairment of assets, and uncollectible receivables. Those are adjustments of the carrying amounts of assets, rather than recognition of liabilities, and therefore are not covered by this section.

Initial recognition of provisions

18.4 An entity shall recognise a provision only when:

(a) the entity has an obligation at the balance date as a result of a past event;

(b) it is probable (ie more likely than not) that the entity will be required to transfer economic benefits in settlement; and

(c) the amount of the obligation can be estimated reliably.

18.5 The entity shall recognise the provision as a liability in the Balance sheet and shall recognise a corresponding expense in profit or loss.

18.6 An obligation at the balance date as a result of a past event means that the entity has no realistic alternative to settling the obligation. This can happen when the entity has a legal obligation that can be enforced by law or when the entity has a constructive obligation because the past event (which may be an action of the entity) has created valid expectations in other parties that the entity will discharge the obligation.

18.7 Obligations that will arise from the entity’s future actions (ie the future operations of its business) do not relate to a past event. A provision is not recognised for future commitments or obligations no matter how likely they are to occur and even if they are contractual.

Initial measurement of provisions

18.8 An entity shall measure a provision at the best estimate of the amount required to settle the obligation at the balance date. The best estimate is the amount an entity would rationally pay to settle the obligation at the end of the reporting period or to transfer it to a third party at that time.

18.9 Provisions are not required to be discounted for the time value of money.

Reimbursement of provisions

18.10 When the entire amount (or part thereof) required to settle a provision may be reimbursed by another party (eg through an insurance claim), the entity shall recognise the reimbursement as a separate asset only when it is virtually certain that the entity will receive the reimbursement on settlement of the obligation. The amount recognised for the reimbursement shall not

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exceed the amount of the provision. The reimbursement receivable shall be presented as an asset and shall not be offset against the provision.

Subsequent measurement of provisions

18.11 An entity shall charge against a provision only those expenditures for which the provision was originally recognised.

18.12 An entity shall review provisions at each balance date and adjust them to reflect the current best estimate of the amount that would be required to settle the obligation at that balance date. Any adjustments to the amounts previously recognised shall be recognised in profit or loss.

Contingent liabilities

18.13 A contingent liability is either a possible but uncertain obligation or a present obligation that is not recognised because it fails to meet one or both of the conditions (b) and (c) in paragraph 18.4. An entity shall not recognise a contingent liability as a liability.

Contingent assets

18.14 An entity shall not recognise a contingent asset as an asset. However, when the flow of future economic benefits to the entity is virtually certain, then the related asset is not a contingent asset, and its recognition is appropriate.

Disclosures

Provisions

18.15 An entity shall provide a breakdown into descriptive line items for each class of provision.

Contingent liabilities

18.16 Unless the possibility of any outflow of resources in settlement is remote, an entity shall disclose, for each class of contingent liability at the balance date, a brief description of the nature of the contingent liability and, when practicable:

(a) an estimate of its potential financial effect;

(b) an indication of the uncertainties relating to the amount or timing of any outflow; and

(c) the possibility of any reimbursement.

18.17 If it is impracticable to make one or more of these disclosures, that fact shall be stated.

Contingent assets

18.18 If an inflow of economic benefits is probable (more likely than not) but not virtually certain, an entity shall disclose:

(a) a description of the nature of the contingent assets at the end of the reporting period; and

(b) when practicable without undue cost or effort, an estimate of their financial effect. If it is impracticable to make this disclosure, that fact shall be stated.

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Appendix to Section 18

Guidance on the recognition and measurement of provisions

18.19 This appendix provides guidance on the application of the recognition and measurement principles for provisions as outlined in paragraphs 18.4 – 18.12. In all cases below, it has been assumed that a reliable estimate can be made of any expected outflows. Where the events described in the examples below have resulted in the impairment of an asset, this has not been dealt within this appendix. Accounting for the impairment of assets is addressed in Section 16 *Impairment of Assets*.

Example 1 – Future operating losses

18.20 An entity determines that it is probable that a segment of its operations will incur future operating losses for several years. There is no past event that obliges the entity to pay out resources, therefore the entity does not recognise a provision for future operating losses. The initial recognition criteria in paragraph 18.4(a) has not been satisfied. Expected future losses do not meet the definition of a liability.

18.21 The expectation of future operating losses may be an indicator that one or more assets are impaired under Section 16 *Impairment of Assets*.

Example 2 – Restructurings

18.22 It is possible for a present obligation as a result of a past obligating event to exist in the instance of a restructuring. That obligation may be either a legal or constructive obligation as outlined in paragraph 18.6. At a minimum, an example of where a constructive obligation to restructure would arise is when an entity:

- (a) has a detailed formal plan for the restructuring, identifying at least:
  - (i) the business or part of a business concerned;
  - (ii) the principal locations affected;
  - (iii) the location, function and approximate number of employees who will be compensated for terminating their services;
  - (iv) the expenditures that will be undertaken; and
  - (v) when the plan will be implemented; and
- (b) has raised a valid expectation in those affected that it will carry out the restructuring by starting to implement that plan or announcing its main features to those affected by it.

18.23 Under these circumstances (and based on limited facts) an entity recognises a provision for restructuring costs only when it has a legal or constructive obligation at the balance date to carry out the restructuring. The entity must also be able to make a reliable estimate of the restructuring obligation.

Example 3 – Onerous contracts

18.24 An onerous contract is one in which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it. The unavoidable costs under a contract reflect the least net cost of exiting from the contract, which is the lower of the cost of fulfilling it and any compensation or penalties arising from failure to fulfil it.

18.25 For example, an entity may be contractually required under an operating lease to make payments to lease an asset for which it no longer has any use. This represents a probable present obligation as a result of a past obligating event. The entity is contractually required to pay out resources for which it will not receive equal benefits.

18.26 Therefore, if an entity has a contract that is onerous, the entity recognises and measures the best estimate of the obligation under the contract as a provision.

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Example 4 – Warranties

18.27 A manufacturer gives warranties at the time of sale to purchasers of its product. Under the terms of the contract for sale, the manufacturer undertakes to make good, by repair or replacement, manufacturing defects that become apparent within three years from the date of sale.

18.28 Under these circumstances (and based on limited facts) there is a present obligation as a result of a past obligating event. The obligating event is the sale of the product with a warranty, which gives rise to a legal obligation. An outflow of resources embodying economic benefits in settlement is probable for the warranties as a whole.

18.29 On the basis of experience, it is probable (ie more likely than not) that there will be some claims under the warranties.

18.30 Under these circumstances (and based on limited facts) the entity recognises a provision for the best estimate of the costs of making good under the warranty products sold before the balance date.

Example 5 – Refund policy

18.31 A retail store has a policy of refunding purchases of unhappy customers, even though it is under no legal obligation to do so. Its policy of making refunds is generally known.

18.32 A present obligation as a result of a past obligating event has been established. The obligating event is the sale of the product, which gives rise to a constructive obligation because the conduct of the store has created a valid expectation on the part of its customers that the store will refund purchases. It is probable that a proportion of goods will be returned for refund.

18.33 Under these circumstances (and based on limited facts) the entity recognises a provision for the best estimate of the amount required to settle the refunds.

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Section 19 Leases

Purpose and scope of section

19.1 This section establishes the principles for initial recognition, subsequent measurement and disclosure of lease arrangements.

Classification of leases

19.2 The classification of leases is based on the extent to which risks and rewards associated with ownership of a leased asset lie with the lessor or lessee and this classification determines the accounting treatment of the lease arrangement.

19.3 Each lease arrangement shall be classified as either:

(a) a finance lease; or

(b) an operating lease.

19.4 Whether a lease is finance lease or an operating lease depends on the substance of the transaction rather than the legal form of the contract.

19.5 Examples of situations that individually or in combination would normally lead to a lease being classified as a finance lease are:

(a) the lease transfers ownership of the asset to the lessee by the end of the lease term;

(b) the lessee has the option to purchase the asset at a price which is expected to be sufficiently lower than the fair value at the date the option becomes exercisable for it to be reasonably certain, at the inception of the lease, that the option will be exercised;

(c) the lease term is for a major part (normally 75%) of the useful life of the asset;

(d) at the inception of the lease the present value of the minimum lease payments amounts to at least the majority (normally 90%) of the fair value of the leased asset; or

(e) the leased assets are of such a specialised nature that only the lessee is able to use them without major modifications.

19.6 Additional examples of situations that individually or combined could also lead to classification of a lease as a finance lease are:

(a) if the lessee can cancel the lease, the lessor's losses associated with the cancellation are borne by the lessee;

(b) gains or losses from the fluctuation in the residual value of the leased asset accrue to the lessee (eg in the form of a rent rebate equalling most of the sales proceeds at the end of the lease); and

(c) the lessee has the ability to continue the lease for a secondary period at a rent that is substantially lower than market rent.

