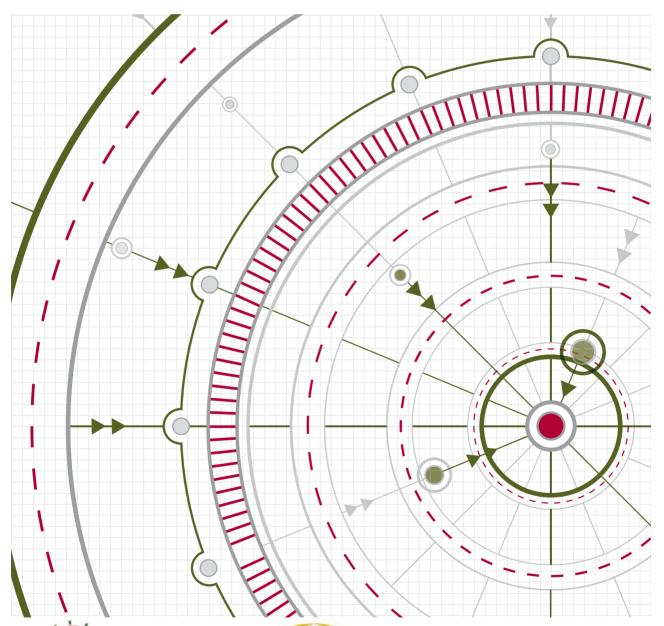
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Day 2—Thursday 25 August 2016

Conference Programme Day 2

09:00 IFRS application issues

Chair: Darrel Scott, IASB Member

Panellists include:

- Hugh Shields, IASB Executive Technical Director
- Matthew Tilling, IASB Member
- CPA Willyson Yanga, Capital Markets Authority

10:30 Tea/Coffee break

11:00 Break-out sessions: IASB projects

Choose **one** of the following:

1. Disclosure initiative

• Hugh Shields, IASB Executive Technical Director

2. Accounting for Islamic finance

- Darrel Scott, IASB Member Main Speaker
- Abdulattif Essajee Former Managing Director and Co-founder of First Community Bank (the first fully fledged Sharia'h compliant bank to be approved in Kenya)

3. Conceptual Framework

• Wei-Guo Zhang, IASB Member

4. Extractive activities

- Matthew Tilling, IASB Director of Education
- · CPA Stephen Obock, KPMG- Kenya

12:30 Lunch

13:30 Break-out sessions: IFRS application issues

Choose **one** of the following:

1. Implementing IFRS 16 Leases

- Darrel Scott, IASB Member
- FCPA Agnes Litukai, KPMG-Nigeria
- CPA Geoffrey Injeni

2. IFRS regulatory issues

- Wei-Guo Zhang, IASB Member
- CPA Willyson Yanga, Capital Markets Authority
- •CPA Joseph Kariuki, KPMG-Kenya

3. Rate regulated activities

• Hugh Shields, IASB Executive Technical Director

15:30 Networking Session -Tea Break







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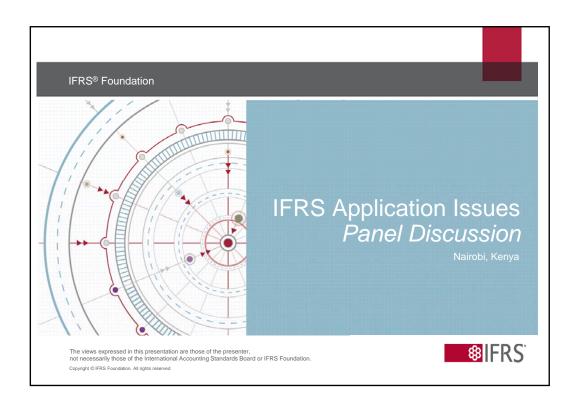
Panel discussion - IFRS application issues

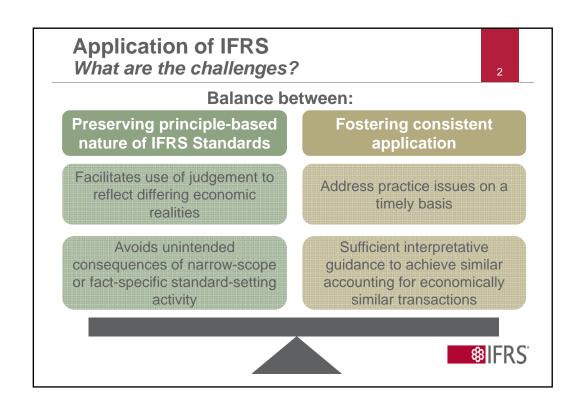
DARREL SCOTT Member IASB

HUGH SHIELDS Executive Technical Director IASB

MATT TILLING
Director of Education
IASB

WILLYSON YANGA Capital Markets Authority





Application of IFRS What does this mean in Practice?

Principled based standards

- A mature framework for exercising and evaluating judgement
- A sound educational process with focus on both IFRS requirements and exercising of judgement
- · An experienced intervention on difficult issues
- Interactive communication between regulators, auditors and preparers, particularly as regards local jurisdiction issues



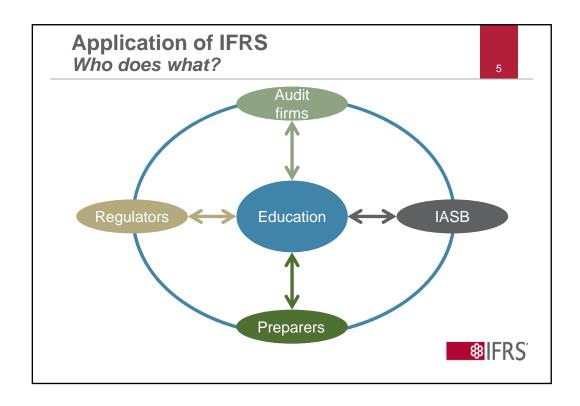
Application of IFRS What does this mean in Practice?

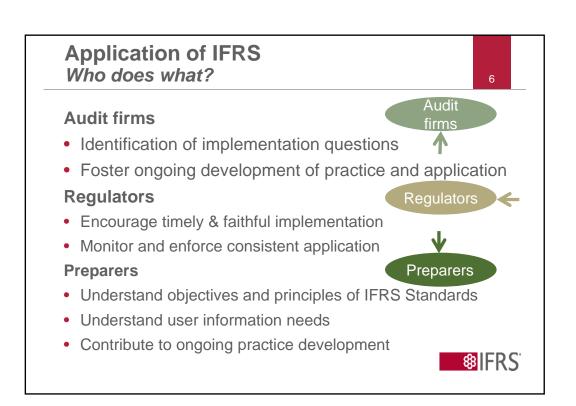
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Consistent application

- Awareness of international developments, particularly interpretation decisions
- Constant communication of regulatory decisions, interventions and actions
- Forums for discussion:
 - Understanding application of (especially new) IFRSs
 - Surface any problems arising early
 - Discuss and conclude on appropriate actions
- Feedback into education processes







Application of IFRS Who does what?

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IASB

IASB

- Maintain IFRS Standards/support consistent application
- Support implementation of new IFRS Standards
- Support those responsible for consistent application
- Support education initiatives

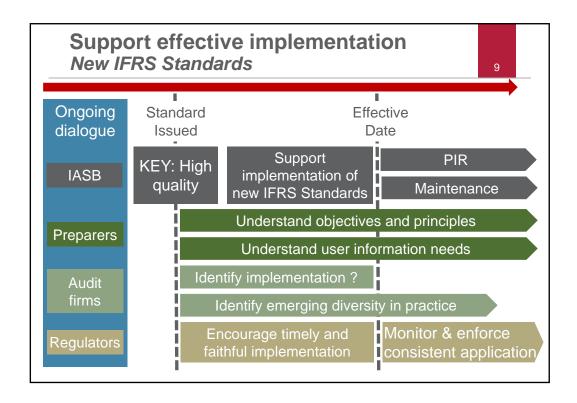
Educators

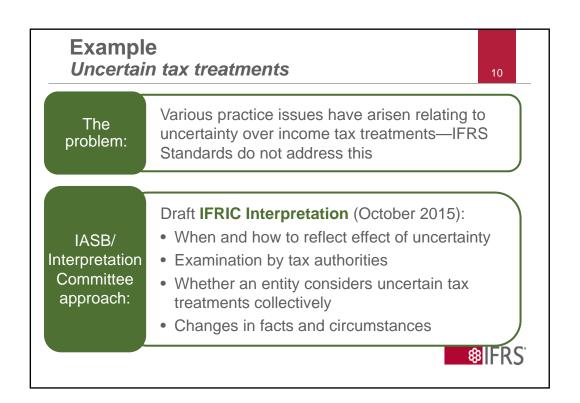
Education

- Initial and continuous education
- Stay aware of developments
- Ensure education stresses judgements (soft skills) as much as technical aspects (harder skills)
- Educate all players



Maintenance of IFRS Standards IASB 'toolbox' Post-implementation reviews Narrow-scope amendments IFRIC Interpretations Annual Improvements Agenda Decisions Education Initiative activities





The problem:

Uncertainty about how to apply requirements in IFRS 11 *Joint Arrangements*, relating to:

- · Classification of joint arrangements
- Accounting by the joint operator

IASB/ Interpretation Committee approach:

Series of Interpretations Committee agenda decisions including comments about how the existing requirements interact (March 2015)



Example Definition of a business

12

The problem:

The **Post Implementation Review** of IFRS 3 *Business Combinations* identified the definition of a business as one of four main concerns with IFRS 3

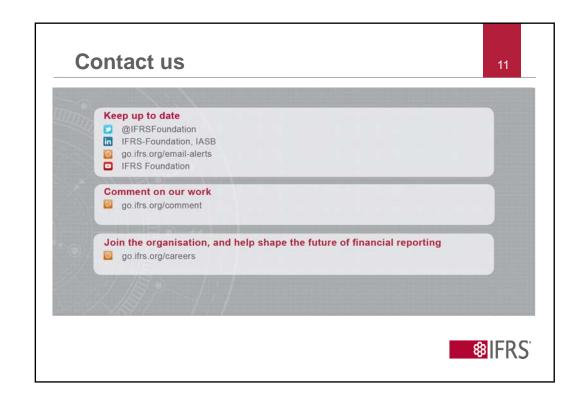
IASB approach:

ED, **Proposed amendments** to IFRS 3, provide clarifications/examples of definition of business:

- revise definition of outputs to focus on goods and services provided to customers
- not a business if substantially all fair value of gross assets acquired is concentrated in single or group of similar identifiable assets







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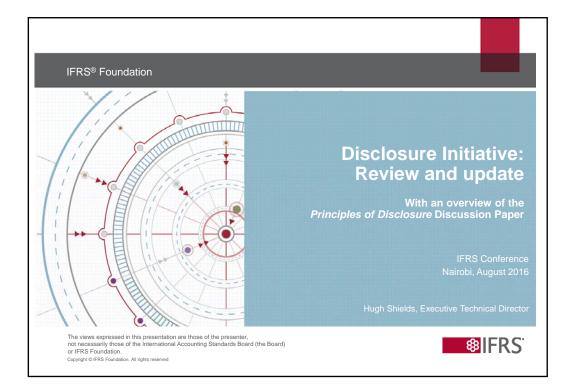
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Break-out sessions:

Disclosure Initiative

HUGH SHIELDS

Executive Technical Director IASB



Agenda

- Board's theme for 2017-2021—Better Communication
 - Includes Disclosure Initiative and other projects
- Disclosure Initiative—Overview and update
- Disclosure Initiative Project updates:
 - Completed Projects
 - Amendments to IAS 1 Presentation of Financial Statements
 - Amendments to IAS 7 Statement of Cash Flows
 - Implementation Projects
 - Draft Practice Statement Application of Materiality to Financial Statements
 - Amendments to IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors Exposure Draft
 - Research Projects
 - Principles of Disclosure Discussion Paper
 - Standards-level review of disclosures
- Disclosure Initiative time line

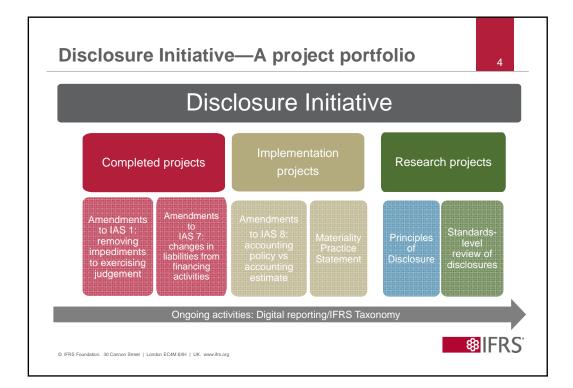


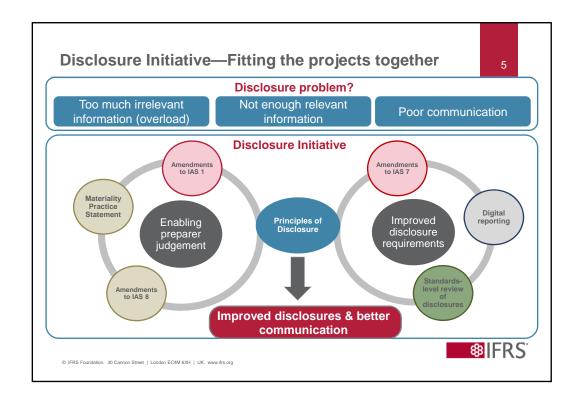
Better communication

- A central theme for 2017-2021.
- Our theme of Better Communication will include our work on:
 - primary financial statements
 - the Disclosure Initiative, including projects on principles of disclosure and materiality
 - the IFRS Taxonomy.[™]
- The scope of some of these projects, such as primary financial statements, is still being developed. Other topics, such as materiality, are more advanced.

