IFRS 9, 15 & 16 – What do I need to know…?

There are **3 new financial reporting standards** that will be affecting your financial statements this year and we are hoping to make it a bit easier for you to understand what you need to do to navigate through them based on our experience with a host of early adopters and first time adopters with interim financial reports in 2018.

The first issue to be aware of is the fact that 2 out of these 3 standards (viz revenue and financial instruments) will affect almost any business.

The second, is being very clear about the effective date of these standards so you can plan your financial reporting cycle accordingly.

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IFRS 9 Financial Instruments

- Effective for reporting periods beginning on or after 1 January 2018

IFRS 15 Revenue from Contracts with Customers

- Effective for reporting periods beginning on or after 1 January 2018

This will affect all companies with December year ends for their 2018 financial statements as well as companies who issue interim reports on or after June 2018.

IFRS 16 Leases

- Effective for reporting periods beginning on or after 1 January 2019

This only affects companies in 2019 but you may need to consider the impact on your 2018 numbers in terms of gathering the necessary information.

Impact Assessment Snapshot

Issue	IFRS 9	IFRS 15	IFRS 16
Recognition	There will be an impact on the categories of financial instruments when moving from IAS 39 to IFRS 9. **LOW IMPACT**	Every contract with a customer needs to be filtered through the 5 step revenue recognition process. This process will determine the various categories of revenue that will form the basis for most of the disclosure in the financial statements. **HIGH IMPACT**	All operating leases that are not short term in nature and don't give rise to low value assets will be impacted by the adoption of IFRS 16. **HIGH IMPACT**
Measurement	Where categories have changed significantly, the impact on measurement going forward could be material. The change in impairment of financial assets and trade receivables will have an impact on the impairment process and documentation thereof. **HIGH IMPACT**	The measurement of revenue could be materially affected by the following key issues: - Variable considerations e.g. rebates, discounts etc - Multiple performance obligations in a single contract - Recognition of contract assets and liabilities **LOW IMPACT**	A lease liability representing the present value of future payments under the lease contract will be recognised along with a corresponding right of use asset. The liability will be unwound throughout the duration of the lease term and the right of use asset amortised and assessed for impairment accordingly. **HIGH IMPACT**
Disclosure	There are material changes to disclosure with specific additional disclosure around the impairment process. **LOW IMPACT**	There are material changes to disclosure with significant additional information being provided about different categories of revenue and their respective drivers. **HIGH IMPACT**	Additional disclosure requirements to capture the effects of the lease liability and right of use asset. **LOW IMPACT**

IFRS 9 Financial Instruments

What are the key changes…

Classification

All financial instruments will now be classified into 1 of 3 categories.

Fair value through profit or loss, Fair value through OCI & Amortised Cost.

IMPACT ASSESSMENT

Low Impact for most businesses

Impairment

An Expected Credit Loss Model (ECL) is applied to all financial assets.

Specific simplification relief offered to trade and other receivables.

IMPACT ASSESSMENT

High Impact for most businesses

Hedging

Primarily relates to greater flexibility allowed with respect to hedging instruments & items.

Moving from a quantitative to qualitative screening process.

IMPACT ASSESSMENT

Low Impact for most businesses

The focus for implementing IFRS 9 will be on companies spending their time on conducting the appropriate impairment exercises on long term loans as well as trade and other receivables. The simplified approach to impairment of trade and other receivables requires the extraction of historical data to support the forward looking impairment assessment process.

What do you need to focus on…

Classification

- Assess your business model for managing financial assets as well as the contractual cash flow characteristics of each financial asset to determine the new categories of financial instruments
- Most companies have had little or no change in the measurement of financial instruments as a result of the adoption of IFRS 9.

Impairment

- Each financial asset needs to be assessed on whether there has been a significant increase in credit risk – this is based on both historical and forward looking information
- Trade receivables need to be grouped based on customer attributes and historical loss patterns to develop a provision matrix for each category of customer.

Disclosure

- Specific transition related disclosure required for 1st time adoption. In addition, policy choices on whether to restate comparatives or not, must be investigated.
- New recurring disclosure to be drafted to capture the revised requirements of IFRS 9.

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IFRS 15 Revenue from Contracts with Customers

What are the key changes…

5 step approach

- Identify a contract
- Performance obligations
- Transaction price
- Allocation of transaction price
- Satisfaction of performance obligations

IMPACT ASSESSMENT

High Impact for most businesses

Variable consideration

- Situations where future revenue may vary
- Discounts, rebates, credits etc
- Variable amount to be estimated upfront and recognized over duration of the contract

IMPACT ASSESSMENT

Low Impact for most businesses

Performance obligations

- Single contract with a customer could include multiple performance obligations
- Transaction price to be separated for each obligation
- Timing of recognition could vary

IMPACT ASSESSMENT

Moderate Impact for most businesses

The numerical impact on companies has been minimal except where there are variable considerations and multiple performance obligations. The focus for most companies will be on the significant additional disclosure required to provide details about each revenue stream.