19.7 If it is clear from the contractual terms of the lease that a lease does not transfer substantially all risks and rewards incidental to ownership, the lease is classified as an operating lease.

19.8 The lease classification is made at the inception of the lease and is not changed during the term of the lease, unless the contractual terms of the lease are substantially amended.

Land and buildings

19.9 When a lease includes both land and building elements, an entity assesses the classification of each element as a finance lease or an operating lease separately. In determining whether the land element is an operating or a finance lease, an important consideration is that land normally has an indefinite economic life.

19.10 For a lease of land and buildings in which the amount that would initially be recognised for the land element is immaterial, the land and buildings may be treated as a single unit for the purpose of lease classification and classified as a finance or operating lease. In such a case, the economic life of the buildings is regarded as the economic life of the entire leased asset.

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Financial statements of lessees – finance leases

Initial recognition and measurement

19.11 At the commencement of the lease term, a lessee shall recognise its rights of use and obligations under finance leases as assets and liabilities in the Balance sheet at amounts equal to the present value of the minimum lease payments, determined at the inception of the lease. Any initial direct costs of the lessee (incremental costs that are directly attributable to negotiating and arranging a lease) are added to the amount recognised as an asset.

19.12 The present value of the minimum lease payments should be calculated using the interest rate implicit in the lease. If this cannot be determined, the lessee's incremental borrowing rate shall be used.

Subsequent measurement

19.13 The lessee shall apportion minimum lease payments between the finance charge and the reduction of the outstanding liability using the effective interest method. The lessee shall allocate the finance charge to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability. The effective interest method is a method allocating the interest expense incurred over the period from initial recognition of the lease to maturity. The effective interest rate is the rate that exactly discounts estimated future payments through the expected life of the lease arrangement to the carrying amount of the lease at maturity date.

19.14 A lessee shall depreciate an asset leased under a finance lease in accordance with Section 11 *Property, plant and equipment and Investment property*.

19.15 A lessee shall assess at each balance date whether an asset leased under a finance lease is impaired in accordance with Section 16 *Impairment of Assets*.

Financial statements of lessees – operating leases

Recognition and measurement

19.16 A lessee shall recognise lease payments under operating leases (excluding costs for services such as insurance and maintenance) as an expense in profit or loss on a straight-line basis.

19.17 Lease inducements are an inseparable part of the lease agreement and, accordingly, are accounted for as reductions of the lease expense over the term of the lease.

Financial statements of lessors – finance leases

Initial recognition and measurement

19.18 A lessor shall recognise assets held under a finance lease in the Balance sheet and present them as a receivable at an amount equal to the net investment in the lease. The net investment in a lease is the lessor's gross investment in the lease discounted at the interest rate implicit in the lease. The gross investment in the lease is the aggregate of:

(a) the minimum lease payments receivable by the lessor under a finance lease; and

(b) any unguaranteed residual value accruing to the lessor.

Subsequent measurement

19.19 The recognition of finance revenue shall be based on a pattern reflecting a constant periodic rate of return on the lessor's net investment in the finance lease. Lease payments relating to the period, excluding costs for services, are applied against the gross investment in the lease to reduce both the principal and the unearned finance revenue.

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Financial statements of lessors – operating leases

Initial recognition and measurement

19.20 A lessor shall present assets subject to operating leases in the Balance sheet according to the nature of the asset.

19.21 A lessor shall recognise lease revenue from operating leases (excluding amounts for services such as insurance and maintenance) in profit or loss on a straight-line basis over the lease term.

19.22 A lessor shall depreciate an asset leased under an operating lease in accordance with Section 11 *Property, plant and equipment and Investment property.*

19.23 A lessor shall assess at each balance date whether an asset leased under an operating lease is impaired in accordance with Section 16 *Impairment of Assets*.

Disclosures

Financial statements of lessees – finance leases

19.24 A lessee shall make the following disclosures for finance leases, in the notes to the financial statements:

(a) for each class of asset, the net carrying amount at the end of the reporting period;

(b) the total of future minimum lease payments at the end of the reporting period, for each separate class of asset and each of the following periods:

(i) not later than one year; and

(ii) later than one year.

Financial statements of lessees – operating leases

19.25 A lessee shall make the following disclosures for operating leases, in the notes to the financial statements:

(a) the total of future minimum lease payments under non-cancellable operating leases, for each of the following periods:

(i) not later than one year; and

(ii) later than one year; and

(b) lease payments recognised as an expense.

Financial statements of lessors – finance leases

19.26 A lessor shall make the following disclosures for finance leases, in the notes to the financial statements:

(a) the gross investment in finance leases, disclosed in the financial statements together with the related unearned finance revenue and unguaranteed residual value of leased assets; and

(b) the gross investment in the lease and the present value of minimum lease payments receivable at the end of the reporting period, for each of the following periods:

(i) not later than one year; and

(ii) later than one year.

Financial statements of lessors – operating leases

19.27 A lessor shall disclose the following for operating leases, in the notes to the financial statements:

(a) the future minimum lease payments under non-cancellable operating leases for each of the following periods:

(i) not later than one year; and

(ii) later than one year.

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19.28 A lessor shall state in the notes to the financial statements that obligations relating to make-good provisions will not be recognised in the financial statements until such costs have been incurred and are payable ie until the liability has crystallised. Refer to paragraph 11.16.

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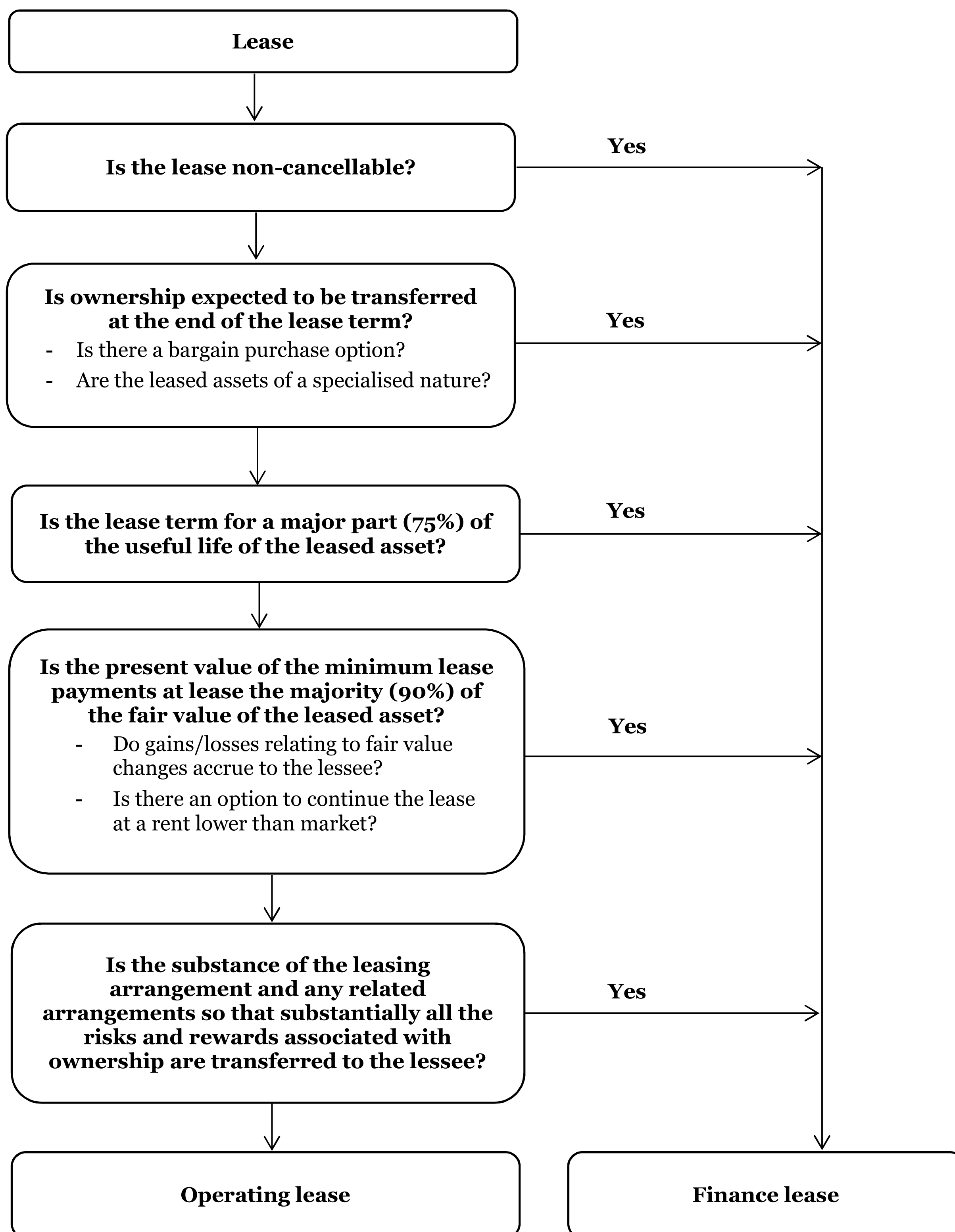
Appendix to Section 19

This flow chart is to assist an entity with the classification of as lease as either a finance lease for which the criteria are outlined in paragraphs 19.5 – 19.8, or as an operating lease.