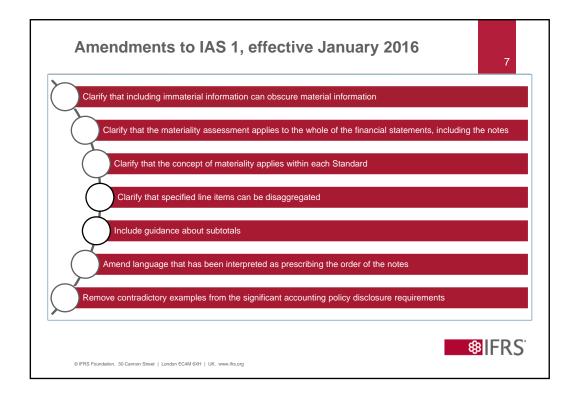
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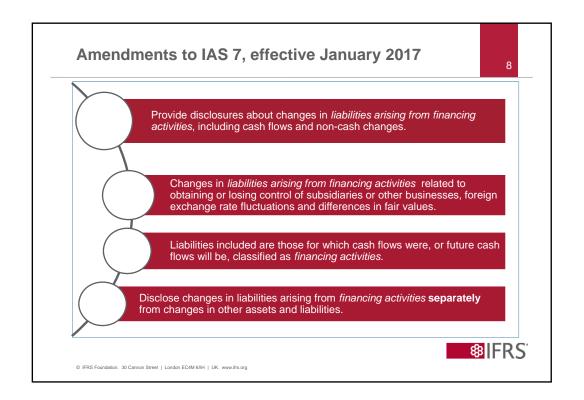
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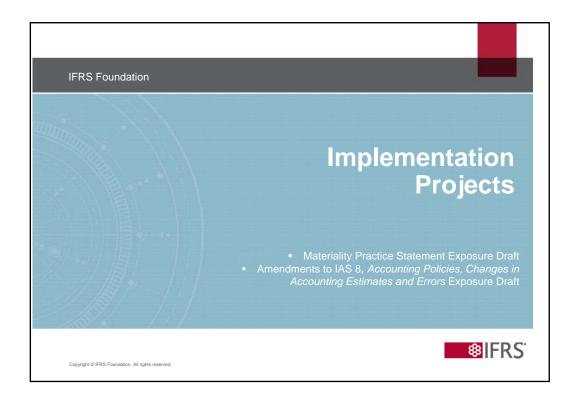












Draft Practice Statement on Materiality

10

Objective

• Help preparers apply the concept of materiality.

- · General characteristics of materiality.
- Materiality within the context of disclosing information.
- Materiality within the context of recognition and measurement.
- Does not consider possible changes to the definition of materiality (covered in Principles of Disclosure (POD) Discussion Paper).

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Q1: Form

Large majority of respondents in favour of a non-mandatory Practice Statement...

Q2: Examples

Majority favoured using examples to illustrate the application of materiality.

Some suggested improvements include:

- more 'grey area' examples;
- examples where the conclusion is 'not material'; and
 decision trees
- decision trees (because it is a thought/judgement process).

Q3: Content

Most respondents agreed with the technical content.

Some questioned whether, in some places, the guidance was an interpretation of IFRS Standards (eg IAS 8, prior period errors).

Q4: Timing

Majority agreed with Board's reasoning on the timing prior to POD project completion.

Because the Board is not planning to significantly change the definition of materiality in the POD project, and application guidance is helpful now.

*****IFRS

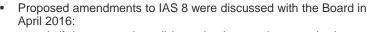
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Amendments to IAS 8

12

Why

 Difficult to distinguish between changes in accounting policies and changes in accounting estimates on the basis of the existing definitions.



- clarify how accounting policies and estimates relate to each other;
- clarify the definitions of accounting policies and of changes in accounting estimates;
- add guidance about whether changes in valuation and estimation techniques are changes in accounting estimates; and
- update examples of estimates provided in IAS 8.
- Exposure Draft of proposed amendments in Q4 2016.

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Output

Principles of Disclosure—Discussion Paper

14

Why

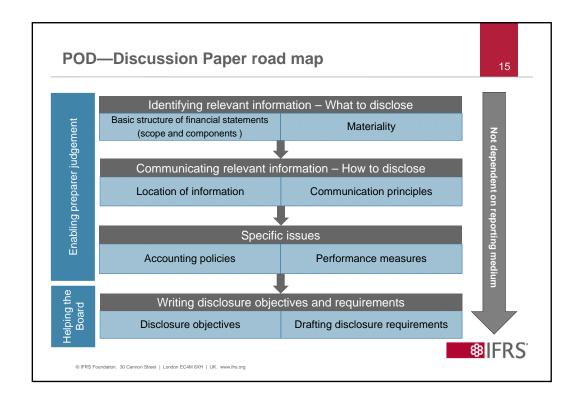
- Requests for the Board to develop presentation and disclosure principles that apply across IFRS Standards.
- Purpose is to:
 - enable preparers to make better judgements about disclosures; and Board set better disclosure requirements.

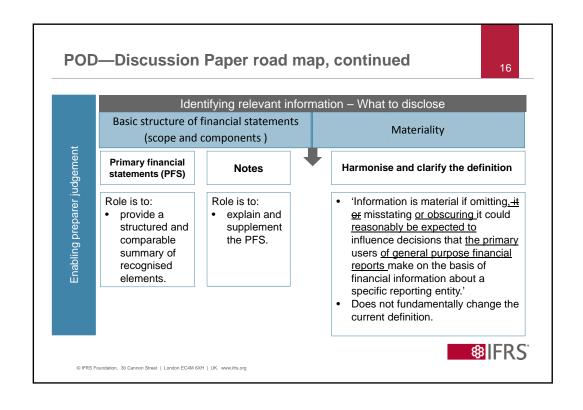
Output

- Discussion Paper (details in subsequent slides)
 - covers overall principles and specific issues.
- ultimate goal is to produce:
 - the basis for a new or revised general disclosure Standard for preparers (IAS 1, currently); and
 - drafting guidance for the Board for its internal use in setting disclosure requirements.

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Location of information

Communication principles

IFRS information,

Non-IFRS, per IAS 1

Drawn from Conceptual Framework DP

per IAS 1

Issues with use of 'IFRS' vs 'non-IFRS'

Enabling preparer judgement

Enabling preparer judgement

- Allow it to be located outside IFRS financial statements and crossreferenced under specific conditions.
- Allow non-IFRS information such as management commentary to be located inside IFRS financial statements under specific conditions.
- Entity-specific Simple and direct writing Highlight what is important

Communicating relevant information - How to disclose

- Appropriate formatting Link related
- information Avoid duplication.
- Mixed Board views on whether and which should be authoritative vs educational materials?

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POD—Discussion Paper road map, continued

18

Specific issues

Accounting policies

Performance measures

Clarifies concepts preparers find difficult

Area where users see disclosure 'overload', too much boilerplate.

- Concepts preparers find difficult to implement:
 - the objectives of accounting policy disclosures;
 - interpretation of 'significant', 'relevant', 'material' policies.
- Immaterial/insignificant policies do not need to be presented in the notes, but are not prohibited.

Does not prohibit, but provides guidelines

- Users find useful if fairly presented.
- Requirements focus on how to ensure fair presentation—eg provide definitions, explanations, reconciliations, comparatives, etc.
- Special cases:
 - EBIT/EBITDA
 - Non-recurring, unusual, or infrequently-occurring items on the statement(s) of profit or loss and OCI.

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Writing disclosure objectives and requirements

Disclosure objectives

Drafting disclosure requirements

A centralised set of objectives

Primarily for the Board, but also would help preparers.

- Possible approaches for organising:
 - by types of information:
 - similar to current approach and to FASB;
 - by how users analyse future cash flows (or another user-based view).
- A step further—create a single disclosure standard, combining all objectives and detailed requirements related to the notes into one Standard.

Focus on how the Board writes

- Some think this is a key contributor to the disclosure problem.
- NZ ASB provided example of possible new drafting/writing:
 - used 'types of information' approach, but could adapt;
 - two tiers of Standards-level objectives/requirements; and
 - emphasised preparer judgement and avoiding overly-prescriptive language.



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Standards-level review of disclosures

20

Why

 The way some disclosure requirements are written has been identified as potentially contributing to the disclosure problem.

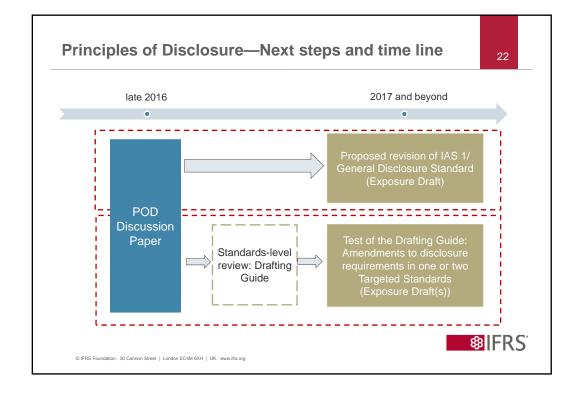
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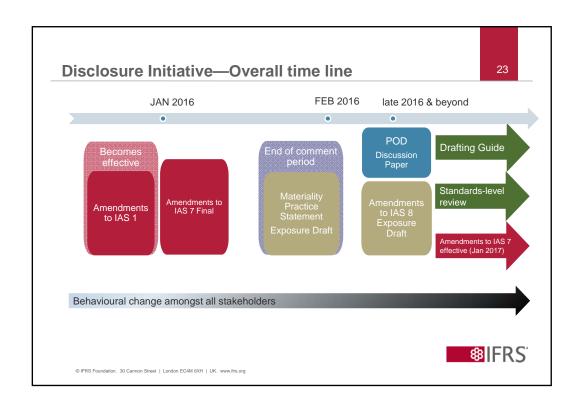
- Drafting guide for the Board's use when writing the notes disclosure requirements of Standards:
- will be informed by POD Discussion Paper feedback; and
- may reflect NZ ASB proposals.
- Test drafting guide against targeted Standards.
- May result in amendments to those Standards.

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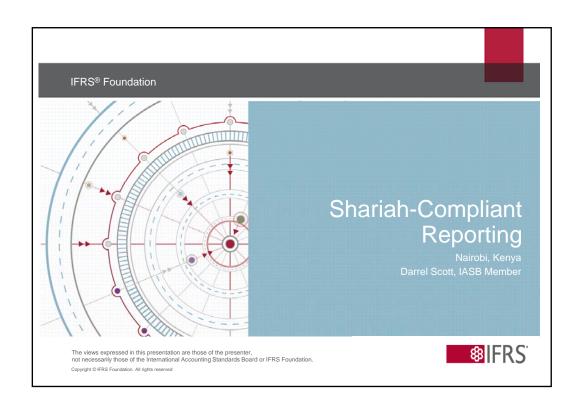
Break-out sessions:

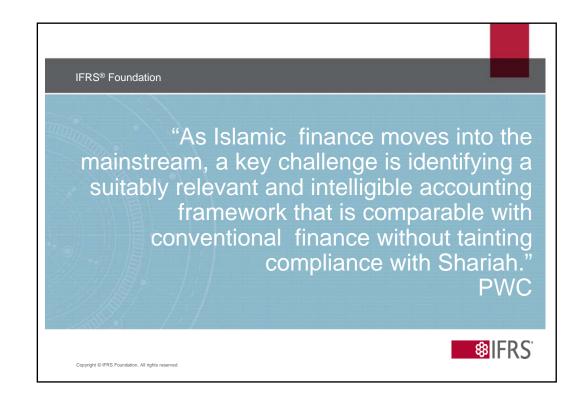
Accounting for Islamic finance

DARREL SCOTT Member IASB

ABDULATTIF ESSAJEE

Former Managing Director and Co-founder First Community Bank Kenya

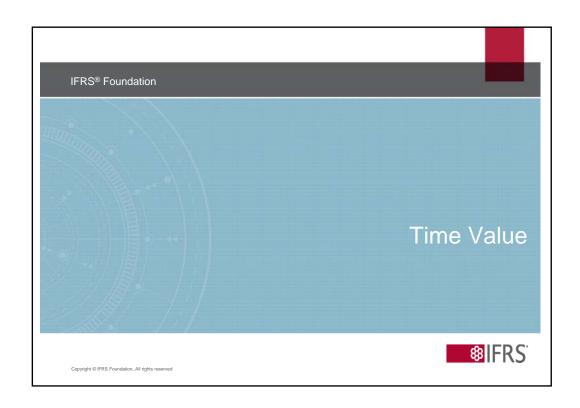




IFRS Principles

- IFRS is a principle based accounting approach
- IFRS focuses on the economic substance of a product or transaction rather than its legal form
- IFRS is <u>not</u> product specific written to focus on the <u>underlying nature and flows</u> of a product or transaction
- In dealing with economic substance, IFRS principles assume that
 - Resource today <u>has</u> greater value then resource in the future
 - Substance should be considered over form





Recognition of value over time Shariah law

5

- Charging of interest is anathema under Shariah law
- Shariah instruments don't include interest (riba)
- Instead, returns are earned from permitted transactions:
 - mark-up on sale contracts eg: Murabaha,
 - certificates of undivided interest in assets eg: Sukuk;
 - profit-share in ventures and other partnership-like contracts eg: *Musharaka*
 - rent in lease contracts eg ljarah;
 - profit, profit-share, rent or fee from undivided pro rata ownership eg Sukuk



Recognition of value over time *IFRS*

- IFRS uses discounted cash flows (net present values) to identify and measure the effect of time on the value of resources
- Discounted cash flows are calculated with reference to discount rates
- This can create the <u>perception</u> of conflict with Shariah law (riba), even for transaction that <u>do not include interest</u> <u>charges</u>

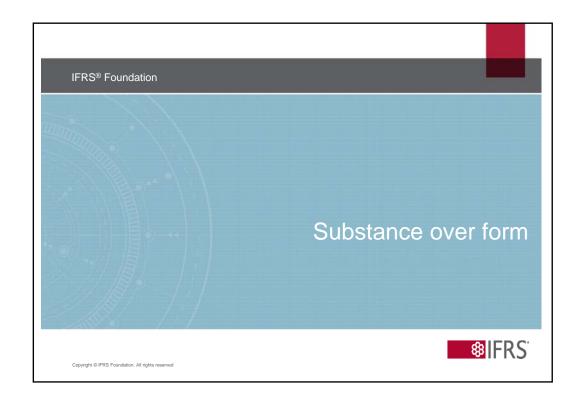


Time value of money in IFRSs

-

- IFRS standards generally use time value of money whenever there is likely difference in timing of cash flows
- Thus, some standards make extensive reference to TVM, such as:
 - IAS 19, Employee benefits
 - IAS 37, Provisions, Contingent Liabilities and Contingent Assets
 - IFRS 9, Financial Instruments
 - IFRS 15, Revenue from Contracts with Customers
 - IFRS 16, Leases
- TVM is generally considered a measurement convention
- Applied irrespective of the <u>underlying nature of contract</u>





Substance over form Shariah Law

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- Shariah products and transactions are <u>legally</u> <u>underpinned</u> by Shariah law
- Many argue that it would be inappropriate to apply substance over form to such transactions
- Substance over form can affect some transactions where TVM is important:
 - Asset backed versus asset dependent eg sukuk
 - Sales transactions with deferred payment
- Can also have an effect on other transactions products:
 - Insurance contracts eg takaful



Substance over form *IFRS*

- Substance and form focusses on identifying and understanding rights and obligations created by contracts
- Reporting these rights and obligations consistently is key to application of IFRS
- Transactions or products should be <u>measured</u> in accordance with their rights and obligations
- An important element for ensuring consistency and comparability:
 - Words not applied consistently across jurisdictions
 - Past practice, side agreements and understanding affect transactions



