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Basis for Conclusions on IAS 34 *Interim Financial Reporting*

This Basis for Conclusions accompanies, but is not part of, IAS 34.

- BC1 This Basis for Conclusions summarises the International Accounting Standards Board's considerations in amending paragraphs 15–18 of IAS 34 *Interim Financial Reporting* as part of *Improvements to IFRSs* issued in May 2010. Those changes aim to emphasise the disclosures principles in IAS 34 and to add further guidance to illustrate how to apply these principles.
- BC2 IAS 34 was developed by the International Accounting Standards Committee (IASC) in 1998 and did not include a Basis for Conclusions.

Significant events and transactions

- BC3 In *Improvements to IFRSs* issued in May 2010, the Board addressed requests for clarification of the disclosures required by IAS 34 when considered against changes in the disclosure requirements of other IFRSs. IAS 34 was issued by the Board's predecessor body, IASC, in 1998. In the light of recent improvements to disclosure requirements, many users of financial statements asked the Board to consider whether particular disclosures required by IFRS 7 *Financial Instruments: Disclosures* for annual financial statements should also be required in interim financial statements. IAS 34 sets out disclosure principles to determine what information should be disclosed in an interim financial report. The Board concluded that amending IAS 34 to place greater emphasis on those principles and the inclusion of additional examples relating to more recent disclosure requirements, ie fair value measurements, would improve interim financial reporting.
- BC4 As part of *Improvements to IFRSs* issued in May 2010, the Board deleted paragraph 18 of IAS 34 because it repeats paragraph 10 of IAS 34 and because the Board's intention is to emphasise those disclosures that are required rather than those that are not required.

Illustrative examples

These illustrative examples accompany, but are not part of, IAS 34.

A Illustration of periods required to be presented

The following examples illustrate application of the principle in paragraph 20.

Entity publishes interim financial reports half-yearly

A1 The entity's financial year ends 31 December (calendar year). The entity will present the following financial statements (condensed or complete) in its half-yearly interim financial report as of 30 June 20X1:

Statement of financial position:

At	30 June 20X1	31 December 20X0
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Statement of comprehensive income:

6 months ending	30 June 20X1	30 June 20X0
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Statement of cash flows:

6 months ending	30 June 20X1	30 June 20X0
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Statement of changes in equity:

6 months ending	30 June 20X1	30 June 20X0
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Entity publishes interim financial reports quarterly

A2 The entity's financial year ends 31 December (calendar year). The entity will present the following financial statements (condensed or complete) in its quarterly interim financial report as of 30 June 20X1:

Statement of financial position:

At	30 June 20X1	31 December 20X0
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Statement of comprehensive income:

6 months ending	30 June 20X1	30 June 20X0
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3 months ending	30 June 20X1	30 June 20X0
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Statement of cash flows:

6 months ending	30 June 20X1	30 June 20X0
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Statement of changes in equity:

6 months ending	30 June 20X1	30 June 20X0
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B Examples of applying the recognition and measurement principles

The following are examples of applying the general recognition and measurement principles set out in paragraphs 28–39.

Employer payroll taxes and insurance contributions

- B1 If employer payroll taxes or contributions to government-sponsored insurance funds are assessed on an annual basis, the employer's related expense is recognised in interim periods using an estimated average annual effective payroll tax or contribution rate, even though a large portion of the payments may be made early in the financial year. A common example is an employer payroll tax or insurance contribution that is imposed up to a certain maximum level of earnings per employee. For higher income employees, the maximum income is reached before the end of the financial year, and the employer makes no further payments through the end of the year.

Major planned periodic maintenance or overhaul

- B2 The cost of a planned major periodic maintenance or overhaul or other seasonal expenditure that is expected to occur late in the year is not anticipated for interim reporting purposes unless an event has caused the entity to have a legal or constructive obligation. The mere intention or necessity to incur expenditure related to the future is not sufficient to give rise to an obligation.

Provisions

- B3 A provision is recognised when an entity has no realistic alternative but to make a transfer of economic benefits as a result of an event that has created a legal or constructive obligation. The amount of the obligation is adjusted upward or downward, with a corresponding loss or gain recognised in profit or loss, if the entity's best estimate of the amount of the obligation changes.
- B4 The Standard requires that an entity apply the same criteria for recognising and measuring a provision at an interim date as it would at the end of its financial year. The existence or non-existence of an obligation to transfer benefits is not a function of the length of the reporting period. It is a question of fact.

Year-end bonuses

- B5 The nature of year-end bonuses varies widely. Some are earned simply by continued employment during a time period. Some bonuses are earned based on a monthly, quarterly, or annual measure of operating result. They may be purely discretionary, contractual, or based on years of historical precedent.
- B6 A bonus is anticipated for interim reporting purposes if, and only if, (a) the bonus is a legal obligation or past practice would make the bonus a constructive obligation for which the entity has no realistic alternative but to make the payments, and (b) a reliable estimate of the obligation can be made. IAS 19 *Employee Benefits* provides guidance.