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Section 20 Foreign currency translation

Purpose and scope of section

20.1 This section establishes principles for accounting for foreign currency transactions and the translation of assets and liabilities denominated in foreign currencies at balance date.

20.2 *SPFR for FPEs* assumes the reporting entity prepares financial statements in New Zealand dollars.

Reporting foreign currency transactions

Initial recognition

20.3 An entity shall record a foreign currency transaction, on initial recognition in the functional currency, by applying to the foreign currency amount the spot rate of exchange between the functional currency and the foreign currency at the date of the transaction.

20.4 Where, due to system limitations, it is not possible for an entity to apply the spot rate on initial recognition at the date of the transaction, an entity may opt to record a foreign currency transaction at the spot rate on the settlement date, that is the date on which transfer of cash or assets is completed.

20.5 The date of a transaction is the date on which the transaction first qualifies for recognition in accordance with *SPFR for FPEs*. For practical reasons, a rate that approximates the actual rate at the date of the transaction is often used; for example, an average rate for a week or a month might be used for all transactions in each foreign currency occurring during that period.

20.6 Foreign exchange rates as provided by the Inland Revenue for tax purposes are also allowed to be used in determining the spot rate and closing rate.

Reporting at the end of subsequent reporting periods

20.7 At the end of each reporting period, an entity shall:

(a) translate foreign currency monetary items using the closing rate;

(b) translate non-monetary items that are measured in terms of historical cost in a foreign currency using the exchange rate at the date of transaction; and

(c) translate non-monetary items that are measured at fair value in a foreign currency using the exchange rate at the date when the fair value was determined.

20.8 An entity shall recognise in profit or loss in the period which they arise, exchange differences arising on the settlement of monetary items or on translating monetary items at rates different from those at which they were translated on initial recognition during the period or in previous periods.

Disclosures

Profit or loss

20.9 The amount of exchange difference gains or losses recognised in profit or loss.

Notes to the financial statements

20.10 An entity shall disclose the currency in which the financial statements are presented.

20.11 An entity shall disclose whether a foreign currency transaction was translated using the spot rate on the date of the transaction, or on the settlement date.

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Section 21 Income taxes

Purpose and scope of section

21.1 This section establishes principles for the initial recognition, subsequent measurement and disclosure of income tax. For the purpose of this section, income tax includes all domestic and foreign taxes that are based on taxable profits.

Accounting policy choice

21.2 An entity is required to make an accounting policy choice to account for income taxes using either:

(a) the taxes payable method; or

(b) the deferred income tax method.

21.3 Under the taxes payable method, income tax expense in respect of the current period is equal to the income tax payable based on the net profit or loss before tax for the current period, calculated in accordance with the rules established by the taxation authorities.

21.4 Under the deferred tax method, income tax is considered to be an expense incurred by the entity in earning revenue and is recognised in the same period as the revenue and expense to which it relates. The income tax effects of temporary differences are included in the income tax expense (benefit) in the Statement of profit or loss and in deferred tax balances in the Balance sheet.

21.5 *SPFR for FPEs* encourages the use of the taxes payable method. However, if an entity chooses the deferred income tax method, then it shall step up to NZ IAS 12 *Income Taxes*.

Recognition and measurement under the taxes payable method

21.6 An entity shall recognise a current liability for the tax payable on taxable profit for the current and past periods. If the amount paid for the current and past period exceeds the amount payable for those periods, a current asset is recognised.

21.7 An entity shall measure a current tax liability (asset) at the amount it expects to pay (recover) using the tax rates and laws that have been enacted or substantially enacted at the balance date.

Unused tax losses

21.8 Under the taxes payable method an asset is not recognised for the carry forward of unused tax losses available to be used in reducing future taxable profits. Therefore the tax expense reported when an entity reports a taxable loss for the year will be nil.

Unusable overseas tax credits

21.9 In the event an entity has forfeited overseas tax credits, the unusable overseas tax credits shall be recognised in profit or loss and disclosed separately in the tax expense for the period.

Imputation credits

21.10 Imputation credits are credits attached to the gross amount of cash dividends.

21.11 Dividends received may be recognised as revenue net or gross of imputation credits.

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Disclosures under the taxes payable method

Profit or loss

21.12 The income tax expense for the period shall be reported on the face of the Statement of profit or loss after the net operating profit or loss before tax.

Accounting policy

21.13 An entity shall disclose in the statement of accounting policies that it has used the taxes payable method to account for income taxes.

Notes to the financial statements

21.14 The following should be disclosed in the notes to the financial statements:

(a) the current tax expense;

(b) any adjustments to prior period income tax expense calculations recognised in the current period;

(c) a reconciliation of net profit or loss before tax to the tax expense for the period and explanation of the reconciling items; and

(d) the balance of unused tax losses at balance date.

21.15 Where the entity is being reviewed by or in dispute with the tax authorities and the outcome is unknown at balance date, this fact along with a brief description of the nature of the review or dispute along with any other relevant information should be disclosed in the notes to the financial statements.

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Section 22 Share-based payments

Purpose and scope of section

22.1 This section establishes principles for accounting for a share-based payment arrangement. In particular, it requires an entity to disclose the key terms of any share-based payment arrangement. It does not, however, require the recognition or measurement of the share-based payment arrangement.

22.2 A share-based payment arrangement is “an agreement between the entity and another party (including an employee) that entitles the other party to receive:

(a) cash or other assets of the entity for amounts that are based on the price (or value) of equity instruments (including shares or share options) of the entity or another group entity; or

(b) equity instruments (including shares or share options) of the entity or another group entity;

That are subject to the fulfilment of specified future conditions.

22.3 Share-based payment arrangements include three types of share-based payment transactions:

(a) equity-settled share-based payment transactions, in which the entity receives goods or services as consideration for equity instruments of the entity (including shares or share options);

(b) cash-settled share-based payment transactions, in which the entity acquires goods or services by incurring liabilities to the supplier of those goods or services (including employees) for amounts that are based on the price (or value) of the entity’s shares or other equity instruments of the entity; and

(c) transactions in which the entity receives or acquires goods or services and the terms of the arrangement provide either the entity or the supplier of those goods or services with a choice of whether the entity settles the transaction in cash (or other assets) or by issuing equity instruments.

22.4 Cash-settled share-based payment transactions include share appreciation rights. For example, an entity might grant share appreciation rights to employees as part of their remuneration package, whereby the employees will become entitled to a future cash payment (rather than an equity instrument), based on the increase in the entity’s share price from a specified level over a specified period of time. Or an entity might grant to its employees a right to receive a future cash payment by granting to them a right to shares (including shares to be issued upon the exercise of share options) that are redeemable, either mandatorily (eg upon cessation of employment) or at the employee’s option.

22.5 An entity shall not apply this section to transactions in which the entity acquires goods or services as part of the net assets acquired in a business combination, as defined in Section 23 *Business combinations*. Hence, equity instruments issued in a business combination in exchange for control of the acquiree are not within the scope of this section.

22.6 For the purposes of this section, a transaction with an employee (or other party) in their capacity as a holder of equity instruments of the entity is not a share-based payment transaction. For example, if an entity grants all holders of a particular class of its equity instruments the right to acquire additional equity instruments of the entity at a price that is less than the fair value of those equity instruments, and an employee receives such a right because they are a holder of equity instruments of that particular class, the granting or exercise of that right is not subject to the requirements of this section.

Disclosures

22.7 An entity shall disclose a description of each type of share-based payment arrangement that existed at any time during the period, including the general terms and conditions of each arrangement, such as vesting requirements, the maximum term of options granted, and the

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method of settlement (eg whether in cash or equity). An entity with substantially similar types of share-based payment arrangements may aggregate this information.

22.8 An entity shall also disclose the number and weighted average exercise price of share options:

(a) outstanding at the beginning of the period;

(b) granted during the period;

(c) forfeited during the period;

(d) exercised during the period;

(e) expired during the period;

(f) outstanding at the end of the period; and

(g) exercisable at the end of the period.

