2017

Desktop survey: Disclosures of the New Accounting Standards in issuers' 2016 annual financial statements

IFRS 9 FINANCIAL INSTRUMENTS,
IFRS 15 REVENUE FROM CONTRACTS WITH CUSTOMERS
IFRS 16 LEASES

DATED: JULY 2017

THE IRSH AUDITING AND ACCOUNTING SUPERVISORY AUTHORITY (IAASA)

MISSION

To contribute to Ireland having a strong regulatory environment in which to do business by supervising and promoting high quality financial reporting, auditing and effective regulation of the accounting profession in the public interest

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1 Introduction – The new standards

As noted in IAASA's 2016 *Observations* document, for certain issuers aspects of IFRS 9 *Financial Instruments*, IFRS 15 *Revenue from Contracts with Customers* and IFRS 16 *Leases* (together the 'new standards') may represent a significant change compared to the existing Standards and, therefore, the recognition, measurement and presentation of assets, liabilities, income, expenses and cash flows may be affected. In addition, the European Securities and Markets Authority ('*ESMA*') issued *Common Enforcement Priorities for 2016 Financial Statements* , which included the impact of the new standards and related disclosures as an area of focus for national accounting enforcers when examining issuers' 2016 financial statements.

IFRS 9 *Financial Instruments*

IFRS 9 is expected to have a significant impact on financial institutions due to the introduction of the expected loss impairment model. Irish financial institutions have high levels of loans in arrears and legacy issues remaining from the financial crisis. Therefore, a high level of non-performing loans, forborne loans or loans that may have no impairment provision under the existing rules in IAS 39 *Financial Instruments: Recognition and Measurement* could have a disproportionate amount of 12 month or lifetime impairment losses requiring recognition on implementation of IFRS 9.

Issuers may benefit from the changes to the hedge accounting requirements in IFRS 9; those changes align hedge accounting and risk management, and apply these new principles to a broader set of risk components.

Section 5 below elaborates on aspects of the implementation of FRS 9.

IFRS 15 *Revenue from Contracts with Customers*

It is expected that adoption of IFRS 15 may have limited impact for some issuers (e.g. straightforward retail transactions). However, for other transactions (e.g. long-term contracts, multiple-element arrangements, transactions with variable consideration, and transactions with financing features) there may be a material impact on the amount and/or timing of revenue recognition.

This topic is covered in Section 6 below.

IFRS 16 *Leases*

IFRS 16 replaces IAS 17 *Leases* and introduces significant changes to lessee accounting. IFRS 16 requires a lessee to recognise almost all leases on the balance sheet (with limited exceptions permitted). Aspects of IFRS 16 that are likely to pose challenging for some issuers include: identifying all relevant contracts, capturing all the necessary data in accounting systems, considering all the practical difficulties such as dealing with contract extensions, termination options, discount rates for operating leases and the new reporting requirements.

For some issuers with significant leasing activities, implementing IFRS 16 may be a complex and significant project.

The implementation of IFRS 16 is addressed in Section 7 below.

Timing for providing disclosures of the impact of the new standards

The timing for providing disclosures of the impact of implementing the new standards is likely to vary between issuers depending on the complexity of the implementation process, the impact and, where relevant, differences in entities' timetables for capturing data and implementing new information systems.

However, it is expected that in many cases it would be inappropriate to delay providing disclosures (IFRS 9 and 15 refers) about any required changes in accounting policies and the financial statement impact in the period of initial application until publication of issuers' 2017 annual financial statements (i.e. in many cases the disclosures should be provided in issuers' 2017 half-yearly financial reports).

Response of ESMA and European national accounting enforcers

ESMA and European national accounting enforcers (including, in Ireland, IAASA) are monitoring the level of transparency that issuers provide in their financial statements regarding the preparation for and implementation of the new standards.

Consequently, IAASA has undertaken a desktop survey of the 2016 annual financial statements of Irish equity issuers to assess the level of preparedness by issuers for the implementation of the new standards in their financial statements in the period of initial application.

The survey examined the 2016 annual financial reports published by all 28 equity issuers listed on the main market of the Irish Stock Exchange and falling within IAASA's financial reporting remit and Allied Irish Banks plc, a debt issuer. Appendix I to this document sets out the individual annual financial statements covered by this survey analysed by sector. In undertaking this survey, IAASA did not seek additional information from any of the selected issuers.

2 Financial reporting examination remit of IAASA

The Irish Auditing and Accounting Supervisory Authority ('IAASA'), Ireland's accounting enforcer, is tasked with examining the annual and half-yearly financial reports (together 'periodic financial reports') of certain equity, debt and closed-ended fund entities with securities admitted to trading on a regulated market within the European Union ('EU') (together 'issuers') for compliance with the relevant reporting framework. The relevant reporting framework for the purposes of this document is confined to those issuers preparing their financial statements under International Financial Reporting Standards ('IFRS') as that is the accounting framework applicable to the 29 issuers forming the basis for this desk-top survey[1].

3 Purposes of this survey

The purposes of this desktop survey are:

(a) to provide an overview of the disclosures of the impact of implementation of the new standards provided in issuers' 2016 annual financial statements;

(b) to observe the extent to which issuers have taken on board the ESMA Statements on IFRS 9, IFRS 15 and IFRS 16; and

(c) to encourage preparers, management and directors to provide timely disclosures about any required changes in accounting policies and the financial statement impact in the period of initial application.

The results of IAASA's observations from this survey will be used to inform IAASA's future examination activities.

4 Disclosures required for accounting standards issued but not yet effective

Paragraph 30 of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* requires disclosure of known or '*reasonably estimable information*' relevant to assessing the possible impact that application of a new IFRS (that has been issued but is not yet effective and which has not been early adopted) will have on an entity's financial statements in the period of initial application. IFRS requires entities to provide qualitative and quantitative disclosures in the reporting periods leading up to adoption of the IFRS.

[1] i.e. Allied Irish Banks plc, a debt issuer at 31 December 2016, and the 28 equity issuers falling with IAASA's financial reporting remit

In addition, ESMA has published:

(a) a statement *Issues for the consideration in implementing IFRS 9:* Financial Instruments; and

(b) a statement *Issues for the consideration in implementing IFRS 15:* Revenue from Contracts with Customers.