What do you need to focus on…

Classification

- The 5 step process needs to be applied to every contract with a customer
- Specific issues i.e. multiple performance obligations, variable considerations, contract assets and liabilities must be assessed for each contract
- Assessment of whether performance obligations are over time vs at a point in time

Transaction price

- Split between fixed and variable consideration to be estimated for affected contracts
- Variable consideration to be estimated at inception of contract
- Allocation of discounts to be done across performance obligations

Disclosure

- Specific transition related disclosure required for 1st time adoption. In addition, policy choices on whether to restate comparatives or not, must be investigated.
- Significant additional disclosure required viz. qualitative & quantitative information, information about contracts with customers, reconciliation of contract balances, details around performance obligations

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IFRS 16 Leases

What are the key changes...

Affected lease contracts

Applied to all leases that:

- Convey the right to use an asset

- The asset is identified

- Contract is for more than 12 months

IMPACT ASSESSMENT

Moderate Impact for most businesses

Right of use asset

Affected assets to be capitalized

Assets to be depreciated and assessed for impairment

IMPACT ASSESSMENT

Moderate Impact for most businesses

Lease liability

Present value of future lease payments

Fixed versus variable payments

Option to extend or cancel lease contract

Exercise price for option to purchase or penalty for cancellation

IMPACT ASSESSMENT

Moderate Impact for most businesses

Companies that have operating leases will definitely be affected. The key is to focus on getting the estimation of the right of use asset and liability as accurate as possible in Year 1 to avoid unnecessary estimation impact on results in future years.

What do you need to focus on...

Classification

- Assessment of which contracts are affected but understanding whether there is an identified asset and the substantive rights attached to the asset
- Exclusion of low value assets or contracts that are short term in nature

Asset & Liability

- Appropriate discount rate for the lease to be determined
- Variable lease payments to be estimated for duration of the lease
- Inclusion of possible extensions to the contract
- Assessment of the impact of modifications to the lease contract

Disclosure

- Specific transition related disclosure required for 1st time adoption. In addition, policy choices on whether to restate comparatives or not must be investigated.
- Specific additional disclosure around the asset, liability and SOCI impact of the leases capitalised

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How can we help?

Our process involves working with the finance and operations team to conduct a **gap analysis** and **benchmark** current reporting practices to the new requirements in order to develop a **discussion paper** for management and auditors in order to finalise the way forward.

Depending on the impact of this discussion paper, we will recommend an **implementation action plan** that will assist in **recalculating** the financial impact under the new standard, determine and draft the relevant **disclosures** for the **transition** year.

We provide an **end-to-end** service for the entire implementation process including post-implementation support.

GAP Analysis

1. Understand existing processes
2. Identification of key IFRS issues unique to the business
3. Discussion paper on proposed action
4. Management training

Implementation & Transition

1. Develop detailed plan of action based on GAP Analysis
2. Perform a test run on a sample of affected contracts
3. Develop financial statement impact for transition year
4. Draft proposed disclosures for inclusion in AFS

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How can we help?

Focused Training Session

Our offering on new standards implementation includes a detailed focused training session for the finance team on the technical aspects of the new standards. This includes the following:

- Training tailored to unique business environment
- Training material and implementation checklists
- CPD hours

Lease Management Tool

We have worked with software experts to develop a lease management tool that is custom-designed to manage high volumes of leases under IFRS 16. The tool is easy to use and has the capability to generate monthly reporting journals for IFRS 16 that can interface seamlessly with almost any ERP system.

The tool is custom designed for each business environment and includes extensive user training and post implementation support.

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About ZKC & Associates

ZKC & Associates is a firm of consulting chartered accountants specialising in the following:

AFS Preparation & IFRS Advisory

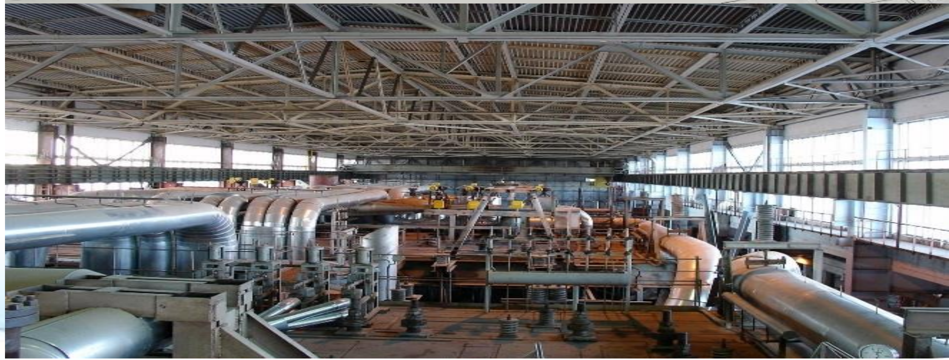
Advising clients on appropriate IFRS treatment and end to end preparation of financial statements including complex entities and consolidations

SMME Management Consulting

Providing cutting edge financial and operational expertise to SMME clients in order to maximise efficiencies, develop sound controls and enhance profitability.

Education & Training

Training clients on IFRS and accounting related issues and developing easy to use material for learning and development within the IFRS space.



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