22.9 For cash-settled share-based payment arrangements, an entity shall disclose information about how the liability was measured in addition to the actual cash payment date if this date is able to be determined. For share options exercised during the period, the weighted average share price at the exercise date shall be disclosed.

22.10 For share-based payment arrangements that were modified during the period, an entity shall disclose an explanation of those modifications.

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Section 23 Business combinations

Purpose and scope of section

23.1 This section establishes principles for the initial recognition, subsequent measurement and disclosure of business combination transactions. In particular it covers how the acquirer of a business:

(a) recognises and measures in its financial statements the identifiable assets and liabilities acquired;

(b) recognises and measures the goodwill acquired in the business combination or the gain from a bargain purchase;

(c) identifies combinations of entities under common control; and

(d) determines what information to disclose to enable the users of the financial statements to evaluate the nature and financial effects of the business combination.

23.2 This section applies to a transaction or other event that meets the definition of a business combination and does not apply to:

(a) the formation of an unincorporated joint venture;

(b) the acquisition of a subsidiary; or

(c) the acquisition of an asset, or group of assets, that does not constitute a business;

(d) the aggregation or consolidation of multiple entities.

23.3 A business combination is an integrated set of activities and assets that is capable of being conducted and managed for the purpose of providing a return in the form of dividends, lower costs, or other economic benefits directly to investors or other owners, members, or participants.

23.4 A business combination may be structured in a variety of ways for legal, taxation or other reasons. It may involve the purchase by an entity of the equity of another entity, the purchase of all the net assets of another entity, the assumption of the liabilities of another entity, or the purchase of some of the net assets of another entity that together form one or more businesses.

Accounting for business combinations

23.5 All business combinations shall be accounted for by applying the acquisition method. Applying the acquisition method involves the following steps:

(a) identifying an acquirer;

(b) determining the acquisition date;

(c) measuring the cost of the business combination; and

(d) allocating, at the acquisition date, the cost of the business combination to the assets acquired and liabilities provision assumed.

Identifying the acquirer

23.6 An acquirer shall be identified for all business combinations. The acquirer is the entity that obtains control in a business combination.

23.7 Although it may sometimes be difficult to identify an acquirer, there are usually indications that one exists. For example:

(a) if the fair value of one of the combining entities is significantly greater than that of the other combining entity, the entity with the greater fair value is likely to be the acquirer;

(b) if the business combination is effected through an exchange of voting ordinary equity instruments for cash or other assets, the entity giving up cash or other assets is likely to be the acquirer; or

(c) if the business combination results in the management team of one of the combining entities being able to dominate the selection of the management team of the resulting

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combined entity, the entity whose management team is able to so dominate is likely to be the acquirer.

Determining the acquisition date

23.8 The acquisition date is the date in which the acquirer obtains control of the acquiree.

23.9 The date the acquirer obtains control of the acquiree is generally the date the acquirer legally transfers the consideration, acquires the assets, and assumes the liabilities of the acquiree, the closing date. However, the acquirer might obtain control on a date that is either earlier or later than the closing date. For example, the acquisition date precedes the closing date if a written agreement provides that the acquirer obtains control of the acquiree on a date before the closing date. An acquirer should consider all pertinent facts and circumstances in identifying the acquisition date.

Measuring the cost of a business combination

23.10 The acquirer shall measure the cost of a business combination as the aggregate of:

(a) the fair value, at the date of exchange, of assets given, liabilities assumed, and equity instruments issued by the acquirer, in exchange for control of the acquiree; and

(b) any costs directly attributable to the business combination.

23.11 When a business combination agreement provides for contingent consideration based on future events, the acquirer shall include the estimated amount of that adjustment in the cost of the combination at the acquisition date if the adjustment is probable and can be measured reliably.

23.12 However, if the contingent consideration is not recognised at the acquisition date but subsequently becomes probable and can be measured reliably, the additional consideration shall be treated as an adjustment to the cost of the combination in the subsequent reporting period.

Allocating the cost of a business combination to identifiable assets and liabilities acquired

23.13 The acquirer shall, at the acquisition date, allocate the cost of a business combination by recognising the acquiree's identifiable assets and liabilities at their fair value at that date.

23.14 Any difference between the cost of the business combination and the acquirer's interest in the net fair value of the identifiable assets and liabilities shall be recognised as goodwill or negative goodwill.

23.15 The acquirer shall recognise separately the acquiree's identifiable assets and liabilities at the acquisition date only if they satisfy the following criteria at that date:

(a) in the case of any assets, it is probable that any associated future economic benefits will flow to the acquirer, and its fair value can be measured reliably; and

(b) in the case of any liabilities, it is probable that an outflow of resources will be required to settle the obligation, and its fair value can be measured reliably.

23.16 An asset is identifiable if it either:

(a) is separable (that is, capable of being separated or divided from the entity and sold, transferred, licensed, rented, or exchanged, either individually or together with a related contract, identifiable asset, or liability, regardless of whether the entity intends to do so); or

(b) arises from contractual or other legal rights, regardless of whether those rights are transferable or separable from the entity or from other rights and obligations.

23.17 An acquirer shall recognise separately only the identifiable assets and liabilities of the acquiree that existed at the acquisition date and satisfy the recognition criteria in paragraph 23.15. Therefore:

(a) the acquirer shall recognise liabilities for terminating or reducing the activities of the acquiree as part of allocating the cost of the combination only when the acquiree has,

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at the acquisition date, an existing liability for restructuring recognised in accordance with Section 18 *Provisions and Contingencies*; and

(b) the acquirer, when allocating the cost of the combination, shall not recognise liabilities for future losses or other costs expected to be incurred as a result of the business combination.

23.18 In addition, to qualify for recognition as part of applying the acquisition method, the identifiable assets acquired and liabilities assumed must be part of what the acquirer and the acquiree (or its former owners) exchanged in the business combination transaction rather than the result of separate transactions.

23.19 If the initial accounting for a business combination is incomplete by the end of the reporting period in which the combination occurs, the acquirer shall recognise in its financial statements provisional amounts for the items for which the accounting is incomplete. Within twelve months after the acquisition date, the acquirer shall retrospectively adjust the provisional amounts recognised as assets and liabilities at the acquisition date (ie account for them as if they were made at the acquisition date) to reflect new information obtained. Beyond twelve months after the acquisition date, adjustments to the initial accounting for a business combination shall be recognised only to correct an error in accordance with Section 8 *Accounting policies, Estimates and Errors*.

Goodwill

Measurement of goodwill on acquisition

23.20 Goodwill is the excess of the cost of the business combination over the acquirer's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities recognised in a business combination.

23.21 The acquirer shall, at the acquisition date:

(a) recognise goodwill acquired in a business combination as an asset; and

(b) initially measure that goodwill at its cost

Measuring goodwill after initial recognition

23.22 After initial recognition, the acquirer shall measure goodwill acquired in a business combination at either:

(a) cost less accumulated impairment losses, whereby goodwill is reviewed annually for impairment in accordance with Section 16 *Impairment of Assets*; or

(b) goodwill can be written off on a straight line basis over ten years and recognised in profit or loss.

Negative goodwill (bargain purchase)

23.23 If the acquirer's interest in the net fair value of the identifiable assets, liabilities and provisions for contingent liabilities recognised in accordance with 23.15 exceeds the cost of the business combination, the acquirer shall:

(a) reassess the identification and measurement of the acquiree's assets, liabilities and the measurement of the cost of the combination; and

(b) recognise immediately in profit or loss any excess remaining after that reassessment.

Combinations of entities under common control

23.24 A business combination involving entities or businesses under common control is a business combination in which all of the combining entities or businesses are ultimately controlled by the same party or parties both before and after the business combination, and that control is not transitory.

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23.25 Examples of common control transactions:

(a) an entity establishes a newly formed entity and then transfers some or all of its net assets to that new entity;

(b) a parent transfers the net assets of a wholly owned subsidiary into the parent and liquidates the subsidiary;

(c) a limited liability company is formed by combining entities under common control; and

(d) an amalgamation.

Recognition

23.26 When accounting for a transfer of assets or exchange of shares between entities under common control, the entity that receives the net assets or the equity interests should initially recognise the assets and liabilities transferred at the date of transfer.

Measurement

23.27 When accounting for a transfer of assets or exchange of shares between entities under common control, the entity that receives the net assets or the equity interests should initially measure the assets and liabilities transferred at their carrying amount in the financial statements of the transferring entity at the date of transfer. The corresponding increase in net assets as a result of the common control transfers shall be recognised directly in equity.