ESMA has urged issuers to take into account ESMA's public statements when preparing their 2016 annual and subsequent annual and half-yearly financial statements. It is ESMA's expectation that, where the impacts are expected to be significant, issuers will:

(a) provide information about the accounting policy choices that are to be taken upon first application of the new standards;

(b) disaggregate the expected impact into elements that issuers use to measure the impact and are useful to users of the financial statements; and

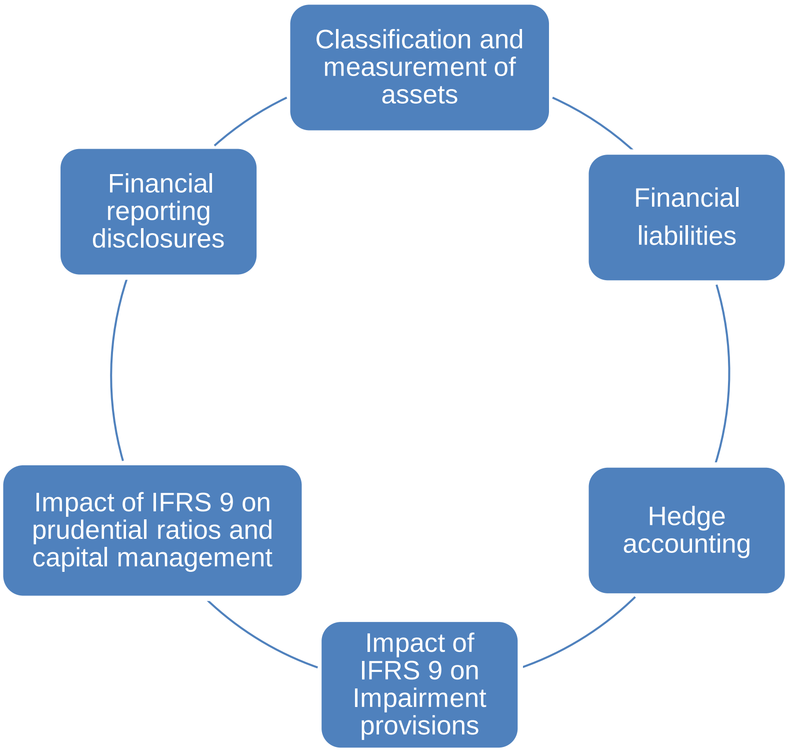
(c) explain the nature of the impacts so that users of the financial statements understand the changes and their key drivers when compared to the existing accounting principles on recognition and measurement.

PART I – IMPACTS OF IFRS 9 *FINANCIAL INSTRUMENTS*

5 Impacts of IFRS 9

5.1 Implementation of IFRS 9 – financial institutions

Financial institutions reported the *impacts of IFRS 9* under the following headings:



5.1.1 Classification and measurement – assets

All three financial institutions[2] stated that IFRS 9 was not expected to result in any significant changes to the classification and measurement of financial assets; however, IFRS 9 is expected to result in the following changes in the classification and measurement of assets:

(a) SPPI[3] test
A small number of instruments, mainly loans and receivables to customers, will fail the SPPI test. Accordingly, such instruments will be measured at fair value through profit or loss.

(b) Equity securities
In one instance, it was noted that all equity securities will continue to be measured at fair value; however, for individual securities, it has yet to be decided if the fair value movements will be presented in profit or loss, or in other comprehensive income ('OCI').

(c) Debt securities classified as available for sale
In all three financial institutions, debt securities classified as available for sale will primarily be measured at amortised cost or fair value through other comprehensive income, with a small minority measured at fair value through profit or loss ('FVTPL'). This is because of the contractual cash flow characteristics or the business model within which they are held. Financial assets that are currently at fair value through OCI (e.g. equity securities) will be measured as FVTPL, or designated at fair value through OCI.

[2] i.e. Allied Irish Banks plc ('AIB') , Bank of Ireland ('BoI'), and Permanent TSB Group Holdings plc ('PTSB')
[3] Solely payment of principal and interest

5.1.2 Financial liabilities

The classification of financial liabilities is largely unchanged under IFRS 9.

IAASA commentary For financial liabilities, there is no change to the classification and measurement for all the financial institutions except for the recognition of changes in own credit risk in other comprehensive income, for liabilities designated at fair value through profit or loss.

5.1.3 Hedge accounting

IFRS 9 includes an accounting policy choice, which allows entities retain the existing IAS 39 hedge accounting requirements until macro-hedge accounting is addressed by the IASB as part of a separate project.

IAASA commentary AIB and Bank of Ireland have disclosed that they will continue to apply the hedge accounting requirements of IAS 39 until the amended standard resulting from an IASB project on macro hedge accounting is effective. PTSB will make a final decision on the measurement basis at that date.

5.1.4 The expected credit loss ('ECL') model being adopted by financial institutions

Bank of Ireland stated that the measurement of ECL will primarily be based on:

> '*… a calculation of an asset's probability of default, loss given default and exposure at default associated with possible default events over either a 12 month horizon for stage 1 assets; or the remaining lifetime of the asset for stage 2 or stage 3 assets. The Group's IFRS 9 ECL modelling framework will leverage the Group's existing credit risk modelling framework used for regulatory capital purposes, appropriately calibrated to meet the requirements of IFRS 9.*'

PTSB stated that they expect to adopt an ECL framework that is:

> '*… consistent with industry best practice, as set out in the Global Public Policy Committee (''GPPC'') paper, and reflects an approach using PD, EAD and LGD components. The Group expects to leverage the systems and data used to calculate regulatory expected credit losses. In particular, key concepts such as the definition of default and measurement of credit risk (i.e. ranking of exposures for risk) are expected to be consistent across the impairment (accounting) and regulatory frameworks.*'

The specific ECL model to be applied by AIB is not readily apparent at this time.

IAASA commentary IAASA notes that the IFRS 9 ECL model to be used by financial institutions appears to leverage existing credit risk modelling frameworks used for regulatory capital purposes that are calibrated to meet the requirements of IFRS 9.