Contingent lease payments

- B7 Contingent lease payments can be an example of a legal or constructive obligation that is recognised as a liability. If a lease provides for contingent payments based on the lessee achieving a certain level of annual sales, an obligation can arise in the interim periods of the financial year before the required annual level of sales has been achieved, if that required level of sales is expected to be achieved and the entity, therefore, has no realistic alternative but to make the future lease payment.

Intangible assets

- B8 An entity will apply the definition and recognition criteria for an intangible asset in the same way in an interim period as in an annual period. Costs incurred before the recognition criteria for an intangible asset are met are recognised as an expense. Costs incurred after the specific point in time at which the criteria are met are recognised as part of the cost of an intangible asset. 'Deferring' costs as assets in an interim statement of financial position in the hope that the recognition criteria will be met later in the financial year is not justified.

Pensions

- B9 Pension cost for an interim period is calculated on a year-to-date basis by using the actuarially determined pension cost rate at the end of the prior financial year, adjusted for significant market fluctuations since that time and for significant curtailments, settlements, or other significant one-off events.

Vacations, holidays, and other short-term compensated absences

- B10 Accumulating compensated absences are those that are carried forward and can be used in future periods if the current period's entitlement is not used in full.

IAS 19 *Employee Benefits* requires that an entity measure the expected cost of and obligation for accumulating compensated absences at the amount the entity expects to pay as a result of the unused entitlement that has accumulated at the end of the reporting period. That principle is also applied at the end of interim financial reporting periods. Conversely, an entity recognises no expense or liability for non-accumulating compensated absences at the end of an interim reporting period, just as it recognises none at the end of an annual reporting period.

Other planned but irregularly occurring costs

- B11 An entity's budget may include certain costs expected to be incurred irregularly during the financial year, such as charitable contributions and employee training costs. Those costs generally are discretionary even though they are planned and tend to recur from year to year. Recognising an obligation at the end of an interim financial reporting period for such costs that have not yet been incurred generally is not consistent with the definition of a liability.

Measuring interim income tax expense

- B12 Interim period income tax expense is accrued using the tax rate that would be applicable to expected total annual earnings, that is, the estimated average annual effective income tax rate applied to the pre-tax income of the interim period.
- B13 This is consistent with the basic concept set out in paragraph 28 that the same accounting recognition and measurement principles shall be applied in an interim financial report as are applied in annual financial statements. Income taxes are assessed on an annual basis. Interim period income tax expense is calculated by applying to an interim period's pre-tax income the tax rate that would be applicable to expected total annual earnings, that is, the estimated average annual effective income tax rate. That estimated average annual rate would reflect a blend of the progressive tax rate structure expected to be applicable to the full year's earnings including enacted or substantively enacted changes in the income tax rates scheduled to take effect later in the financial year. IAS 12 *Income Taxes* provides guidance on substantively enacted changes in tax rates. The estimated average annual income tax rate would be re-estimated on a year-to-date basis, consistent with paragraph 28 of the Standard. Paragraph 16(d) requires disclosure of a significant change in estimate.
- B14 To the extent practicable, a separate estimated average annual effective income tax rate is determined for each taxing jurisdiction and applied individually to the interim period pre-tax income of each jurisdiction. Similarly, if different income tax rates apply to different categories of income (such as capital gains or income earned in particular industries), to the extent practicable a separate rate is applied to each individual category of interim period pre-tax income. While that degree of precision is desirable, it may not be achievable in all cases, and a weighted

average of rates across jurisdictions or across categories of income is used if it is a reasonable approximation of the effect of using more specific rates.

- B15 To illustrate the application of the foregoing principle, an entity reporting quarterly expects to earn 10,000 pre-tax each quarter and operates in a jurisdiction with a tax rate of 20 per cent on the first 20,000 of annual earnings and 30 per cent on all additional earnings. Actual earnings match expectations. The following table shows the amount of income tax expense that is reported in each quarter:

	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter	Annual
Tax expense	2,500	2,500	2,500	2,500	10,000

10,000 of tax is expected to be payable for the full year on 40,000 of pre-tax income.