Disclosures

23.28 For each business combination and common control transaction that was effected during the period, the acquirer shall disclose the following:

(a) the names and descriptions of the combining businesses;

(b) the details of the assets acquired, disclosed by asset class;

(c) the acquisition date; and

(d) the accounting treatment of goodwill chosen under paragraph 23.22.

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Section 24 Events after balance date

Purpose and scope of section

24.1 This section establishes principles for accounting for events that occur after balance date.

24.2 Events that occur after balance date are those events, favourable and unfavourable, that occur between the end of the reporting period and the date when the financial statements are authorised for issue. There are two types of events:

(a) adjusting events – those that provide evidence of conditions that existed at the end of the reporting period; and

(b) non-adjusting events – those that are indicative of conditions that arose after the end of the reporting period.

Recognition and measurement

Adjusting events

24.3 An entity shall adjust the amounts recognised in its financial statements, including related disclosures, to reflect adjusting events.

24.4 The following are examples of adjusting events that require an entity to adjust the amounts recognised in its financial statements, or to recognise items that were not previously recognised:

(a) the settlement after the end of the reporting period of a court case that confirms that the entity had a present obligation at the end of the reporting period. The entity adjusts any previously recognised provision related to this court case in accordance with Section 18 *Provisions and Contingencies* or recognises a new provision. The entity does not merely disclose a contingent liability. Rather, the settlement provides additional evidence to be considered in determining the provision that should be recognised;

(b) the receipt of information after the end of the reporting period indicating that an asset was impaired at the end of the reporting period, or that the amount of a previously recognised impairment loss for that asset needs to be adjusted (see Section 16 *Impairment of Assets)*. For example, the bankruptcy of a customer that occurs after the end of the reporting period usually confirms that a loss existed at the end of the reporting period on a trade receivable and that the entity needs to adjust the carrying amount of the trade receivable;

(c) the determination after the end of the reporting period of the amount of profit-sharing or bonus payments, if the entity had a legal or constructive obligation at the end of the reporting period to make such payments as a result of events before that date (see Section 26 *Employee benefits*); or

(d) the discovery of fraud or errors that show that the financial statements are incorrect.

Non-adjusting events

24.5 An entity shall not adjust the amounts recognised in its financial statements to reflect non-adjusting events.

24.6 Examples of non-adjusting events after the end of the reporting period include a decline in market value of investments between the end of the reporting period and the date when the financial statements are authorised for issue. The decline in market value does not normally relate to the condition of the investments at the end of the reporting period, but reflects circumstances that have arisen subsequently.

Dividends

24.7 If an entity declares dividends to holders of its equity instruments after the end of the reporting period, the entity shall not recognise those dividends as a liability at the end of the reporting period.

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Disclosures

Date of authorisation for issue

24.8 An entity shall disclose the date when the financial statements were authorised for issue and who gave that authorisation. If the entity's owners or others have the power to amend the financial statements after issue, that fact shall be disclosed.

Non-adjusting events after the end of the reporting period

24.9 An entity shall disclose the following for each category of non-adjusting event:

(a) the nature of the event; and

(b) an estimate of its financial effect, or a statement that such an estimate cannot be made.

24.10 The following are examples of non-adjusting events after the end of the reporting period that would generally result in disclosure. The disclosures will reflect information that becomes known after the end of the reporting period but before the financial statements are authorised for issue:

(a) a major business combination or disposal of a major subsidiary;

(b) announcement of a plan to discontinue an operation;

(c) major purchases of assets, disposals or plans to dispose of assets;

(d) the destruction of a major production plant by a natural disaster;

(e) announcement, or commencement of the implementation, of a major restructuring;

(f) issues or repurchases of an entity's debt or equity instruments;

(g) entering into significant commitments or contingent liabilities; or

(h) commencement of major litigation arising solely out of events that occurred after the end of the reporting period.

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Section 25 Related party transactions

Purpose and scope of section

25.1 This section requires an entity to include in its financial statements the disclosures necessary to draw attention to the possibility that its financial performance or financial position have been affected by the existence of related parties and by transactions and outstanding balances with such parties.

25.2 Disclosure of certain related party transactions and the relationship underlying those transactions is necessary for accounting purposes, and enables users to better understand the entity's financial performance and financial position. This is because:

(a) related party relationships can influence the way in which an entity operates with other entities;

(b) related party relationships might expose an entity to risks, or provide opportunities that would not have existed in the absence of the relationship; and

(c) related parties may enter into transactions that unrelated parties may not enter into, or may agree to transactions on terms and conditions that differ from those that would normally be available to unrelated parties.

Related party defined

25.3 Entities generally enter into transactions on an arm's length basis, the interests of each party being completely independent. However, transactions often take place between parties who, because of their relationship, are not independent of one another – a related party relationship.

25.4 Parties are considered to be related if one party has the ability, directly or indirectly, to control or exercise significant influence over the other party in making operating, investing and financing decisions to the extent that one of the parties might be prevented from fully pursuing its own separate interests. Parties are also considered to be related when they are subject to common outside control or significant influence.

25.5 Related parties include:

(a) other entities that control, or are controlled by, the entity;

(b) other entities or individuals that have significant influence over the entity, including close members of the family or any such individual; and

(c) the entity's governance personnel (whether employed or volunteer), and close members of their families.

25.6 Governance personnel are people involved in the decision-making process about the strategy of the entity. Parties are not considered related parties if they are involved in the day-to-day running of the entity but have no involvement in making decisions about the strategy of the entity.

25.7 In considering each possible related party relationship, an entity shall assess the substance of the relationship and not merely the legal form.

Disclosures

Parent-subsidiary relationships

25.8 Relationships between a parent and its subsidiaries shall be disclosed irrespective of whether there have been related party transactions.

25.9 An entity shall disclose the name of its parent and, if different, the ultimate controlling party (if applicable).

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Related party transactions

25.10 An entity shall disclose in the notes to the financial statements transactions with a related party that have been incurred in the year, when and only when:

(a) the transaction is significant to the entity (individually or in aggregate with similar transactions); or

(b) the transaction is on terms and conditions that are likely to be different from the terms and conditions of transactions in similar circumstances between parties that are not related.

25.11 An entity shall report the following information for each significant transaction with a related party, including those with governance personnel:

(a) a description of the related party relationship;

(b) a description and the amounts of the transactions during the financial year (ie transactions reported within the Statement of profit or loss); and

(c) any payments due from or to related parties at balance date (ie balances reported within the Balance sheet).

25.12 When significant payments due from or to related parties are on terms that are different from the terms and conditions of transactions in similar circumstances between parties that are not related, those terms shall be disclosed.

25.13 The following are examples of transactions that shall be disclosed if they are with a related party:

(a) purchases or sales of goods;

(b) purchases or sales of property and other assets;

(c) rendering or receiving of services;

(d) leases; and

(e) loans advanced or borrowings.

25.14 In some instances there will be a clear indication that the parties are related even if they do not strictly meet the definition of a related party as outlined in paragraphs 25.3 – 25.7. The definition of a related party should be interpreted in the widest possible sense, and in considering each possible related party relationship, an entity should assess the substance of the relationship and not merely the legal form.

25.15 In order to meet the Inland Revenue minimum financial reporting requirements, entities shall also maintain a reconciliation of moments in current accounts and loan balances with owners and other associated persons (as defined by subpart YB of the Income Tax Act 2007). The reconciliations are not required to be disclosed as part of the financial statements but may be maintained in a separate schedule for disclosure to Inland Revenue on request.

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Section 26 Employee benefits

Purpose and scope of section

26.1 This section establishes principles for the initial recognition, subsequent measurement and disclosure of employee benefits.

26.2 Employee benefits are all forms of consideration given by an entity in exchange for service rendered by employees, including directors and management. Employee benefits covered by this section include:

- (a) short-term employee benefits, which are employee benefits (other than termination benefits) that are wholly due within twelve months after the end of the period in which the employees render the related services;
- (b) long-term employee benefits, which are employee benefits (other than termination benefits) that are not wholly due within twelve months after the end of the period in which the employees render the related services; and
- (c) termination benefits which are employee benefits payable as a result of either:
  - (i) an entity's decision to terminate an employee's employment before the normal retirement date; or
  - (ii) an employee's decision to accept voluntary redundancy in exchange for those benefits.
- (d) defined contribution plans (for example KiwiSaver).

26.3 A post-employment benefit in the form of a defined benefit plan is out of scope of this section. Entities involved in these types of arrangements, should step up to NZ IAS 19 *Employee Benefits*.