5.1.5 Impact of IFRS 9 on impairment provisions

The three Irish financial institutions have stated that IFRS 9 will result in either:

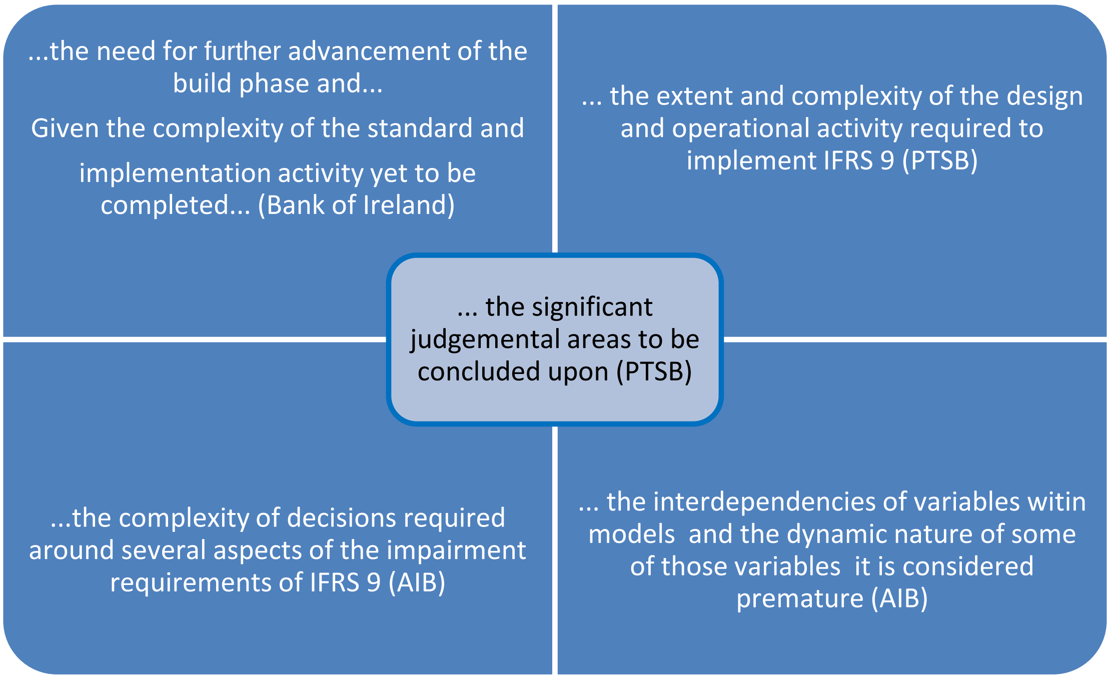
(a) higher impairment provisions;

(b) more volatile impairment charges; and/or

(c) significant disclosure impact.

IAASA commentary
Financial institutions did not quantify the possible impact that IFRS 9 will have on the impairment provision in the period of initial application of IFRS 9.

The three financial institutions did not disclose the '*possible impact*' in quantitative terms that initial application of IFRS 9 will have on entities. The reasons attributed for not disclosing the quantitative impact made reference to the following factors:



When will financial institutions quantify the impacts of IFRS 9 on impairments?
AIB disclosed that quantitative information of the impact of IFRS 9 on impairment provisions will be provided in its 2017 financial statements. Bank of Ireland and PTSB have not specified when known or reasonably estimable information relevant to assessing the impact of IFRS 9 on impairment provisions will be provided.

5.1.6 Impact of IFRS 9 on prudential ratios and capital management

All three financial institutions concluded that IFRS 9 may negatively affect their capital position. Each institution stated that it was not possible to quantify the impact on regulatory capital at this stage.

> *IAASA commentary*
>
> IAASA notes that none of the financial institutions provided an estimate of the magnitude of the impact of IFRS 9 in the period of initial application, in terms of either:
>
> (a) impairment provisions;
>
> (b) prudential ratios;
>
> (c) regulatory capital; or
>
> (d) alternative performance measures ('APMs').

AIB stated that:

'*It is not currently possible to estimate the precise financial effects of this new standard on the Group's results of operations, although it is expected that IFRS 9 will have a significant impact for the Group, as is the case for the banking industry as a whole. The introduction of IFRS 9 may also affect the Group's capital position.*'

Bank of Ireland stated that:

'*… the Group cannot reliably estimate, at this point, the quantitative impact on classification and measurement, impairment provisions and capital on initial application and thereafter.*'

Bank of Ireland noted that a key mitigating factor in assessing the impact of IFRS 9 on capital is that:

'*… Potential arrangements for transitional relief for the impact of IFRS 9 on regulatory capital are under consideration at both Basel Committee on Banking Supervision and EU level. The Basel Committee is also considering the longer-term interaction between ECL accounting provisions and regulatory capital. The outcome of these considerations is expected to be known during 2017.*'

PTSB disclosed the basis for the uncertainty around the impact of IFRS 9 on regulatory capital as follows:

'*The Group continues to assess the potential impact on its capital base. The impact is difficult to estimate at this stage given that the relationship between specific and general credit risk adjustments (in accordance with regulatory definitions) and the IFRS 9 stages is unclear.'*

and

'The Basel Committee is considering the implications of the new accounting requirements for existing regulatory requirements and has proposed a phasing of the impact over 5 years. The European Commission is also proposing a phase-in of the impact on IFRS 9, as set out in the draft proposals to amend the CRR published in November 2016. Despite the proposed phasing of the impact of IFRS 9, the new approach may negatively affect regulatory capital as at 1 January 2018 though it is still unclear on how regulators will ultimately treat the interaction between the accounting and regulatory frameworks for expected loss. PTSB will continue to closely monitor developments in relation to regulatory capital.'

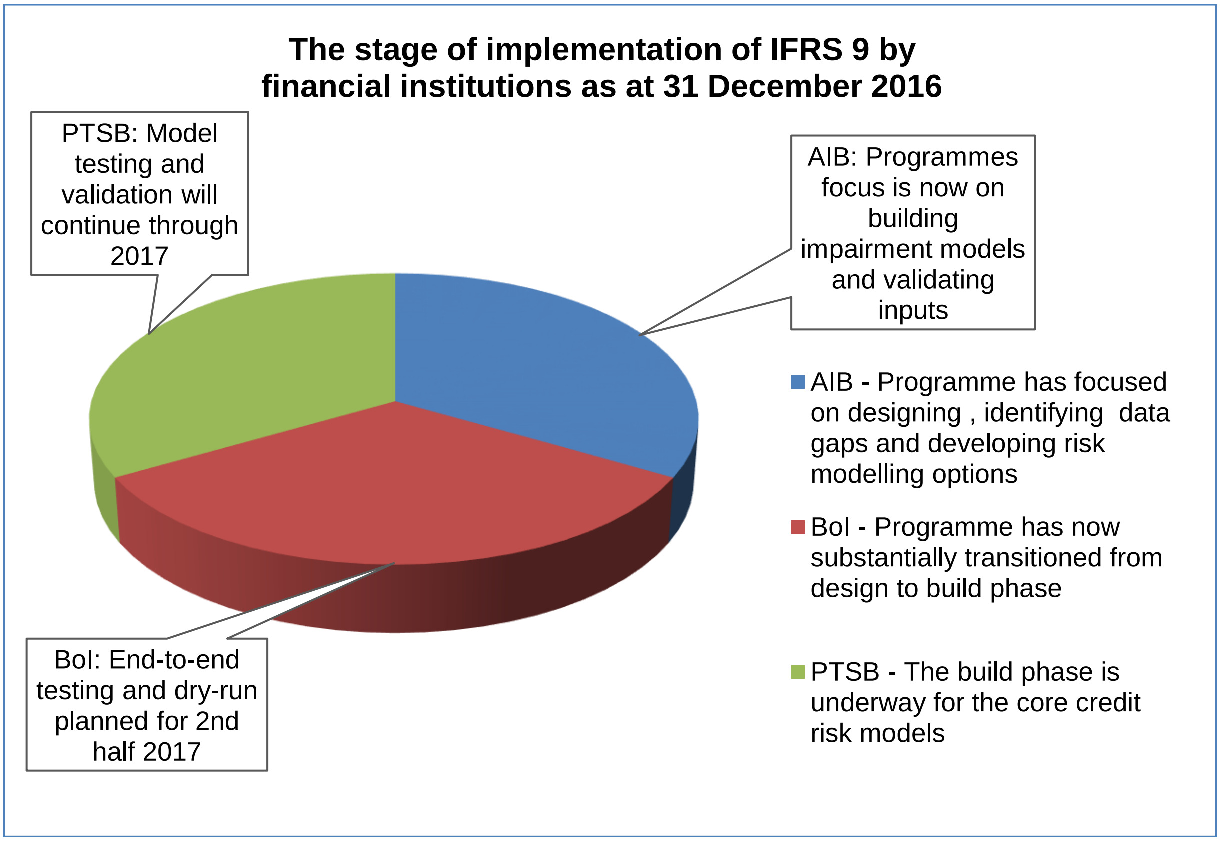
Findings of the European Banking Authority ('EBA')
The EBA published a [Report]() which confirmed the [EBA's initial observations]() on the level of preparedness for the implementation of IFRS 9 and the estimated impact of IFRS 9 on regulatory own funds. The EBA Report highlights that:

> '*… banks have made further progress on the implementation of IFRS 9 since the previous exercise, but smaller banks are still lagging behind in their preparation compared with larger banks …*
>
> *On the quantitative side, the estimated increase of provisions is on average 13% compared to the current levels of provisions under IAS 39 [86% of respondents estimated an increase in IFRS 9 provisions of up to 22% in the second exercise]. The Common Equity Tier 1 (CET1) ratios are expected to decrease on average by up to 45 basis points (bps) [up to 75 bps for 86% of respondents]. Smaller banks, which mainly use the Standardised Approach (SA) for measuring credit risk, estimated a larger impact on own funds ratios than larger banks of the sample.*'

It would appear to IAASA that uncertainty as to how regulators will treat the interaction between the accounting and regulatory frameworks, for expected losses, may be one factor in delaying the quantification of the impact of IFRS 9 disclosed by financial institutions.

IAASA commentary It is IAASA's expectation that as reliable data becomes available financial institutions will strike an appropriate balance between not providing any quantitative data and providing reliable quantifiable data on the impact on impairment provisions, prudential ratios, regulatory capital and relevant APMs.

5.1.7 Implementation timetable



5.1.8 IFRS 9 disclosures

AIB and Bank of Ireland have stated they are planning to provide a comprehensive suite of transitional disclosures including disclosures outlining:

(a) the impact on transition; and

(b) new disclosures that are being developed for disclosure on an on-going basis.

PTSB is currently assessing the impact of IFRS 9 on its financial reporting requirements.

AIB and Bank of Ireland have stated that they will apply the various provisions of IFRS 9 with effect from 1 January 2018, however, prior periods will not be restated. Any difference between the previous carrying amount under IAS 39 and the carrying amount at the date of initial application of IFRS 9 will be recognised in opening retained earnings (or other component of equity as appropriate) at 1 January 2018.

5.1.9 Conclusion: IFRS 9

The three financial institutions have provided detailed qualitative descriptions of the key concepts and expected impacts of the transition to IFRS 9 that is of a good quality in their 2016 annual financial statements. The banks have disclosed the implementation of IFRS 9 in the front-end reports and in the notes to the financial statements.

The IFRS 9 disclosures appear consistent with the implementation programmes being at various stages of completion. The IFRS 9 programmes represent a significant project for each financial institution. It is clear that implementing an ECL model poses significant challenges that are technical in nature and involve the need for complex management judgements, restructuring of data being captured for lifetime losses and changes to reporting systems. Subjective management judgements includes the following:

(a) staging assessment;

(b) defining default;

(c) data availability for forward looking information;

(d) incorporation of multiple scenarios in models; and

(e) other complex factors.

The ECL models in financial institutions appear to be models that leverage the existing credit risk models used for regulatory capital purposes and which are calibrated to meet the requirements of IFRS 9. IAASA has noted that the findings are consistent with surveys on the implementation of IFRS 9 by financial institutions across Europe in that few institutions have quantified the impacts on impairment provisions to date.

IAASA commentary

It is a matter of concern to IAASA that some financial institutions first quantification of the magnitude of the impact of IFRS 9 will not be disclosed in the financial statements until the publication of the 2017 annual financial statements (i.e. a date after IFRS 9 becomes effective).

IAASA reminds financial institutions that if ‘reasonably estimable’ quantitative information exists this should be disclosed notwithstanding that the actual amounts in the 2018 financial statements might be different owing to changes in the composition of the portfolios or different economic conditions [IAS 8.30 – 31 and the ESMA public statement on IFRS 9 refer].

IAASA also reminds financial institutions that ESMA is of the view that in most cases it would be not be appropriate to provide disclosures about the changes in the accounting policies and their impacts only in the 2017 annual financial statements.

IAASA calls on issuers to consider the extent of disclosures to be included in future financial reports, for example:

(a) updates to qualitative and quantitative information regarding the implementation and impact of IFRS 9;

(b) disaggregation of the expected impacts into elements that issuers use to measure the impact and are useful to users of financial statements; and