Substance over form in IFRSs

- Substance and form is pervasive in IFRS
- Is however particularly important in:
 - IAS 37, Provisions, Contingent Liabilities and Contingent Assets
 - IFRS 9, Financial Instruments
 - IFRS 15, Revenue from Contracts with Customers
 - IFRS 16, Leases





- IFRSs do not <u>change the nature</u> of transactions, or the rights and obligations that attach to transactions
- IFRS focus on consistent measurement and reporting of economic phenomena that arise from transactions
- IFRS should therefore <u>not</u> change the nature, rights or obligations of Shariah products
- Shariah law focuses on rights and obligations so influences but does not necessarily change accounting
- Conflicts between IFRS and Shariah law are often more perception than reality
- None-the-less have capacity to cause concern



IASB's Consultative Group

- Conflicts are not always just perception
- This is a critical sensitivity
- Important that the IASB remains
 - aware of developments,
 - sensitive to concerns, and
 - engages with this important constituency
- Consequently, the IASB in consultation with interested constituents has formed the <u>Shariah-Compliant</u> <u>Instruments and Transactions</u> consultative group



Shariah-Compliant Instruments and Transactions Group

15

- Group first met in 2013
- Recent meeting was cosponsored with Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI)
- Group does not judge whether products are compliant with the requirements of Shariah law
- Group's discussions focus on challenges that arise in application of IFRS Standards to Shariah compliant instruments and transactions
- Recently produced a paper to discuss application of IFRS



Shariah-Compliant Instruments and Transactions Group

16

- Participation from constituent jurisdictions with significant Shariah compliant transactions
- Includes Saudi Arabia, Malaysia, Indonesia and Pakistan among others
- Chaired until recently by IASB vice Chairman

Way Forward

- IASB will continue to engage with Islamic Constituents
- In particular, engagement with other standard setters will remain important part of IASB process



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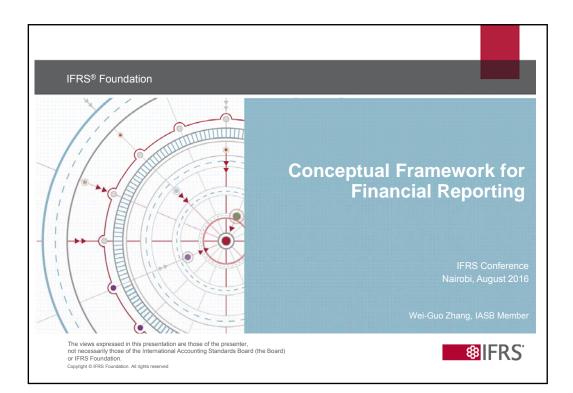
Break-out sessions:

Conceptual Framework

WEI-GUO ZHANG

Member

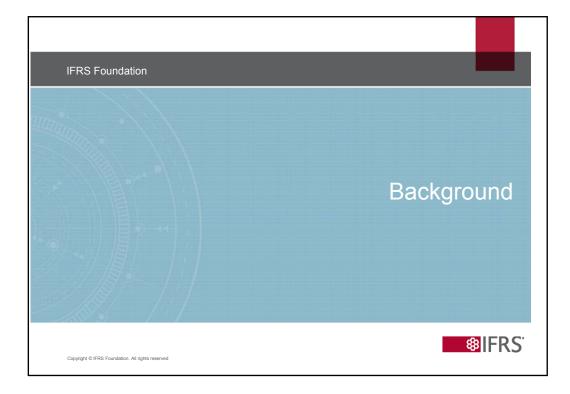
IASB



Session overview

- Background
- Objectives and qualitative characteristics
- Elements
- Recognition and de-recognition
- Measurement
- Reporting financial performance
- Other proposals





Do we need a Conceptual Framework?

4

- YES because it supports principle-based standards by
 - providing a consistent starting point
 - focusing on principles rather than rules
- It addresses fundamental issues

Objectives What is the objective of

objective of financial reporting?

Qualities

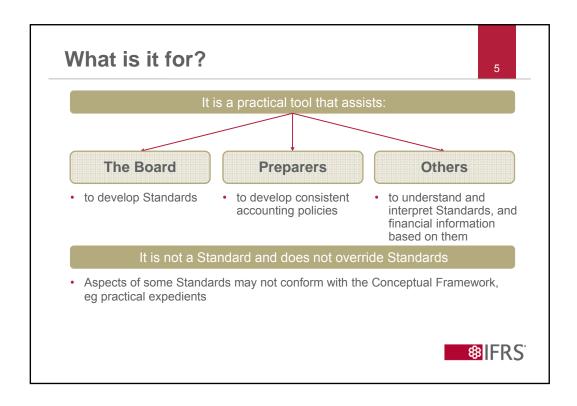
What makes financial information useful?

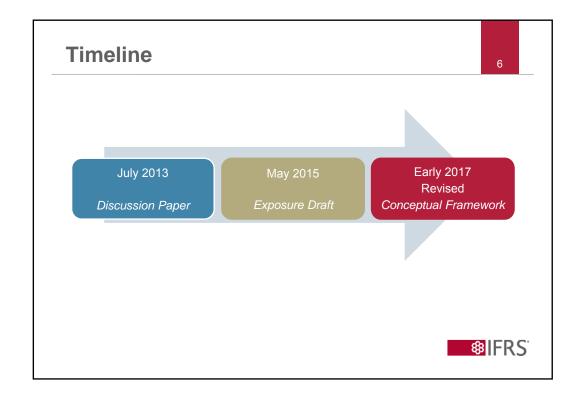
Elements, recognition, measurements

What are assets, liabilities, equity, income and expenses, when should they be recognised and how should they be measured, presented and disclosed?

...it underpins the decisions made by the Board when setting Standards







Approach to finalisation

What we heard

- Feedback mostly supportive
- Measurement chapter needs more guidance
- Proposals on other comprehensive income (OCI) need more work
- Support for dealing with distinction between liabilities and equity in a separate research project
- Some want more research before finalising

What we decided

- · Build on existing proposals
- Develop proposals further
- Develop high-level proposals on use of OCI. Look at presentation of financial performance in a separate project
- Address uncertain liabilities but also undertake further research in separate project
- Finalise early 2017 based on ED





Objective and qualitative characteristics

o

The objective of general purpose financial reporting is to provide useful financial information

Relevance

 Relevant financial information is capable of making a difference in a decision made by users

Faithful representation

- Representation of relevant economic phenomena and faithful representation of the substance of the phenomena that it purports to represent
- Complete, neutral and free from error

Enhancing characteristics

Comparability • Verifiability • Timeliness • Understandability

Cost constraints



Stewardship

Exposure Draft

 Give more prominence to the need to provide information to assess management's stewardship of the entity's resources

What we heard

- Many welcomed proposal
- Some wanted stewardship as additional objective
- Some asked for more guidance on implications of proposal
- Some disagreed with proposal

Tentative decisions

- As in ED but clarify link between objective of financial reporting and stewardship. Resource allocation decisions include decisions:
- to buy, sell or hold
- to provide or settle loans
- needed while holding investments



Exposure Draft

- Reintroduction of explicit reference to prudence (exercise of caution when making decisions under conditions of uncertainty)
- No overstatement or understatement of assets, liabilities, income or expenses (ie neutral)

What we heard

- Many welcomed proposal
- Some would like asymmetric prudence or acknowledgement of asymmetric accounting treatment
- Some objected to proposal because of concerns it could lead to bias

Tentative decisions

- As in ED—include reference to 'cautious' prudence
- Rejected asymmetric prudence
- Explore further acknowledgement of asymmetric accounting treatment



12

Measurement uncertainty (reliability)

Exposure Draft

- If an estimate is too uncertain, it might not provide relevant information
- Trade-off against other factors that affect relevance
- Retain faithful representation as a label for that qualitative characteristic

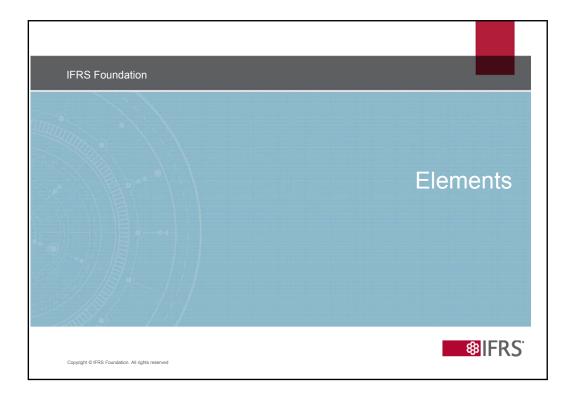
What we heard

- Some argued measurement uncertainty is a factor affecting faithful representation
- Some would like a return to 'reliability'

Tentative decisions

- Describe measurement uncertainty as factor affecting faithful representation
- Clarify in Basis that a trade-off can exist between relevance and faithful representation
- Do not relabel as 'reliability'

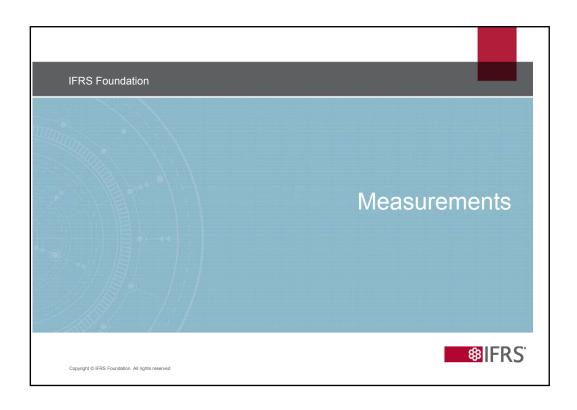


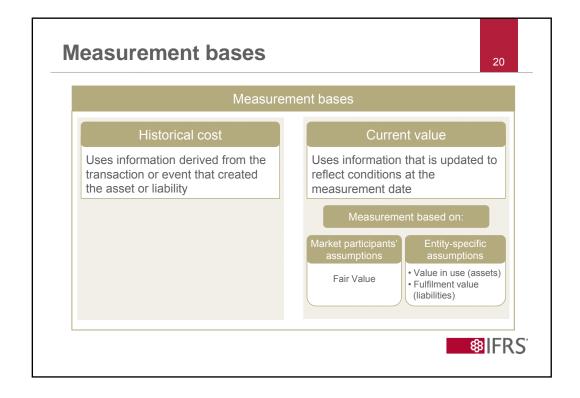


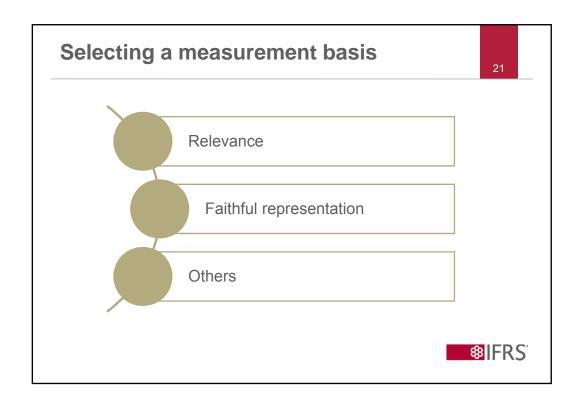
Elements: Definitions of assets and liabilities Exposure Draft **Existing definitions** Asset A resource controlled by the entity A present economic resource (of an entity) as a result of past events and from controlled by the entity as a which future economic benefits result of past events are expected to flow to the entity Liability A present obligation of the entity A present obligation of the entity (of an entity) arising from past events, the to transfer an economic resource settlement of which is expected to as a result of past events result in an outflow from the entity of resources embodying economic benefits Economic Not defined A right that has the potential to produce economic benefits resource **Definitions of assets and liabilities** Broadly supportive of the proposed changes **\$IFRS**

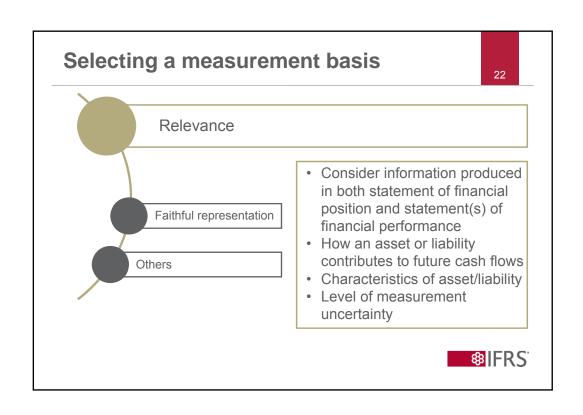


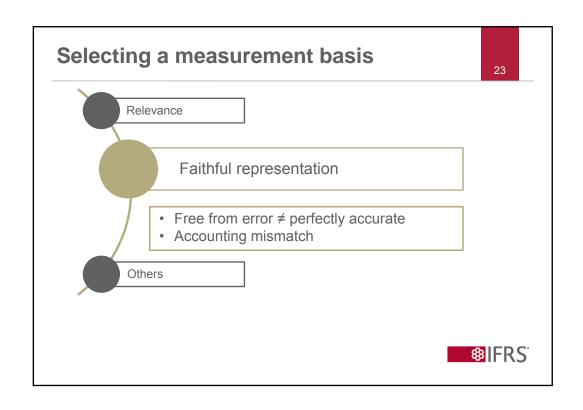
De-recognition 18 **Existing criteria Exposure Draft** · Aim is to faithfully represent De-recognition None both: · the entity's retained assets and liabilities; and any resulting changes in its assets and liabilities related effects on performance **De-recognition** Broadly supportive of the proposed approach Some expressed the view that de-recognition should mirror recognition **BIFRS**

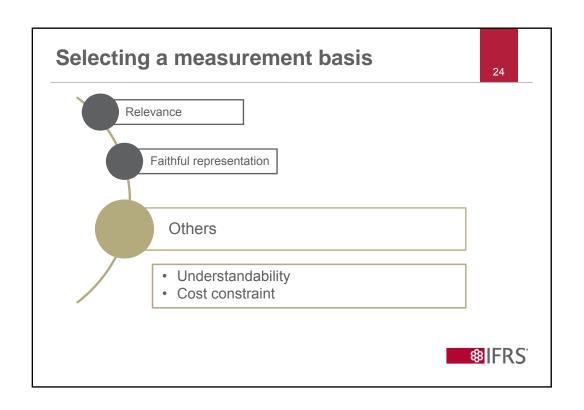












Measurement

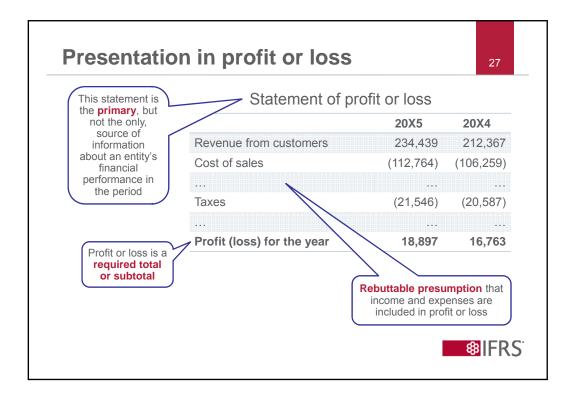
- Support for mixed measurement approach and suggested measurement bases
- Some suggested undertaking more research before issuing Conceptual Framework or to start a separate research project