General recognition principle

26.4 An entity shall recognise the cost of all employee benefits to which its employees have become entitled as a result of service rendered to the entity during the reporting period:

- (a) as a liability, after deducting amounts that have been paid to the employees. If the amount paid exceeds the obligation arising from service before the balance date, an entity shall recognise that excess as an asset to the extent that the prepayment will lead to a reduction in future payments or a cash refund; or
- (b) as an expense, unless another section of *SPFR for FPEs* requires the cost to be recognised as part of the cost of an asset such as inventories or property, plant and equipment.

Short-term employee benefits

26.5 Examples of short-term employee benefits are:

- (a) salaries and wages;
- (b) annual leave (holiday pay) entitlements;
- (c) profit-sharing and bonuses payable within twelve months after the end of the period in which the employees render the related service; and
- (d) non-monetary benefits (such as medical care, housing, cars and free or subsidised goods or services) for current employees.

Annual leave entitlements

26.6 When an employee has rendered services to an entity during the reporting period, short-term employee benefits expected to be paid in exchange for those services shall be recognised in accordance with paragraph 26.4.

26.7 An entity shall recognise the expected cost of accumulated annual leave (holiday pay) entitlements when the employees carry out services that increase their entitlement. The entity

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shall measure the expected cost of annual leave entitlements at the undiscounted additional amount that the entity expects to pay as a result of the unused entitlement that has accumulated at the end of the reporting period. The entity shall present this amount as a current liability at the balance date.

Profit-sharing and bonus plans

26.8 An entity shall recognise the expected cost of profit-sharing and bonus payments only when:

(a) the entity has a present legal or constructive obligation to make such payments as a result of past events (this means that the entity has no realistic alternative but to make the payments); and

(b) a reliable estimate of the obligation can be made.

Other long-term employee benefits

26.9 A liability for long-term employee benefits shall be recognised when it is probable that the entity will be required to provide the entitlement and recognised over the periods in which the related services are provided. The liability is measured based on current salaries. No discounting for the time value of money is permitted.

26.10 Other long-term employee benefits include, for example:

(a) long service leave;

(b) profit-sharing and bonuses payable twelve months or more after the end of the period in which the employees render the related service; and

(c) deferred compensation paid twelve months or more after the end of the period in which it is earned.

Termination benefits

Recognition

26.11 An entity shall recognise termination benefits as a liability and an expense only when the entity is demonstrably committed either:

(a) to terminate the employment of an employee or group of employees before the normal retirement date; or

(b) to provide termination benefits as a result of an offer made in order to encourage voluntary redundancy and voluntary redundancy has been accepted by the employees.

26.12 An entity is demonstrably committed to a termination only when the entity has a detailed formal plan for the termination and is without realistic possibility of withdrawal from the plan.

Measurement

26.13 An entity shall measure termination benefits at the best estimate of the expenditure that would be required to settle the obligation at the balance date. In the case of an offer made to encourage voluntary redundancy, the measurement of termination benefits shall be based on the number of employees who have accepted the offer at the balance date.

Disclosures

26.14 The total liability in relation to accrued employee entitlements shall be disclosed in the notes to the financial statements, appropriately allocated between current and non-current liabilities based on when the entitlement is expected to be settled.

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Section 27 Goods and Services Tax

Purpose and scope of section

27.1 This section establishes the accounting treatment of Goods and Services Tax (GST).

27.2 In this section, the terms “exempt”, “input tax”, “supply”, “goods”, “person”, “registered person”, “services”, and “taxable activity” have the same meaning as defined in the Goods and Services Tax Act 1985.

27.3 GST in New Zealand is designed to be a broad based system with few exemptions. Exemptions that do exist include rents collected on residential rental properties, donations, precious metals and financial services. Entities pay GST on all liable goods and services directly, in that the purchase price of goods and services includes GST.

Recognition and measurement

27.4 Except where paragraph 27.5 applies, this section requires an entity to state all revenue and expenses, assets and liabilities (except for accounts receivable and accounts payable) net of GST.

27.5 Irrecoverable GST input tax shall be recognised as part of the related asset or, where the expenditure relates to an expense item, expensed. Registered persons providing exempt supplies or services, and all persons other than registered persons, incur irrecoverable GST on their related inputs. For these persons this irrecoverable GST increases the costs of the goods and services they supply. In such instances, GST shall be included in these costs or, where it relates to expense items, as an expense. In particular and in these circumstances, GST on non-current assets is to be included in the purchase cost of the fixed assets concerned.

Disclosures

27.6 An entity shall disclose in its statement of accounting policies its GST registration status, and the basis it has used to account for GST (being either exclusive, or for non-registered persons inclusive).

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Glossary of Terms

accrual basis of accounting	The effects of transactions and other events are recognised when they occur (and not as cash or its equivalent when it is received or paid) and they are recorded in the accounting records and reported in the financial statements of the periods to which they relate.
active market	A financial instrument is regarded as quoted in an active market if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service (eg Reuters and Bloomberg), or regulatory agency, and those prices represent actual and regularly occurring market transactions on an arm's length basis. For example the quoted price from the New Zealand stock exchange.
agricultural activity	The management by an entity of the biological transformation of biological assets for sale into agricultural produce or into additional biological assets. The processing of agricultural produce after harvest is excluded from the definition of agricultural activity.
agricultural produce	The harvested product of the entity's biological assets.
amortisation	The systematic allocation of the depreciable amount of an asset over its useful life.
amortised cost	The amount at which a financial asset or financial liability is measured at initial recognition minus principal repayments, plus or minus the cumulative amortisation using the effective interest method, of any difference between that initial amount and the maturity amount, and minus any reduction (directly or through the use of an allowance account) for impairment or uncollectibility.
arm's length transaction	A transaction in which the buyers and sellers of a product act independently and have no relationship to each other. The concept of an arm's length transaction is to ensure that both parties in the deal are acting in their own self-interest are not subject to any pressure or duress from the other party.
associate	An entity, including an unincorporated entity such as a partnership, over which the investor has significant influence and that is neither a subsidiary nor an interest in a joint venture.
bearer biological assets	Biological assets predominantly used in the production or supply of agricultural produce to others and are expected to be used for more than one period.
biological asset	An asset that consists of a living animal or plant. Grass or other pasture grown on agricultural land is excluded from the definition of a biological asset.
biological transformation	The processes of growth, degeneration, production, and procreation that causes qualitative or quantitative changes in a biological asset.
bonus issue	The issue of new shares to shareholders in proportion to their existing holdings, otherwise known as capitalisation. For example, an entity may give its shareholders one dividend or bonus share for every five shares held.
business	An integrated set of activities and assets conducted and managed for the purpose of providing: (a) return to investors; or

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(b) lower costs or other economic benefits directly and proportionately to policyholders or participants.

A business generally consists of inputs, processes applied to those inputs, and resulting outputs that are, or will be, used to generate revenues. If goodwill is present in a transferred set of activities and assets, the transferred set shall be presumed to be a business.

business combination The bringing together of separate entities or businesses into one reporting entity.

cash and short term deposits Short-term highly liquid investments held to meet short-term cash commitments rather than for investment or other purposes. An investment normally qualifies as a cash and cash and short term deposit only when it has a short maturity of, say, three months or less from the date of acquisition.

change in accounting estimate An adjustment of the carrying amount of an asset or a liability, or the amount of the periodic consumption of an asset, that results from the assessment of the present status of, and expected future benefits and obligations associated with, assets and liabilities. Changes in accounting estimates result from new information or new developments and, accordingly, are not corrections of errors.

closing rate The exchange rate on the balance date of the entity reporting.

compound financial instrument A financial instrument that, from the issuer's perspective, contains both a financial liability component and an equity component.

consolidated financial statements The financial statements of a parent and its subsidiaries presented as those of a single economic entity.

construction contract A contract specifically negotiated for the construction of an asset or a combination of assets that are closely interrelated or interdependent in terms of their design, technology and function or their ultimate purpose or use.

constructive obligation An obligation that derives from an entity's actions where:

(a) by an established pattern of past practice, published policies or a sufficiently specific current statement, the entity has indicated to other parties that it will accept certain responsibilities; and

(b) as a result, the entity has created a valid expectation on the part of those other parties that it will discharge those responsibilities.

contingent asset A possible asset that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity.

contingent consideration An obligation of an acquirer to transfer additional assets or equity interests to the former owners of an acquiree as part of the exchange for control of the acquiree if specified future events occur or conditions are met. However, contingent consideration also may give the acquirer the right to the return of previously transferred consideration if specified conditions are met.

contingent liability (a) A possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity; or

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(b) A present obligation that arises from past events but is not recognised because:

  (i) it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation; or

  (ii) the amount of the obligation cannot be measured with sufficient reliability.

control (of an entity) Exposure, or rights, to variable returns from involvement with an entity and the ability to affect those returns through power over the entity.

costs to sell The incremental costs directly attributable to the disposal of an asset, excluding finance costs and income taxes.

current tax The amount of income tax payable (refundable) in respect of the taxable profit (tax loss) for the current period or past reporting periods.

degeneration A process of biological transformation resulting in a decrease in the quantity or deterioration in quality of an animal or plant. For example the death of a sheep.

depreciation The systematic allocation of the depreciable amount of an asset over its useful life.

derivative A contract with all three of the following characteristics:

(a) its value changes in response to the change in a specified interest rate, financial instrument price, commodity price, foreign exchange rate, index of prices or rates, a credit rating or credit index, or other variable (sometimes called the “underlying”), provided that, in the case of a non-financial variable, the variable is not specific to a party to the contract;

(b) it requires no initial net investment or an initial net investment that is smaller than would be required for other types of contracts that would be expected to have a similar response to changes in market factors; and

(c) it is settled at a future date.

development The application of research findings or other knowledge to a plan or design for the production of new or substantially improved materials, devices, products, processes, systems or services before the start of commercial production or use.

employee benefits All forms of consideration given by an entity in exchange for service rendered by employees.