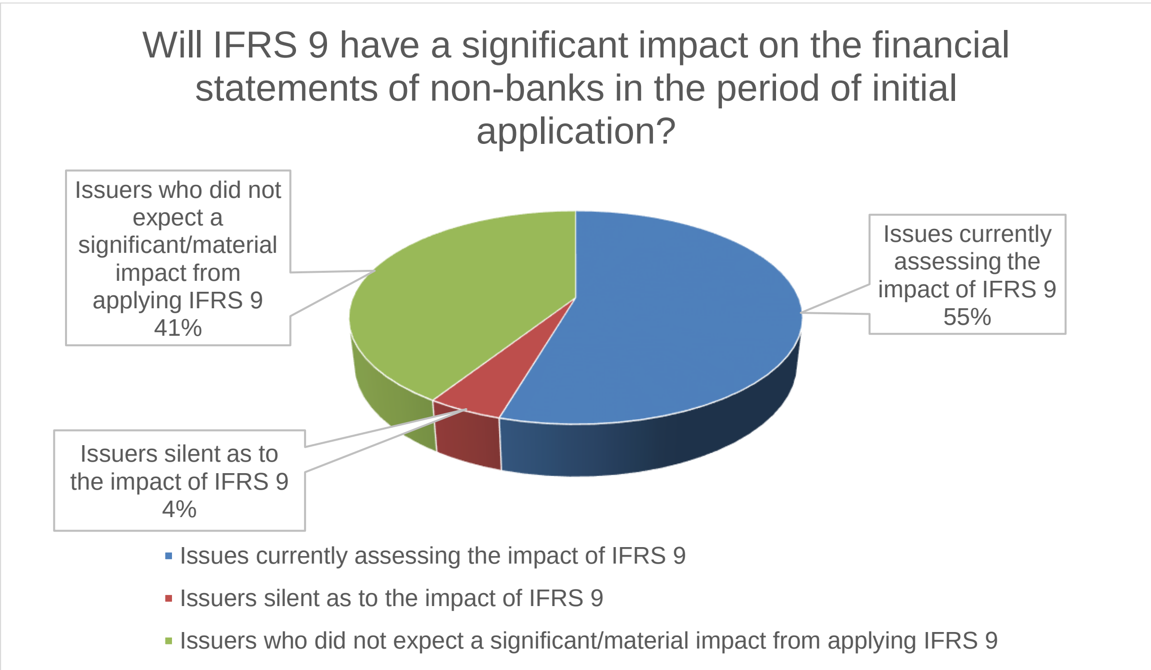
(c) quantitative information on impairment provisions, prudential ratios, regulatory capital and key APMs where a significant impact from implementation of IFRS 9 is expected and reliable quantitative data becomes available.

Financial institutions are encouraged to take into account ESMA public statement on IFRS 9 when preparing their 2017 interim and annual financial statements.

5.2 Impacts of IFRS 9 – non-financial institutions

22 issuers were examined (i.e. the 29 equity issuers excluding the 3 financial institutions (described in section 6.1 above) and 4 equity issuers whose 2016 financial reports were not published in sufficient time for evaluation in this survey).

5.2.1 FRS 9 impact on non-financial institutions



Twelve of the 22 (55%) issuers stated they are currently assessing the impact of IFRS 9 on their financial statements in the period of initial application. Nine of the 22 (41%) issuers stated they did not expect a significant/material impact from IFRS 9. One issuer was silent as to whether or not IFRS 9 would have a significant impact. There is no evidence to suggest that the one issuer will be materially impacted.

5.2.2 Impact on presentation and disclosure

Five of the 22 (23%) issuers disclosed that expanded disclosures and/or changes in presentation will be required once IFRS 9 is adopted. The remaining issuers did not refer to new disclosures required by IFRS 9.

5.2.3 *Timing of adoption of IFRS 9*

Eight of the 22 (36%) issuers disclosed that they would be applying IFRS 9 from its effective date of 1 January 2018 and the remaining 14 non-bank issuers were silent on this matter; however, none indicated they intended to early adopt IFRS 9.

Three of the 22 (14%) issuers disclosed that IFRS 9 may result in the earlier recognition of credit losses.

5.2.4 Conclusion: IFRS 9 non-financial institutions

IAASA commentary While IAASA notes that many non-bank issuers are still evaluating the impacts of implementing IFRS 9, all are planning to implement it from its effective date and entities expect earlier recognition of credit losses together with expanded disclosures required by IFRS 9.

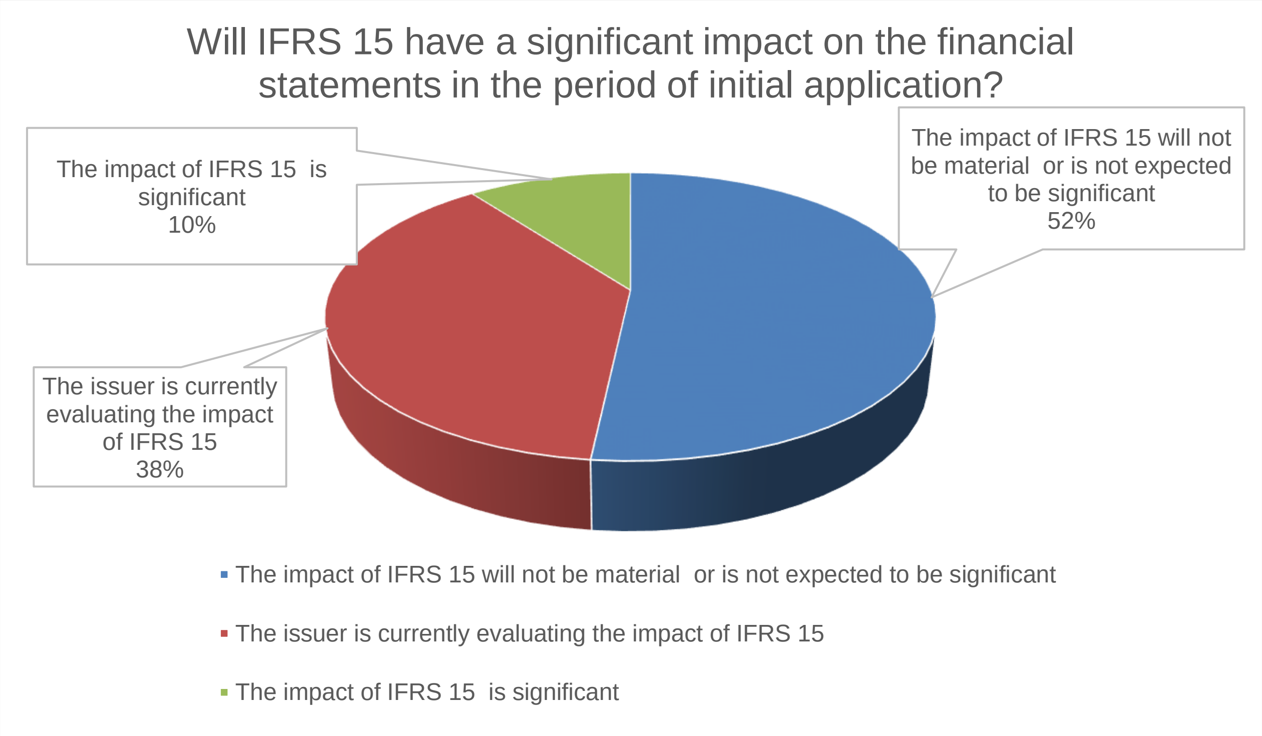
PART II – IMPACTS OF IFRS 15 *REVENUES FROM CONTRACTS WITH CUSTOMERS*

6 Impacts of IFRS 15

For some entities, it will be necessary for them to undertake a detailed analysis of all revenue contracts for each type of revenue stream in order to determine the full impacts of IFRS 15. Areas likely to require detailed analysis include entities with long-term contracts, multiple-element arrangements, variable consideration arrangements, contracts with financing features and contracts with multiple performance obligations.