Tentative decisions

- Expand discussion of ED proposals to provide a clearer link between the factors to consider and the selection of a measurement basis
- Continue with mixed measurement approach







Presentation in OCI 28 Income and Statement of comprehensive income expenses included in 20X5 20X4 OCI only if Profit (loss) for the year that 18,897 16,763 enhances Currency translation (51)relevance of profit or loss FV adjustment cash flow hedging (2,764)6,259 in the period Rebuttable (215)87 presumption that income Other comprehensive income for the year (2,546)4,253 and expenses Total comprehensive income for the year 16,351 21,016 included in OCI in one period are OCI only for some income and subsequently expenses from changes in current included in measures of assets and liabilities profit or loss (recycled) **BIFRS**

Profit or loss and OCI

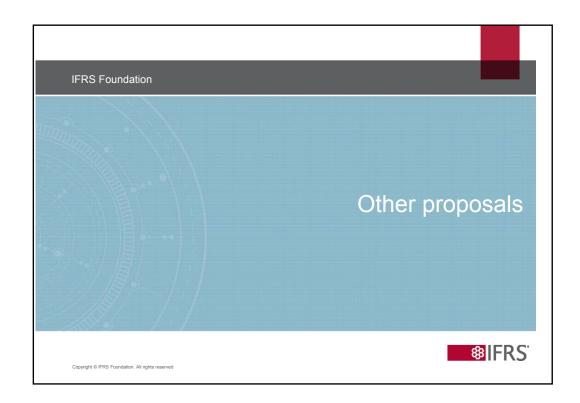
Mixed feedback

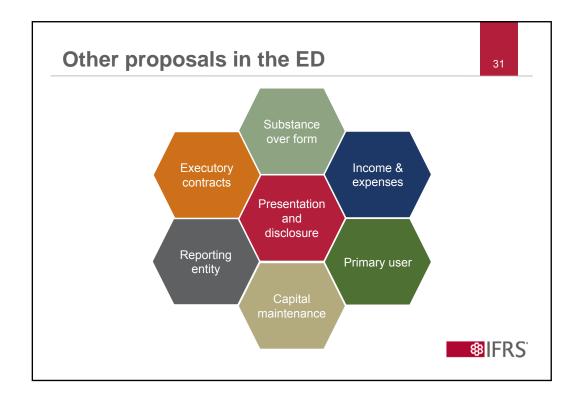
- Roughly half agreed with description of statement of profit or loss
- Many disagreed with proposals and stated proposed guidance is insufficient
- · Many disagreed with proposals on use of OCI
- Roughly half agreed that OCI items should be recycled
- Many would like us to define profit or loss/ financial performance

Tentative decisions...

- Confirm the basic principles
- Remove rebuttable presumptions
- Carefully select examples

\$IFRS





Further information

- Exposure Draft Conceptual Framework for Financial Reporting http://go.ifrs.org/ED-CF-May2015
- Conceptual Framework website http://go.ifrs.org/Conceptual-Framework
- Snapshot http://go.ifrs.org/CFSnapshot2015
- Register for email alerts http://eifrs.ifrs.org/eifrs/Register



Joint IFRS® Foundation, PAFA and ICPAK IFRS Conference and *IFRS for SMEs* workshop

24–26 August 2016 Safari Park Hotel, Nairobi, Kenya

Break-out sessions:

Extractive activities

MATT TILLING
Director of Education
IASB

Why undertake this research project?

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- IFRSs do not provide specific guidance for extractive activities
 - IFRS 6 is an interim standard

IFRS® Foundation

- scope exclusions in other standards
- no specific disclosure requirements
- Some question the relevance of existing accounting and disclosure practices

Accounting and disclosure practices often vary by industry, by jurisdiction, and by company size



Key research questions

- What should be the scope of a future IFRS?
- How should mineral and oil & gas reserves and resources be defined?
- When should an asset relating to mineral and oil & gas reserves and resources be recognised on the balance sheet?
- How should this asset be measured?
- What information about mineral and oil & gas reserves and resources should be disclosed in the financial report?



Scope

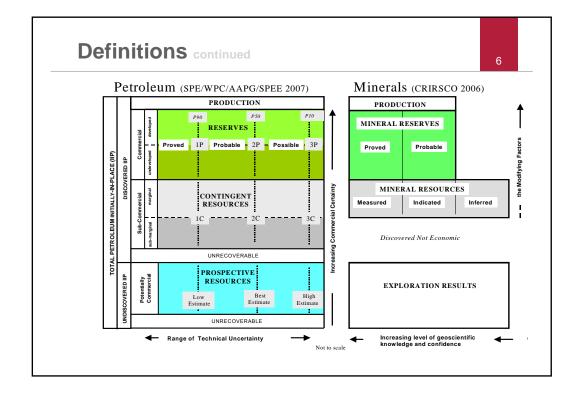
- Discussion paper proposes a single model for mining and oil & gas extractive activities
 - main business activities of exploration, evaluation, development and production are similar
 - subject to similar geological, economic and political risks and uncertainties



Reserves definitions

- · Definitions key for disclosures
 - No existing set of broadly accepted definitions
- Discussion paper proposes
 - Oil & gas PRMS
 - Minerals CRIRSCO template
- Why
 - Wide acceptance
 - Broad and comprehensive scope
 - Broad equivalence between key concepts





Asset recognition

- Discussion paper proposes that an entity should account for the minerals or oil & gas property
- Initial recognition when acquire legal rights to explore
- Over time this asset is enhanced by
 - information from exploration & evaluation activities
 - development to access the minerals or oil & gas
 - additional rights and approvals
- Unit of account
 - evolves from an area defined by the exploration rights (in initial exploration) to the field or mine (in development)

Asset measurement

8

BIFRS

- Historical cost is verifiable but has limited relevance to users
 - no correlation between finding & development costs incurred and future cash flows that will be generated
- Fair value requires too many subjective assumptions and estimates to be useful or comparable
- Discussion paper proposes measuring at historical cost
 - neither cost or fair value provide significant benefit to users
 - historical cost measurement is less costly for preparers

- Reserves
 - Quantities: proved and probable, changes
 - Disaggregate by risk: commodity, geography
 - Key inputs: assumptions, sensitivities
 - Value?
- Financial
 - Revenue by commodity
 - Exploration, development and production costs



Disclosure

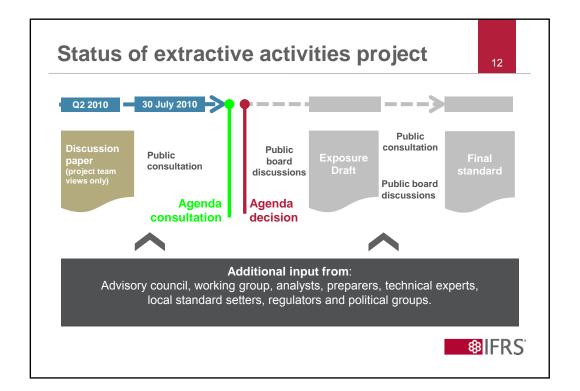
- Publish What You Pay (PWYP)
 - PWYP are concerned that resource wealth is not benefiting citizens of many resource-rich developing countries
 - Intended to complement EITI ("publish what you earn")
 - Disclosure of country-specific information including information on payments to governments
 - How useful is that information to investors and lenders?
 - investment and reputational risk evaluations



Disclosure considerations

- If included in an IFRS, the disclosures will have to be audited
 - Do auditors have the knowledge?
 - What will it cost?
 - Can filing deadlines be met?
- If disclosures are not in an IFRS, how can they be mandatory on a global basis?
- Publish What You Pay
 - Do such disclosures have a place in financial reports?
 - Preparation and audit concerns





IFRS Foundation

IFRIC 20 Stripping costs in the production phase of a surface mine

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Why the need for an interpretation?

• US GAAP: variable production cost

Diversity in existing practice

- Canadian GAAP: variable production costs, but may be capitalised if a 'betterment' exists
- IFRS:
 - No specific guidance
 - excluded from relevant standards
 - diversity of practices
 - 'Strip ratio approach' is common:
 - life-of-mine strip ratio
 - 'normal' levels of stripping costs: current period operating costs
 - 'excess' stripping costs: capitalised and amortised over remaining life of mine

Scope 15

Waste removal costs incurred in:

- Surface mining
- Production phase
- Does not address:
 - Underground mining
 - Application to oil sands extraction
 - Pre-production stripping



Asset recognition

- Two potential benefits from stripping activity:
 - Production of usable ore (inventory)
 - Improved access to ore that will be mined in future
- Ore produced accounted for in accordance with IAS 2 Inventories
- Benefit of improved access recognised as an asset if:
 - Probable future economic benefits
 - Can identify component of ore body for which access improved
 - Costs can be measured reliably
- 'Stripping activity asset' is part of an existing asset



Initial measurement

- Stripping activity asset measured at cost:
 - Directly incurred costs
 - Allocation of attributable overheads
- Measure cost directly if separately identifiable from cost of inventory
- If cost not separately identifiable, allocate stripping costs using relevant production measure
 - Don't allocate using sales values



Subsequent measurement

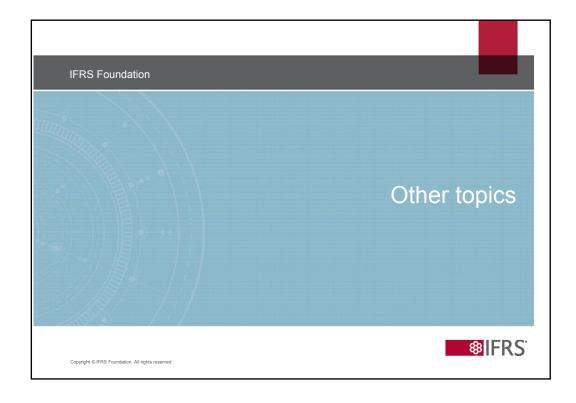
- Measure stripping activity asset consistently with larger asset of which it is a part
 - Cost, or revalued amount
 - less depreciation / amortisation
 - less impairment
- Depreciate / amortise over component of ore body for which access was improved



Transition and effective date

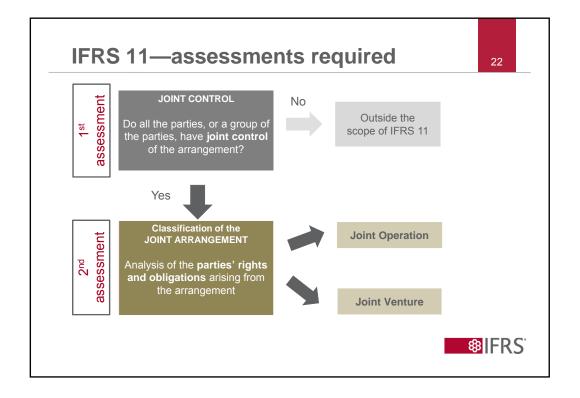
- Apply to stripping costs incurred on or after beginning of earliest period presented
- Opening balances to be linked to components of ore for which access was improved
 - If no such ore remains / can be identified, write off against opening retained earnings

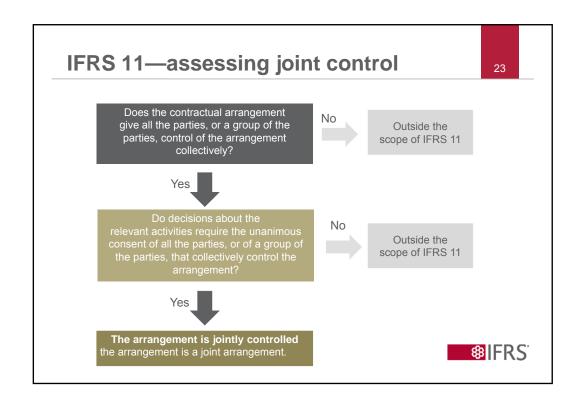


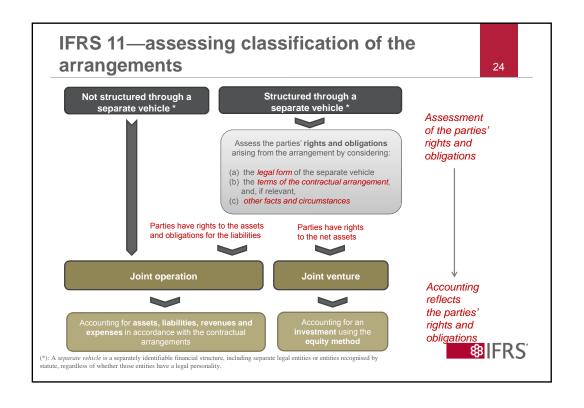


- IFRS 11 Joint Arrangements
- Leases
- Revenue

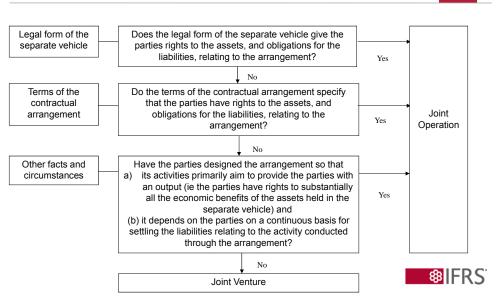








IFRS 11—assessing the classification (arrangements structured through a separate vehicle)



Leases—Definition of a lease

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Contract in which the right to use an asset (the underlying asset) is conveyed, for a period of time, in exchange for consideration

- Fulfilment depends on identifiable asset
- Right to control use of underlying asset
- Notion of control changed
 - Update to 'direct the use' and receive benefits
 - Change from IFRIC 4/ED if entity obtains substantially all output ≠ control



Leases—Industry issues

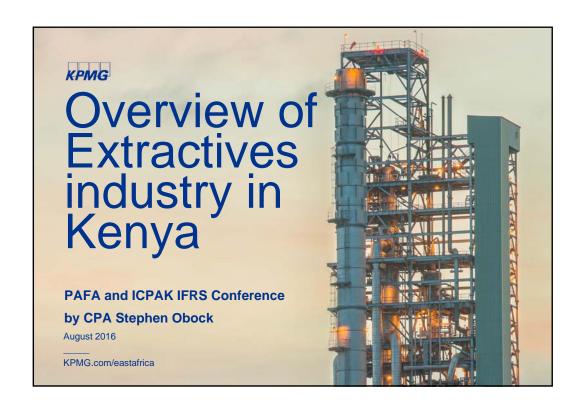
- Scope: What is a lease, what is a service?
 - Tolling arrangements
 - Drilling rig contracts
 - Pipelines
- Recognition and measurement
 - Contingent consideration (variable payments/receivable)
 - No change for embedded derivatives



Revenue—industry issues

- Scope: What is a customer?
 - Underlift and overlift
 - Production sharing contracts
- Recognition and measurement
 - Provisional pricing
 - Take or pay contracts





Contents Slide Oil & Gas sector Mining sector 14 IFRS 6 21 Discussions 35

Oil & Gas Sector



Oil & Gas value chain



Upstream

Comprises exploration and production (E&P) of petroleum crude oil and natural gas.