- B16 As another illustration, an entity reports quarterly, earns 15,000 pre-tax profit in the first quarter but expects to incur losses of 5,000 in each of the three remaining quarters (thus having zero income for the year), and operates in a jurisdiction in which its estimated average annual income tax rate is expected to be 20 per cent. The following table shows the amount of income tax expense that is reported in each quarter:

	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter	Annual
Tax expense	3,000	(1,000)	(1,000)	(1,000)	0

Difference in financial reporting year and tax year

- B17 If the financial reporting year and the income tax year differ, income tax expense for the interim periods of that financial reporting year is measured using separate weighted average estimated effective tax rates for each of the income tax years applied to the portion of pre-tax income earned in each of those income tax years.
- B18 To illustrate, an entity's financial reporting year ends 30 June and it reports quarterly. Its taxable year ends 31 December. For the financial year that begins 1 July, Year 1 and ends 30 June, Year 2, the entity earns 10,000 pre-tax each quarter. The estimated average annual income tax rate is 30 per cent in Year 1 and 40 per cent in Year 2.

	Quarter ending 30 Sept	Quarter ending 31 Dec	Quarter ending 31 Mar	Quarter ending 30 June	Year ending 30 June
	Year 1	Year 1	Year 2	Year 2	Year 2
Tax expense	3,000	3,000	4,000	4,000	14,000

Tax credits

- B19 Some tax jurisdictions give taxpayers credits against the tax payable based on amounts of capital expenditures, exports, research and development expenditures, or other bases. Anticipated tax benefits of this type for the full year are generally reflected in computing the estimated annual effective income tax rate, because those credits are granted and calculated on an annual basis under most tax laws and regulations. On the other hand, tax benefits that relate to a one-off event are recognised in computing income tax expense in that interim period, in the same way that special tax rates applicable to particular categories of income are not blended into a single effective annual tax rate. Moreover, in some jurisdictions tax benefits or credits, including those related to capital expenditures and levels of exports, while reported on the income tax return, are more similar to a government grant and are recognised in the interim period in which they arise.

Tax loss and tax credit carrybacks and carryforwards

- B20 The benefits of a tax loss carryback are reflected in the interim period in which the related tax loss occurs. IAS 12 provides that 'the benefit relating to a tax loss that can be carried back to recover current tax of a previous period shall be recognised as an asset'. A corresponding reduction of tax expense or increase of tax income is also recognised.
- B21 IAS 12 provides that 'a deferred tax asset shall be recognised for the carryforward of unused tax losses and unused tax credits to the extent that it is probable that future taxable profit will be available against which the unused tax losses and unused tax credits can be utilised'. IAS 12 provides criteria for assessing the probability of taxable profit against which the unused tax losses and credits can be utilised. Those criteria are applied at the end of each interim period and, if they are met, the effect of the tax loss carryforward is reflected in the computation of the estimated average annual effective income tax rate.
- B22 To illustrate, an entity that reports quarterly has an operating loss carryforward of 10,000 for income tax purposes at the start of the current financial year for which a deferred tax asset has not been recognised. The entity earns 10,000 in the first quarter of the current year and expects to earn 10,000 in each of the three remaining quarters. Excluding the carryforward, the estimated average annual income tax rate is expected to be 40 per cent. Tax expense is as follows:

	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter	Annual
Tax expense	3,000	3,000	3,000	3,000	12,000

Contractual or anticipated purchase price changes

- B23 Volume rebates or discounts and other contractual changes in the prices of raw materials, labour, or other purchased goods and services are anticipated in interim periods, by both the payer and the recipient, if it is probable that they have been earned or will take effect. Thus, contractual rebates and discounts are anticipated but discretionary rebates and discounts are not anticipated because the resulting asset or liability would not satisfy the conditions in the *Conceptual Framework* that an asset must be a resource controlled by the entity as a result of a past event and that a liability must be a present obligation whose settlement is expected to result in an outflow of resources.

Depreciation and amortisation

- B24 Depreciation and amortisation for an interim period is based only on assets owned during that interim period. It does not take into account asset acquisitions or dispositions planned for later in the financial year.

Inventories

- B25 Inventories are measured for interim financial reporting by the same principles as at financial year-end. IAS 2 *Inventories* establishes standards for recognising and measuring inventories. Inventories pose particular problems at the end of any financial reporting period because of the need to determine inventory quantities, costs, and net realisable values. Nonetheless, the same measurement principles are applied for interim inventories. To save cost and time, entities often use estimates to measure inventories at interim dates to a greater extent than at the end of annual reporting periods. Following are examples of how to apply the net realisable value test at an interim date and how to treat manufacturing variances at interim dates.

Net realisable value of inventories

- B26 The net realisable value of inventories is determined by reference to selling prices and related costs to complete and dispose at interim dates. An entity will reverse a write-down to net realisable value in a subsequent interim period only if it would be appropriate to do so at the end of the financial year.

- B27 [Deleted]

Interim period manufacturing cost variances

- B28 Price, efficiency, spending, and volume variances of a manufacturing entity are recognised in income at interim reporting dates to the same extent that those variances are recognised in income at financial year-end. Deferral of variances that are expected to be absorbed by year-end is not appropriate because it could result in reporting inventory at the interim date at more or less than its portion of the actual cost of manufacture.