Issuers' IFRS 15 disclosures should describe the differences between IFRS 15 and current practice.

6.1 The impact of IFRS 15 on entities' financial statements



Fifteen of the 29 issuers (52%) disclosed that the impact of IFRS 15 would not be material or that the impact was not expected to be significant. A more detailed analysis of the remaining issuers found the following trends:

(a) fourteen of 29 issuers or 48% characterised their assessment of the impact of IFRS 15 as on-going and/or will have a significant impact; and

(b) of these 14 issuers, 11 (or 38% of the total) are currently evaluating the impact that IFRS 15 will have on revenue. The remaining 3 issuers (or 10% of the total) described the impact of IFRS 15 on revenue as significant.

A closer analysis of the disclosures made by 'relevant issuers' (i.e. excluding issuers where the impact of IFRS 15 is not expected to be significant) is set out below.

6.2 Implementing the key concepts of IFRS 15

Eleven of 14 (79%) relevant issuers did not provide a description of the key concepts. Three of 14 (21%) of relevant issuers disclosed a description of key concepts that had been identified in their analysis to-date.

> *IAASA commentary*
>
> It is not readily apparent as to whether or not the lack of disclosure of the key concepts of IFRS 15 is because many issuers are at an early stage of their analysis or because of other factors not apparent from a desktop examination.
>
> It is IAASA's expectation that when issuers expect IFRS 15 to have a significant impact on the financial statements they will enhance their disclosures and explanations of how key concepts of IFRS 15 will be implemented in accordance with the requirements of IAS 8.30 – 31 [and also have regard to ESMA's public statement on IFRS 15].

6.3 Key concepts of IFRS 15 identified by issuers

The key concepts identified by issuers in applying IFRS 15 were as follows:

(a) revenue derived from construction contracts;

(b) variable consideration;

(c) warranty obligations;

(d) bundling and unbundling of contracts to determine performance obligations;

(e) identification of performance conditions after go-live;

(f) loss making contracts;

(g) revenue recognition over time or at a point in time;

(h) accounting for additional costs incurred in obtaining or fulfilling a contract;

(i) accounting for certain costs which are currently expensed e.g. sales commissions;

(j) timing of recognition of revenue in certain long term service elements of revenue contracts; and

(k) disclosure requirements.

> *IAASA commentary*
>
> Disclosures of the expected impact of IFRS 15 presented by a small number of companies (3) was of good quality and indicative of the type of information that is useful to users of financial statements.
>
> However, a large number of issuers provided little or no disclosure of the key concepts of IFRS 15.

6.4 Highlighting differences to the current approach

IAASA commentary

Twelve of 14 (86%) relevant issuers did not highlight important differences to current practices arising from the initial application of IFRS 15.

Only two of 14 (14%) relevant issuers included a description of the key concepts of IFRS 15 in their 2016 financial statements (as set out at item 6.3 above).

6.5 Implementation timetable for IFRS 15

All issuers disclosed that they will apply IFRS 15 from its effective date and none chose to early adopt IFRS 15. However, in most cases, the issuers' description did not describe:

(a) what were the key implementation milestones;

(b) what stage(s) of implementation are completed; and

(c) what was the expected timeline(s) to complete each stage of the implementation programme.

IAASA commentary

Issuers' boilerplate reference to applying IFRS 15 from its effective date does not constitute a description of the timeline for implementation referred to in ESMA Public Statement on IFRS 15.

The absence of detailed disclosure of the timetable for the implementation of IFRS 15 contrasts with the detailed disclosure of the timetable for implementing IFRS 9 provided by financial institutions [section 5 refers].

6.6 Expected use of practical expedients

IAASA commentary

Thirteen of 14 (93%) issuers (where the assessment of IFRS 15 is ongoing) did not refer to the use of practical expedients available under IFRS 15. One issuer stated it will apply the modified retrospective application approach.

6.7 Quantification of the possible impact of IFRS 15

No issuer disclosed a quantification of the impact of IFRS 15 on initial application either (e.g. in relation to the amount or timing of the revenue recognised in relation to the different revenue streams).

6.8 IFRS 15 Disclosures

Four of the 29 (14%) issuers stated that the implementation of IFRS 15 will result in significant changes in disclosures of revenue from contracts with customers. Twenty-five of 29 (86%) of issuers' were silent as to the changes in disclosures that will arise from the implementation of IFRS 15.

IAASA commentary

IAASA reminds all issuers that entities are required by IFRS 15 to disclose more information about contracts with customers than is currently required under IAS 18 *Revenue* and IAS 11 *Construction Contracts*, including more disaggregated information about revenue and more information about performance obligations. [IFRS 15.114 – 128 refer.]

6.9 Conclusion: IFRS 15

IFRS 15 was issued in May 2014. Issuers' 2016 annual reports indicate that for 48% of issuers, the IFRS 15 analysis was characterised as '*preliminary*' or '*on-going'*. IAASA has noted that for many issuers a preliminary analysis of IFRS 15 may be insufficient to provide users with a complete understanding of the potential impact of IFRS 15 in the period of initial application.

IAASA commentary

Disclosures of the expected impact of IFRS 15 presented by a small number of companies was of good quality and indicative of the type of information that is useful to users of financial statements.

However, a large number of issuers provided little or no disclosure of the key concepts of IFRS 15.

IAASA reminds issuers that under IFRS 15, all entities are required to disclose more information about their contracts with customers than is currently required under IAS 18 Revenue and IAS 11 Construction Contracts for example, disaggregation of revenue, performance obligations, assets recognised to obtain or fulfil a contract, and significant judgements in the application of the standards.

PART III – IMPACTS OF IFRS 16 *LEASES*

7 Impacts of IFRS 16

IFRS 16 *Leases* was issued in January 2016 and is effective for annual reporting periods beginning on or after 1 January 2019. This new standard replaces IAS 17 *Leases* and introduces significant changes to lessee accounting.