Midstream

Involves storage and transportation from exploratory wells to storage terminals.



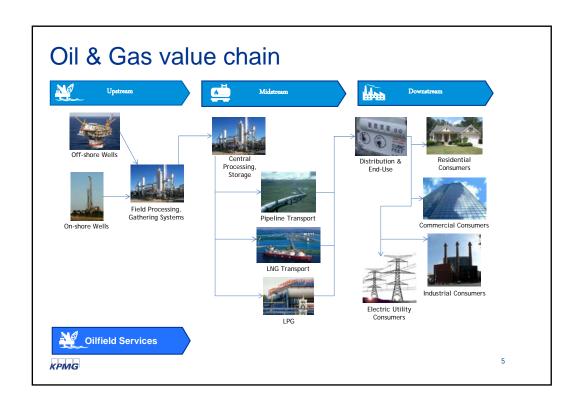
Downstream

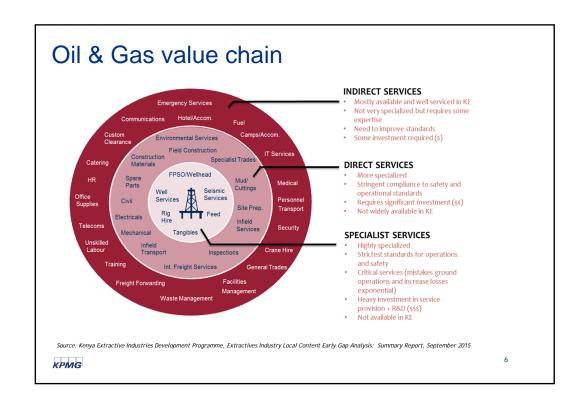
Involves refining, processing and marketing, after the production phase, through to the point of sale.



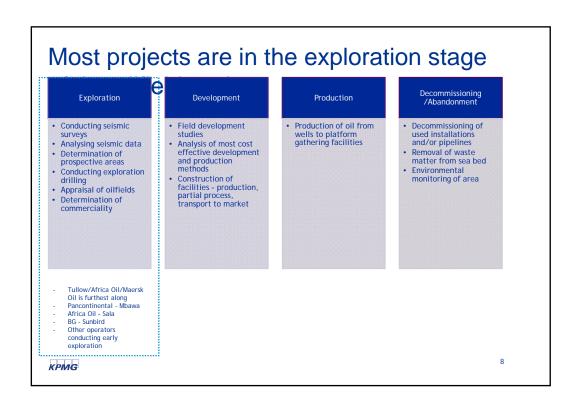
Oil Field Services

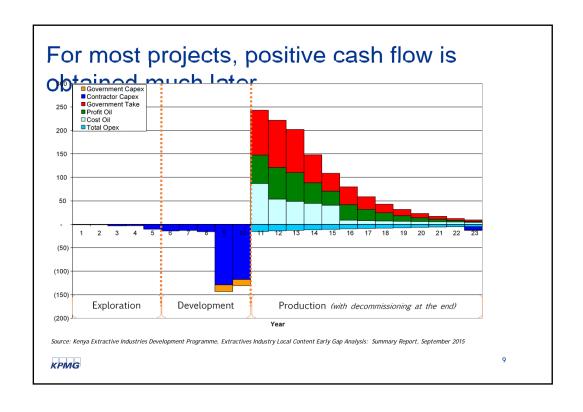
Includes companies involved in the operation, manufacture and provision of services across the value chain – at various levels of complexity.

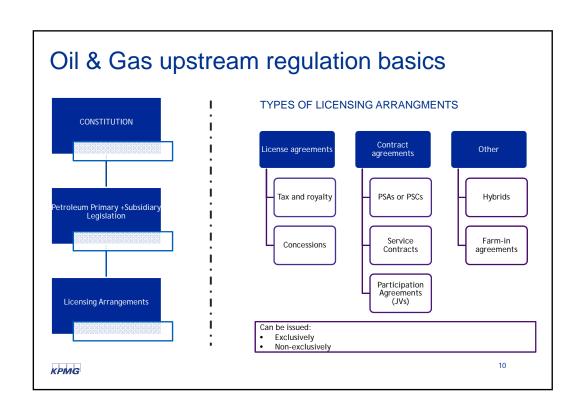


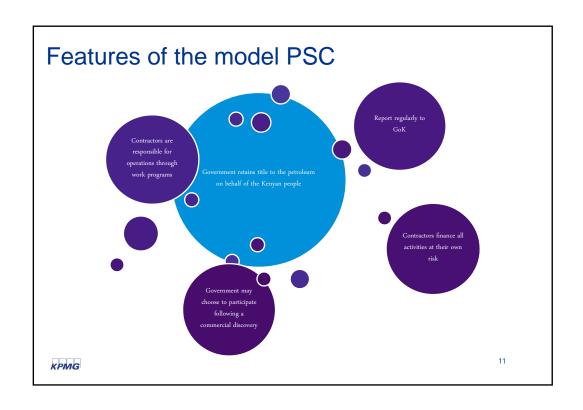


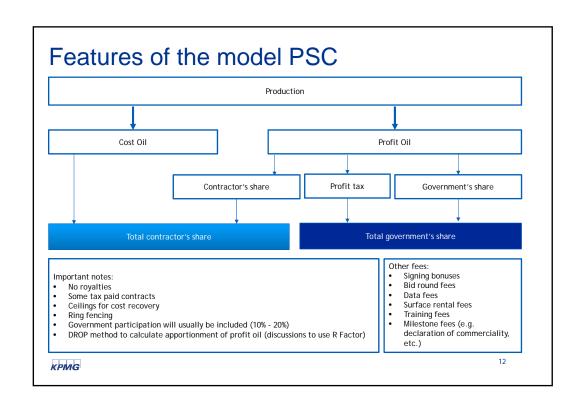
Upstream Oil & Gas in Kenva Kenya Exploration Blocks Kenya has four (4) petroleum exploration basin: - Lamu - Anza - Tertiary Rift 46 petroleum exploration blocks currently - Based on geological potential to find oil - Licensed under PSCs - 44 licensed blocks - 23 operators - 9 relinquished blocks to be gazetted Seventy four (74) wells drilled to date - One additional well (Cheptuket) in 2016 with active petroleum system ■ Twelve (12) hydrocarbon discoveries to date - Nine (9) of which are in Turkana County - Others are offshore Lamu and Northeastern Kenya Currently debating the midstream options for route-to-market Source: National Oil Corporation of Kenya KPMG

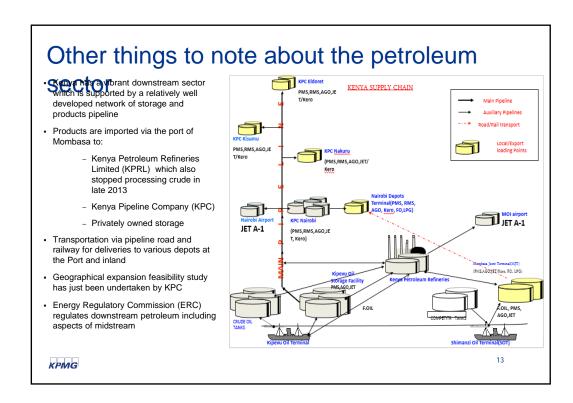




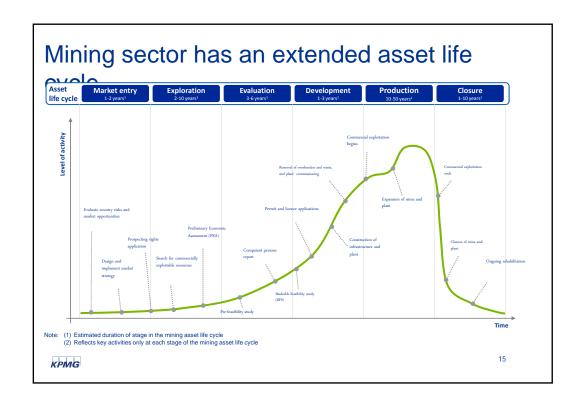


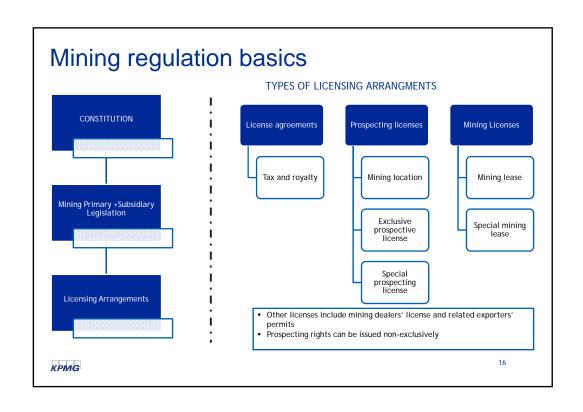


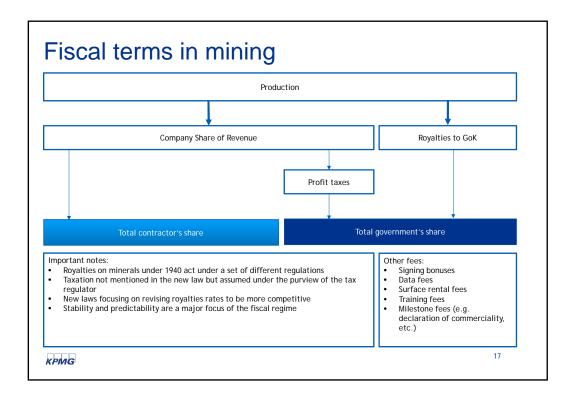


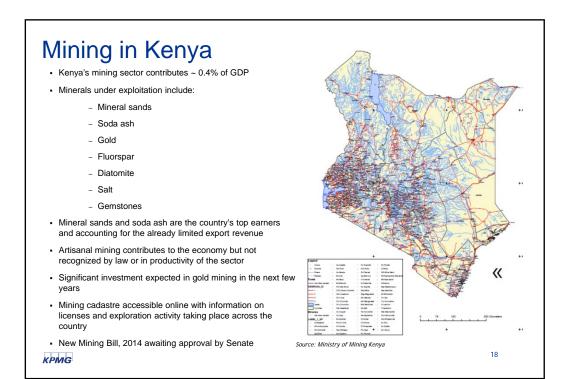


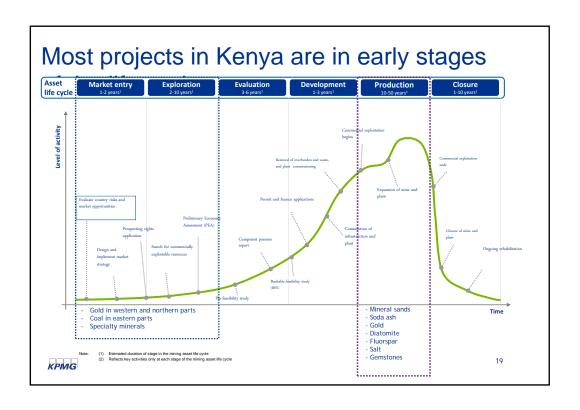
Minin g sector











Other things to note about the mining

mapped out by geological data

- Data on geological potential of Kenya remains a challenge
- Not surprisingly, Kenya is underexplored and expenditure in mining is relatively low
- Many licenses have no activity
- Value chain will differ slightly from mineral to mineral e.g. gold vs. mineral sands, but essentially it has the same cycle from exploration to closure/decommissioning
 - Heavy reliance on infrastructure for route-to-market
 - Water and energy are key resources to make operations viable
- Cash profile of the mining sector not very different from that of upstream oil and gas
 - Upfront investment in exploration is very high risk
 - Recovery based on quality and quantity of mineral deposits discovered





IFRS 6



Scope

- The scope of IFRS 6 Exploration for and Evaluation of Mineral Resources is limited to the recognition, measurement and disclosure of expenditure incurred in the phase covering the E&E of mineral resources.
- Although the term used is 'mineral resources', the definitions in IFRS 6 clarify that this extends to
 cover minerals, oil, natural gas and other similar non-regenerative resources meaning that it
 applies across the extractives industry sector
 - The limitation of scope to cover the exploration and evaluation phase means that IFRS 6 does not apply to expenditure incurred:
 - > In the previous prospecting phase
 - > In all phases after the E&E phase has been completed, including development, production, closure and rehabilitation.



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Overview

- IFRS 6 Exploration for and Evaluation of Mineral Resources has the effect of allowing entities
 adopting the standard for the first time to use accounting policies for exploration and evaluation
 assets that were applied before adopting IFRSs.
- It also modifies impairment testing of exploration and evaluation assets by introducing different impairment indicators and allowing the carrying amount to be tested at an aggregate level (not greater than a segment)



Issue date

IFRS 6 was issued in December 2004 and applies to annual periods beginning on or after 1 January 2006



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Key aspects of IFRS 6

- · Applies only to Exploration and Evaluation (E&E) expenditure
- Contains an exemption from certain of the requirements of IFRS, meaning that there are fewer restrictions placed on what qualifies to be capitalised as an asset (or part of an asset)
- Permits a choice of whether an entity expenses all E&E expenditure as incurred, or capitalizes
 that expenditure (in which case there is a choice about how much of that expenditure might be
 capitalized)
- Contains certain exemptions from the requirements of IAS 36 Impairment of Assets, for the purposes of assessing whether E&E expenditure which has been capitalized is impaired.