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effective interest method

A method of calculating the amortised cost of a financial asset or a financial liability (or group of financial assets or financial liabilities) and of allocating the interest revenue or interest expense over the relevant period.

The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability.

The effective interest rate is determined on the basis of the carrying amount of the financial asset or liability at initial recognition.

When calculating the effective interest rate, an entity shall estimate cash flows considering all contractual terms of the financial instrument (for example, prepayment, call and similar options) but shall not consider future credit losses.

equity instrument

Any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities.

errors

Omissions from, and misstatements in, the entity's financial statements for one or more prior periods arising from a failure to use, or misuse of, reliable information that:

(a) was available when financial statements for those periods were authorised for issue; and

(b) could reasonably be expected to have been obtained and taken into account in the preparation and presentation of those financial statements.

fair presentation

Faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, revenue and expenses.

fair value

The amount of the consideration that would be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act.

fair value less costs to sell

The amount of consideration obtainable from the sale of an asset in an arm's length transaction between knowledgeable, willing parties, less the costs of disposal. The best evidence of the fair value less costs to sell of an asset is a price in a binding sale agreement in an arm's length transaction or a market price in an active market. If there is no binding sale agreement or active market for an asset, fair value less costs to sell is based on the best information available to reflect the amount that an entity could obtain, at the balance date, from the disposal of the asset in an arm's length transaction between knowledgeable, willing parties, after deducting the costs of disposal. In determining this amount, an entity considers the outcome of recent transactions for similar assets within the same industry.

finance lease

A lease that transfers substantially all the risks and rewards incidental to ownership of an asset. Title may or may not eventually be transferred. A finance lease includes contracts for the hire of assets which contain a provision transferring title to the asset upon the fulfilment of agreed conditions.

financial asset

Any asset that is:

(a) cash;

(b) a contractual right to receive cash or another financial asset from another party;

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(c) a contractual right to exchange financial instruments with another party under conditions that are potentially favourable; or

(d) an equity instrument of another entity.

The cost incurred by an entity to purchase a right to reacquire its own equity instruments from another party is a deduction from its equity, not a financial asset.

financial guarantee contract A contract that requires the issuer to make specific payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the original or modified terms of a debt instrument.

financial instrument A contract that gives rise to a financial asset for one entity and a financial liability or equity instrument for another entity.

financial liability Any liability that is a contractual obligation:

(a) to deliver cash or another financial assets to another party; or

(b) to exchange financial instruments with another party under conditions that are potentially unfavourable to the entity.

Financial Reporting Standard (FRS) Standards created in New Zealand between 1993 and 2002 for application by certain reporting entities (including most entities in the public sector) when preparing their GPFR. The standards were issued by the Financial Reporting Standards Board (FRSB), a committee of the NZICA and approved by the Accounting Standards Review Board (ASRB).

financing fees Amounts that compensate the lender for the risk of providing funds to the borrower. Financing fees, sometimes referred to as fees in lieu of interest, loan fees, or financing costs, include:

(a) fees charged to originate, arrange, or syndicate a loan or debt financing;

(b) commitment, standby, and guarantee fees; and

(c) refinancing, restructuring, and renegotiation fees.

Financing fees may be refundable or non-refundable. Financing fees do not include transaction costs. Integral fees are a subset of financing fees.

firm commitment A binding agreement for the exchange of a specified quantity of resources at a specified price on a specified future date or dates.

for-profit entity An entity that does not meet the definition of a public benefit entity.

foreign currency transaction A transaction that is denominated or requires settlement in a foreign currency, including transactions arising when an entity:

(a) buys or sells goods or services whose price is denominated in a foreign currency;

(b) borrows or lends funds when the amounts payable or receivable are denominated in a foreign currency; or

(c) otherwise acquires or disposes of assets, or incurs or settles liabilities, denominated in a foreign currency.

general purpose financial reports (GPFR) Financial statements directed to the general financial information needs of a wide range of users who are not in a position to demand reports tailored to meet their particular information needs.

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generally accepted accounting practice (GAAP)
A common set of accounting principles, standards and procedures used in the preparation of financial statements. The authoritative standards in New Zealand for for-profit entities are NZ IFRS issued by the New Zealand Accounting Standards Board (NZASB) of the External Reporting Board (XRB).

grant date
The date at which the entity and another entity (including an employee) agree to the terms of conditions of a share-based payment transaction. At the grant date the entity confers on the counterparty the right to cash, other asset, or equity instruments of the entity, provided the specified vesting conditions, if any, are met. If that agreement is subject to an approval process (for example, by shareholders), grant date is the date when that approval is obtained.

gross margin
A measure of profitability which is arrived at by subtracting cost of sales/services, including salaries and wages to staff, from sales/revenue, excluding exceptional items.

gross margin ratio
The gross margin ratio can be calculated as follows:

$$\frac{\text{Revenue}^{6} - \text{Cost of Sales}^{7}}{\text{Revenue}^{8}} \times 100$$

group of assets
More than one asset with similar characteristics.

harvest
The detachment of produce from a biological asset or the cessation of a biological asset's life processes.

herd scheme
A methodology for the valuation of specified livestock prescribed in the Income Tax Act 2007 whereby each income year, herd livestock on hand at both and closing dates are valued at the National Average Market Value announced for that income year by Inland Revenue.

holding gain (or loss)
Unrealised gains (or losses) arising from changes in the value of a unit or group of livestock at balance date. Excluded from this are quantitative (numerical) changes resulting from procreation or degeneration of livestock. For example the increase in value of a herd of sheep between two balance dates, excluding the net increase resulting from births and deaths during that period.

inception (of a lease)
The earlier of the date of the lease agreement and the date of a commitment that is signed by the parties to the lease transaction and includes the principal terms of the lease (this is the effective date used for classification of the lease).

insurance contract
A contract under which one party (the insurer) accepts significant insurance risk from another party (the policyholder) by agreeing to compensate the policyholder if a specified uncertain future event (the insured event) adversely affects the policyholder.

integral fees
Fees that form an integral part of the effective interest rate of a financial instrument and are therefore recognised over the expected life of the instrument, or a shorter period if appropriate. A loan origination fee is an example of an integral fee. Integral fees have the same meaning as contingent fees, as defined in the Income Tax Act 2007.

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[6] Excluding exceptional items.
[7] Including salaries and wages to staff.
[8] Excluding exceptional items.

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Inland Revenue minimum financial reporting requirements	The minimum requirements for the preparation of financial statements prescribed in the Tax Administration (Financial Statements) Order 2014.
interest rate implicit in the lease	The discount rate that causes the aggregate present value of: (a) the minimum lease payments; and (b) the unguaranteed residual value accruing to the benefit of the lessor to be equal to the fair value of the leased property to the lessor at the inception of the lease.
joint control	The contractually agreed sharing of control over an economic activity. It exists only when the strategic financial and operating decisions relating to the activity require the unanimous consent of the parties sharing control (the venturers).
joint venture	A contractual arrangement whereby two or more parties undertake an economic activity that is subject to joint control. Joint ventures can be unincorporated and take the form of a jointly controlled operation or a jointly controlled assets, or they can be incorporated in the form of a jointly controlled entity.
jointly controlled entity	A joint venture that involves the establishment of a corporation, partnership or other entity in which each venture has an interest. The entity operates in the same way as other entities, except that a contractual arrangement between the venturers establishes joint control over the economic activity of the entity.
lease	An agreement whereby the lessor conveys to the lessee in return for a payment or series of payments the right to use an asset for an agreed period of time.
lease inducements	Incentives for a lessee to sign a lease (for example, an upfront cash payment to the lessee, an initial rent-free period or reduced rent payments in early periods, or reimbursement of costs of the lessee, such as moving costs or leasehold improvements).
lease term	The fixed, non-cancellable period of the lease. The lease term is considered to be non-cancellable if cancellation is possible only: (a) upon the occurrence of some unlikely contingency; (b) with permission of the lessor; (c) upon the lessee entering into a new lease for the same or equivalent property with the same lessor; or (d) upon payment by the lessee of a penalty sufficiently large that continuation of the lease appears, at the inception of the lease, reasonably assured.
lessee's rate for incremental borrowing	The interest rate that, at the inception of the lease, the lessee would have incurred to borrow, over a similar term and with similar security for the borrowing, the funds necessary to purchase the leased asset.