Under IFRS 16, a contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

For lessors, the accounting is largely unchanged; however, the IASB has updated the guidance on the definition of a lease (as well as the guidance on the combination and separation of contracts). Under IFRS 16, a lessee recognises a right-of-use asset and a lease liability. The right-of-use asset is treated similarly to other non-financial assets and is depreciated accordingly. The lease liability is initially measured at the present value of the lease payments payable over the lease term, discounted at the rate implicit in the lease if that can be readily determined.

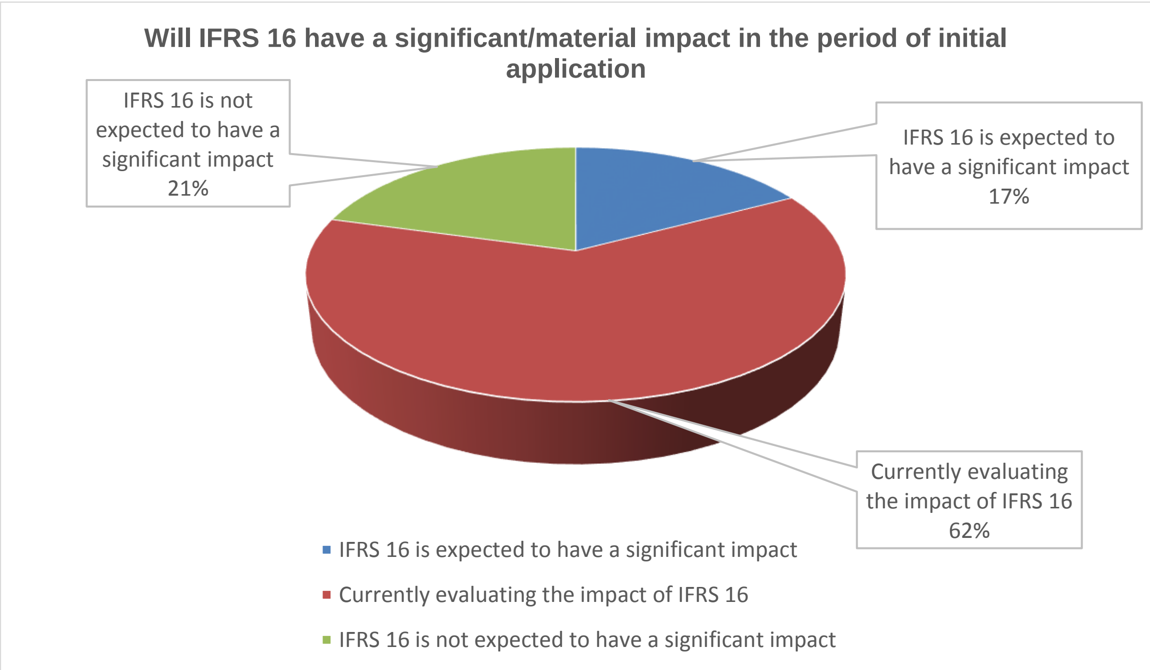
> *IAASA commentary*
>
> IAASA note that a number of factors can influence issuers' calculation of the lease liability including but not limited to, the discount rate, the expected term of leases including renewal options and optional transition exemptions for short-term leases and low-value items.

IAASA has observed the following information from issuers' 2016 annual financial statements:

7.1 Early adoption of IFRS 16

All 29 issuers referenced IFRS 16; however, none indicated they intended to early adopt the Standard.

7.2 The impact of IFRS 16 in the period of initial application



Five of the 29 issuers (17%) stated that IFRS 16 is expected to have a significant impact on the financial statements. These issuers often had commitments to a range of assets principally relating to property leases, plant, machinery, vehicles, equipment and other long-term term leases.

A further 18 of the 29 issuers (62%) disclosed that they were currently evaluating the impact of IFRS 16. Of these 18 issuers, IAASA noted that a large majority reported a significant amount of operating lease commitments in the notes to the financial statements.

Six of the 29 (21%) issuers disclosed that IFRS 16 is not expected to have a material impact on the financial statements. Most of the issuers falling into this group have limited or no exposure to operating lease commitments and, therefore, are unlikely to be materially impacted by bringing operating leases on balance sheet.

IAASA commentary
IAASA note that the existence of significant amounts of operating lease commitments is only an indication that an issuer has significant leasing activities, however, it may not be an accurate proxy for the amount of leases to be recognised under IFRS 16. The amount of lease assets and liabilities recognised (under IFRS 16) is subject to applying the optional transitional exemptions permitted by IFRS 16 related to short-term and/or low-value leases and a detailed analysis of all contracts that may contain leases.

7.3 Timeline for implementation of IFRS 16

Eighteen of the 29 issuers or 62% of issuers described the progress in their implementation programmes for IFRS 16 as either on-going, being assessed, or under review. Six issuers or (21%) were silent as to the status of their IFRS 16 implementation timetable (and three of these six issuers disclosed material amounts of operating lease commitments). The remaining five issuers did not expect IFRS 16 to have a significant impact and therefore detailed implementation disclosures were not relevant. In most cases, the issuers did not provide a description of the following:

(a) the key implementation milestones;

(b) the current stage of implementation and whether or not those stages were completed; and/or

(c) the expected timeline(s) to complete each stage of the implementation programme.

IAASA commentary
IAASA has noted that in most cases the absence of an implementation timetable limits the ability of users to understand the timeline for implementing IFRS 16, progress achieved therein and key milestones achieved. IAASA encourages issuers to enhance the details of their IFRS 16 implementation timetable in future reports.

7.4 Impact on the statement of financial position ('SOFP')

A contract is, or contains, a lease if it conveys the right to control the use of an identified asset for a period of time in exchange for consideration. [IFRS 16:9 refers].

Thirteen of the 22 (59%) of relevant issuers (i.e. excluding six issuers where the IFRS 16 is not expected to have a material impact) have stated that IFRS 16 will require the recognition of the following:

(a) a liability to make lease payments (i.e. the lease liability); and

(b) an asset representing the right to use the underlying asset during the lease term (i.e. the right-of-use asset).

The remaining issuers' were silent as to the recognition of right-of-use assets or financial lease liabilities arising from applying IFRS 16.

Only four of the 22 (18%) issuers stated that some differences may arise following updated guidance on the definition of a lease contained in IFRS 16. The remaining issuers' were silent as to the impact of the updated guidance on the definition of a lease and, in particular, the identification of leases.

IAASA commentary

IAASA note that IFRS 16 introduces new estimates and judgement thresholds that affect the identification, classification and measurement of leases. IAASA note that many issuers are currently evaluating the implication of IFRS 16 including:

(a) identifying all leases;

(b) separating components of a contract that may qualify as a lease.