Foreign currency translation gains and losses

- B29 Foreign currency translation gains and losses are measured for interim financial reporting by the same principles as at financial year-end.
- B30 IAS 21 *The Effects of Changes in Foreign Exchange Rates* specifies how to translate the financial statements for foreign operations into the presentation currency, including guidelines for using average or closing foreign exchange rates and guidelines for recognising the resulting adjustments in profit or loss or in other comprehensive income. Consistently with IAS 21, the actual average and closing rates for the interim period are used. Entities do not anticipate some future changes in foreign exchange rates in the remainder of the current financial year in translating foreign operations at an interim date.
- B31 If IAS 21 requires translation adjustments to be recognised as income or expense in the period in which they arise, that principle is applied during each interim period. Entities do not defer some foreign currency translation adjustments at an interim date if the adjustment is expected to reverse before the end of the financial year.

Interim financial reporting in hyperinflationary economies

- B32 Interim financial reports in hyperinflationary economies are prepared by the same principles as at financial year-end.
- B33 IAS 29 *Financial Reporting in Hyperinflationary Economies* requires that the financial statements of an entity that reports in the currency of a hyperinflationary economy be stated in terms of the measuring unit current at the end of the reporting period, and the gain or loss on the net monetary position is included in net income. Also, comparative financial data reported for prior periods are restated to the current measuring unit.
- B34 Entities follow those same principles at interim dates, thereby presenting all interim data in the measuring unit as of the end of the interim period, with the resulting gain or loss on the net monetary position included in the interim period's net income. Entities do not annualise the recognition of the gain or loss. Nor do they use an estimated annual inflation rate in preparing an interim financial report in a hyperinflationary economy.

Impairment of assets

- B35 IAS 36 *Impairment of Assets* requires that an impairment loss be recognised if the recoverable amount has declined below carrying amount.
- B36 This Standard requires that an entity apply the same impairment testing, recognition, and reversal criteria at an interim date as it would at the end of its financial year. That does not mean, however, that an entity must necessarily make a detailed impairment calculation at the end of each interim period. Rather, an entity will review for indications of significant impairment since the end of the most recent financial year to determine whether such a calculation is needed.

C Examples of the use of estimates

The following examples to illustrate application of the principle in paragraph 41.

- C1 **Inventories:** Full stock-taking and valuation procedures may not be required for inventories at interim dates, although it may be done at financial year-end. It may be sufficient to make estimates at interim dates based on sales margins.
- C2 **Classifications of current and non-current assets and liabilities:** Entities may do a more thorough investigation for classifying assets and liabilities as current or non-current at annual reporting dates than at interim dates.
- C3 **Provisions:** Determination of the appropriate amount of a provision (such as a provision for warranties, environmental costs, and site restoration costs) may be complex and often costly and time-consuming. Entities sometimes engage outside experts to assist in the annual calculations. Making similar estimates at interim dates often entails updating of the prior annual provision rather than the engaging of outside experts to do a new calculation.
- C4 **Pensions:** IAS 19 *Employee Benefits* requires that an entity determine the present value of defined benefit obligations and the market value of plan assets at the end of each reporting period and encourages an entity to involve a professionally qualified actuary in measurement of the obligations. For interim reporting purposes, reliable measurement is often obtainable by extrapolation of the latest actuarial valuation.
- C5 **Income taxes:** Entities may calculate income tax expense and deferred income tax liability at annual dates by applying the tax rate for each individual jurisdiction to measures of income for each jurisdiction. Paragraph B14 acknowledges that while that degree of precision is desirable at interim reporting dates as well, it may not be achievable in all cases, and a weighted average of rates across jurisdictions or across categories of income is used if it is a reasonable approximation of the effect of using more specific rates.
- C6 **Contingencies:** The measurement of contingencies may involve the opinions of legal experts or other advisers. Formal reports from independent experts are sometimes obtained with respect to contingencies. Such opinions about litigation, claims, assessments, and other contingencies and uncertainties may or may not also be needed at interim dates.
- C7 **Revaluations and fair value accounting:** IAS 16 *Property, Plant and Equipment* allows an entity to choose as its accounting policy the revaluation model whereby items of property, plant and equipment are revalued to fair value. Similarly, IAS 40 *Investment Property* requires an entity to determine the fair value of investment property. For those measurements, an entity may rely on professionally qualified valuers at annual reporting dates though not at interim reporting dates.
- C8 **Intercompany reconciliations:** Some intercompany balances that are reconciled on a detailed level in preparing consolidated financial statements at financial year-end might be reconciled at a less detailed level in preparing consolidated financial statements at an interim date.

- C9 **Specialised industries:** Because of complexity, costliness, and time, interim period measurements in specialised industries might be less precise than at financial year-end. An example would be calculation of insurance reserves by insurance companies.