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legal obligation	An obligation that derives from: (a) a contract (through its explicit or implicit terms); (b) legislation; or (c) other operation of law.
livestock	Animals farmed or dealt in for profit.
material	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. Materiality depends on the size and nature of the omission or misstatement judged in the surrounding circumstances. The size or nature of the item, or a combination of both, could be the determining factor.
minimum lease payments	(a) From the point of view of the lessee, minimum lease payments comprise: (i) the minimum rental payments called for by the lease over the lease term; and (ii) any penalty required to be paid by the lessee for failure to renew or extend the lease at the end of the lease term. (b) From the point of view of the lessor, minimum lease payments comprise: (i) minimum lease payments for the lessee as described previously; and (ii) any residual value or rental payments beyond the lease term guaranteed by a third party unrelated to either the lessee or lessor, provided that the guarantor is financially capable of discharging the obligations under the guarantee.
monetary items	Units of currency held and assets and liabilities to be received or paid in a fixed or determinable number of units of currency.
National Standard Cost	A methodology for the valuation of specified livestock as prescribed in the Income Tax Act 2007, using entities actual costs for purchased livestock and standard costs published annually by Inland Revenue for livestock that are bred or further reared by the entity.
net realisable value	The estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.
non-monetary items	Assets and liabilities that are not monetary items.
not-for-profit (NFP) entity	An entity that is a public benefit entity but is not a public sector entity.
NZ IFRS	New Zealand equivalents to International Financial Reporting Standards (NZ IFRS). Standards and Interpretations issued by the NZASB of the XRB. They comprise New Zealand Equivalents to: (a) International Financial Reporting Standards (IFRS); (b) International Accounting Standards (IAS); (c) International Financial Reporting Interpretations Committee (IFRIC) Interpretations; and (d) Standard Interpretations Committee (SIC) Interpretations.

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obligating event	An event that creates a legal or constructive obligation that results in an entity having no realistic alternative to settling that obligation.
operating lease	A lease that is not operating lease is a finance lease.
owners	Holders of instruments classified as equity.
parent	An entity that has one or more subsidiaries.
PBE SFR-A (NFP)	Public Benefit Entity Simple Format Reporting – Accrual (Not-for-profit). The Tier 3 accounting standard for PBE NFPs issued by the XRB.
PBE SFR-C (NFP)	Public Benefit Entity Simple Format Reporting – Cash (Not-for-profit). The Tier 4 accounting standard for PBE NFPs issued by the XRB.
presentation currency	The currency in which the financial statements are presented.
primary financial statements	The Balance sheet, Statement of profit or loss, Statement of changes in equity (if presented) and Statement of cash flows (if presented).
procreation	A process of biological transformation resulting in the creation of additional living animals or plants. For example, the birth of a lamb.
provision	A liability of uncertain timing or amount.
public benefit entity (PBE)	An entity whose primary objective is to provide goods or services for community or social benefit and where any equity has been provided with a view to supporting that primary objective rather than for a financial return to equity holders.
public sector entity	An entity that is a public entity as defined by the Public Audit Act 2001, and all Offices of Parliament.
realisable value	The amount of cash or cash equivalents that could currently be obtained by selling an entity's assets in an orderly disposal. Liabilities are recorded at the amount of cash or cash equivalents required to settle the debt in the short term. Anticipated liabilities for future expenses should also be included. (a) it is probable that any future economic benefit associated with the item will flow to or from the entity; and (b) the item has a cost or value that can be measured with reliability.
recoverable amount	An asset's fair value less costs to sell at the balance date.
related party transaction	A transfer of resources, services or obligations between related parties, regardless of whether a price is charged.
research	Original and planned investigation undertaken with the prospect of gaining new scientific or technical knowledge and understanding.
residual value (of an asset)	The estimated amount that an entity would currently obtain from disposal of an asset, after deducting the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life.

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restructuring	A programme that is planned and controlled by an entity, and materially changes either: (a) the scope of a business undertaken by an entity; or (b) the manner in which that business is conducted.
right of set-off[9]	Debtor's legal right, by contract or otherwise, to settle or otherwise eliminate all or a portion of an amount due to a creditor by applying against that amount an amount due from the creditor. In unusual circumstances, a debtor may have a legal right to apply an amount due from a third party against the amount due to a creditor provided that there is an agreement between the three parties that clearly establishes the debtor's right of set-off. Because the right of set-off is a legal right, the conditions supporting the right may vary from one legal jurisdiction to another and the laws applicable to the relationships between the parties need to be considered.
settlement date	The settlement date of a foreign currency transaction refers to the actual day on which transfer of cash or assets is completed.
share-based payment transaction	A transaction in which the entity receives goods or services (including employee services) as consideration for equity instruments of the entity (including shares or share options), or acquires goods or services by incurring liabilities to the supplier of those goods or services for amounts that are based on the price of the entity's shares or other equity instruments of the entity.
share option	A contract that gives the holder the right, but not the obligation, to acquire the entity's shares at a fixed or determinable price for a specified period of time.
share split	The dividing of an entity's existing shares into multiple shares. For example, each shareholder may receive one additional share for each share held. In some cases, the previously outstanding shares are cancelled and replaced by new shares.
specified livestock	Types and classes of livestock as specified in Schedule 17 of the Income Tax Act 2007.
spot rate	The exchange rate for immediate delivery of currencies to be exchanged.
Statement of Standard Accounting Practice (SSAP)	Accounting standards created in New Zealand until 1993 for application by all entities preparing GPFR. The standards were written by the FRSB, a committee of the NZICA.
subsidiary	An entity, including an unincorporated entity such as a partnership that is controlled by another entity (known as the parent).
substantively enacted	Tax rates shall be regarded as substantively enacted when future events required by the enactment process will not change the outcome.
taxable profit (loss)	The profit (loss) for a reporting period upon which income taxes are payable or recoverable, determined in accordance with the rules established by the taxation authorities. Taxable profit equals taxable income less amounts deductible from taxable income.

[9] NZ IAS 32 *Financial Instruments: Presentation*, paragraph 45

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termination benefits Employee benefits payable as a result of either:

(a) an entity's decision to terminate an employee's employment before the normal retirement date; or

(b) an employee's decision to accept voluntary redundancy in exchange for those benefits.

transaction price The amount of consideration paid or received to acquire a financial asset or a financial liability; less deductions for transaction costs.

transaction costs Incremental costs that are directly attributable to the acquisition, issue, or disposal of a financial asset or financial liability. An incremental cost is one that would not have been incurred if the entity had not acquired, issued, or disposed of the financial instrument. Transaction costs include expenditures such as legal fees, reimbursement of the lender's administrative costs, and appraisal costs associated with a loan. Transaction costs do not include financing fees, debt premiums, or discounts. For the avoidance of doubt, contingent fees are considered to be directly attributable.

treasury shares An entity's own equity instruments, held by the entity or other members of the consolidated group.

unguaranteed residual value The portion of the value of the leased asset (estimated at the inception date of the lease), the realisation of which by the lessor, at the expiry of the lease term, is not assured, or is guaranteed only by a party related to the lessor.

useful life The period over which an asset is expected to be available for use by an entity or the number of production or similar units expected to be obtained from the asset by an entity.

vest To become an entitlement. Under a share-based payment arrangement, a counterparty's right to receive cash, other assets or equity instruments of the entity vests when the counterparty's entitlement is no longer conditional on the satisfaction of any vesting conditions.

vested benefits Benefits, the rights to which, under the conditions of a retirement benefit plan, are not conditional on continued employment.

vesting conditions A condition that, under a share-based payment arrangement, determines whether the entity receives the goods or services that entitle the counterparty to receive cash, other assets or equity instruments of the entity.

vesting period The period during which all the specified vesting conditions of a share-based payment arrangement are to be satisfied.

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