IFRS 6 – Recognition and Measurement of

Expensing all related costs to fully capitalizing them

Therefore, exploration and evaluation assets are defined in terms of the policy each

KPING

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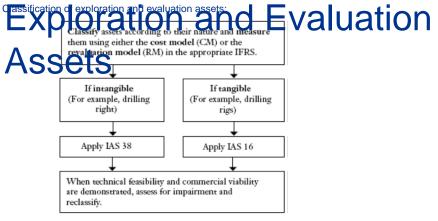
IFRS 6 – Recognition and Measurement of

Examples of costs that may be capitalized:

Cost of exploration rights, geological studies, exploratory drilling and sampling, and







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Measurement

- Exploration and evaluation assets shall be measured at cost.
- After recognition, an entity shall apply either the cost model or the revaluation model to the
 exploration and evaluation assets. If the revaluation model is applied (either the model in IAS 16
 Property, Plant and Equipment or the model in IAS 38) it shall be consistent with the classification
 of the assets

Impairment

- The exploration and evaluation assets are tested for impairment when facts and circumstances suggest that the carrying amounts may not be recovered. The assets are also tested for impairment before reclassification out of exploration and evaluation.
- The impairment is measured, presented and disclosed according to IAS 36, 'Impairment of assets', except that exploration and evaluation assets are allocated to cash-generating units or groups of cash-generating units no larger than a segment.

Consider the following:

- the right to explore expires and is not expected to be renewed
- no other substantial expenditures are planned for exploration or evaluation in the area
- the entity decides to stop exploration and evaluation activities because viable quantities have not been found in the area
- although development is likely, the costs capitalized as exploration and evaluation assets exceed the amounts that are likely to be recovered

Impairment losses are taken to profit or loss - may be reversed



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Presentation

- Classification of exploration and evaluation assets
 - An entity shall classify exploration and evaluation assets as tangible or intangible according to the nature of the assets acquired and apply the classification consistently.
- Some exploration and evaluation assets are treated as intangible (e.g. drilling rights), whereas
 others are tangible (e.g. vehicles and drilling rigs). To the extent that a tangible asset is
 consumed in developing an intangible asset, the amount reflecting that consumption is part of the
 cost of the intangible asset.
- However, using a tangible asset to develop an intangible asset does not change a tangible asset into an intangible asset.



Disclosure

- IFRS 6 has an overriding disclosure requirement to include information in the financial statements
 that identifies and explains the amounts that have been recognized as exploration and evaluation
 assets. Such information should include the entity's accounting policy for the recognition and
 measurement of exploration and evaluation assets.
- An entity is also required to identify the amount of assets, liabilities, income and expense arising
 from the exploration and evaluation of mineral resources. In relation to the statement of cash flows
 the amount of operating and investing cash flows arising from the exploration and evaluation of
 mineral resources should be disclosed
- Disclosure objective: to identify and explain amounts recognized in the financial statements that result from exploration and evaluation activities
- · If classified as PP&E, use IAS 16
- If classified as intangible asset, use IAS 38



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IFRS 6 - Disclosure

- · Minimum disclosure:
 - Accounting policies for exploration and evaluation expenditures and their capitalization as assets
 - The amount of assets, liabilities, income, expense, and operating and investing cash flows from exploration and evaluation activities



Discussions



KPMG

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kpmg.com/eastafrica





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Joint IFRS® Foundation, PAFA and ICPAK IFRS Conference and *IFRS for SMEs* workshop

24–26 August 2016 Safari Park Hotel, Nairobi, Kenya

Break-out sessions:

Implementing IFRS 16 Leases

DARREL SCOTT Member IASB

AGNES LUTUKAI Head, Department of Professional Practice West Africa KPMG Professional Services

GEOFFREY INJENI

Faculty and Consultant in Accounting and Finance
Strathmore Business School and
Trainer and Member of Research and Development Committee
ICPAK

New Leases Standard





- IFRS 16 Leases published in January 2016
 - replaces IAS 17 and related interpretations
 - changes lessee accounting substantially
 - little change for lessors
- Effective date 1 January 2019
 - early application permitted (only with application of IFRS 15 Revenue from Contracts with Customers)



The need for change

Leases are an important and flexible source of financing listed companies using IFRS Standards or US GAAP estimated to have US\$3.3trillion lease commitments

Over 85% of lease commitments do not appear on balance sheet today

Therefore, it is <u>difficult</u> for investors and others to:

- Get accurate picture of entity's lease assets and liabilities
- Compare companies that lease assets with those that buy
- Estimate the amount of off balance sheet obligations: often overestimated



The need for change Currently a lack of information

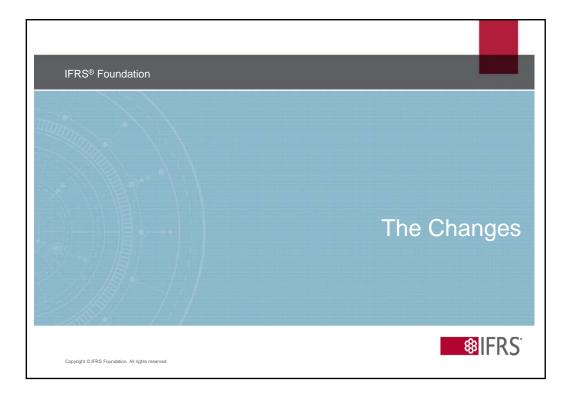
· 6 retail chains that ultimately went into liquidation

| Retailer | Off balance sheet leases | | On balance | Discounted leases |
|--------------------|--------------------------|---------------------------|-------------|----------------------------------|
| Retailei | (undiscounted)1 | (discounted) ² | sheet debt1 | as multiple of debt ³ |
| Borders (US) | \$2,796M | \$2,152M | \$379M | 5.68 |
| Circuit City (US) | \$4,537M | \$3,293M | \$50M | 65.86 |
| Clinton Cards (UK) | £652M | £525M | £58M | 9.05 |
| HMV (UK) | £1,016M | £809M | £115M | 7.03 |
| Praktiker (DEU) | €2,268M | €1,776M | €481M | 3.69 |
| Woolworths (UK) | £2,432M | £1,602M | £147M | 10.90 |

<sup>Based on averaged published financial statement data available for 5 years before company entered Chapter 11 (US), liquidation (UK) or bankruptcy (DEU).
Estimated using (i) a discount rate of 5% and (ii) estimated average lease terms based on the information disclosed in the financial statements.

Off balance sheet leases (discounted) as a multiple of on balance sheet debt</sup>





What's changed for lessors & lessees?

6

Changes to lessor accounting

 Substantially carry forward IAS 17 accounting requirements; some additional disclosure requirements

Changes to Lessee accounting

• Former operating leases capitalised. All¹ leases accounted for similarly to today's finance leases

Balance Sheet

Income statement

Cash flow statement

- 1 Leased assets
- Operating expense
- Operating flows

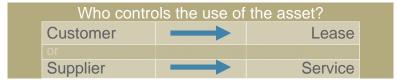
- † Financial Liabilities
- ♠ Finance cost
- **†** Financing flows

- Equity
- ¹ Exemptions for short-term leases and leases of low-value assets



Definition of a lease

- Similar to previous definition, changed guidance on control
- Control = directing the use and obtaining the benefits from use
- Based on control of the use of an identified asset

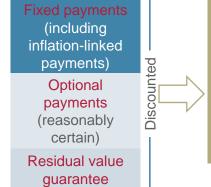


- Separate services provided with leases
 - Separate using available information (including estimates)
 - Option to not separate components



Lessee Accounting Balance sheet: what's included?

 Increase in lease assets and financial liabilities—all leases reported on balance sheet (other than short-term leases and leases of low-value assets)



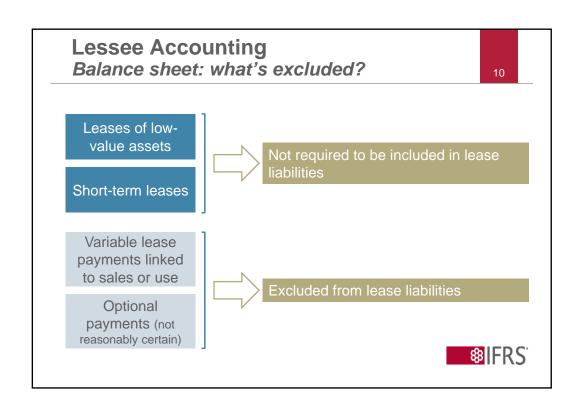
Included in lease liabilities:

- Fixed payments (including inflationlinked payments)
- Optional payments if lessee is reasonably certain to extend beyond non-cancellable period
- Expected amount of residual value guarantees



- A lease conveys the <u>right to use</u> an asset for a period of time in exchange for cash payments
- Lessee reports lease assets and liabilities on balance sheet, except for short-term and for low-value asset leases, at present value of future lease payments
- Discount rate: the rate implicit in the lease, or, if rate implicit not available, lessee's incremental borrowing rate
- Exclude variable payments and most optional payments
- · Portfolio application, simplified reassessment





- Short-term leases
 - Leases with lease term <12 months
- Low-value asset leases
 - Leased assets in order of magnitude of <\$5,000
 - Examples: laptops, office furniture, mobile phones

*IFRS

Lessee Accounting Initial measurement

12

Right of use asset (at cost)



Lease liability (present value of lease payments)

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Initially measure equal to lease liability, adjusted for:



Prepayments



Lease incentives



Initial direct costs



Dismantling/restoration costs



Lessee Accounting Initial measurement

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- Assets and liabilities measured on a present value basis
- Lease payments
 - Those payable during non-cancellable period <u>plus</u> optional periods that the lessee is reasonably certain to exercise
 - Include fixed payments and inflation-linked payments
 - Exclude variable payments linked to future sales or use
- Discount rate
 - Rate in the contract or lessee's incremental borrowing rate



Lessee Accounting Subsequent measurement

- Right of Use (ROU) Asset
 - Balance sheet presentation separately as an asset
 - Depreciated over the life of the lease
 - Depreciation carried in profit and loss
 - · Reassessed for impairment
- Liability
 - Balance sheet presentation separately as a liability
 - Interest expense (discount unwind) through profit and loss as interest
 - Simplified reassessment



Lessee Accounting Presentation

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Balance sheet

- ROU assets together with PPE or as own line item
- Lease liabilities in accordance with IAS 1

Income statement

- Depreciation of all leased assets
- Interest expense for all lease liabilities

Cash flow statement

- Principal within financing activities
- Interest within either operating or financing activities (IAS 7 option)



Subleases, Sale and leaseback

- Subleases—Intermediate lessor
 - Account for head lease and sublease as two separate contracts
 - Classify a sublease with reference to the ROU asset arising from the head lease
 - Should not offset lease assets and liabilities, or income and expenses, unless meets existing IFRS guidance for offsetting
- Sale and leaseback transactions
 - Sale must meet the requirements in IFRS 15
 - Seller/lessee recognises only gain related to rights transferred
 - Adjustment made for off market terms



Lessor Accounting

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- In essence, no change to lessor accounting in IAS 17
- Feedback on 2013 ED
 - Lessor accounting in IAS 17 is not broken
 - Concerns about cost and complexity
- IFRS 16: enhanced disclosures
 - Information about the residual value risk
 - Operating leases: separate disclosures for leased assets and assets used by a lessor for other than leasing



Quantitative disclosures

- Breakdown of lease costs
- Total lease cash flows
- Maturity analysis of undiscounted commitments
- Information about ROU assets by major class of leased asset

Entity-specific information

- Additional information, if relevant
- Extension and termination options
- Variable lease payments
- Residual value guarantees
- Sale and leaseback



Transition Former operating leases

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Fully retrospective approach

In accordance with IAS 8:

- Restate as if IFRS 16 always applied
- Provide line by line comparison disclosure

OR

Do not restate comparatives

- Adjust opening retained earnings
- Provide additional transition disclosure

Cumulative catchup approach

Optional practical expedients:

- Do not transition if ending <12 months
- Simplified asset measurement
- Onerous lease provisions
- Portfolio application
- Use of hindsight

BIFRS

Transition Other issues

- Definition of a lease optional practical expedient:
 - Not required to reassess contracts applying IFRS 16:
 - transition ongoing operating leases to IFRS 16
 - apply new definition requirements only to new contracts entered into after the date of initial application
- Subleases
 - Lessors must reassess classification of subleases
- Sale and leaseback transactions
 - Do not reassess whether a sale occurred
 - · Transition the leaseback like any other lease



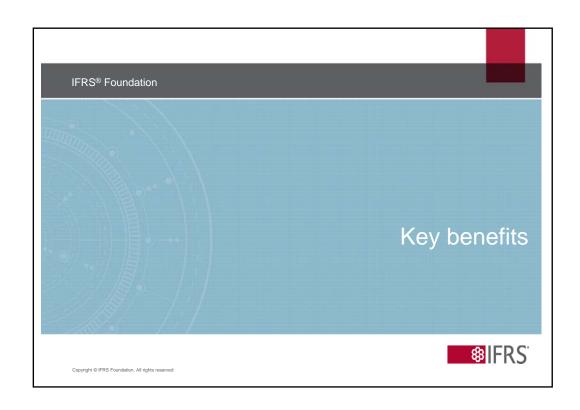


Lessee—who will be affected?

| % of IFRS/US GAAP listed entities reporting material off balance sheet leases | | | | |
|---|-----------|--|--|--|
| North America | 62% | | | |
| Europe | 47% | | | |
| Asia / Pacific | 43% | | | |
| Africa / Middle East | 23% | | | |
| Latin America and Caribbean | 23% | | | |
| Future minimum payments for off balance sheet leases ¹ | US\$2.9tl | | | |
| PV future minimum payments for off balance sheet leases ² | US\$2.2tl | | | |

- Off-balance-sheet lease financing numbers substantial
- About 50% of listed companies report material off balance sheet leases
- Use of off balance sheet leases is highly concentrated





^{1 2014} annual reports for the vast majority of companies. 2 Estimate using the average cost of debt for these companies, that was 5%.