7.5 Impact on the statement of comprehensive income ('SOCI')

One issuer disclosed that IFRS 16 would result in increased debt being recognised on the Statement of Financial Position without any further commentary of other effects.

Only four of the 13 (13%) issuers that are currently assessing the impact of IFRS 16 disclosed that increased depreciation (within operating costs in the SOCI) would be separately recognised on right-of-use leased assets. Three of 13 (23%) of relevant issuers disclosed that increased interest expense (within finance costs) will be recognised on lease liabilities. Only two issuers noted that the operating lease expense would be reduced. The remaining issuers were otherwise silent as to the impacts of IFRS 16 on the SOCI.

IAASA commentary

IAASA note that there is room for improvement in the description of differences from current accounting practices arising from the initial application of IFRS 16 Leases. Most, but not all, issuers disclosures:

(a) lacked sufficient detail of the key changes to accounting for leases; or

(b) the descriptions were incomplete; or

(c) issuers' are silent on any key changes (SOFP, SOCI) arising from IFRS 16.

However, IAASA has noted a small number of issuers that presented good quality disclosures as evidence of the quality of disclosures that can be achieved by issuers.

It is IAASA's expectation that as implementation of IFRS 16 progresses, issuers will enhance the level of detail of their transition to IFRS 16 in future half-yearly and annual financial statements.

7.6 IFRS 16 disclosures

Only four issuers disclosed that IFRS 16 will result in significantly increased disclosures. IAASA are cognisant that that there are still circa 18 months before IFRS 16 becomes effective. It is likely that many issuers with significant leasing activities are currently assessing the additional data that is required to be captured by their systems and are still in the design phase of their IFRS 16 implementation plans.

7.7 Expected use of practical expedients

Nine of 23 relevant issuers (39%) (i.e. excluding 6 issuers where IFRS 16 is not expected to have a significant) have disclosed that a lessee can choose not to apply IFRS 16 to leases of a low-value (e.g. personal computers) and short-term leases (i.e. leases with a term of 12 months or less). In cases where issuers have not referred to their expected use of the optional practical expedients available, it remains unclear whether or not there are significant factors that alter the amount of operating leases that may be recognised.

> *IAASA commentary*
>
> IAASA reminds issuers (where relevant) to disclose the expected use of transitional practical expedients, so that users can be informed of the judgements made by directors on initial application of IFRS 16 and to enable comparability across financial statements.

7.8 Quantification of the impact of IFRS 16

Two issuers (9%) of affected issuers provided a quantification (or part quantification) of the amount of right-of-use assets that may be recognised arising from applying IFRS 16. Another issuer stated that the application of IFRS 16 is not expected to have a material effect on its '*net*' assets, and the effects on its profit are expected to be immaterial on a '*net*' basis. Three issuers (13%) who did not quantify the impact of IFRS 16 did explicitly refer to the amount of operating lease commitments in the notes.

One issuer noted that the amount of operating lease commitments should not be used as a proxy for the impact of IFRS 16 on the financial statements.

Issuers described a number of factors that limit their ability to quantify the impact for IFRS 16 at this time. These include uncertainty about the following matters:

(a) the discount rate and/or the entity's marginal borrowing costs are not known and/or may not be readily determined;

(b) some of the (operating lease) commitments may be covered by the optional practical expedients for short-term and low value leases;

(c) uncertainty related to the expected term of leases including renewal options;

(d) some commitments may be related to arrangements which do not qualify as leases; and

(e) uncertainty regarding the contractual terms at the date of adoption.

> *IAASA commentary*
>
> The small number of issuers that quantified the impact of IFRS 16 in their 2016 annual financial statements is consistent with surveys of European entities.
>
> It is IAASA's expectation that as issuers progress their preparations for IFRS 16, where relevant, they will disclose a quantification of the impact on the financial statements where known or reasonably estimable information becomes available.

7.9 Conclusion

As of the time of compiling this document (July 2017), there is less than 18 months to IFRS 16 becoming effective on 1 January 2019. A small number of issuers have already provided significant disclosures of the expected impact of IFRS 16, having described:

(a) the key IFRS 16 concepts;

(b) changes to current practice; and

(c) the impact of IFRS 16 on the SOCI and the SOFP.

However, the majority of potentially affected issuers appear to be at an early stage of their analysis of IFRS 16. The lack of detail in many issuers' financial statements reflects this.

IAASA commentary IAASA recommends that where entities are expected to be significantly impacted by IFRS 16 the following information should be included progressively in future annual and half-yearly financial statements: (a) additional qualitative and quantitative information regarding the implementation and impact of IFRS 16 in the period of initial application; (b) disaggregate the expected impacts into elements that are useful to users of financial statements; and (c) quantitative information on the impact on profitability, loan covenant agreements, and key APMs where a significant impact from implementation of IFRS 16 is expected and reliable quantitative data becomes available.

In addition, IAASA encourages entities to take into account ESMA's public statements when preparing their 2017 interim and annual financial statements.

Appendix I – Classification of Irish issuers, by sector

Sector	Issuer	Reporting date
Airline & Transportation	Irish Continental Group plc Ryanair Holdings plc	31 December 2016 31 March 2016
Beverages	C&C Group plc	28 February 2017
Biotech & Pharmaceutical	Mainstay Medical International plc UDG Healthcare plc	31 December 2016 30 September 2016
Building Material & Construction	CRH plc Grafton Group plc Kingspan Group plc	31 December 2016 31 December 2016 31 December 2016
Casino & Gaming	Paddy Power Betfair plc	31 December 2016
Containers, Paper & Packaging	Smurfit Kappa Group plc	31 December 2016
Financial Institution & Financial Services	Allied Irish Banks plc Bank of Ireland IFG Group plc Permanent TSB Group Holdings plc	31 December 2016 31 December 2016 31 December 2016 31 December 2016
Food, Convenience Foods, Nutrition & Ingredients	Aryzta plc Glanbia plc Greencore Group plc Kerry Group plc	31 July 2016 31 December 2016 30 September 2016 31 December 2016
Hotel & Leisure	Dalata Hotel Group plc	31 December 2016
Homebuilding	Cairn Homes plc	31 December 2016
Insurance	FBD Holdings plc	31 December 2016
Oil, Gas & Mining	Aminex plc Kenmare Resources plc	31 December 2016 31 December 2016
Publishing & Broadcasting	Independent News and Media plc	31 December 2016
Real Estate Investment Trust	Green REIT plc Hibernia REIT plc Irish Residential Property REIT plc	30 June 2016 31 March 2017 31 December 2016
Sales, Marketing, Distribution & Business Support Services	DCC plc	31 March 2017
Technology: E-business Infrastructure	Datalex plc	31 December 2016