Key benefits of IFRS 16

- Greater transparency about financial leverage and capital employed
- More level playing field for all market participants
- Reduce the need to make adjustments and to provide 'non-GAAP' information
- Improve comparability between those who lease and those who borrow to buy

Facilitate better capital allocation by enabling better credit and investment decision-making by both investors and companies



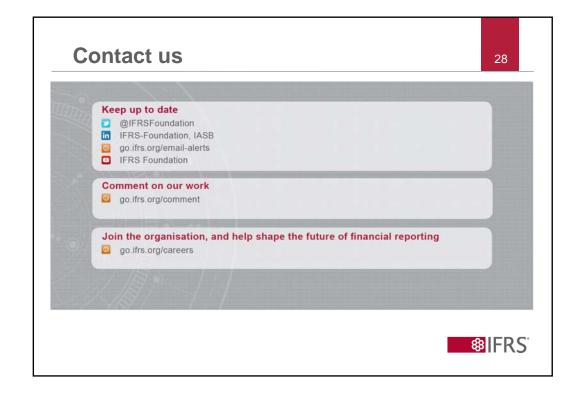
Further information

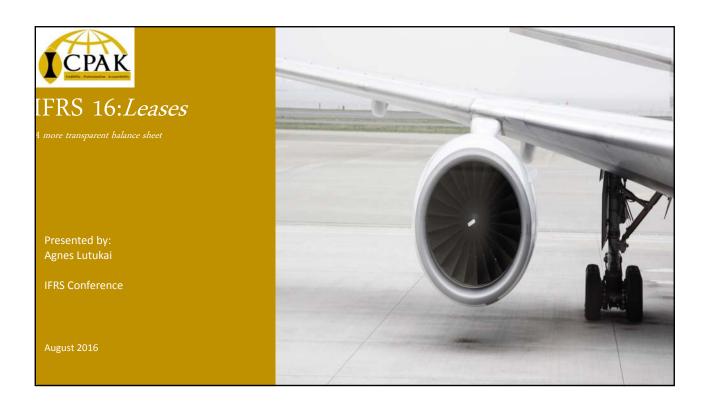
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- Leases website http://www.ifrs.org/Current-Projects/IASB-Projects/Leases
- Effects analysis
 http://go.ifrs.org/Leases/effects-analysis
- Project summary and feedback statement <u>http://go.ifrs.org/Leases/project-summary</u>
- Register for email alerts
 http://eifrs.ifrs.org/eifrs/Register











IFRS 16 – An Overview



Quotable Quote

Change is the law of life.

And those who look only to
the past or present are certain
to miss the future.

~ John F Kennedy

An Overview...

On 13 January 2016, the International Accounting Standards Board ("IASB") issued a new standard - IFRS 16: Leases, thereby realising its long-standing goal of ensuring that entities that engage in lease transactions present more transparent balance sheets by providing relevant information in a manner that faithfully represents the transactions.

IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of lease transactions and replaces the following standards and interpretations:

- IAS 17 Leases
- IFRIC 4 Determining whether an Arrangement contains a Lease
- SIC-15 Operating Leases Incentives
- SIC-27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease

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The \$3 trillion standard

"One of my great ambitions before I die is to fly in an aircraft that is on an airline's balance sheet..."

Sir David Tweedie (Former IASB Chairman) April 2008 "Listed companies are estimated to have US\$3.3 trillion of lease commitments, over 85% of which do not appear on their balance sheets..."

Hans Hoogervorst (IASB Chairman) January 2016

Why is this important?

- Most companies lease assets and there is a radical overhaul of lessee accounting.
- Under IFRS 16, both operating and finance leases will be on balance sheet.
- On/off-balance sheet test for leases will be based on whether the contract meets the definition of a lease.
- Significant changes in key reporting metrics.
- Stakeholders/investors will want to understand the impact on their businesses.



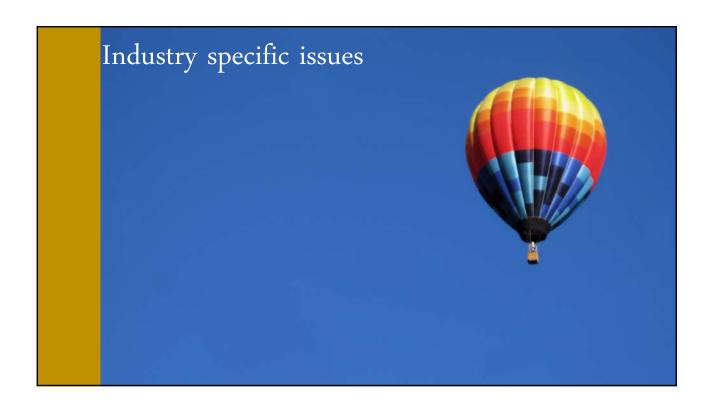
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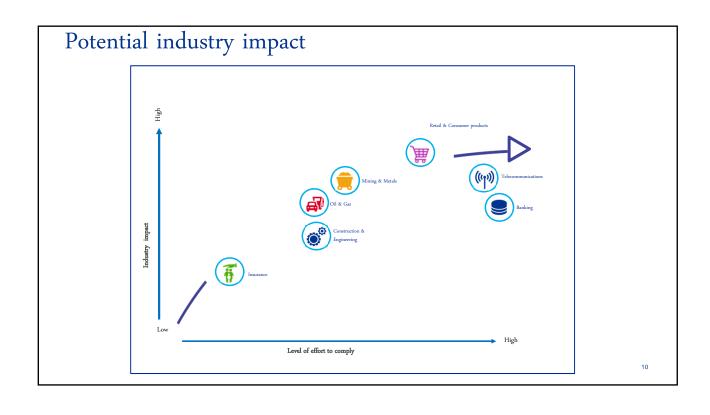
Impact on financial ratios

Profit/loss Balance sheet Ratios

EBITDA Total assets Gearing

EPS (in early years) Net assets Interest cover Asset turnover





Lessees face major changes

Leases on balance sheet

Balance sheet

Asset

= 'Right-of-use' of underlying asset

Liability

= Obligation to make lease payments

P&L

Lease expense

Depreciation

- + Interest
- = Front-loaded total lease expense

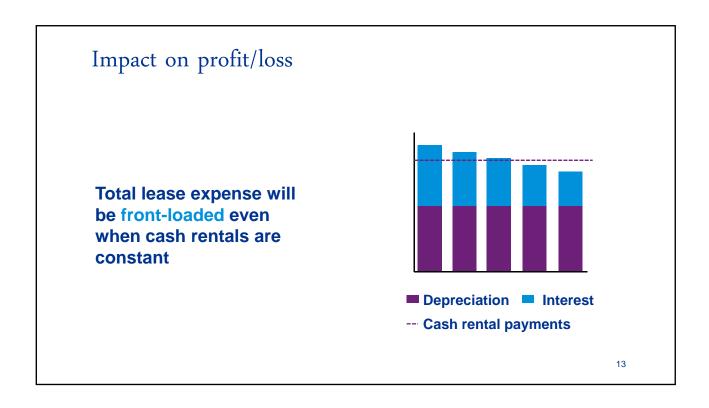
Improved comparability between companies that lease and companies that borrow to buy assets.

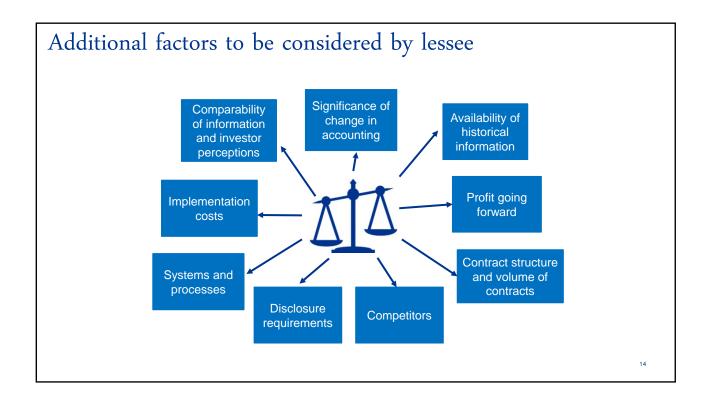
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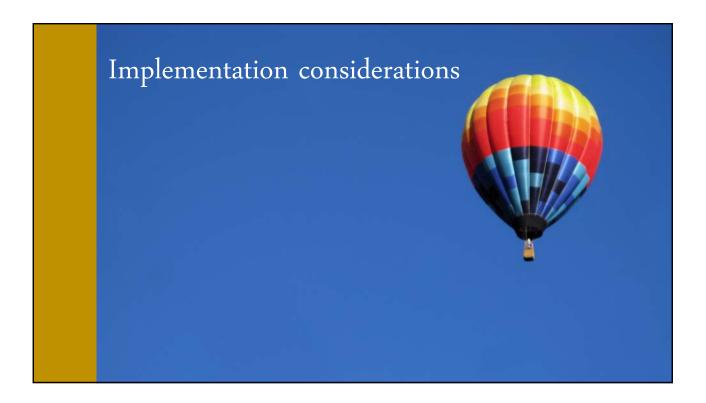
Impact on balance sheet over lease period

Companies with operating leases will appear to be more asset-rich, but also more heavily indebted



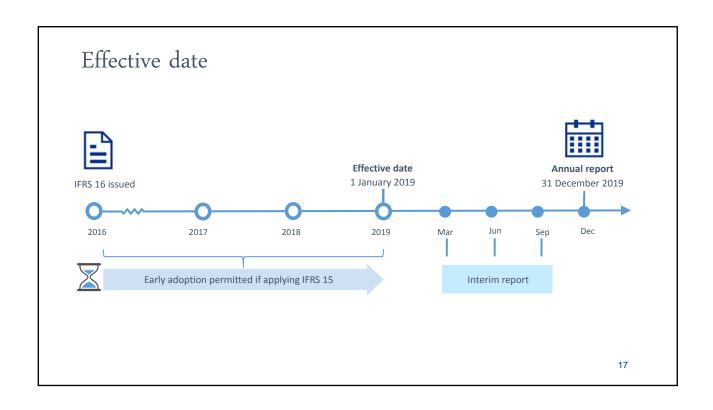


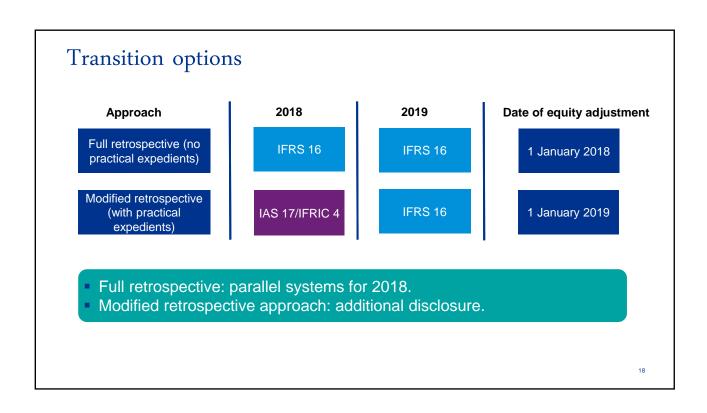




Why is this important?

- Multiple transition options are available.
- The choice of transition option impacts:
 - Opening balance sheet.
 - Income statements in subsequent years.
 - Information required.
 - Implementation costs.
- An early decision is key to a successful implementation project!!!





Applying the new standard

Apply the new definition to all contracts (Retrospectively to all accounting periods)

OR

Grandfather existing contracts and apply the new definition only to new contracts (Practical expedient)



Comparability







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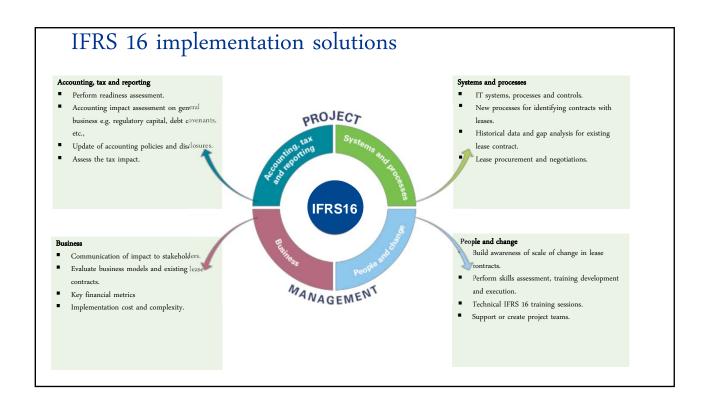
Implementation and transition



Preparing for an accounting change of this magnitude presents a considerable challenge.

Understanding how the new standard will affect your company is critical. All companies with significant leasing activities should review the new standard and begin thinking about the implications now.

Starting early is the best way to reduce the overall cost of implementation, avoid unwanted surprises and costly mistakes.





Next steps...

Initial discussion points

- Discuss initial thoughts on the expected impact of IFRS 16.
- Highlight non-accounting areas potentially affected.
- Start reviewing existing lease contracts and inform suppliers (i.e. lessors) of impact of IFRS 16.
- Planned communications with external stakeholders, where relevant.



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Key points to remember

- New leases standard will impact most companies.
- Assessing whether there is a lease can be very judgemental.
- There are optional exceptions for short-term leases and leases of low value items.
- IFRS 16 improves comparability between companies that lease and companies that borrow to buy assets.
- Multiple transition options are available.
- Process of assessing impact should start now.





Thank you!

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- 1. Planning for IFRS 16 Implementation
- 2. Specific Issues for different sectors
- 3. Activities by various stakeholders in terms of supporting implementation of IFRS 16





1. Planning for IFRS 16

2

IFRS 16 was issued in January this year (2016) and is effective from January 2019, so no entity has applied. Yet to discuss with various stakeholders on potential impact of the standard but some issues that may arise are as follows especially for LESSEES:





1. Planning for IFRS 16

1. Accounting systems (Processes and records) will need to be revised to enable proper preparation of financial reports, mainly to comply with on-balance sheet treatment of previous operating leases.





1. Planning for IFRS 9

4

2. Training is required so that accountants identify potential problems and gaps that may make it difficult to implement IFRS 16 for lessees. For example valuation issues and thresholds for assets treated previously as operating leases and now required to be treated as finance leases. This includes transition.





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- 3. Some issues still rise that require judgment like the lease period.
- 4. The need to link IFRS 16 with other important standards like IFRS 15 (Dealers in lease assets) and IFRS 9 (finance lease obligations).





1. Planning for IFRS 9

6

5. IFRS 16 may impact on practical issues on disclosures and taxes.





2. Specific Sector Issues

1. Non Financial entities

There could be a major impact on reporting especially where such entities are using leases to finance substantial portions of their assets and issues of transioning.





2. Specific Sector Issues

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2. Financial Entities - Banks

Most banks are lessors and hence no significant impact on their financial. However, those banks that have been using operating leases may need to transition to finance leases, hence may increase liabilities in their balance sheet. An Indirect effect on risk measures and may also increase the interest expense.





2. Specific Sector Issues

2. Financial Entities - Pension Firms

Most pension firms would be classified as lessors hence minimal impact expected here, unless some assets that are under operating leases and need to be classified as finance leases.





2. Specific Sector Issues

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2. Financial Entities - Insurance Co.s

Mostly lessors, but if having operating leases, then the leases may need to be reclassified into finance, hence increasing liabilities.





2. Specific Sector Issues

2. Financial Entities – Investment co.s Mostly lessor, so less effect on finacials.





3. What is being done to prepare

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1. ICPAK has several IFRS workshops, nearly every month and some sessions cover Leases. These sessions are also customized for specific sectors. ICPAK also has inhouse trainings for companies that have specific issues in accounting for leases and other assets. In addition we have the Financial Reporting Excellence awards.





3. What is being done to prepare

- 2. KASNEB/ACCA, curriculum also provides avenues for examining current issues such as the new accounting standard for leases in the accounting exams.
- 3. Audit firms also have sessions for training and materials in these areas.





Joint IFRS® Foundation, PAFA and ICPAK IFRS Conference and *IFRS for SMEs* workshop

24–26 August 2016 Safari Park Hotel, Nairobi, Kenya

Break-out sessions:

IFRS regulatory issues

WEI-GUO ZHANG

Member

IASB

JOSEPH KARIUKI

Partner, Audit

KPMG Kenya

WILLYSON YANGA Capital Markets Authority



International Financial Reporting Standards Conference

IFRS regulatory issues

August 2016

Why are we discussing this topic?

- To obtain an understanding of regulatory perspective on the application of IFRS
- Practical application can be complex



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Agenda

What to expect from the session

- Approach to regulating IFRS
- · Collaboration with the regulators/ICPAK
- Specific issues identified

Approach to regulating IFRS

What are the advantages of converting to IFRS:

- Businesses present financial statements on same basis as its foreign competitors
- Makes comparisons easier
- Companies with subsidiaries in countries that permit IFRS use one accounting language company-wide
- Companies may need to convert to IFRS if they are a subsidiary of a foreign company that must use IFRS
- Companies may also benefit by using IFRS if they wish to raise capital abroad
- Facilitates Good Governance & accountability

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Approach to regulating IFRS (cont)

- All the countries within the East Africa region have adopted IFRS
- The local institutes are mandated to oversee the implementation of IFRS in the respective countries
- Through the Council, the Institute has delegated this role to the Professional Standards Committee (PSC) to provide guidance on the implementation of IFRS
- The PSC collaborates with the regulators, practioners and preparers of the financial statements to harmonise the application of IFRSs

ICPAK Collaboration with regulators

The main regulations we see in the market are:

- The Capital Markets Authority
- Central Banks
- Insurance Regulatory Authority
- SASRA
- Revenue Authorities
- Companies Act
- Competition Authority
- Unclaimed Financial Assets Authority

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ICPAK Collaboration with regulators (Cont)

Areas of collaboration:

- Review of exposure drafts and making comments on areas that may conflict with regulations
- IFRS trainings/workshops
- · Lobbying for specific matters on regulations especially taxes
- Joint conferences with the regulators
- IFRS technical guidance
- Awareness conferences/meetings

Specific issues identified -**Central Banks**

- Central Banks
 - Central Banks requires impairment losses to be determined based on a set % of loans balances having certain characteristics e.g. age rather than actual incurred losses
 - In addition banks are required to suspend interest on non performing accounts
 - The aggressive approach to impairment in some instances results in impairment losses in excess of incurred losses as determined under IFRS
 - The approach adopted by the Central Banks is not permissible under IFRS

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Specific issues identified – Central Banks (Cont)

- Central Banks (continued)
 - Banks therefore reports the impairment losses under IFRS
 - To comply with Central Bank requirements, any excess impairment above the amount determined under IFRS is recognized by transferring amounts from retained earnings to a separate category of equity – Credit risk reserve
 - The same approach noted above applies to SASRA
 - In Tanzania, Quarterly Financial Reports for Banks are not compliant with IAS 34
 - NBAA is in discussion with BOT to mandate application of IAS 34 for all interim/quarterly reports published for use by general public

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Specific issues identified – Income Tax

- Income Tax
 - For purposes of corporation tax the revenue authorities recognizes impairment losses as allowable when the following conditions are met:
 - Loss of contractual right through a court order
 - No form of security is realizable or security has been realized and proceeds could not cover entire amount
 - 3. Debtor is insolvent or bankrupt
 - 4. Cost of recovering debt exceeds the debt
 - Efforts to recover the debt are abandoned for another reasonable cause

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Specific issues identified – Income Tax (cont)

- Income Tax (Continued)
 - IFRS requires impairment losses to be determined by comparing the carrying amount to the estimated future cash flows discounted to the present value.
 - The revenue authority is yet to harmonise its requirement with the IFRS requirement
- Others
 - Deemed interest
 - Investments outside municipalities Nairobi, Kisumu, Mombasa

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Specific issues identified – CMA

- Capital Markets Authority
 - Generally CMA regulations are largely aligned to IFRS
 - Specific disclosures under CMA relates to directors remuneration
 - The Institute is currently in discussion with the CMA on the Corporate Governance Guidelines & New Companies Act which are effective in 2017

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Specific issues identified – IRA

- Insurance Regulatory Authority
 - Generally regulations are largely aligned to IFRS
 - Specific issue that the PSC has dealt with in the past was recognition of deferred tax on Life Fund
 - PSC facilitated an awareness session with the regulator and CFO of insurance companies



Specific issues identified – ISA's

- New Auditors report
 - Effective for audits of financial statements for periods ending on or after 15 December 2016
 - Audit reports on listed entity financial statements will include "key audit matters" (KAMs) – a significant change
 - The PSC has engaged all the stake holders concerned to obtain clarity and views from the regulators before implementation
 - In Tanzania NBAA is debating on extending the requirement to include "KAMs in audit reports of ALL Public Interest Entities as opposed to only listed entities

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Challenges in implementing of IFRS

Some of the challenges we see in the implementation of IFRS:

- Technical difficulties in understanding and interpreting IFRS requirements
- Inability of MIS to accurately record, maintain and produce accurate financial reports related to IFRS
- Financial constraints for training and purchase of IFRS materials

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Thank you

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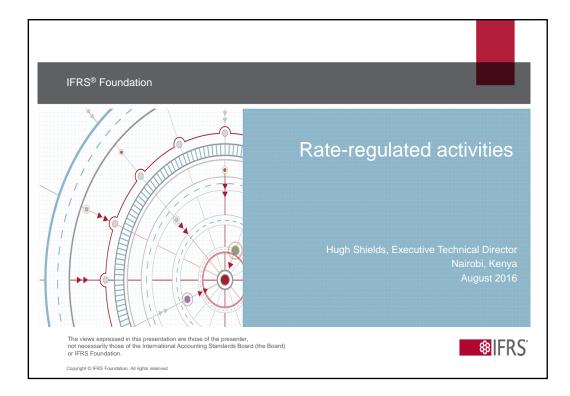
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Break-out sessions:

Rate regulated activities

HUGH SHIELDS

Executive Technical Director IASB



Agenda

- Introduction
 - Why we are doing the project
 - Discussion Paper: Reporting the Financial Effects of Rate Regulation
- Conceptual Framework
 - Elements
 - Executory contract
- Defined Rate Regulation
 - What is 'Defined rate regulation'?
 - The revenue requirement
 - Accounting question



- Many stakeholders have told the Board that, for entities that are subject to some types of rate regulation,
 - current predominant IFRS practice does not reflect the economic substance of the rights and obligations created by the rate regulation; and
 - IFRS financial statements currently do not provide investors and lenders with sufficient relevant information needed to make investing and lending decisions.

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Current predominant IFRS practice

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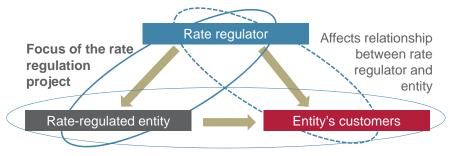
- Except for specified first-time adopters that apply IFRS 14 *Regulatory Deferral Accounts*, almost all entities:
 - eliminate 'regulatory deferral account balances' when adopting IFRS Standards; and
 - do not recognise such balances in IFRS financial statements; and
 - recognise revenue by using the regulated rate and the quantity of goods or services delivered to customers in the period (ie based on the entity's contracts with its customers).

Revenue = **P**rice (rate) x **Q**uantity



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- Identified rights and obligations created by different types of rate regulation, focusing on 'defined rate regulation'
- Explored possible viable financial reporting approaches to reflect the 'overlay' of the regulatory agreement between entity and rate regulator



Existing IFRS Standards [Price (rate) x Quantity]

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Discussion Paper

Reporting the financial effects of rate regulation

- Responses to DP suggest strong support for recognising some 'regulatory deferral account balances'
- Most common suggestion is focus on a 'revenue-based' approach, using either:
 - an Interpretation of / amendment to IFRS 15 Revenue from Contracts with Customers; or
 - a separate Standard based on the principles in IFRS 15
- Many requests to relate the rights and obligations to the definitions of asset and liability in the revised Conceptual Framework



- Is the regulatory agreement analogous to an executory contract?
- · Do the rights and obligations create assets/liabilities?
- If so:
 - Should they be recognised?
 - What is the nature of those assets/ liabilities?
 - When should they be recognised?
 - How should they be measured?
 - How should they be presented?
- How should changes in any assets/ liabilities recognised be presented in the statement(s) of profit or loss and other comprehensive income?
- What is meant by 'performance'?
 - Transfer to customers?
 - Transfer to rate regulator?
 - Other?

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Conceptual Framework Proposed revisions

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- In May 2015, the Board published proposals to revise the Conceptual Framework
- Project objectives: To improve financial reporting by providing a more complete, clearer and updated *Conceptual* Framework that can be used by:
 - the Board when it develops International Financial Reporting Standards (IFRS Standards); and
 - others to help them understand and apply IFRS Standards.

The Board is currently considering the feedback from the Exposure Draft



Conceptual Framework Elements

a

 Elements are the basic building blocks from which financial statements are constructed



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Conceptual Framework Proposed definitions of Elements

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Asset: Present
economic resources
controlled by the
entity as a result of
past events

Liability: Present obligations of the entity to transfer an economic resource as a result of past events

Equity: Assets - Liabilities

- An economic resource is a right that has the potential to produce economic benefits.
- A present obligation is an obligation [that has the potential to require the entity] to transfer economic resources that:
 - the entity has no practical ability to avoid; and
 - has arisen from a past event (ie economic benefits already received or activities already conducted)

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Conceptual Framework Proposed concepts—executory contracts

- An executory contract is a contract that is **equally unperformed**:
 - neither party has fulfilled any of its obligations, or
 - both parties have fulfilled their obligations partially and to an equal extent.
- An executory contract establishes a right and an obligation to exchange economic resources. The entity has:
 - an asset if the terms of exchange are favourable; or
 - a liability if the terms of exchange are unfavourable.
- To the extent that a party fulfils its obligations under the contract, the contract ceases to be executory.
 - If the reporting entity performs first under the contract, that performance is
 the event that changes the reporting entity's right and obligation to
 exchange economic resources into a right to receive an economic resource
 (ie an asset).

Conceptual Framework ED paragraphs 4. 40-4.42.
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Defined rate regulation:

- Restricts the setting of prices that an entity can charge to customers for essential goods or services
- Regulates the timing and amount of revenue (and profit) that an entity can bill to its customers
- Requires an entity to adjust the selling price (rate) to
 - recover 'allowable' costs and unbilled revenue amounts, or
 - eliminate 'excess' revenue or profits
- Establishes rights and obligations for an entity (and a rate regulator) through a 'regulatory agreement'

Defined rate regulation creates differences between amounts reported to the rate regulator and those reported in IFRS financial statements ('regulatory deferral account balances')

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The regulatory agreement Rights and obligations

- The regulatory agreement establishes the entity's:
 - obligations to:
 - ensure the rate-regulated services are available without disruption to supply;
 - deliver rate-regulated services on demand;
 - carry out other specified activities to achieve other government policies, eg social, environmental, fiscal policies.
 - right to receive a determinable amount of consideration in exchange for satisfying its obligations (the revenue requirement).



- The revenue requirement for the period is the amount of consideration that an entity has a right to bill its customers in exchange for satisfying its regulatory obligations
- The regulatory agreement includes a mechanism for determining the revenue requirement. This mechanism establishes:
 - the regulated rate for the period, which is based on the combination of:
 - estimated revenue requirement; and
 - estimated demand

Regulated rate comprises: a rate per unit, and/or a 'standing charge', ie a fixed amount.

- a rate adjustment mechanism to:
 - 'correct' for variances from estimates
 - adjust the timing of when the revenue requirement is billed to customers to enable the rate regulator to moderate rate fluctuations/ cash flows

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Revenue requirement Regulated rate

- The regulated rate typically includes amounts related to:
 - goods or services delivered to customers:
 - in the current period; and
 - in a different period
 - other specified activities (that may not meet the definition of a 'performance obligation' in IFRS 15), which are carried out
 - in the current period; and
 - in a different period
 - adjustments for variances from estimates relating to past periods



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Should the entity recognise a 'regulatory asset' or 'regulatory liability' when:

- the regulated rate reflects activities that:
 - occur in a different period?
 - do not meet the definition of a 'performance obligation' in IFRS 15?
- the regulated rate will be adjusted in the next or subsequent period(s) to reverse any under- or over-recovery by the entity

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Revenue Requirement Example

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Fact Pattern

- Entity A's rate regulator determines a fixed revenue requirement of CU200million per year for 3 year period (x1, x2 and x3)
- Determination includes:
 - CU7m per year for project to install insulation free of charge in the homes of specified customers (project starts in x2)
 - CU10m per year for storm repair costs (no costs in x1 or x2, CU30m in x3)
 - CU5m per year for CU15m under-recovered in periods prior to x1
- In x1, A actually receives CU210m due to higher than estimated demand

How much revenue should Entity A report in x1? If not CU210m, what should happen to the difference?

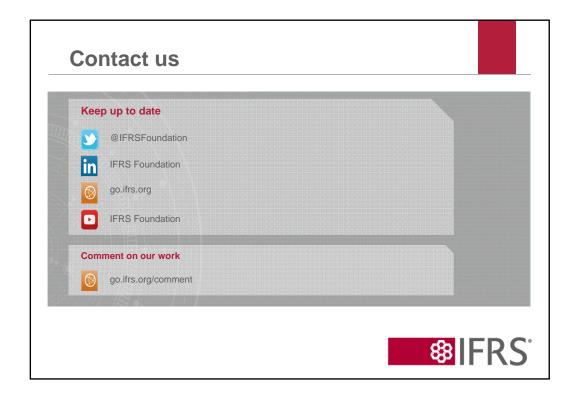


Next steps

- Continue research with targeted consultation/ field work
- Develop proposals for an accounting model
- Consider implications of the responses to the *Conceptual Framework* proposals
- Consult more widely through a second Discussion Paper



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Day 3—Friday 26 August 2016

Conference Programme Day 3

09:00 Soft Topic: Coping with disruptive technology and information overload

Jonah Owitti

Excursions: National Museums of Kenya, Nairobi Animal Orphanage and Game drive 10.30-18.00

End of Conference





